

1 A To provide information to shareholders and other users of the accounts.

2 Q What sort of information is that?

3 A They prepare accounts that include a financial review, income statement, balance sheet, and
4 accompanying notes.

5 Q You say annual reports. What are the annual reports? What is the purpose of an annual
6 report?

7 A To provide the financial position of the company at the year end at which they're reporting
8 and to provide a review of the financial information for the year then ending.

9 Q The financial statements - what purpose do they serve?

10 A To support the information that forms part of that annual review.

11 Q In these annual reports and financial statements you generally find turnover. Is that
12 correct?

13 A Yes.

14 Q Out of interest, why is it called turnover?

15 A Because it's the turnover of goods or services for the entity.

16 Q So, the amount of services or goods you are turning over.

17 A Yes.

18 Q You say in your first report at para. 3.1.1 - you do not have to turn it up - that turnover is
19 sometimes called 'revenue'; it is sometimes called 'sales' or 'income'. Why is that? Why
20 are those interchangeable?

21 A Because it can be called, and represented in various different forms in various different
22 entities.

23 Q Basically, as I take your opinion, the financial metric - whether you call it sales, turnover,
24 income - indicates the extent to which a company is providing a particular service.

25 A It indicates the extent to which the company is providing a particular service. It can do, yes.

26 Q It is a transaction-based metric.

27 A Yes.

28 Q With that in mind, could you go to NCB4, Volume 1, p.109? This is essentially the 2009
29 annual reports and accounts for Hays.

30 A Yes.

31 Q At p.111 you see the contents of the annual report in the financial statements. I think we
32 can agree that, broadly, they are similar contents to that which you would find in most
33 companies' accounts.

1 A Yes, the framework for what is included in a company's accounts is set by, firstly, the
2 Companies Act and then the accounting framework within which they operate - whether
3 that be International Accounting Standards, UK GAAP, or otherwise.

4 Q So, you would get the financial operational highlights, you have a chairman's statement ----
5 A Yes.

6 Q If we go on to p.113, this is the financial and operational highlights which I think you have
7 just said you would see in most annual reports and accounts.

8 A Yes.

9 Q In most financial operational highlights, I think you would agree that you would see the
10 turnover figure, or a revenue figure?

11 A It would depend upon the industry in which the business operates and how the business
12 carries out its operations and in certain companies, for example, a bank you wouldn't see a
13 turnover number because it would report net interest income. In businesses where you
14 would have a mix of services, for example, a bank and an insurance company, then it may
15 have splits between those in the notes, so it would really depend on the relevance of that
16 turnover figure as a metric as to whether it was included in the operational highlights as a
17 figure on its own.

18 If you are looking at faithful presentation of the accounts under the international accounting
19 standards framework under which these financial statements are prepared, then the
20 overriding requirement is to produce a set of financial statements that includes all of those
21 disclosures at some point that would inform a user of the accounts, so it may not necessarily
22 be in the financial highlights but if it is relevant it would be somewhere in the financial
23 statements.

24 Q Broadly you would, as I understand your evidence you have given to the Tribunal you
25 would expect the turnover figure in the financial operational highlights but, depending on
26 the industry you might find another figure?

27 A Yes, you might, or you might find a split in the notes to the financial statements or
28 elsewhere.

29 Q Why is it, in your opinion, we see net fees there and not turnover?

30 A Because in this particular industry there is a mix of services that is provided and the first
31 point at which these financial statements hit solid rock in terms of comparability of the
32 services is at the net fees level.

1 Q It is slightly more than comparability, is it not? What is the purpose of presenting the net
2 fees figure on this page which is the highlights page? What is the purpose of presenting the
3 net fees figure?

4 A It is to give the user of the financial statements the information that they require to track the
5 performance of the business in summary.

6 Q Precisely. It gives the true indication of the performance of the business?

7 A Yes, it gives the relevant statistics that in summary the company believes should be drawn
8 out in the operational highlights.

9 Q Why should operating profit be just below net fees? What is that indicating to the reader?

10 A That that's the next relevant indicator that they believe should be drawn out in the summary.

11 Q Do you accept on this page that "net fees" is being used to judge the performance of Hays
12 as a business?

13 A Yes, for good reason, because where you have a mix of business, as I say the first line
14 where you can actually judge the performance of the overall business is net fees.

15 Q Why in your opinion do they not put turnover here?

16 A Because they believe that turnover is relevant to part of their business and not all of it.
17 Therefore, in terms of segmental reporting, which is carried out elsewhere in the financial
18 statements they believe it's relevant in terms of determining how that net fees figure is
19 arrived at and it is disclosed separately in the financial statements as such. So the turnover
20 number is in the financial statements, and in the financial review.

21 Q We will come on to that, obviously we have seen the word "turnover" mentioned, and my
22 question to you is why, in the highlights, is a company such as Hays presenting net fees
23 rather than turnover?

24 A Because turnover is for a segment of its business, not for the business overall.

25 Q Only for a segment?

26 A Yes.

27 Q What I would suggest to you here is that essentially Hays is substituting ----?

28 A Sorry, could I correct what I just said?

29 Q Certainly, yes.

30 A The turnover is not just a segment of the business, because it includes both the permanent
31 and the temporary staff but the mix in turnover is confused because you have commission
32 based permanent employee business in it and temporary business, so it's a combination of
33 for the permanent business the turnover is equivalent to the net fees, and for the temp ----

34 Q Could you say that again?

1 A The turnover is equivalent to the net fees essentially.

2 Q For the business?

3 A For the permanent side of the business, but in the temporary side of the business the
4 turnover is not equivalent to net fees, so the first point at which the permanent side of the
5 business, and the temporary side of the business equate in terms of financial performance is
6 when you come to the net fees line, and that is why I would imagine the net fees line is
7 pulled out in terms of the financial summary.

8 Q Here we are looking at the whole of Hays' business?

9 A Yes.

10 Q And there is one figure "net fees"?

11 A Yes, well there are several figures including net fees. Net fees is the starting point for the
12 financial summary.

13 Q If you had turnover there and not net fees, what you have just said to the Tribunal is that it
14 would provide a confusing picture?

15 A Well it would not necessarily give you the first point at which the business demonstrates a
16 real trend in its profitability because within the turnover for the temporary business, as I
17 say, you have costs associated with that before you come to net fees, and the company's
18 determination is that that information, to give a fair representation, is disclosed not on here,
19 but in the financial statements.

20 Q And it would not give a real indication of the growth of the business, if we just had a
21 turnover figure and not net fees?

22 A Yes, it could do.

23 Q "It could do"?

24 A Yes.

25 Q How?

26 A Because if you looked at – it's confused because you have a combination of essentially
27 gross profit plus turnover, if you reported a turnover line, but it would still give some
28 indication of the performance of the business. If you talk about turnover growth or decline,
29 that would represent the sum of commissions on permanent worker placements and the
30 gross value of the sales on temporary worker placements, so it would give some indication
31 of the trend in the business.

32 Q But you would accept that net fees gives a better indication?

1 A Yes, because the two are consistent, the two lines of business become consistent at that
2 point. The gross profit essentially of the business is consistent across all services lines. It is
3 inconsistent for temporary and for permanent workers.

4 Q Why, in your opinion, if you look at the “net fees” column do these accounts show a growth
5 - well it is actually a decline – in net fees? What is that telling the reader of these
6 accounts?

7 A That the gross profit has declined.

8 Q Then the operating profit has declined?

9 A Yes.

10 Q So the performance of the business has declined?

11 A Yes.

12 Q So that is the financial highlights of this page. If you look at the operational highlights we
13 see: “temporary placement, net fees down 7 per cent”?

14 A Yes.

15 Q And we see permanent placement fees down 29 per cent. Can you tell the Tribunal why the
16 scale of permanent placements are being judged by net fees?

17 A So they can be compared with the decline in permanent placements at the same point. The
18 two figures, the percentages are consistent in terms of where the businesses are being
19 compared. So if temporary placement net fees are down 7 per cent, and permanent
20 placement fees are down 29 per cent, then that tells you what the trend is in the gross profits
21 of each of those businesses.

22 Q Does that not indicate to you that the activity of Hays is declining?

23 A Potentially, yes.

24 Q And that the activity declining is placements?

25 A The “net fees” is down 7 per cent, that could be as a result of the two metrics that create that
26 number working in different directions or in the same direction.

27 Q If you look at “Temporary Placement, net fees down 7 per cent”, is that not indicating to
28 you that net fees are being earned from placements.

29 A Sorry? Net fees are being earned from temporary placements?

30 Q The placement is the activity. Net fees are being earned from the placements.

31 A It’s the gross profit from the temporary business.

32 Q Can you go on to p.117? Is this normal to have this in a set of accounts - a business
33 overview?

34 A Yes.

1 Q What is this suggesting to the reader?

2 A It's giving some statistics that it believes are of use to the users of the accounts in forming a
3 view on the financial performance.

4 A Again, I ask the same question: why, in your opinion, is there a reference to net fees here
5 and not turnover?

6 A Because, as I said before, net fees is the first comparable across the business as to where
7 you have a consistent metric to measure different segments of the business.

8 Q Isn't net fees being used interchangeably with turnover in this industry?

9 A For permanent placements and for agency business, yes.

10 Q And for temporary?

11 A For temporary, no.

12 Q Where on this page do you see any other measure than net fees to judge temporary
13 placements?

14 A You don't.

15 Q You do not.

16 A And I wouldn't necessarily expect to see it because that is a segment of the business which
17 has its own metrics. It has turnover, cost of sales, and net fees which are disclosed
18 separately to give a faithful presentation of the accounts elsewhere. This is pulling out
19 certain highlights from the financial performance at a summary level to give, on a page, the
20 profile of the group. So, there are very few statistics here. The statistics that the company
21 considers are relevant are the split between the various divisions, and those areas at which
22 you can compare performance. So, net fees -- It doesn't surprise me that net fees is the
23 statistic they pull out because it's a good comparator between the different parts of the
24 business.

25 Q Normally on this page you would see turnover.

26 A Yes, and if Hays was only engaged in the provision of temporary placements and those
27 were accounted for on a principal basis, then I would expect to see turnover on this page.

28 Q But, Hays has a mix.

29 A Yes, which is why it's not here.

30 Q What do you understand by 'net fees by specialism'?

31 A It depends on the sector in which the business is operated, I would imagine. I don't prepare
32 the accounts. As a user, I would imagine that that depends on where the permanent or
33 temporary placements are recorded within the different segments in the business.

1 THE CHAIRMAN: Is it not explained in the little table that accountancy and finance is one
2 specialism?

3 A Yes. That's why I say it's the different sectors.

4 MR. BREALEY: Would you accept that what this page is telling the reader is that the degree to
5 which net fees are earned by the specialist departments within Hays.

6 A Yes.

7 Q Then net fees by division -- This is telling the reader the net fees earned by the various
8 worldwide divisions ---

9 A Geographically, yes - which is a requirement. You need to give performance by sector and
10 by geographic region.

11 Q Again, 'net fees' is being used here as an indication of the amount of money being earned
12 by the specialist department and the geographic departments.

13 A Yes.

14 Q If one goes on to p.120, again we have the chief executive's strategic review. Again, I think
15 you would agree with me that this is standard in accountancy. You usually have a chief
16 executive's statement.

17 A Yes.

18 Q What is the purpose of the chief executive's strategic review?

19 A To give a review of the business - in overview.

20 Q Again, I would suggest to you the same point: that normally in a chief executives strategic
21 review you would have reference to turnover or revenue.

22 A Yes, if it was representative across the entire business, yes.

23 Q Because we only have net fees here I think you would accept that having a turnover figure
24 would not be representative of Hays' overall business.

25 A Correct - because of the mix.

26 Q Can we go on to p.130? This is an operating review. Would you explain to the Tribunal
27 what this is doing? What is an operating review?

28 A Again, giving financial highlights from the operation. So, the chief executive is giving the
29 strategic view which is key considerations with regard to strategy. This is looking back at
30 the operating profits, etc. of the business over the year.

31 Q What are the operations, in your view, that are being referred to?

32 A The operations of the company.

33 Q Which are?

34 A Which are the various sectors set out here.

1 Q No. The sectors are not operations. What are the actual activities -- the operations being
2 carried out by these sectors?

3 A Well, they're divided between specialisms - permanent, public sector, regions, private
4 sector market, public sector market, etc. - within this operational review So, they consider
5 those to be the operations.

6 Q I suggest to you that the operations here are placements.

7 A Okay.

8 Q Yes? I take 'Okay' on the record to be a 'Yes'?

9 A It doesn't say that here, but ----

10 Q If you look up p.131,
11 "In the United Kingdom and Ireland, net fees declined by 27 per cent ...with
12 operating profit down ... Permanent placement net fees decreased ... temporary
13 placement net fees decreased ---"
14 The net fees are related to placements. That is correct, is it not?

15 A That seems to be the case, in terms of the operational review, yes.

16 Q So, when we are looking at the operations of Hays in its operating review, we are looking at
17 placements.

18 A That's who they decide to review it, yes.

19 Q That is how they decide to review it.

20 A Yes, that's how they decide to present their operations.

21 Q So, when we are looking at the net fees in the various divisions and specialisms, we are
22 looking at the fees earned on the placements.

23 A Yes.

24 Q Again, I suggest to you that here, in this operating review, across the mix of Hays' business,
25 Hays is representing net fees as turnover.

26 A No.

27 Q I thought we started off with your evidence that turnover was a metric which measured the
28 activity of a company.

29 A Yes, but net fees are not turnover. Net fees are only turnover for what you would call the
30 permanent placement business. That's the only point where net fees are equivalent to
31 turnover.

32 Q I will ask you the question again. We established at the beginning that turnover - you can
33 call it revenue; you can call it sales; you can call it income - represents the scale of activity
34 of a company.

1 A Yes.

2 Q Here we are looking at the scale of activity of Hays in his operating review.

3 A Yes.

4 Q The figure which is being put forward to judge that scale of activity is net fees.

5 A Yes, which is equivalent to gross profit.

6 Q In light of the agreement with both of those statements net fees is being put forward by
7 Hays on these two pages as equivalent to turnover.

8 A No, it cannot be. Under accounting definition it cannot be equivalent to turnover.

9 Q Under a realistic market definition?

10 A It's gross profit because it's the ----

11 Q You accept that under a realistic market definition net fees is indicating the scale of the
12 activity of the company.

13 A Yes, because that's the first line at which you can draw a comparison with regard to the
14 performance of the business - because of the mix.

15 Q If we go over the page to p.132, we see the same operating review for Asia Pacific.

16 A Yes.

17 Q If we go on to p.134 we have the operating review for continental Europe and the rest of the
18 world.

19 A Yes.

20 Q I think you accept - because it is there on the page - that Hays does not present a turnover
21 figure to measure the scale of its activity across the mix of its business.

22 A Correct.

23 Q We then get to the financial review, which I am sure you have read several times, at p.137.
24 That is the very first time we see the reference to turnover.

25 A Yes.

26 Q Just looking at this page on p.137, I would suggest to you that on any fair reading of this
27 that net fees is being greater prominence than turnover to measure the performance of Hays'
28 business.

29 A Yes, and for the reasons I gave previously that's what I would expect.

30 Q You fairly accept that. If we go to p.142 this is Key Performance Indicators. What would a
31 key performance indicator mean in a set of accounts?

32 A Exactly what it says - a measure of key performance or an indicator of key performance.

33 Q Of the scale of its business? How it is performing?

34 A A measure of key performance - not necessarily the scale, but of the key performance.

1 Q We see there the first net fees growth.
2 “The year-on-year growth in our net fees provides a measure of the business
3 development and growth in each period.”
4 Do you agree with that?
5 A Yes, because it does. Net fees for consultant.
6 “The average net fees generated per sales consultant represents how productive
7 fee earners are in the business.”
8 Do you agree with that?
9 A Yes.
10 Q What do you think these fee earners are doing?
11 A They are generating revenue and profit for the business.
12 Q By what sort of activity?
13 A By creating opportunities for temporary or permanent placements.
14 Q How do you measure, in the sense of a financial metric, what those fee earners are doing?
15 You are doing it by net fees per consultant?
16 A Yes.
17 Q You are not doing it by turnover per consultant?
18 A No, because if a consultant was selling both permanent and temporary business that would
19 give you a skewed comparator.
20 Q Precisely. Let me go to p.182, please. We have almost finished on the accounts. I am
21 looking at Note 6. This is operating profit from continuing operations.
22 “The following costs are deducted from turnover to determine net fees from
23 continuing operations.”
24 Are you able to give an opinion on what the ‘continuing operations’ are?
25 A ‘Continuing operations’ are the operations of the business - what it is engaged in.
26 Q You see turnover figure and then remuneration of temporary workers. Just over £1.7 billion
27 is being deducted.
28 A Yes.
29 Q Why would the accounts draw the readers’ attention to this amount of money being
30 deducted - this £1.7 billion?
31 A To give a fair presentation of the results, but also to disclose the turnover, cost of sales, and
32 gross profit of the business in standard format. The labels attached to it in this note are
33 turnover, remuneration of temporary workers and net fees, but that’s essentially what the
34 note is doing.

1 Q Under that do you see,
2 "Prior to 1st April, 2009, turnover and remuneration of the workers excluded
3 transactions relating to contracts performed under the staff hire concession".
4 A Yes.
5 Q Can you remind the Tribunal what the staff hire concession was?
6 A That is the concession that was taken advantage of with regard to VAT exempt clients
7 where Hays accounted for those relationships on an agency basis prior to the removal of the
8 staff hire concession in 2009 when they switched to account for those on a principal basis.
9 Q In the various evidence - and I think you have discussed this with Mr. Hall - are you aware
10 that the effect of that concession meant that approximately £200/250 million was put in the
11 turnover figure?
12 A Yes. That figure was a figure that was quoted in Mr. Hall's expert report.
13 Q So, as a result of the withdrawal of this concession on 1st April, 2009 the turnover figure
14 increased, in broad terms, by 10 percent.
15 A Yes.
16 Q £2.5 billion -- £250 million. 10 per cent.
17 A Yes.
18 Q Clearly, Hays has not increased its scale of activity by 10 per cent, has it?
19 A It is responding to a change that it believes it has taken in the substance of those
20 arrangements. To change from accounting on an agency basis to a principal basis Hays
21 must have made the determination that the substance of those arrangements has changed
22 from an agency basis to a principal basis.
23 Q I will ask the question again. Clearly Hays has not increased the scale of its activity by 10
24 per cent, has it?
25 A The substance of those arrangements has changed. So they are therefore recording the
26 activity under IAS18 now, from April 2009 onwards, as a gross inflow of economic benefit.
27 Q Has it increased the scale of its activity? It is a simple question. Has it increased the scale
28 of its activity?
29 A The nature of those arrangements, I would imagine, has not changed. The substance, it
30 appears, must have changed because they have moved from one form of accounting to
31 another. So, something must have changed with relation to the arrangements carried out in
32 relation to those particular activities. In substance accounts have to be prepared on the basis
33 of substance over form. So, the substance of those arrangements must have changed from

1 March to April 2009, or over the period that the VAT hire concession was removed -- the
2 VAT mitigation concession was removed.

3 Q The turnover figure has just, overnight, gone up by 10 per cent. I suggest to you that
4 normally when turnover goes up by 10 per cent - certainly on a £2.5 billion company - the
5 scale of an activity has changed, has it not?

6 A Yes, it would normally have changed - or there has been some change in the underlying
7 accounting that has caused that change. In this instance the company is clearly disclosing
8 that there has been a change in the underlying accounting that has caused that change. They
9 don't actually give the magnitude of that change in this note, even though it is 10 per cent of
10 the revenue. But, they are advising the user of the accounts that there has been a change in
11 turnover because of the removal of the staff hire concession. They are saying they were not
12 in there before, and now they are. So, in terms of the faithful presentation for the user of the
13 accounts, they have the information. They don't actually have the number, but they have
14 the information to determine that the turnover number has changed because of a change in
15 accounting rather than a change in the performance of the business.

16 THE CHAIRMAN: So, they are indicating, explaining that this change is not due to a change in
17 the performance of the business, but a change in the underlying accounting.

18 A Yes, and the substance of the arrangements that give rise to the accounting.

19 MR. BREALEY: The substance of the arrangements, I suggest to you, have not changed because
20 net fees have not changed.

21 A The substance of the arrangements in terms of recognising revenue have changed. The
22 business has made a determination under IAS18 that there is a gross inflow of economic
23 benefit from these transactions. That is the driver of the recognition of revenue.

24 Q Would it give any indication of an increase in placements, the fact that turnover ----

25 A No, no.

26 Q So the operational activity, we are none the wiser because turnover has gone up by 10 per
27 cent?

28 A Yes, due to a change in the substance of these arrangements.

29 Q The fact that £250 million goes in to the overall turnover of the company and the fact that
30 net fees does not change, what does that suggest to you?

31 A That the change in the substance of the arrangements has not altered the gross profit, and
32 you wouldn't expect it to.

33 Q Would that suggest to you that the remuneration, the temporary workers' remuneration
34 being paid to Hays by its client is being passed straight through to the worker?

1 A The no change in the net fees? Sorry.

2 Q Yes?

3 A The fact that net fees doesn't change, does that indicate ----

4 Q Turnover has gone up £250 million?

5 A Yes.

6 Q Net fees has not changed. Would that not suggest to you that temporary workers'

7 remuneration essentially get passed on to the temporary worker through Hays?

8 A No, because to recognise those arrangements is revenue, you must record that you are

9 recording the gross inflow of economic benefit, the business is recording a gross inflow of

10 economic benefit in relation to the sale and the separate transaction that it is able to record

11 as a result of that, the cost of sale is the payment to the temporary worker.

12 Q In substance is their remuneration not being passed on?

13 A No, the way that Hays is accounting for these transactions is as two separate transactions.

14 In order to record the revenue it is collecting hourly rates times hours on to an invoice, and

15 that invoice is having VAT applied to it, and those figures are being collected in Hays'

16 accounts as revenue and that number appears in the turnover figure quoted in the operating

17 profit note here. The payable side of the business is taking the cost of the temporary

18 workers recording that and putting that into remuneration of temporary workers equivalent

19 to the cost of those sales. Hays cannot record the revenue unless it has gross inflow of

20 economic benefit from the sales' side of the transaction so it's treating the transaction as

21 two separate transactions and not a pass-through. If it was a pass-through it would record it

22 as an agency relationship. If it was just collecting on behalf of but had not gross inflow of

23 economic benefit from it would not record it as revenue, and could not.

24 Q If I say to you the following: Although the revenues relating to temporary workers' wages,

25 costs are passed through to the temporary worker, they are nevertheless revenues recorded

26 by the recruitment agencies. I will say it again for you, although the revenues relating to

27 temporary workers wage costs are passed through to the temporary worker, they are

28 nevertheless revenues recorded by the recruitment agencies. Do you disagree with that

29 statement?

30 A I disagree with the "pass through" part of it. In terms of the cost of sales of any business, if

31 a business acquires something and then sells it on to somebody else, that is always a pass

32 through, so if it buys cars and sells them to consumers then the car passes through that

33 business. The separate transactions are the sale of the car and the purchase of the car. In

1 this instance it's the sale of the temporary worker service and the cost being the payments to
2 them.

3 Q Can you just take out bundle CB1, which is the Decision, and turn to p.251 and para.5.125.
4 What I just quoted to you was the OFT's own case, which is that:

5 " . . . although the revenues relating to temporary workers' wage costs are passed
6 through to the temporary worker they are nevertheless revenues recorded by the
7 Recruitment Agencies."

8 A. Yes.

9 Q Are you saying that the OFT is wrong?

10 A I wouldn't - I mean I wasn't involved in drafting this Decision but I wouldn't have called it
11 a "pass-through" because in accounting terms it's two separate transactions.

12 Q From a market reality point of view is it a pass-through?

13 A No.

14 Q Is it a pass through in any shape or form?

15 A No, it's a revenue and a cost of sales.

16 THE CHAIRMAN: Does it not rather depend how you use the term? You could say when a
17 main contractor bills the employer, and the main contractors use sub-contractors, so the bill
18 to the main employer includes the costs of the sub-contractor, they might even be shown
19 "Sub-contractor X – electrical works", "Sub-contractor Y", and he gets the money and then
20 he has to pay it on, one could call that the "pass-through" ----

21 A Yes.

22 Q In a general sense it is a pass-through.

23 A. Yes.

24 Q I think you are saying in accounting terms ----

25 A. Correct.

26 Q -- you would not describe that as a "pass-through", although people might say it really is a
27 pass-through because you are not keeping the money, you are just going to pay it on?

28 A Yes, in the way that if the consumer buys the car you will be paying for your profit margin
29 on the car plus the cost of the car, so the cost of the car is a pass-through in the same sense.

30 MR. BREALEY: Could you go to your first report and to p.213 and para.2.2.8, and if you could at
31 the same time also take out the witness statement bundle CB3 and have tab 7 open. You
32 say at 2.2.8:

1 “In my view it makes sense to focus on Net Fees as the comparator between
2 entities within this industry sector because the entities within the sector appear to
3 have a variable mix of business as regards temporary and permanent workers.”

4 Essentially you have confirmed that in your cross-examination?

5 A Yes.

6 Q What actually is being compared? You talk about “comparator”, but what actually is being
7 compared?

8 A Between entities?

9 Q Yes, you talk about it makes sense to focus on net fees, this is in the context of looking at
10 the performance of Hays internally and externally. I am asking you what actually is being
11 compared – you say it makes sense to have net fees as a comparator ----

12 A Yes.

13 Q -- what actually is being compared?

14 A The performance of the entities in the industry.

15 Q You would accept that the market considers net fees as the true measure to judge the
16 performance of the recruitment business?

17 THE CHAIRMAN: Mr. Brealey, I thought this is one of the points that is now agreed, if one
18 looks at the agreed statement 5.1.1, that has been confirmed now, I do not think ----

19 MR. BREALEY: That is, but I am trying to work out what – if we have a look at Mr. Shepperd’s
20 statement at para. 7?

21 A Yes.

22 Q I understand it Mr. Allen is agreeing that you can use net fees as a comparator and if one
23 looks at para. 8 of Mr. Shepperd’s statement on Mr. Allen, we see after the quotation:

24 “In fact, I would go further to say that the only way in which recruitment agencies
25 can be compared is by reference to Net Fees ...”

26 A Yes.

27 Q “ This is the reason that all recruitment industry analysts focus on Net Fees
28 generated by Hays and other recruitment agencies.”

29 Then the next sentence:

30 “That is, Net Fees is the figure that allows analysts to assess the actual economic
31 performance and activity of the business carried out by recruitment agencies.”

32 What I was going to ask you is where Mr. Shepperd says: “That is, Net Fees is the figure
33 that allows analysts to assess the actual economic performance and activity of the business
34 carried out by recruitment agencies”, whether you agree with that statement?

1 THE CHAIRMAN: I thought that is agreed in 5.1.1 of the agreed statement?

2 A It is agreed, I don't disagree with anything Mr. Shepperd says, it makes sense – as I've said
3 before – that the analyst community focuses on net fees. If a business in the sector had 10
4 per cent of temporary and 90 per cent of permanent it would be wrong to compare it with
5 the business that had the opposite, 10 per cent of 90 per cent, because the two would not be
6 comparable at the turnover levels, so analysts focus on net fees in my view quite logically.

7 MR. BREALEY: It is essentially para. 9, Sir, that I was going to ask about. Mr. Shepperd goes
8 on:

9 “Mr. Allen, however, goes on to say in the same paragraph that: ‘*turnover (being*
10 *the combination of the value of services provided both as proposed and agreed) is*
11 *the true measure of the scale and magnitude of a business.*’ ”

12 He disagrees with you on that. Mr. Shepperd's evidence is unchallenged and, as I
13 understand it, you have just agreed with everything that Mr. Allen says, sorry Mr. Shepperd.
14 (Laughter)

15 A I agree with everything Mr. Allen says.

16 Q Except in this paragraph. Do you agree with Mr. Shepperd at para. 9?

17 A Yes, I do in terms of the recruitment industry. My statement in my expert report was that
18 turnover was, I think he quotes it here, is a metric for a business in general, and if we were
19 in a world where recruitment agencies only provided temporary workers, and everybody
20 accounted for it on a principal basis turnover would be a relevant metric, and analysts
21 would, I imagine, focus on turnover. The fact that we're not in that perfect world where
22 they can perform that comparison means that they focus on net fees across the industry.

23 Q In the light of that, just to be clear, if you look at the last sentence of para. 10:

24 “Due to the characteristics of the recruitment industry, the market considers the
25 Net Fees figure to be the equivalent of the turnover figure form most other
26 industries.”

27 You would agree with that as well?

28 A Yes, on the basis that, for example, if you were comparing department stores and their sales
29 turnover would be relevant in the recruitment industry because of the mix turnover is not,
30 and therefore net fees is the figure that they use as the first point where they can perform a
31 valid comparison across the different entities.

32 Q In your joint report (tab 5), para. 2.2.3 you say that you do not believe, and you also say that
33 Mr. Hall can't either, that you do not believe that you are able to form a view on the nature
34 of Hays' transactions?

1 A Yes, and this is an important point from an accounting perspective.

2 Q Why is it important?

3 A Because the framework for international accounting standards requires that the accounting
4 for transactions is carried out on the basis that the substance of the transactions is the
5 overriding requirement and not their legal form.

6 Q Why is it that you feel unable then to come to a concluded view?

7 A Because I believe that the view on the substance of the transactions could only properly be
8 arrived at by management; management is in the position to determine how the transactions
9 operate in practice, and they are, as Mr. Venables testified, working with the contracts on a
10 day to day basis, and determining what the substance of those contracts is for the purposes
11 of accounting, and they are making the determination based on the substance of those
12 transactions and that in respect of temporary workers they are largely to be accounted for as
13 a principal, and that is driven by the substance. I as an expert coming in to look at this
14 independently can only form a very limited, if any, view on the substance of the transactions
15 because I don't have that day to day operational ability that others that run the business do
16 have, and I don't believe that Mr. Hall does either.

17 Q That is why, as I understand it, in the joint report at para. 4.1.1(b) at p.9, your opinion is that
18 Hays could, under certain circumstances account for net fees and turnover?

19 A If Hays reached a determination that the substance of its transactions was such that they
20 were operating as an agent then it would account for them as an agent, as would any other
21 recruitment business.

22 MR. BREALEY: I have no further questions but I am afraid Mr. Harris and Miss Kreisberger
23 will.

24 THE CHAIRMAN: Yes, Mr. Harris.

25 Cross-examined by Mr. HARRIS

26 Q Good morning, Mr. Allen, I am afraid Mr. Brealey is right, it is a little bit of a tag team
27 performance this morning and going into this afternoon. I would like to address you with
28 some questions on a different topic, if I may, the topic of principal and agency in your
29 report. I think you would agree with me, would you not, that there are six principal factors
30 identified in the accountancy literature that bear upon the issue of whether or not there is a
31 principal or an agency relationship?

32 A If you are drawing the six from the list in Mr. Hall's report where he lists other factors, then
33 I think you are missing one of the ones from FRS 5.

1 Q Well let us take them from your report instead, shall we? If you would look at your first
2 report, which is in the expert bundle CB4, tab 3 at p.242. Do you see at the top of that page
3 you have identified the six principal factors as (a), (b), (c), (d), (e) and (f)?

4 A Yes, with sub-divisions within (a). So there are in fact six principal factors. These are
5 principal relationship, yes, whether they include ----

6 THE CHAIRMAN: You are summarising what Mr. Hall has set out in his figure 4.1 ----

7 A Yes.

8 Q -- derived from UK and US standards?

9 A Yes. In terms of determining, there are two sides to the coin. There is determining whether
10 it is a principal or determining whether it is an agent, and I set out in the joint statement the
11 factors from FRS in relation to the other side of the coin which is how you determine, this is
12 at p.2 of the joint statement, under "UK GAAP Agency Arrangements" etc. and they are
13 not necessarily there, so these are one side of the coin, so these are the principal, the factors
14 in relation to determining whether it was a principal, and then the other side of the coin is
15 you look at the obverse and say "are they therefore an agent?" So the factors set out in the
16 joint statement in that paragraph on pp.2 and 3 would also be relevant.

17 Q Yes, but I think we are agreed, Mr. Allen - though we may not agree at later points, that in
18 relation to ----

19 A In relation to principal specifically, yes.

20 Q Right. You would agree with me, would you not, that these factors in your report and in
21 Mr. Hall's report (a), (b), (c), (d), (e), and (f) bear relevantly upon the question of whether
22 or not there is a principal or agency relationship in any particular circumstance.

23 A In combination with the factors in relation to agency as set out. That is particularly why I
24 put those agency factors in the joint statement - to make sure there was a balance between
25 both sides of the determination, and that one just doesn't look at the principal side, but one
26 also looks at the agency side. I think this became more relevant in the light of Mr.
27 Venables' evidence in that he was saying that essentially what Hays have followed was UK
28 GAAP in terms of the determination of the disclosed agent requirement where you disclose
29 that you are an agent and then you account for it as an agent. There is a rebuttable
30 presumption that you don't account for it as an agent where you haven't disclosed that
31 you're an agent. That was what he said was the policy that Hays was following. Therefore,
32 the factors in relation to the agent follow on from that determination. So, it appeared that
33 that was more what he was applying in terms of how to apply Hays' judgment.

1 Q I follow that. But, effectively, all that comes out of pp.2 and 3 of the joint statement is that
2 there is another factor - namely, the seller has disclosed the fact that it is acting as an agent.

3 A No ----

4 Q If you look at (b), (c), and (d) they are all already included within the (a), (b), (c), (d), (e),
5 and (f) on your para. 5.3.4.

6 THE CHAIRMAN: Well, disclosure of the agent is (f).

7 MR. HARRIS: In fact, they are all included, yes. I am grateful.

8 A For example, (b) on p.3:
9 “-- once the seller has confirmed its customer’s order with a third party, the seller
10 will normally have no further involvement in the performance of the ultimate
11 supplier’s contractual obligations.”

12 Yes, I guess that’s involved in the determination of service specification.

13 Q Yes. Precisely. That is effectively encompassed within (a), is it not?

14 A Yes. Yes.

15 Q You do accept then that these six factors, whether expressed in the form (a) to (f) in your
16 first report or in (a) to (d) in the joint report, are relevant factors to be considered for the
17 purposes of determining principal or agency.

18 A Yes, and I think the way they are set out in the joint report I would defer to because the
19 expert reports are characterising them generally rather than looking at the actual wording of
20 the indicators. I think the actual wording of the indicators is relevant to the determination
21 rather than just following either mine or Martin Hall’s characterisation of them.

22 Q I take that point. But, you would also agree with me that all of the factors have to be taken
23 into consideration before reaching a view on principal or agency, do they not?

24 A Well, in terms of accounting judgment the judgment is made based on the framework that
25 applies to International Accounting Standards or UK GAAP. So your overriding
26 requirement no. 1 is substance over form. How you apply your accounting policy is then set
27 by the indicators. So, there is an umbrella within which an accountant is operating in
28 making their determination. These indicators fall within the specifics in relation to
29 particular transactions within that umbrella.

30 Q But within the umbrella you should consider all other factors, should you not?

31 A There’s no requirement to consider all of the factors. They are indicators.

32 Q You say there’s no requirement to consider all of the factors, but I’m reading from CB4, tab
33 3, p.242, para. 5.3.5 of your first report, five lines down. I thought it was your evidence to

1 the Tribunal - and I quote - that “the relevant strength of each of the indicators should be
2 considered”.

3 A Relevant strength. The accounting Guidance - and this is Guidance in IAS18 and in the
4 Application Note - is that you should consider these indicators.

5 Q Yes. All of them.

6 A So, you have got a list of indicators. You can determine that, for example, inventory risk is
7 not applicable or that others are. So, if one does not apply to your business you would not
8 really consider it.

9 Q We will look at them individually in a moment, but I think you just said - and correct me if I
10 am wrong - that within the accountancy standard framework you should consider these
11 factors.

12 A Indicators.

13 Q These indicators.

14 A Yes, these are indicators.

15 Q There are six of them, are there not?

16 A Yes. They are not mandatory requirements. They are indicators.

17 Q But in your analysis you have not considered all of the indicators, have you?

18 A Yes.

19 Q Well let us just have a look at that. Your Indicator (a), taking it from your p.242, Tab 3, is
20 primary responsibility for providing goods or services.

21 A Yes.

22 Q If you turn over in your first report, to the next page, p.244, do you see that you analyse
23 that?

24 A Yes.

25 Q So, one could put a little (a) next to that heading, just above 5.3.8.

26 A Yes. I mean, I’m not analysing the indicators here. I’m commenting on Mr. Hall’s
27 assessment of the indicators. So, I haven’t commented on all of the indicators in my report.
28 Mr. Hall pointed that out in his response to my expert report. So, I don’t comment on what
29 he’s saying about particular indicators because I didn’t have a comment to make, because I
30 didn’t have enough information to make a comment.

31 Q Mr. Allen, your expert evidence in 5.3.5 is that “the relative strength of each of the
32 indicators should be considered”. I just want to see to identify with you the fact that in your
33 report you have not covered three of the indicators, the relative strength of which you say
34 should be considered.

1 A Yes. I haven't commented on them.

2 Q Right. Well, let us just identify which ones you have not commented on in giving your
3 expert opinion. Perhaps we can take this rather more quickly in light of what you have just
4 said. You accept with me that you have covered in your report factor (a).

5 A Yes.

6 Q Then, on p.246, sub-paragraph (f) discloses that it is acting as an agent.

7 A Yes.

8 Q Then on the next page, p.247 of the bundle, 'Exposure to the Customer's Credit Risk' - that
9 is sub-paragraph (d), is it not?

10 A Yes.

11 Q So, that means that you have not opined in your expert report upon the relative strength, or
12 indeed any evidence on indicators -- Let me get this right: your (b), (c), and (e) - 'exposure
13 to inventory risk', 'discretion in establishing prices', and 'amount earned is pre-
14 determined'.

15 A Yes. I haven't commented on them.

16 Q The truth is that each of those other three indicators, or factors, all support Mr. Hall's thesis,
17 do they not, that it would be reasonable for a professional accountant to come to the view
18 that the appellant could account for temporary wages on an agency basis rather than a
19 principal basis. That is right, is it not?

20 A In relation to inventory risk, I believe inventory risk in the accounting standards is really in
21 relation to goods since it talks about despatch, shipping, return, etc. In terms of 'discretion
22 in establishing selling price and the amount earned is pre-determined' I gave no comment
23 on that in my expert report under the general caveat that I was not able to make judgment in
24 relation to certain elements because the information before me did not allow me to
25 comment. So, I didn't believe I had enough information in relation to particularly the
26 contracts or the substance of the contracts in order to comment on 'discretion in establishing
27 selling price' or 'amount earned is pre-determined'. So, I gave no comment on it. I had
28 nothing to say.

29 Q Right. Well, I will be completely fair to you, Mr. Allen. I am going to take you to each of
30 these factors which you have omitted to mention in your expert report, but if your evidence
31 in response to my questions is, "I simply cannot say. I do not know", fair enough.

32 A Yes.

33 Q Let us have a look at each of them briefly, shall we? I am going to take one of the factors
34 you have omitted - your factor (c) - discretion in establishing the prices. My proposition to

1 you, Mr. Allen, is that this factor points towards a principal because if it is present it shows
2 an undertaking acting in its own capacity in taking important Decisions in its own names
3 and on its own account. Discretion in establishing prices. That is right, is it not?

4 A Sorry? Where are you quoting from?

5 Q No. I am putting a proposition to you - that the reason that discretion -- If an undertaking
6 has discretion in establishing prices, that points towards it being a principal, does it not?

7 A It's one of the indicators in the accounting literature.

8 Q Yes. So, if it is present it points towards there being a principal relationship; is that right?

9 A Let me just look at the actual wording from the Standards. (After a pause): The wording
10 under IAS18 - and I am reading from p.2 of the joint statement at (c),
11 "The entity has latitude in establishing prices, either directly or indirectly. For
12 example, by providing additional goods or services".

13 Now, I would take that to mean that the latitude in establishing selling prices comes from
14 the ability to, for example, add an extra service at no charge or at a reduced charge, or
15 where you have a bundle of services you have latitude in establishing selling price because
16 you have a group of factors that you can provide to an entity. Therefore you have latitude
17 in determining what margin you are going to earn from the price that you are charging.

18 Q The selling price of a temporary worker is his wage, is it not?

19 A The selling price of the service in relation to temporary workers is whatever Hays is
20 charging for in relation to its service under its contract with its client.

21 Q Let us try the question again. The selling price for a temporary worker is the wage of the
22 temporary worker, is it not?

23 A The selling price ----

24 Q Yes. The temporary worker sells his services in return for the wages that he receives, does
25 he not.

26 A If the temporary worker is engaged by the ultimate client, then, yes, directly.

27 Q Right. It is fair to say, is it not, that the appellants do not have any discretion in establishing
28 the wages of the temporary worker, do they?

29 A But we are talking about something else there. We are talking about the temporary worker
30 being engaged directly by the client. I am talking about the service -- the cost of the service
31 -- what Hays is billing for in totality. It is billing for the service of providing a group of
32 temporary workers under a contract.

1 Q You would accept from me, would you not, that it is Hays' client which determines the
2 wage levels which it is willing to pay for the labour service - not Hays which determines
3 those wage levels, is it?

4 A I don't know.

5 Q Perhaps I could take you to the witness statement bundle, CB3, Tab 1, page 15, para. 44.
6 This is Mr. Venables' first witness statement. Do you see in that statement, about eight
7 lines down, the very words I just put to you which you said you do not know? They are in
8 fact the very words of Mr. Venables which were not challenged by your counsel. I will read
9 them to you again:

10 "It is Hays' client which determines the wage levels it is willing to pay for the
11 labour services."

12 Do you see those?

13 A Yes, but my point is that that is only part of a package of services. When I, as an
14 accountant, am looking at the indicator under IAS 18 I am looking at the price for the
15 service, and the price for the service does not just include the wages of the temporary
16 worker. Under the indicator here, (c) - does the entity have latitude in establishing the
17 overall price? - yes, it does, because it is able to provide a service for free, or at a reduced
18 rate on top of the service it is providing in relation to the temporary worker. So, it does
19 have, in the overall price, which would be the hourly rate for the service -- Because Hays is
20 being remunerated based on hours times rate, that rate would include the bundle of services
21 that Hays is providing. It would have latitude in setting that rate.

22 Q One of the other factors that you omit to mention in your report is the pre-determined
23 amount. I will come on to that in a minute, Mr. Allen. You will have an opportunity to
24 comment on that as well. But, just sticking with this point, I think I heard you right to say a
25 moment ago that it is critical in your expert accountancy opinion to have regard to the
26 Decisions about the substance of the operations of the business that are made by the
27 management of the business. Was that right?

28 A Yes.

29 Q Here is Mr. Venables saying that it is Hays' client which determines the wage levels it is
30 willing to pay for the labour services. So, that is his evidence and his view of the substance
31 of this business.

32 A Yes. I am sorry. Mr. Venables, in his evidence, which I sat through on Monday and
33 Tuesday, said that. There were comments like: "It's currently a buyer's market". So the
34 buyer sets the rate, presumably meaning the hourly rate. But, it was not previously. So,

1 | there is obviously an economic dynamic in terms of the rate that is being agreed with the
2 | client. The supply/demand consideration is what he appeared to be explaining in his
3 | testimony.

4 | Q Perhaps I will put this in another way and then we will move on. You are not in a position,
5 | are you, Mr. Allen, to gainsay this evidence that Hays' client, which determines the wage
6 | levels it is willing to pay for the labour.

7 | A No, I am not.

8 | Q So, as regards this first factor that you have not referred to, insofar as it amounts to
9 | discretion in establishing the temporary worker's wages, that is not a discretion that lies in
10 | the hands of Hays, is it?

11 | A Mr. Venables, in his evidence, says not.

12 | Q Right. In that sense, this factor points towards agency, does it not?

13 | A No, because you are looking at the service as a whole. You may not have discretion in
14 | relation to a particular part of what you're selling, but in relation to setting a price for the
15 | service as a whole, you clearly have discretion.

16 | Q Let us move on to that one then. The second of the three factors that you do not refer to in
17 | your report is your factor (e) - the amount earned is pre-determined. I put it to you that if
18 | an entity earns a pre-determined amount or a fixed percentage per transaction, then that
19 | indicates that it is acting as an agent. You would agree with that, would you not?

20 | A It's an indicator, but it's not definitive.

21 | Q I entirely accept that. It's a fair point. It is one of six. They all have to be considered. It is
22 | an indicator.

23 | A Yes.

24 | Q Right. But, you would accept it is an indicator in the manner that I have just myself
25 | indicated.

26 | A Yes, and it could be an indicator of an agency relationship, yes That's what it says. I agree.
27 | I agree.

28 | Q I am very pleased to hear it. So, basically, the people to act for commission - they are
29 | agents, are they not?

30 | A Yes.

31 | Q That commission is what should be counted in their case as revenue, is it not - not the gross
32 | amount.

33 | A Yes. If the determination under IAS18 is that there is no gross inflow of economic benefit,
34 | then you record only the commission.

1 Q The appellants - whether that be Eden Brown or Hays or, for that matter AndersElite, they
2 do generate a pre-determined amount, do they not? A percentage of the value of the
3 transaction? That is what they earn, is it not?

4 A I was presented with seven contracts in the expert evidence of Mr. Hall and one contract in
5 relation to another entity from the submissions that Hays had put in in response to the OFT.
6 So, I had eight contracts. There are others. There's the AndersElite standard contract.
7 There are other contracts that have appeared in evidence. My opinion from looking at those
8 contracts was that I was not able to establish from the sample presented to me whether or
9 not that factor represented either agency or principal, or indicated either (1) because I didn't
10 believe the sample was representative - and I pointed that out in my first report; and (2)
11 because it wasn't clear to me from the interpretation of the ones that I could review that that
12 was the case.

13 Q I follow that.

14 A That is really an evidential point.

15 Q Yes. You have just said that you were reviewing evidence, the contracts.

16 A Yes, but I didn't believe them to be representative.

17 Q But you just agreed with me ----

18 A You would need to look at the substance of the negotiations in practice as to how that
19 selling price is determined or pre-determined.

20 Q Just a minute ago you agreed with me, without me needing to take you to the IAS18 that
21 agents earn commission and the commission is what should be accounted for as their
22 revenue figure - not the gross amount.

23 A If they satisfy the requirement and the overriding requirement of substance over form.

24 Q Right. Perhaps we can have a look at a contract for Eden Brown and then one for Hays on
25 this point. If you could take up, please, NCB2, tab 7, this is Eden Brown's terms and
26 conditions of business.

27 A Yes.

28 Q On the first page it covers permanent staff. Do you see that at the top of the right-hand
29 column - Section 1?

30 A Yes.

31 Q Then, the next page is the one I am interested in since we are debating temporary staff.
32 Section 2 - "temporary staff". If you could just read to yourself Clause 2.3, please? (Pause
33 whilst read): That is Eden Brown describing itself, is it not, as "charging a commission for
34 our service".

1 A
2 "The hourly charge consists of the hourly rate paid to the temp, including amounts
3 in respect of PAYE and employer's and employee's national insurance
4 contributions and the commission we charge for our service."
5 Yes.
6 Q Yes. So, in line with what we just agreed a moment ago that would be indicative of acting
7 as an agent, would it not, earning a commission?
8 A Yes.
9 Q One would expect to see that commission figure as the one reported for turnover under
10 IAS18. Right?
11 A Yes - unless Eden Brown, in its own determination, looking at this contract overall, had
12 determined that this represented a principal relationship, either as a result of the other
13 indicators or as a result of substance over form.
14 Q I accept that again. We are not looking at this factor in isolation.
15 A Not an indicator in isolation.
16 Q Yes. I am not looking at this in isolation. But, when one does just look at this, as we go
17 through the factors one by one, that would be indicative, would it not, of an agency
18 relationship?
19 A Yes.
20 Q Right. Can I also take you to a Hays contract on a very similar point? NCB4, Volume 2.
21 Tab 3 Page 1735. This is a document which we, in the courtroom, have looked at many
22 times. It is the terms of business for the introduction and supply of temporary workers by
23 Hays. Do you see Clause 2.1, half-way down the left-hand column?
24 A Yes.
25 Q If you could just read that to yourself? There is no need to read it out. (Pause whilst read):
26 Do you see that in the middle of that they also describe themselves in a very similar way on
27 this point to Eden Brown as "charging a commission calculated as percentage of the
28 temporary worker's hourly rate and employer's NIC". Do you see that?
29 A Yes.
30 Q So, again, just focusing on this factor for a moment - one of the ones you have not
31 mentioned in your report - this would be indicative of an agency relationship, would it not?
32 A Yes, it could be.
33 Q Just to wrap up on this point with two references to the evidence -- You can put down NCB
34 2 and 4, and if you could locate the witness statement bundle again, CB3. Look at Mr.

1 Venables' evidence in his first statement at Tab 1, and in particular, page 24, para. 71, the
2 very final paragraph. (After a pause): Do you see that Mr. Venables also there refers to the
3 amounts being pre-determined for the duration of any contractual arrangement?

4 A Yes. In this paragraph he is referring particularly to construction clients that use an
5 intermediary, such as Parc, where they have open book arrangements, which I assume is
6 giving the end user the breakdown between the cost and the margin that they're earning, and
7 accordingly the amounts derived from Hays in relation to those particular types of service
8 will be pre-determined for the duration of any contract.

9 Q Right. To be fair to Mr. Venables, if one looks at para. 70, what he says is that large clients
10 often enter into open book type arrangements.

11 A Yes.

12 Q At para. 71 he gives an example of a large client using an intermediary.

13 A Yes.

14 Q So, in his evidence here he is talking about all his large clients, is he not?

15 A With open book arrangements, yes.

16 Q Yes. What he is saying is that there is a pre-determined margin for all of those clients.

17 A Yes.

18 Q Right. You would accept from me that that also points, when we are just focusing on that
19 within the mix of these factors, towards ----

20 A It could do.

21 Q Does it not

22 A It could do.

23 Q So, that is two of the three that you do not analyse in your report. I said that I would go to
24 all three of them. That is only being fair to you. You mentioned inventory earlier. That is
25 the other one that you do not cover. But, just taking this as a broad proposition first, I
26 would be right to say, would I not, that running an inventory points to a principal
27 relationship because it means that there is a risk being held by that undertaking - a risk
28 connected with whether or not the inventory can actually be sold at some point.

29 A Yes.

30 Q It is right, is it not, that the appellants do not have any such risk because they do not run any
31 inventory of temporary workers, do they?

32 A My reading of IAS18 is that this relates principally to goods. It talks about shipping or
33 return -- shipping or on return. That is set out in the joint statement at p.2(b) If you look at
34 the way that IFRS and others have discussed this, then they are really, it appears, talking

1 about goods rather than services. That's how inventory is typically referred to in
2 accountancy terms.

3 Q I take that. There was, of course, Mr. Hall's evidence yesterday which was that this one is
4 not, even in his view, as of central relevance as the other factors, but nevertheless he said
5 that it was not completely or utterly irrelevant. Do you accept what Mr. Hall said about that
6 - it has some relevance, but not as central as ----

7 THE CHAIRMAN: I think he said 'limited relevance'. That was his expression.

8 MR. HARRIS: Yes. Precisely. Yes, I accept that.

9 A I think in relation to the fact that it refers to goods, it has no relevance.

10 Q There is the point of principle, is there not, Mr. Allen, which is why it has some limited
11 relevance? The principle is that if you have an inventory you take on a commercial risk that
12 you might not be able to dispose of the inventory. But, by analogy, there is no such risk in
13 the case of Hays or Eden Brown as regards temporary workers; is there?

14 A Well, it has no inventory, no goods.

15 Q But by analogy it does not have a bench of temporary workers whom it is paying before it
16 can assign them to its clients, does it?

17 A No, it doesn't have that.

18 Q So, insofar as there is any relevance to this factor, it could only point towards being agency,
19 could it not.

20 A If one made a determination that there was no inventory risk, then it would point towards
21 agency, yes.

22 Q Right. So I put it to you, Mr. Allen, that it is not a very auspicious start for you, is it, on this
23 topic of principal and agency because of the six factors in your expert report which you say
24 the relative strength of each of which should be considered, in fact you have not considered
25 three of them. That does not inspire one with the notion that you have conducted a
26 systematic or thorough review of this topic, does it?

27 A I have no problem with the opinion that I have given as a result of my review. My review
28 was based on the evidence that I had before me and I made no comment on those particular
29 indicators because I didn't believe that I had the representative material in front of me to
30 make a comment.

31 Q Perhaps one would be forgiven for thinking, Mr. Allen, that you have agreed with me that
32 when focusing on two of those omitted three factors, and, to the extent that it is relevant, the
33 third, they all point towards agency. Your omission of reference to them is perhaps not the
34 most independent or impartial way of proceeding, is it?

1 A My report was in response to Mr. Hall's report and I made comment in relation to those
2 factors where I believed I could make comment.

3 Q Certainly where you do comment, Mr. Allen is on another of the factors, credit risk. In fact,
4 of the three factors that you do analyse on this topic in your report, you place significant
5 weight on credit risk, do you not?

6 A Yes. In analysing how Hays and the other appellants reached their judgment that the
7 substance of the relationships is such that they should be accounted for as principal, credit
8 risk is mentioned as one of the recurrent factors in both the witness statements and in the
9 evidence.

10 Q But for you it is a peculiarly important factor, is it not? Let me just show you what you say
11 about this in your first report at CB 4, tab 3, page 248, para.5.3.21. If you would like to see
12 the sub-heading on the previous page "Exposure to the Customer's Credit Risk", and you
13 say here that the legal requirement has significant implications impacting upon the
14 substance of the transaction?

15 A Yes.

16 Q But just taking this in stages, the credit risk is just one of six factors, is it not?

17 A Yes. The reason that I refer to credit risk here so significantly is because based on my
18 reading of Hays' own submission and the evidence of Mr. Venables, it appeared to form a
19 key factor or determinative factor as I described it. Actually, I didn't say it was a
20 "determinative factor" I said it was one of the factors that they were considering; Mr.
21 Venables was certainly considering it as something that he believed was highly relevant to
22 the determination of principal or agent, and that was my interpretation of his first witness
23 statement and Hays' submission on the point, the fact that there was a requirement to pay
24 these temporary workers thereby imputing a credit risk, was a significant factor.

25 Q Yes, I follow that.

26 A And I was looking at the judgment made by management because in my view the judgment
27 made by management is what is being questioned here.

28 Q I follow that.

29 A That is what Mr. Venables had told me in his witness statement.

30 Q Thank you, Mr. Allen. Sir, may I just take one moment? (After a pause) Mr. Allen, it is
31 right is it not that if credit risk were so important and determinative then there would be two
32 consequences at least, would there not? The first would be that where there is credit risk,
33 and on the approach that it is very significant or determinative, that would mean such
34 undertakings that do have credit risk should account for income on a principal basis?

1 THE CHAIRMAN: Can I just clarify, are you saying it is determinative, or it is of significance?
2 A I am saying it was obviously a significant factor. My understanding of the evidence of Mr.
3 Venables is that it was a significant factor in the determination of the principal/agency
4 relationship. There was some dispute as to whether or not it was the determinative factor,
5 and that was dealt with in my expert report backwards and forwards between myself and
6 Mr. Hall.
7 Q Yes, but that is whether for Hays it was the determinative factor?
8 A Yes.
9 Q But for you, when you look at it, is it the determinative factor?
10 A No, but it is a very significant factor, but not determinative.
11 MR. HARRIS: But just focusing on credit risk for the moment, as an indicator if there is credit
12 risk that points towards accounting for income on a principal basis, does it not?
13 A Yes.
14 Q And if there is no credit risk then on this approach it would point to accounting for that
15 income on an agency basis?
16 A It depends.
17 Q It depends on what?
18 A If you look at Application Note G to FRS5 and it is quoted in the joint statement at p.3,
19 looking at the obverse in terms of an agency relationship, so (d) towards the top of p.3 of
20 the joint statement: "*The seller bears no stock or credit risk ...*" so this is an indication that
21 it is an agent, so there is no stock or credit risk:
22 *"... other than in circumstances where it receives additional consideration from*
23 *the ultimate supplier in return for its assumption of this risk."*
24 So there is a caveat to that.
25 Q Yes, I take that point, Mr. Allen, but I am just focusing for a moment on exposure to
26 customer's credit risk, which is what you are commenting on in your first report at the
27 passages I have just identified?
28 A Yes.
29 Q So insofar as we focus on credit risk, and the two consequences that I have just set out in
30 relation to this factor would follow?
31 A Yes.
32 Q Where there is credit risk it points towards principal, where there is not credit risk it points
33 towards agency ----?
34 A That's correct.

1 Q -- as an indicator?

2 A Oh yes, as an indicator.

3 Q But that is correct, is it not?

4 A Yes.

5 Q But in the real world it doesn't work like that, does it, Mr. Allen? Let us take a few
6 examples, looking at the joint report that you were just referring to a moment ago, on p.8 of
7 10, this is the dispute between you and Mr. Hall regarding 'del credere' timber agents, you
8 recall that dispute?

9 A Yes.

10 Q And the fact is that those agents do accept credit risk, do they not, and yet they do not
11 account for the monies as an agent?

12 A Yes, they would fall squarely within the passage that I just referred to in terms of that they,
13 back on p.3 of the joint statement at (d), receive consideration from the ultimate supplier in
14 return for the assumption of the risk. 'del credere' agents are essentially credit insurance
15 brokers, so they are receiving a fee for taking on the credit risk.

16 Q I follow that, Mr. Allen, there is no dispute between us on that but what I am focusing on is
17 the credit risk, and this is an example of an undertaking who does accept credit risk and yet
18 does not account for the turnover as a principal, instead it accounts as an agent, does it not?

19 A Yes, in compliance with UK GAAP.

20 Q So that points in a particular direction, and then there is the HPPS example, that is the staff
21 hire concession, the VAT exemption. When HPPS was being used as a payroll agency by
22 Hays it had credit risk, did it not, in the sense that it had to pay the temp irrespective of
23 whether or not it got paid, do you accept that?

24 A Yes, a structure was arranged involving two subsidiaries of Hays, which accounted for the
25 margin and the cost separately.

26 Q But it did accept the credit risk, did it not?

27 A Yes, it did.

28 Q And yet it did not account for it as a principal?

29 A Correct, and that would be the result of a determination that the substance of those
30 arrangements was of an agency nature and there has been some debate in my expert report
31 between myself and Mr. Hall and with Deloitte as the auditors as to how that determination
32 was arrived at.

1 Q Yes, but the fact remains that in both of the examples I have just give you the timber agents
2 and the HPPS there is an acceptance of the credit risk, and yet not accounting for it as a
3 principal.

4 THE CHAIRMAN: Well on the first example, Mr. Harris, Mr. Allen made clear that the
5 summary in his report at 5.3.4 is just a summary of what is in the accounting principles,
6 and the accounting principle on credit risk has that caveat, and he explained that ‘del
7 credere’ agents are firmly within the caveat. So I do not think that point particularly
8 applies. You can ask about the second point but I think Mr. Allen has responded to the first
9 point saying: “Actually when you look at the actual standard for which that is just a
10 shorthand summary, it firmly fits within the way credit risk has a qualification.

11 MR. HARRIS: Well, Sir, perhaps I can put a similar point a different way. I take that point, and I
12 take plainly what the caveat is in one expression of the credit risk indicators. Let us look at
13 the flip side of the same coin, there are situations, are there not, where there is no credit risk
14 and yet Hays and Eden Brown and the other appellants do account for the income as a
15 principal, for example ----

16 A Yes, and I think – sorry, continue.

17 Q I was just going to say, it may not assist you because I think you are on the point, but for
18 example, when Hays and Eden Brown source their temporary workers through other
19 recruitment agencies, they do account for those wages as principal even though they do not
20 have any credit risk?

21 A Yes, and this is another point that has been the source of some debate between myself and
22 Mr. Hall, and Deloitte as the auditors, and the most recent response from Deloitte in their
23 letter of 4th June I think it was, was that ----

24 THE CHAIRMAN: Just pause a moment. Mr. Brealey, is what is said in that letter still
25 confidential? It is so marked and I am not sure whether, unwittingly, Mr. Allen might be
26 straying into dealing with that letter.

27 MR. HARRIS: The mere existence of the letter ----

28 THE CHAIRMAN: Mr. Harris, if you ask the question carefully?

29 MR. HARRIS: I am grateful to the Tribunal. The mere existence of the letter does not pose a
30 problem, and I do not propose to ask any detailed questions about that leg of the debate.

31 A I can give the general point that is made by the letter ----

32 THE CHAIRMAN: I am not sure.

33 MR. HARRIS: Just in terms of the principle, but I am not sure you need to, Mr. Allen.

34 THE CHAIRMAN: I think, just pause, Mr. Allen, because there seem to be sensitivities here.

1 A Yes.

2 THE CHAIRMAN: I do not know how far you want to explore this.

3 MR. HARRIS: We do not need to look at the content of that letter or anything because Mr. Allen,
4 you accepted the basic point that where Hays and Eden Brown source their temporary
5 workers through other recruitment agencies there is no credit risk and yet they account for
6 them as principal?

7 A I think the point there was that even though credit risk was there, the credit risk had been
8 mitigated by the back to back arrangements that were entered into, and therefore in terms of
9 an indicator, and I think this was touched on yesterday with Mr. Hall, the existence of risk is
10 the indicator, the mitigation of it does not exclude the fact that it is included in the
11 indicators. So credit risk is an indicator, if it is mitigated it is still an indicator.

12 Q At one point in your second report, Mr. Allen – expert bundle (CB4), tab 4, p.304 at para.
13 3.3.16, one of the examples that I just put to you, that is in the middle – subparagraph (b) of
14 the preceding paragraph, the HPPS example?

15 A Yes.

16 Q As I read your 3.3.16 amongst the points you make are that actually although they may
17 appear “. . . to be at odds with relevant accounting practice, I also noted that any potential
18 errors would not have been material.”

19 A Yes.

20 Q Do correct me if I am wrong but as I read it the suggestion that you give there is: “Okay,
21 there are these differences on certain aspects”?

22 A Yes.

23 Q “I am not quite sure how they fit in in some respects with accountancy guidelines, but in
24 any event they are not really that big or important”?

25 A My assessment was that they were not necessarily material to the accounts because they are
26 not disclosed. When the HPPS arrangement was removed the figure, as we saw in the
27 operating profit note previously was not disclosed as a separate figure, therefore if it was it
28 would be material.

29 Q Well come on, Mr. Allen, that is a rather odd way of going about it, is it not? On any
30 stretch of the imagination the figure that we have been talking about in respect of HPPS, the
31 change to the turnover overnight, for Hays, when the staff hire concession is removed, is
32 £250 million or 10 per cent of the gross turnover figure. On any stretch of the imagination
33 that is material, is it not?

34 A Well Hays did not appear to think it was.

1 Q I see, but what about you, Mr. Allen, you would take the view that that is material 10 per
2 cent, would you not?

3 A 10 per cent is borderline materiality for accounting terms, yes, 10 per cent is a benchmark.

4 Q But £250 million is borderline material in your view, is that right?

5 A Yes, it is on turnover, yes.

6 Q Oh, I see. Then we have established, and we are in agreement that one exercises one's
7 professional accountancy judgment by reference to these factors that we have been
8 discussing, but would it not be fair to say that there are other factors of some relevance as
9 well, for example, the issue of control, who has control over the goods or services in
10 question?

11 A Yes, the accounting judgment is made in the round.

12 Q So the issue of control over the goods or services would be made in the round by references
13 to other commonsense considerations such as who has control over the goods and services?

14 A Potentially, yes.

15 Q But that is another factor that would point towards these appellant companies being agents,
16 would it not ? I will happily turn up the provisions of the contract, if you like, but they
17 clearly say, do they not, that the control and the direction of the temporary worker is to be
18 exercised by the end client rather than the recruitment agency, do they not?

19 A In accounting terms I was presented with the contracts and my review and read of the
20 contracts, and I used the phrase I think in my first and second expert report, and in the joint
21 statement, "managing a body of workers" came from phrases within contracts where it
22 appeared that there was a contract for a group of workers and therefore there is a service to
23 provide a group of workers to a client and that is the contract that Hays and the other
24 appellants are entering into.

25 Q But you would accept, would you not, that Hays or Eden Brown, or any of the appellants
26 do not exercise the control over the worker when performing the worker's job, do they?

27 A No, and I made this point clear because I think there was some misunderstanding from my
28 comment in my first report about managing the body of workers that it did not extend to
29 supervision of the workers.

30 Q Yes, but insofar as that bears, as you I think expressed it a minute ago, "in the round" on
31 this question of principal and agency?

32 A Yes.

33 Q It does not point towards Hays or Eden Brown being a principal, does it, because they do
34 not have direction and control over the provision of those services, do they?

1 A They have control over the provision of the service as a whole being the supply of the group
2 of workers.

3 Q Well I understand your point. Now, just asking you a little bit about the nature of the
4 exercise of the judgment as regards these various factors as a professional accountant. I
5 think you would accept from me that the judgment is essentially subjective, is it not, in the
6 sense that each accountant could come to a different view subjectively on the same set of
7 facts, that is right, it not?

8 A Yes, what typically tends to happen in the world of accounting, is that standards are
9 developed over time, and they become generally more prescriptive over time, as the
10 standards become generally more prescriptive the accounting profession considers them and
11 accounts and financial information develop in concurrence with the development of those
12 standards and what you see in relation to the question of principal/agency relationship is the
13 development of the accounting Guidance over time from FRS 3 and its application in
14 November 2003 through to IAS 18 and the new example added in the appendix at no.21 in
15 November 2009. So as that Guidance develops accountants as a group look at how they
16 exercise their judgment in that framework, and the general framework develops as well,
17 because accountants tend to apply judgment in consultation with their peers and with others
18 that operate in the industry, so they do not operate on their own, they are guided by the
19 standards, the framework, their auditors, other accountants, etc. so judgment develops over
20 time. What tends to happen in the accounting profession, we are not sheep but we tend to
21 follow a view, and therefore judgment is applied in that context, the context is that one sits
22 and looks at all the factors, and generally look at how things are done in general. So
23 accountants would sit, apply judgment based in that general context.

24 Q I follow that, Mr. Allen, I am just slightly conscious of the ticking of time because, as I
25 said, there is a tag team, and Miss Kreisberger has some questions for you and I have some
26 more. My question was quite specific, it was that inherently the judgment is of a subjective
27 nature, is it not?

28 A Yes, in that context.

29 Q In that context you would agree?

30 A Yes, it was important for me to set the context.

31 Q Right, I take that point, thank you. In reality that is what is going on between you here and
32 Mr. Hall, is it not? You have reached, as professional expert accountants, different
33 subjective views as to the judgment that should be exercised in regard to a particular set of
34 facts, that would be fair, would it not?

1 A Yes, but I think there is quite a significant difference between the opinion that I have
2 arrived at and the opinion that Mr. Hall has arrived at because I have tried to look at
3 applying judgment in the context that I just described, and I do not believe that Mr. Hall
4 has.

5 Q I see. But it is also fair for me to say that given you have agreed that this is subjective
6 professional accountancy judgment it would be legitimately possible to come to a different
7 view of the correct accountancy treatment. To pick up on Mr. Sterling's phrase of
8 yesterday, it is a "finely balanced" judgment, is it not, in certain circumstances?

9 A Yes, and I would look at that. I was interested in Mr. Sterling's evidence yesterday for a
10 couple of reasons, (i) he talked about the finely balanced judgment; and (ii) he talked about
11 potentially looking at changing his accounting treatment, or his judgment in relation to these
12 particular contracts, and he referred in his evidence I think to the framework, that I referred
13 to as the preamble, when applying judgment in that he looked at consistency with his peers
14 is what I believe he was referring to ----

15 Q Correct, he did.

16 A -- in accordance with the accounting standards framework. In preparing my report I also
17 looked at how the other industry players account for temporary workers in their accounts,
18 and I reviewed, what I got was 20 accounts – it was not a sample that was in any way
19 biased, it was the accounts that I could get in the time to review and the result of that review
20 was that in all cases – I think in two of them there was some small agency business – but in
21 all case those entities accounted for these transactions on a principal basis. In terms of the
22 framework and applying the judgment that would be a significant guide to how one would
23 interpret the accounting pronouncements in this area, you would look at how others had
24 interpreted them and you would come to a view in that context.

25 Q But still on this issue of judgment it is right that those very sets of accounts to which you
26 have just referred they illustrate, do they not, that there can be a differing professional
27 accountancy judgment on this very question of whether to report gross or net at the
28 turnover level on the same fact set, do they not? Do you want me to give you an example of
29 that?

30 A Yes.

31 Q If you could turn to Mr. Hall's second report, it is the example of Robert Walters at p.147,
32 tab 2 of CB4. Do you have that?

33 A Yes.

34 Q Do you see the Robert Walters' example?

1 A Yes.

2 Q You are familiar with the example, are you not?

3 A Yes.

4 Q What Mr. Hall has done is he indented citation within para. 3.4.9, he is citing there from the
5 Robert Walters' 2003 Financial Statements, is he not?

6 A Yes.

7 Q And what that reveals is that they, Robert Walters, had reviewed the Guidance, identified
8 certain transactions, only involved them in an intermediary role, and they go on to say that
9 they now only recognise the net income from those transactions, do they not?

10 A Yes, and this is exactly what I was referring to in my preamble, is that when this accounting
11 Guidance came out in 2003, and this is the 2003 Financial Statements of Robert Walters, so
12 FRS 5 Application Note G is issued, and is relevant to those financial statements, that as the
13 new more prescriptive Guidance appeared, and that Guidance was called "Accounting for
14 the Substance of Transactions" that Robert Walters obviously formed the view that the
15 substance of these particular transactions was not that of principal but was that of agent.

16 Q Yes, precisely, they formed that view by reviewing certain transactions and now coming to
17 the view that they should be accounting for differently, have they not? There is no
18 suggestion, is there, that the underlying factual nature of their operations has changed one
19 jot, is there?

20 A No, but the accounting framework has changed quite considerably.

21 Q So what they have done is change their accountancy presentation notwithstanding that the
22 underlying factual nature of their activities has not changed at all, that is right, is it not?

23 A Well I don't know what they have done, but all I can say in accounting terms is that they
24 have responded to the issue of Application Note G to FRS 5 in 2003 and they have looked
25 at it appears, because they say that they have reviewed the Guidance, they have reviewed
26 that new Guidance, and the new Guidance, which is considerably more prescriptive than
27 anything that was around before, has set out the indicators that we have been referring to.
28 They have looked at the indicators and the indicators have told Robert Walters that actually
29 transactions that they were accounting for as a principal should in fact be accounted for as
30 an agent.

31 Q But you have no basis whatsoever for saying, have you, that the underlying nature of their
32 factual activities has changed at all?

33 A They determine that the substance of those transactions in accounting terms determined how
34 the revenue should be recovered.

1 Q I follow that, Mr. Allen, but the question is: you have no basis for saying that the facts of
2 what they do have changed?

3 A No, I have not, no.

4 Q And let us just have a look at the box, if I may, in paragraph 3.4.11, this is Mr. Hall
5 extracting the impact of the change in Robert Walters' change in accounting treatment. You
6 follow the figure, do you not?

7 A Yes.

8 Q The gross profit line figures, when one compares them, are identical, are they not,
9 notwithstanding the restatement?

10 A Yes.

11 Q And one can very clearly work out what the difference is in the headline turnover figure
12 because it is those restatement figures on the right hand side?

13 A Yes.

14 Q So one can see the same numbers ----

15 A Yes.

16 Q -- on the page, they have just been reconfigured, or reformulated in terms of their
17 presentation, have they not?

18 A Yes, because Robert Walters have re-assessed the substance of those transactions, and I
19 totally disagree with what Mr. Hall says at 3.4.13 that that is a result of subjective
20 professional judgment, it is not.

21 Q But there is no suggestion here, is there, that Robert Walters has taken the view that this is
22 an error in their accounts, is it? They describe it as a restatement, and they set out the
23 numbers?

24 A Yes, because that is clearly allowed under FRS 3.

25 Q So this is not an error, notwithstanding that the change in their turnover line is 78, and I am
26 assuming that these are millions?

27 A Yes.

28 Q So £78,540,000 change in the turnover figure, but not an error?

29 A Yes, because under accounting literature under FRS 3, an error is not defined as something
30 in response to a change in the accounting framework, that would be grossly unfair to say
31 that accounts would include errors if you changed the landscape that they are prepared in.
32 So the landscape that Robert Walters prepared its accounts in changed, they responded to
33 that change, it is never going to be an error.

1 Q There may be a bit of confusion here between us, Mr. Allen, because in your second report,
2 tab 4 of the expert bundle (CB4), at page 306, para 4.1.3(b) you say in parenthesis at the
3 end:

4 “(which, on the basis of the value of the amounts involved, would appear to
5 constitute a material error)”.

6 Here you are talking about potential changes in the format or presentation of the appellants,
7 namely Hays, Eden Brown and Anders?

8 A Yes.

9 Q So what you say here is: “it is on the value of the amounts involved” that it goes towards
10 material error?

11 A There are two factors. If you are comparing this with the Robert Walters’ treatment, the
12 Robert Walters’ treatment was in response to a change in the accounting framework, which
13 is clearly not an error, it is a change as a result of changes in accounting standards. The
14 position here is that if Hays were to change its basis for forming a judgment under these
15 particular contracts to go from principal to agent, it would have to recognise that it had
16 erred in its previous judgment. I believe Mr. Hall agreed with that statement in his evidence
17 yesterday.

18 Q This is maybe where the confusion lies. What you say in 4.3.1(b) is that on the basis of the
19 value of the amounts involved that leads one to conclude that it is a material error. But, that
20 is not right, is it?

21 A Well, it will be most of the turnover.

22 Q Let me just see if I can establish that proposition with you. Take up NCB4, Volume 2,
23 p.1773, para. 5(c). This is IAS8. You will recognise this, will you not, Mr. Allen? You
24 referred to it yourself.

25 A Yes.

26 Q Changes in accounting estimates and errors. The IAS standard. Paragraph 5(c) at p.1773.
27 Do you see the definition there of ‘material omissions’?

28 A Yes.

29 Q So, whether or not something is a material omission or error depends not just upon the size
30 of it, but the nature of it. That has to be judged in the surrounding circumstances.

31 A Yes.

32 Q You were here yesterday, were you not, when Mr. Sterling gave his evidence. I will
33 happily take you to the transcript, if you like. His evidence was that one could re-state --
34 He was talking about the Eden Brown accounts. It would not be material; it would just be a

1 change of terminology, and all the numbers would remain the same, would they not? He
2 was talking about changing the turnover figure to become gross transaction value, and
3 changing the net fees figure and labelling it turnover, but all the numbers staying the same.

4 A Yes.

5 Q That would not be a material error, would it?

6 A It would because the turnover number would have changed. I would disagree with Mr.
7 Sterling on that point.

8 Q I see. But, how is that a material error when one has regard to para. 6 of this IAS8 which
9 talks about

10 “--assessing whether an omission or mis-statement could influence economic
11 Decisions of users, and so be material, requires consideration of the characteristics
12 of those users ... [those] users are assumed to have a reasonable knowledge of the
13 business and accounting and a willingness to study the information with
14 reasonable diligence”.

15 Surely, Mr. Allen, it must be right, must it not, with a reasonably diligent user of the
16 account who knows about the business and he sees the exact same numbers are in the
17 accounts - they are just re-stated and they have got different labels -- Surely, Mr. Allen, that
18 is not going to be a user who is being materially misled, is it?

19 A Here, we're in International Accounting Standards which is the set of standards that Hays
20 prepares its accounts to. If Hays were to move to an agency basis for reporting, as it did
21 with the HPPS arrangement, and as we saw, caused a reduction of £200/£250 million in
22 turnover, then if Hays were to do the same in respect of these particular transactions then
23 one would imagine that it would do the same in respect of recording them, i.e. they would
24 disappear from the turnover. It is not even a requirement. The Guidance under UK GAAP
25 says that you can report the gross throughput value. We looked at this yesterday with
26 regard to department stores and concessions. They are not sales of the business. They are
27 billings on which you are purely earning a commission. So, they are very different in
28 nature. That is what Mr. Sterling was referring to yesterday - that he was going to move his
29 turnover into what would potentially be an optional disclosure. Now, under International
30 Accounting Standards - which is what we're looking at here and which is the framework
31 that Hays operates under - they do not have that option. Now, they could disclose that if
32 they wanted to, if they felt that that gave a fairer presentation. But, in relation to the change
33 that they made in relation to HPPS, they simply removed those amounts from their turnover

1 - as did Robert Walters, as we just saw. So, effecting the impact of this error would remove
2 a significant chunk of turnover.

3 Q Thank you, Mr. Allen. I have just one more topic left with you, briefly You mentioned a
4 moment ago that you had analysed twenty sets of recruitment agency accounts.

5 A Yes.

6 Q One of them was not the set of accounts for Comensura, was it?

7 A No.

8 Q Can you just turn to Mr. Hall's report - the second report? That is in the expert bundle
9 (CB4), Tab 2, page 158, para. 3.5.14. Mr. Hall first starts his references to Comensura.
10 You are obviously familiar with that passage, are you not? Just before I ask you any
11 detailed questions, you are familiar with this passage of his report, are you not?

12 A Yes.

13 Q Where he talks about Comensura and Matrix as being recruitment process outsourcing
14 companies. Yes?

15 A Yes.

16 Q You know what they are, do you not?

17 A I mean, I had a look at the accounts of Comensura as attached to Mr. Hall's report. I don't
18 know where I would find that in the bundles, but it was one of the exhibits. The principal
19 activity of the company was described as something like ----

20 THE CHAIRMAN: Would you like to see it?

21 A Yes. It might help. But, it was something like the management of contingent labour
22 services for neutral vendors, and something else. It was an odd description.

23 MR. HARRIS: I will happily take you to it, Mr. Allen, in the time we have left. NCB4. This is
24 the one that is referred to as Mr. Hall's Exhibit 16. It is NCB4, Volume 2, Tab 3, p.1589.

25 THE CHAIRMAN: I think that is the vendor agreement. You want the annual report.

26 A Yes.

27 THE CHAIRMAN: Page 1483.

28 A If we turn to p.1486 - this is the passage I was trying to recall.

29 "The principal activity of the company is the management of contingent labour
30 spend for both private and public sector clients on both a vendor independent and
31 a vendor neutral basis."

32 Now, I actually don't know what that means. I was trying to determine what the activity of
33 the company actually was. I did go as far as looking at the parent company, which I think
34 was called Impellam, to see how Comensura was dealt with in its parent company. It was

1 squarely not placed within the provision of temporary workers in their financial statements.

2 I obviously followed this point through from Mr. Hall's report.

3 MR. HARRIS: As I have no doubt you should have done. Maybe I could short-circuit this in a
4 different way. Take the witness statement bundle (CB3) and turn to Tab 5. That is the
5 second witness statement of Mr. Venables. Turn to page 84, para. 36. Mr. Venables is a
6 man who, in evidence orally, described himself as having twenty years' experience in the
7 recruitment business and having been financial director of Hays, one of the biggest
8 operators since 2006. Do you see how, half-way down, he refers to the very paragraphs of
9 Mr. Hall's report to which I have just taken you. He said that,

10 "-- where Mr. Hall considers the accounting treatment of Matrix, Alexander Mann
11 and Comensura. Hays supplies temporary workers to each of these recruitment
12 process outsourcing companies (RPOs). Although the services is offered by each
13 of the RPOs is essentially the same, as Mr. Hall demonstrates, if Matrix and
14 Alexander Mann account on a principal basis, while Comensura accounts on an
15 agency basis".

16 My first question to you is: You have no reason to dispute Mr. Venables when he describes
17 the services offered by the three RPOs as being essentially the same, have you?

18 A Yes, but I don't know what an RPO is actually doing or what the substance of its
19 arrangements are.

20 Q I accept that. But, as regards the essentiality of the sameness, to use rather odd English, that
21 you cannot dispute, can you? (Laughter)

22 A I am not really sure how to answer that.

23 THE CHAIRMAN: Rephrase the question.

24 MR. HARRIS: I will rephrase the question. I am coming to the end, Mr. Allen. Bear with me.

25 Mr. Venables describes the activities of these three companies as essentially the same. You
26 have no basis to dispute that evidence from him, have you?

27 A No, but he does not actually say what they are doing.

28 Q Right. But, the important point is that they are essentially the same, and yet they have
29 accounted for their recruitment process outsourcing - whatever exactly that may mean - on a
30 different basis, have they not, when it comes to agency and principal and hence the
31 presentation in the turnover figure of either gross turnover or net fees.

32 A Yes. My point in relation to the industry was in relation to the twenty sets of accounts that I
33 was able to look at, but I was looking at the services in relation to temporary workers, and
34 for that service line the accounting was uniform across the industry.

1 Q I am grateful, Mr. Allen. Thank you for bearing with me, particularly at the end there. I
2 have no further questions, Sir.

3 Cross-examined by Miss KREISBERGER

4 Q Mr. Allen, you will be pleased to hear I only have a very few questions for you this
5 morning. They are on behalf of CDI. Mr. Allen, can I ask you to take your first report and
6 turn up p.223 (CB4, Tab 3) Can I ask you to have a look at para. 3.4.8 which is at the
7 bottom of that page? Sub-paragraph (a): you summarise AndersElite's argument there. It
8 is an argument relating to the case law. I do not think I need to read it out. Then, if we go
9 over the page, to para. 3.4.9 you say,

10 "On the basis of the above arguments, the appellants contend that net fees or gross
11 profit (in the case of Eden Brown and AndersElite) constitutes applicable turnover
12 under the 2000 order definition".

13 A Yes.

14 Q Mr. Allen, is that statement, as it relates to CDI, based on our Notice of Appeal?

15 A Yes.

16 Q Could you just point me to the part of the Notice of Appeal on which that is based? There is
17 no source on that paragraph cited.

18 A Let me just read the paragraph before giving that.

19 Q The Notice of Appeal is in CB2.

20 A Sorry. I was just reading my report as to what I've said. (Pause whilst read): Sorry. Could
21 you take me to the ----

22 Q It is CB2, Tab 7. Mr. Allen, if you are unable to find it, perhaps in the interests of saving
23 time, will you take it from me that that is not stated in our Notice of Appeal?

24 A Okay.

25 Q In fact, if I take you to Footnote 20 on p.243, at the bottom of the page there -- You can just
26 read that to yourself, Mr. Allen. But, we note there that in defining relevant turnover, which
27 is what this ground is directed at, the OFT is not bound by the terms of the 2000 order. So,
28 that actually contradicts what you say at 3.4.9 of the report.

29 A Okay. I mean, obviously, I haven't read the whole thing, but I'll take your representation.

30 Q So, we can just accept that 3.4.9 is wrong as it applies to CDI.

31 A Yes, if that's what the Decision says.

32 Q Thank you, Mr. Allen. Mr. Allen, if I could ask you to take up an authorities bundle 1, Tab
33 19.

34 A I do not have that.

1 Q There is another way round this. We can take it in the core bundle.

2 THE CHAIRMAN: One can be passed over. (Same handed) A Commission Notice.

3 MISS KREISBERGER: Mr. Allen, could I ask you to turn to p.35 of that tab? You will see there

4 is the heading there, 'Turnover' - the concept of turnover.

5 A Yes.

6 Q This is the Commission Notice - the jurisdictional notice in the merger context. It is

7 something which you address in your report. If we just turn to para. 158, there the Notice

8 starts out by saying - and I am paraphrasing here - that turnover essentially equates to the

9 total amount of sales for providers of services. We get that from the last sentence there.

10 "The turnover of the undertaking concerned consists of the total amount of sales

11 for the provision of services in the last financial year."

12 A Yes.

13 Q You agree with that, Mr. Allen?

14 A It is so, yes.

15 Q It is just the language. So, if we then go to the next paragraph - and, again, this is purely on

16 the wording of the Notice - it says that that principal may have to be adapted in certain

17 circumstances, even if the intermediary invoices the entire amount to the final customer

18 because turnover in that case equates to commission -- You see that is at the second

19 sentence of 159. So, the principal may have to be adapted to the specific conditions, and

20 even if the intermediary invoices the entire amount, the turnover of the intermediary

21 consists solely of the amount of its commission.

22 A Yes, if the intermediary invoices the entire amount the turnover consists solely of the

23 commission, yes, and they may have to adapt in those circumstances.

24 Q Yes. So, we are agreed. So, what the Commission is saying there is that if you are dealing

25 with an intermediary you look at its turnover as it appears in the accounts and you isolate

26 that element of it which represents commission, however that may appear.

27 A Yes. I mean, I am looking at this as an accountant - not as a lawyer.

28 Q Absolutely. I would not ask you to stray outside of that territory. Mr. Allen, you agree with

29 that. That is what the Commission there is saying. It is quite plain.

30 A It is difficult for me to take a piece of legislation in isolation and look at definitions of

31 turnover.

32 Q Mr. Allen, this is something you address quite specifically in your report.

33 A Yes. I deal with the point in relation to the example here, where it gives examples such as

34 media or travel agencies as an intermediary. I talk about ----

1 Q We will turn to your report in a moment. But, you give an interpretation of this paragraph.
2 So, I am not asking you to do anything that is not covered in your report, just to be clear. I
3 am not asking a very specific question as to the definition of turnover. All I have put to you
4 - and I just want to be clear that you agree with me - is that if you are dealing with an
5 intermediary - and this is what the Commission says - you look at its turnover as it appears
6 in the accounts and you say, "That part of the turnover which equates to commission is what
7 we treat as turnover. Even it invoices the entire amount to the final customer, the turnover
8 of the undertaking acting as an intermediary consists solely of the amount of its
9 commission".

10 A No, I don't think it is saying that.

11 Q I have just read this sentence out to you.

12 A I think it's saying that even if the service is sold through intermediaries, they might bill the
13 whole amount, but the commission is only the bit -- that's only the part they're recording.

14 THE CHAIRMAN: Miss Kreisberger, I know that Mr. Allen does address this in his report. But,
15 what the Commission is saying -- or what it means when they are dealing with turnover for
16 the purpose of merger regulation is obviously not in an accounting sense, and really it is
17 then a question for us, and, I think, not for Mr. Allen, whether he has expressed an opinion
18 on it, or not.

19 MISS KREISBERGER: Except, Sir, that he does give a very specific accounting interpretation of
20 these paragraphs. I can take you to his report ----

21 THE CHAIRMAN: I think it might be better if, having reminded Mr. Allen of what the Notice
22 says, you ask him with regard to what he says in his report.

23 MISS KREISBERGER: Sir, I am grateful. If we then turn to the report at p.235, para. 4.4.13, this
24 is where you draw your conclusion, Mr. Allen, and I admit to being somewhat baffled by
25 this. I should just clarify. You say 'the regulation may be directed at clarifying the value of
26 turnover'. You mean the Notice that we have just been looking at?

27 A Yes.

28 Q Yes. So, that is an error. So,
29 -- the [Notice] may be directed at clarifying the value of turnover in instances
30 where an entity is acting as an agent or intermediary ... and presents in its financial
31 statements the gross value of sales throughput ---"

32 A Yes. I mean, all I'm saying here - and I'm saying 'may be', quite carefully - is that the
33 regulation refers to the media companies and package holidays and advertising -- certain
34 sectors whether agents or intermediaries, and under UK GAAP, having looked at certain

