**DECISION**

IN THE MATTER OF a review of the maximum margins, maximum delivery costs and maximum full service charge conducted under the authority of Section 14(1) of the Petroleum Products Pricing Act (S.N.B., Chapter P-8.05)

**December 19, 2008**

NEW BRUNSWICK ENERGY AND UTILITIES BOARD

IN THE MATTER OF a review of the maximum margins, maximum delivery costs and maximum full service charge conducted under the authority of Section 14(1) of the Petroleum Products Pricing Act (S.N.B., Chapter P-8.05)

## NEW BRUNSWICK ENERGY AND UTILITIES BOARD ("BOARD"):

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**PARTICIPANTS:**

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| Canadian Federation of Independent<br>Business (CFIB) | Leanne Hachey<br>Andreea Bourgeois<br>Richard Dunn |
| Canadian Independent Petroleum<br>Marketers Association (CIPMA) | Jane Savage |
| Canadian Oil Heat Association,<br>And Canadian Oil Heat Association/Clark Oil | William Gould<br>Peter Clark |
| Cooke's Quik Mart | Jeff Cooke |
| Co-op Atlantic | Peter T. Zed, QC |

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| | Daniel Chaisson<br>Stephen Davies |
| New Brunswick Department of Energy | Patrick Ervin<br>Alain Bilodeau |
| Everett’s Car Care | Dwight Everett<br>Matthew Everett |
| Gabriel Haché Ltée | Paul Haché |
| Global Fuels Inc. | Gary Maddock<br>Guy Gaudet |
| Greenwood Enterprises Ltd | Dale Dyker |
| Hunter’s One Stop | Eldon Hunter |
| Irving Oil Marketing Limited | Len Hoyt, QC<br>Matthew Holland<br>Lisa Rogers |
| Magnetic Hill Esso | Jason Lutes |
| Michaud Petroleum Inc. | Hermel Michaud<br>Marco Lavoie |
| Murray’s Esso | Calvin Grant |
| Notre-Dame Express | Jim McDowell |
| Richard Service Station and<br>Richibucto Corner Store Ltd. | Gabriel Richard<br>Jean-Marie Richard |
| Salisbury Road Gas and Convenience | Ted Nicholson |
| Scholten’s Group | Chris Scholten<br>Jerry Scholten<br>Alex Scholten |
| Ultramar Ltd. | Warren Maynard |
| Voice of Real Poverty Inc. | Bethany Thorne-Dykstra |
| Westmount Esso & Service Centre, 1992 Ltd. | Ronald Roy |
| XTR Energy Company Limited | Ken Wootton |

## INTRODUCTION

This is a decision of the New Brunswick Energy and Utilities Board (“Board”) following a review of maximum margins, maximum delivery costs and the maximum full service charge with respect to motor fuels and heating fuels. The review was conducted pursuant to the Board’s authority as set out in Section 14(1) of the Petroleum Products Pricing Act (“PPPA”). A public hearing was held as part of the review on October 6 and 7, 2008.

On July 1, 2006 the Province of New Brunswick began price regulation on the sale of heating and motor fuels, under the auspices of the PPPA and its attendant regulation, New Brunswick Regulation 2006-41 (“General Regulation”). On that date the initial maximum wholesale and retail margins, maximum delivery costs and the maximum full service charge for heating and motor fuels as set by the Minister of Energy (“Minister”) came into effect.

The considerations for the Minister in setting the total allowed margin are set out in Section 7 of the General Regulation. Section 7 reads as follows:

> ***Initial setting of the total allowed margin***
>
> *7(1) For the purpose of setting the total allowed margin for each type of heating fuel and motor fuel, the Minister shall consider*
>
> *(a) the historical margin between prices for the base product and the prices that have been charged to consumers within the province for the type of heating fuel or motor fuel, excluding applicable taxation and estimated*

*delivery costs, for the period of time that the Minister considers appropriate;*

*(b)* *whether the historical margins identified as a result of paragraph (a) are reasonable, taking into account*

*(i) the costs of transporting heating fuel or motor fuel from New York Harbour or, in the case of propane, from Sarnia to the province,*

*(ii) volume of sales,*

*(iii) storage costs, and*

*(iv) inventory turnover rates;*

*(c)* *that the maximum retail price only sets a maximum price for the sale of heating fuel and motor fuel by retailers to consumers and should, to the extent possible, allow competition between retailers; and*

*(d)* the other considerations that the Minister considers relevant.

Maximum margins for motor fuels were set by the Minister, effective July 1, 2006, at six cents per litre for wholesalers and five cents per litre for retailers, for a total allowed margin of eleven cents per litre. Maximum margins for furnace oil were set at five cents per litre for wholesalers and thirteen cents per litre for retailers, for a total allowed margin of eighteen cents per litre. Maximum margins for propane were set at twenty-five cents per litre for wholesalers and twenty-five cents per litre for retailers, for a total allowed margin of fifty cents per litre. Section 4(4) of the PPPA allows wholesalers and retailers to apportion the total allowed margin between them in such manner as they see fit, provided that they agree to this in writing.

Maximum delivery costs were set by the Minister at two cents per litre for motor fuels, five cents per litre for heating oil and ten cents per litre for propane. The maximum full service charge for motor fuels was set at 2.5 cents per litre.

Gardner Pinfold Consulting Economists Ltd. ("Gardner Pinfold"), an independent expert, was engaged to advise the Board on the matters in issue and to prepare a report. The Board corresponded with petroleum products wholesalers and retailers encouraging them to cooperate with Mr. Michael Gardner of Gardner Pinfold. The report prepared by Gardner Pinfold provided recommendations concerning the maximum margins, maximum delivery costs and the full service charge. It is critical to understand, as was stated at the commencement of the hearing, that the Gardner Pinfold report "*represents the recommendations of the consultant and not the opinions of the Board*".

Participants in the industry and the general public were informed of their right to participate in the review process, including the right to file evidence and to question other parties' evidence, both in writing and at the public hearing. While 23 companies or individuals registered as participants in the review process, only the New Brunswick Department of Energy filed evidence. This evidence was a report by MJ Ervin and Associates ("MJ Ervin") and was a critique of the Gardner Pinfold report. No evidence was filed by any industry participant and Mr. Gardner testified that much of the information requested by Gardner Pinfold from industry was not forthcoming. The Board is disappointed by the lack of cooperation with Gardner Pinfold and the lack of evidence provided by the New Brunswick petroleum industry and encourages the industry to provide appropriate evidence as part of any future review.

## MATTERS BEFORE THE BOARD

The purpose of this review was to determine if the current maximum margins, maximum delivery costs and maximum full service charge allowed for heating and motor fuels are “justified” and, if not, to order adjustments to said margins, delivery costs and full service charge that the Board deems appropriate.

Section 1.1 of the PPPA provides guidance to the Board. It states:

> ***Considerations by Board***
>
> **1.1** *The Board shall, when making a decision under this Act respecting prices, margins, delivery costs or full service charges, consider the fact that consumers should benefit from the lowest price possible without jeopardizing the continuity of supply of petroleum products.*

The maximum margins, maximum delivery costs and the maximum full service charge are each discussed below.

## MAXIMUM MARGINS

Section 9 of the General Regulation sets out the matters that the Board must consider in determining whether the maximum margins should be changed. It is noteworthy that these considerations are nearly identical to those used by the Minister in setting the initial margins. Section 9 reads as follows:

***Application for adjustment of maximum margins***

***9****(1)* *Where an application has been made to the Board under section 12 of the Act for a change in the maximum margin that may be charged by a wholesaler or retailer, the Board shall consider the following:*

*(a)* *whether, since the maximum margin was last set, an adjustment would be justified as a result of a change to*

*(i)* *the costs of transporting heating fuel or motor fuel from New York Harbor or, in the case of propane, from Sarnia to the province,*

*(ii)* *volume of sales,*

*(iii)* *storage costs,*

*(iv)* *inventory turnover rates, and*

*(v)* *applicable levies and insurance costs; and*

*(b)* *any other factors that the Board considers relevant.*

Section 9 lists certain specific matters that the Board must consider but also requires the Board to consider "other factors", if the Board determines that those "other factors" are relevant. The Board considers that there are "other factors" that are relevant. These "other factors" relate to the cost structure of the industry and include matters such as: capital costs, maintenance costs, staffing levels, and the sharing of costs between the petroleum business and other businesses that are operated at the same location. The Board believes that an examination of all relevant cost factors is necessary before it can determine if any change, up or down, to the maximum margins is justified. In order to justify any change to the maximum margins, the Board must be satisfied that the cost of operation has significantly changed in the period since the introduction of regulation.

Gardner Pinfold examined the matters set out in Section 9(1)(a) of the General Regulation. The report also examined certain aspects related to some of the “other factors” that the Board believes are relevant. The Gardner Pinfold report provided some evidence of increased operating costs in specific areas. The report addressed only a portion of the cost factors that are important to the industry. Further, the Board does not believe that all of the relevant aspects related to each of the operating costs were adequately considered by Gardner Pinfold. In addition, no other party provided evidence concerning the relevant “other factors”. The Board is therefore unable to determine if any change has taken place with respect to the costs of operation for either wholesalers or retailers. In the absence of such evidence, the Board cannot adjust the maximum margins, up or down, for heating fuel or motor fuel. The Board finds that the current maximum margins for wholesalers and retailers of heating fuel and motor fuel are justified.

The Board believes that it is helpful to provide the following comments on the evidence that was provided concerning the factors, listed in Section 9(1) of the General Regulation, related to maximum margins.

Factors under Section 9(1)(a) of the General Regulation

The Board notes that, with a few exceptions, there was no evidence provided on the items enumerated in Section 9(1)(a). The Gardner Pinfold Report did identify changes relating to transportation costs, storage costs and to applicable levies and insurance costs.

Dealing first with the transportation cost for propane, the Gardner Pinfold report recommended a change in the wholesale margin due to an increase in the cost of transporting propane from Sarnia to New Brunswick.

After consultation with industry, and assuming a fifteen percent increase in the cost of diesel fuel, Gardner Pinfold recommended an increase to the wholesale margin of 1.35 cents per litre.

This recommendation was based partly on anecdotal evidence and was not based on an analysis of overall cost structure.

With respect to those calculations that were based on an increase in the price of motor fuel, the Board notes that we are presently in a period of much lower cost for these products.  The Board recognizes that the price of the product may affect certain costs. The Board is not prepared to accept that a significant change to a particular cost, up or down, has occurred due to a change in the price of a petroleum product unless that change in price has occurred since the introduction of regulation and has been demonstrated to be a sustained change.

Further, the Board was not presented with evidence that supported allocating 100% of any fuel cost increase to freight rates. The Board notes that while fuel is a significant component in freight costs, other factors such as labour, capital costs and maintenance have a significant effect on total transportation costs.

Dealing with storage costs, the Gardner Pinfold report recommended an increase of 0.30 cents per litre in the retail margin for heating fuel due to an increase in storage costs. The report conceded a lack of data stating that *"A verifiable estimate of the impact on margins of higher carrying charges is not available from industry."* In the absence of evidence on this subject, the report also stated *"It is possible to derive indicative estimates based on known price, quantity and interest rate values and assumptions about payment terms."* The Board finds the evidence insufficient to conclude that there has been a change in storage costs for retailers of heating fuel. The recommendation was not based on an analysis of the overall cost structure, is supported by insufficient data and is based upon pricing levels much higher than currently exist.

A complete analysis related to storage costs was not available to the Board. Such an analysis should address all related matters, for example, capital costs, frequency of delivery and maintenance costs. Without such information, the Board is unable to determine if a change in the total costs of storage has taken place since the margin was first set. The Board, therefore, cannot adjust the retail margin for heating fuel based on storage costs.

With respect to applicable levies and insurance costs, Gardner Pinfold found that there was no appreciable increase in insurance costs and recommended no change relating to that factor. The report stated that the 0.025 cent per litre levy paid by motor fuel wholesalers to defray the Board's expenses under the PPPA represented a new cost not experienced prior to regulation and recommended that the wholesale margin on motor fuel be increased to recognise this cost. The Board notes that the Legislature made the levy a stand-alone charge, separate from the wholesale margin and that it has been in place since the beginning of regulation. In the absence of any change to the levy, the Board cannot adjust the wholesale margin for motor fuel due to this factor.

Factors under Section 9(1)(b) of the General Regulation

The Gardner Pinfold report proposed increases to the maximum retail margins for heating fuel and motor fuel based upon an analysis of "other factors", specifically credit card costs, wage costs and other input costs.

With respect to credit card fees and usage, Gardner Pinfold recommended that the retail margin for motor fuel be increased by 0.58 cents per litre based on three factors:

1) An increase in the fees charged by credit card companies from 1.65% to 1.75% (of the total value of each transaction),
2) A rise in credit card usage from 30% to 45% of all motor fuel transactions, and
3) A 37% rise in the price of motor fuel (gasoline in particular) over the two years since petroleum regulation had been in effect.

There was some evidence at the hearing to support the increase in credit card fees from 1.65% to 1.75%. While some parties indicated in argument that the increase was even greater, no evidence to this effect was filed.  The Board notes the relative ease with which such evidence could have been supplied by the petroleum industry ether to Gardner Pinfold or to the Board directly.  Based on the evidence at the hearing, the Board accepts that credit card fees have increased by 0.1%.  Such an increase, on its own, does not justify an increase in the margin.

With respect to the increase in credit card usage, the conclusion was based on anecdotal evidence and no other evidence was filed in support of an increase in use of credit cards.  In the absence of any reliable evidence, the Board cannot conclude that there has been any increase in credit card usage.

With respect to those calculations that were based on an increase in the price of motor fuel, the Board has already commented on the impact that prices may have in an earlier section.

The Gardner Pinfold report recommended an increase in the margins to compensate heating fuel and motor fuel retailers for wage increases since regulation came into place. The report proposed using 19% as the appropriate increase in wages.  The MJ Ervin report suggested a much lower increase had taken place.  The Board finds that while there has been an increase in the minimum wage, this is insufficient to support an increase in the margin.  The Board has no evidence of any change in total labour costs. No evidence was led as to whether staffing levels have remained constant, increased or decreased.  More broadly, the Board has no evidence of other cost factors which might permit it to form a conclusion about any change in the cost structure of the industry.

Gardner Pinfold recommended an increase to the maximum retail margins for heating fuel and motor fuel to reflect other input costs such as general operating expenses for retailers including: utilities, licence fees, municipal taxes, equipment leases and carrying costs. As part of its review, Gardner Pinfold analysed municipal taxes and carrying costs. In both cases the consultant found very marginal cost increases, not sufficient to warrant a stand-alone increase on their own. However, the consultant did recommend rolling these factors into "a general adjustment of input costs based on a price index." With respect to the other input costs Mr. Gardner stated that industry data was often impossible to obtain, requiring him to base his conclusions on anecdotal evidence or broad economic data.

The Board is not inclined to approve any adjustment to the margins based solely on general trends or price indices. The Board was not provided with any industry-specific evidence that there has been an increase in the cost structure. In order to justify a change, up or down, to the retail margins, the Board must be satisfied that the cost of operation has significantly changed in the period since the introduction of regulation.

## MAXIMUM DELIVERY COSTS

The specific items that the Board is to consider when reviewing the maximum delivery costs allowed for specific fuel types are itemized at Section 11 of the General Regulation.

**** ***Adjustment of maximum delivery costs***

***11*** *Where an application has been made to the Board to adjust the maximum delivery costs that may be charged by a wholesaler or retailer under section 13 of the Act, the Board shall consider*

*(a) fuel costs,*

*(b) insurance costs,*

*(c) capital costs,*

*(d) volume of sales,*

*(e) in the case of an application for delivery costs that are particular to the applicant, the cost effectiveness of the applicant's operation, and*

*(f) any other factors that the Board considers relevant.*

<u>Motor fuels</u>

The issue of delivery costs for motor fuels was one topic on which the Board had detailed evidence to consider. Gardner Pinfold provided evidence of a number of communities where the actual cost of delivery paid by the retailer exceeded 2.0 cents, and in a few cases, exceeded 3.0 cents. The retailer, however, can only pass on to the consumer the actual delivery costs up to a maximum of 2.0 cents per litre. While an increase in maximum delivery costs would affect only a small portion of retailers, those affected tend to be located in rural areas. A maximum delivery cost which is less than their actual cost puts these retailers at a significant disadvantage and could jeopardize the continuity of supply in certain areas of the province.

The Board notes that diesel fuel prices have declined since the information provided by Gardner Pinfold was compiled, but given that some retailers paid delivery costs that exceeded 2.0 cents per litre by a very considerable margin, the Board considers it appropriate to increase the maximum delivery cost for motor fuels by 0.5 cents per litre to 2.5 cents per litre. This will allow these retailers to pass on to consumers the actual delivery costs paid by the retailer up to a maximum of 2.5 cents per litre. Accordingly, the Board orders that effective January 1, 2009 the maximum delivery cost for motor fuel shall be 2.5 cents per litre.

If there are locations where the delivery costs exceed the newly authorized maximum, the Board reminds retailers and wholesalers of their option to file for a delivery cost adjustment, under Section 13(1) of the PPPA, that is specific to their circumstances. In most cases the Board expects that these would be straight forward reviews, based on verifiable delivery expenses, which should not be financially onerous on an applicant.

<u>Heating Fuels</u>

With respect to the delivery costs for furnace oil and propane, the Board was provided with no specific data.  Gardner Pinfold took the same approach it had with respect to assessing whether the cost of transporting propane into New Brunswick had increased; it applied a15% increase in diesel fuel prices against the current maximum delivery costs. This approach is, in the opinion of the Board, not sufficient to “justify” the adjustments recommended by Gardner Pinfold. Once again, the analysis does not take place in the context of a review of the total transportation cost, the data is insufficient and the calculation is based pricing levels which are not current. The Board will make no adjustment to maximum delivery costs for furnace oil or propane.

## MAXIMUM FULL SERVICE CHARGE

In its report, Gardner Pinfold made no recommendation with respect to adjusting the maximum full service charge (for dispensing fuel at a retail motor fuel outlet). While the consultant noted that the current maximum charge of 2.5 cents per litre is not sufficient to allow a retailer to recover the cost of employing an attendant (Gardner Pinfold observed that a retailer would need to pump 2.25 million litres of full service motor fuel to recover the wages of the attendants) he noted that full service is still offered as a convenience by a dwindling number of stations. That being the case, Gardner Pinfold recommended that the full service cap be lifted entirely. The Board notes that the MJ Ervin report concurs that the full service charge be entirely removed from the regulatory regime.

The PPPA authorizes the Board to adjust the maximum full service charge but does not authorize it to remove the cap on the full service charge. Removal of the cap would require an amendment to the PPPA by the Legislature.

No evidence was placed before the Board about what the amount of any adjustment to the maximum full service charge should be. Therefore, the Board cannot make an adjustment.

## SUMMARY

The Board finds that the current maximum wholesale and retail margins are justified.

The Board finds that the current maximum delivery costs for heating fuel are justified.

The Board finds that a change in the maximum delivery cost for motor fuel to 2.5 cents per litre is justified. This change is to be effective as of January 1, 2009.

The Board finds that the current maximum full service charge is justified.

Dated at the City of Saint John New Brunswick this 19th day of December, 2008

Raymond Gorman, Q.C., Chairman

Cyril W. Johnston, Vice-Chairman

Edward McLean, Member

Robert Radford, Member

Steve Toner, Member