MTA Submission

Commerce Commission
Market Study into the Retail Fuel Sector – Draft Report

13 September 2019

Dear Sir / Madam

Submission: Market study into the retail fuel sector – draft report

This submission is from:

Motor Trade Association (Inc)
PO Box 9244
Marion Square
Wellington 6141

The contact person in respect of this submission is:

Name:	Ian Baggott
Title:	Sector Manager – Energy and Environment
Ph:	(04) 381 8843
Email:	ian.baggott@mta.org.nz

Thank you for the opportunity for MTA to provide comment on the market study into the retail fuel sector (draft report) regarding the views of and its effect on the independent retail fuel market sector (service stations).

MTA notes that submissions on the *Preliminary Issues Paper* were due on 21 February 2019 and the *Draft Report* was published on 20 August. In that six-month period the Commission produced a commendable 424-page document. Unfortunately, submitters were given less than a month to respond to that comprehensive document. This made the task of robust analysis very difficult.

Yours sincerely,

Greig Epps
Advocacy & Strategy Manager

Contents

Introduction 4
Submission 4
A brief overview 4
Comments regarding the findings in the Draft Report 5
The impact of inflexible contracts 6
Vertically integrated oligopoly vs independent retailers 6
Wholesale competitiveness 9
Transparency..10
Comments regarding the proposals for change contained in the Draft Report..................10
What else should be considered?...10
What more could be done? 14
Next steps?...16
Schedule 1 – table of responses to Draft Report questions (invited comments) 17

Introduction

The Motor Trade Association (Inc) (MTA) was founded in 1917 and in 2017 celebrated 100 years of trust with the NZ motoring community. MTA currently represents approximately 3,600 businesses within the New Zealand automotive industry and its allied services. Members of our Association also operate businesses including automotive repairers (both heavy and light vehicle), collision repair, service stations, vehicle importers and distributors and vehicle sales. The automotive industry employs 57,000 New Zealanders and contributes around $3.7 billion to the New Zealand economy.

We appreciate the opportunity to comment on the market study into the retail fuel sector (draft report) and have the following comments to make on behalf of MTA's independent (dealer owned and operated) service stations.

Submission

Thank you for the opportunity to provide comment on the Market study into the retail fuel sector, Draft report, dated 20 August 2019 ("**the Draft Report**"). This submission responds to the Draft Report, and associated documents released by the Commerce Commission together with the Draft Report, and the invitation from the Commission to provide written comments on the draft report.

A brief overview

1. The MTA generally supports the findings and analysis in the Draft Report, is delighted that the report has confirmed MTA's own views and concerns. MTA further applauds the way that the Commission has engaged with these complex issues, and identified that the primary issues impacting on consumer prices relate to contractual constraints and other issues in the wholesale market.

2. In respect of issues regarding Wholesale supply arrangements, MTA endorses the "Summary of our findings" at the beginning of Chapter 6 of the Draft Report, at page 172, particularly the following points:

   "*In addition, it appears that dealers and distributors have stable, long-term relationships with the majors from which they obtain wholesale supply. This has arisen from a range of explicit contractual and implicit non-contractual factors.*

   2.1 Explicitly, many wholesale supply agreements contain restrictive provisions that appear to lock dealers and distributors into relationships with their wholesale suppliers. This has a similar effect to structural vertical integration and reduces the scope for competition at the wholesale level.

   2.2 Implicitly but supported by the wholesale supply agreements, majors are able to influence the commercial decisions of dealers and distributors in a variety of ways.

The combination of vertical integration and restrictive wholesale supply arrangements that has emerged since deregulation appears to have prevented the emergence of a workably competitive wholesale market."

3. However, there is a lack of direction in terms of how to address the issues, particularly those that could improve competition at the retail level: in some respects, the Draft Report does not (yet) go far enough.

4. Also, given that the focus of the report is aimed at the major fuel suppliers and their vertically integrated network of retail outlets, any incomplete solution could adversely impact on workable competition involving independents operating in the reseller and (particularly) the dealer/independent retailer sector part of the market.

5. The MTA's comments regarding the Draft Report are summarised below, responding first to the substantive findings in the Draft Report (from para 6, below), and secondly to the discussion regarding change in the Draft Report (from para 8, below). MTA has tried to keep these comments at a fairly high level, as much of the ground has been covered already in previous submissions and in the Draft Report. In addition, a specific response to the particular issues identified for comment in the Draft Report appears in table form in Schedule 1.

Comments regarding the findings in the Draft Report

6. MTA generally agrees with and accepts the analysis identifying the issues arising in the wider fuel market, including in particular:

   6.1 the effect of inflexible contracts preventing resellers (dealers/retailers and resellers/intermediate wholesalers) from switching suppliers;

   6.2 the description of the market as a vertically integrated oligopoly[1]; and

   6.3 the impact of:

      6.3.1 a lack of competition, and market liquidity, at wholesale level;

      6.3.2 limitations on access to essential wholesale/distribution market infrastructure, amounting to a barrier to entry to the wholesale market[2]; and

      6.3.3 a lack of transparency and clarity around actual pricing, including discounting which confuses real prices, higher-octane fuels not appearing on price boards, and fuel firm strategies obfuscating price competition.

[1] Draft Report, paragraphs 2.70, 3.3 and 3.4. Paragraph X99 in the Draft report - Executive summary summarises the position usefully: "*Z Energy, BP and Mobil supply over 90% of the fuel consumed by New Zealand motorists through their own retail sites and wholesale supply agreements with other retailers (also known as resellers). All retailers other than Gull are dependent on the majors for their fuel supply.*"

[2] Draft Report, Chapter 5, paragraph 5.36. This could be characterised as an "infrastructure lock-in".

7. MTA considers that there are four main issues to be clarified:

The impact of inflexible contracts

7.1 There should be more emphasis on the contractual and practical commercial constraints on wholesale pricing, particularly:

7.1.1 the impact of some of the identified contractual constraints (on resellers and dealers), which:

(a) lock in retailers and resellers to:

(i) long term exclusive supply contracts;

(ii) the price available from a major, or a price available from a reseller that is supplied exclusively by a major (save for Gull); and

(iii) one-sided terms and conditions dictated by the supplier (often that supplier is a major, but where there is a reseller in some respects terms imposed by the major that supplies the reseller); and

(b) prevent retailers from being anything other than wholesale price takers - as opposed to being active participants in an active competitive wholesale market (which would in turn be stimulated by retailers actively engaging with a wholesale market); and

7.1.2 the impact of practical commercial constraints, given that even if sites come up for renewal of supply on shorter cycles:

(a) there may not be incentives for other wholesalers to compete to offer wholesale supply to a particular site – other wholesalers may have their own branded network outlets nearby so there may be an effective stalemate between the majors, and thus a lack of competition to supply unless another wholesaler happens to be actively competing in that area (which would generally require accessible retail sites in reasonable numbers); and

(b) established existing sites will only relatively rarely be offered to market, and viable new/alternative sites will only relatively rarely be available.

Vertically integrated oligopoly vs independent retailers

7.2 The report should clarify that the findings relating to the returns obtained by fuel firms do not relate to independent retailers.

7.2.1 The Draft Report identifies significant returns on investment in the region of 20% being obtained by the “fuel firms” (large and small – majors/Gull/resellers);

7.2.2 in addition, in some contexts, the study appears (perhaps unintentionally) to link those returns more generally to "New Zealand retail fuel firms"[3], "New Zealand retail fuel industry"[4] and even more generally to "retailers", suggesting (especially if these references are then taken out of context) that those returns are not just substantial "fuel firm" returns but returns taken by dealers/retailers, including independent retailers and smaller retailers[5];

7.2.3 <u>but</u> the Draft Report does not identify <u>any</u> evidence that independent retailers are achieving profits at the levels enjoyed by the fuel firms.

7.2.4 To the contrary, the Draft Report:

(a) clarifies that the market study focussed on the larger players (understandably in a vertically integrated market)[6] and did not seek a large cross-section of data evidence as to independent retailer returns[7];

(b) notes that there were discussions with a number of service station owner-operators supplied by a variety of firms[8], and identifies that "some dealer-owned retail sites are operating on quite slim margins and facing financial pressure"[9], and that "not all players in the retail fuel industry are as profitable as this analysis of the profitability of the majors and resellers seems to indicate", before referring to "the large number of dealer-owned and operated service stations active in the retail market"[10].

7.2.5 As it happens, regrettably, independent retailer profitability is difficult and impractical to assess (as the Draft Report acknowledges[11]) because:

(a) retailers are reluctant to disclose returns/profitability details – this is unsurprising, as (MTA understands) most supply contract terms require confidentiality; independent retailers would require absolute assurances as to confidentiality to disclose such

---

[3] For example, Draft Report, paragraph 3.29.3, the heading above D173, D180

[4] Draft Report, paragraph 3.67.

[5] These inferences may explain the numerous statements by the Prime Minister and others that consumers were being "fleeced at the pump", which unfairly tarnished the practices of independent retailers. In contrast, the concerns about the opacity of the wholesale market may mean that consumers are being poorly served ***before*** the pump.

[6] For example, Draft Report, D54 and D206.1

[7] See the Attachment D to the Draft Report, paragraphs D212 and D214.

[8] Attachment D to the Draft Report, paragraphs D214 and D215.

[9] Draft Report, paragraph 3.25

[10] Attachment D to the Draft Report, paragraph D213. See also Draft Report, D212 and D214, and also the references to "*low and inconsistent profitably of such sites*" at D218, and to the distribution of margins at D221.

[11] Attachment D to the Draft Report, paragraph D214.

information to MTA, but MTA is not in a position to provide absolute assurances;

(b) there are relatively few site sales (given contract terms/market conditions) against which to benchmark perceived value/profitability; and

(c) independent retailer operations often involve other retail or repair business operations[12], so detailed site by site analysis would be required to separate out the fuel retailer component; and

(d) it is likely the case studies identified in the Draft Study to assess retailer profitability provide an optimistic retailer profitability benchmark because the case studies are likely to focus sites expected to be viable (otherwise why do a study) and have been provided by wholesalers (majors/Gull/resellers) based on the favourable retailer conditions they can deliver.

7.2.6 In any case:

(a) as MTA submitted in its 7 May 2019 Comments on the working papers, returns on investment may not be a useful measure for fuel retailers that are not on the scale of the larger fuel firms, particularly small independent retailers, as owner-operator labour may be a significant component of the investment[13]. Also, as noted above, the business model (often fuel plus retail, in various different models) clouds any assessment of return on investment in the fuel component of the business;

(b) independent retailers are operating in a relatively high risk environment, with capital and labour investment tied in for long periods and in many instances with commitments to make good the site (tanks/pumps etc) at the end of a relationship with a fuel/equipment supplier, such that reasonable retail returns (albeit not necessarily in the ranges attributed to the fuel firms in the Draft Report) might reasonably be expected in a workably competitive market;

(c) the Draft Report properly identifies that for some dealer-owned retail sites “this seems to reflect the high wholesale price they pay for fuel”[14] and that “difficulties faced by some dealers in respect of some sites seem, in large part, a function of how the total margin was split between the wholesale and retail level”[15]:

[12] With the accompanying differences in business risk profiles.
[13] See Attachment D to the Draft Report, paragraph D214.4.
[14] Draft Report, paragraph 3.25.
[15] Attachment D to the Draft Report, paragraph D221

(i) self-evidently resellers and retailers, and particularly independent resellers and retailers, can only compete within the confines of the margins available to them net of the cost of acquiring fuel from a long term arrangement with a major and in the context of market prices on offer from others including vertically integrated participants; and

(ii) it is submitted that these conclusions in the Draft Report apply more generally to the wider retail market, or at least the wider independent retail market.

(d) The best information available to the MTA (from its dealings with members over the years, piecemeal, anecdotally and in confidence) suggests independent retailers are operating in a competitive retail environment, and that margins and profitability are generally far short of the 20% ROACE the Draft Report attributes to "fuel firms" – which is supportive of conclusions that independent retailers and smaller retailers, at least, are not achieving that level of return.

7.2.7 In that context, the final report should record that the returns analysed for "fuel firms" are vertically integrated wholesaler/reseller "fuel firm" returns, not returns obtained by "retailers" generally or by dealers/independent retailers.

Wholesale competitiveness

7.3 The Draft Report is right to identify that, for various reasons, the ad hoc effect of the small number of resellers (all with long term contracts with a major) and Gull serves to highlight the issues and constraints within the wholesale market, and do not address the concerns the Commission has identified[16] or suggest meaningful progress towards workable effective wholesale market competition.

7.3.1 The fact that the market can on occasions respond to competition from Gull and other resellers highlights that there is headroom for wholesale price competition, particularly given the evidence in the Draft Report of fuel firms cross-subsidising competition where there is an alternative provider against other sites where there is less competition[17].

7.3.2 But the limited impact that such other wholesalers are having generally highlights the significant constraints that continue to impact on the wholesale market.

[16] See page 14 of the presentation on the Retail Fuel Market Study DRAFT REPORT, provided by the Chair, 20 August 2019 ("**the Draft Report Presentation**").
[17] Draft Report, paragraph 3.104.

Transparency

7.4 MTA agrees with the suggested focus on achieving a more workably competitive wholesale market, with lower/more transparent wholesale prices and fewer retailers tied (directly and indirectly) to one or other of the majors.

7.4.1 That includes the findings regarding discounting, the absence of high-octane fuels from price boards[18], which appears to be part of an implicit more general finding regarding overall price transparency/clarity for retailers in wholesale markets and for retailers and consumers operating in retail markets.

7.4.2 However, MTA does not support the publication of prices[19], which has led to some unintended outcomes in other jurisdictions.

Comments regarding the proposals for change contained in the Draft Report

8. MTA considers that the Commission needs to go further in some key areas, and to recognise some different considerations arising in respect of the independent retailer component of the market.

9. In that context, MTA considers that there are two main types of additional issues:

What else should be considered?

9.1 Complete solutions to create wholesale market liquidity are unlikely to come from the fuel firm entities that comprise the existing oligopoly wholesale market suppliers - their input is essential to ensure changes are workable, but those fuel firms' focus is to maintain, not erode, their profits.

9.2 An effective response to the lack of an active wholesale market will need to consider options to remove impediments to market participation by alternative wholesalers/resellers and also impediments to market participation by retailers.

9.3 Opening up infrastructure (processing, storage, and transport), together with shortening retailer/reseller contract terms (and relaxing other contract terms/reducing the impact of discounting through card programmes etc), is unlikely to be a complete solution, in itself, to create market liquidity and ensure competition at wholesale levels as:

9.3.1 most existing retail operations are tied to the majors directly or indirectly; and

9.3.2 other market conditions (such as whether a wholesaler already has supply arrangements nearby) may impact site by site on whether alternative supply options will be viable/on offer at the end of the

---

[18] See Schedule 1, comments re paragraph 7.63 of the Draft Report.

[19] See Schedule 1, comments re paragraph 8.61 of the Draft Report. "…while price-tracking apps, such as Motormouth, were designed to help consumers find the cheapest price, they were also helping competitors quickly detect and match price movements …": https://thenewdaily.com.au/money/your-budget/2019/05/09/petrol-prices-high-coles-express/

current supply contract term - otherwise the retailer/reseller will likely be stuck with the status quo.

9.4 Although the Draft Report identifies wholesale market issues[20], and that retailers compete within the margins remaining after they take supply, the Draft Report also highlights the contractual and market constraints that are impediments to those retailers, particularly independent retailers, actively participating in the wholesale market.

9.4.1 In that context, there needs to be more emphasis on how retailers and resellers, particularly independents, engage with the wholesale market.

9.5 Any changes that seek to free up competition in the wholesale market should <u>also</u> focus on the ability of retailers including independent retailers to be active buyers in that wholesale market; retailers, including independent retailers, should have more options to more actively participate in the market in which they buy fuel:

9.5.1 to impact actively on the price they pay for fuel, and thus the price they are able to deliver to consumers; and

9.5.2 still achieve reasonable commercial market returns reflecting the commercial risks that they are taking.

9.6 A solution that addresses some not all issues could have unintended anticompetitive consequences for aspects of the retail market, particularly on independent retailers:

9.6.1 in the current market it appears that, although the precise number/proportions are not clear, a substantial proportion of retailers – less than 50% but perhaps as high as 40% - operate as independent retailers[21];

9.6.2 independent retailers are price takers in the wholesale market, are not themselves part of a vertically integrated wholesale/retail arrangement and will only be "in the market" to potentially obtain a different

---

[20] MTA agrees with the observations in paragraph 4.24 of the Draft Report that: "… *if we focused solely on entry conditions at the retail level, we could miss important factors affecting competition arising at other levels of the supply chain which affect retail prices. Although there are many retailers competing in some local retail markets, all of them ultimately rely on one of the importers for fuel supply*."

[21] Detailed data on independent retailer numbers/proportions in the retailer market is not readily available. But taking a conservative view of the summary contained in Figure 8 of the 2017 New Zealand Fuel market financial performance study, and counting *only* those sites specifically identified as dealer owned and those non-major sites that appear to be independently owned, there appear to be a substantial number of independents – perhaps in the 40-50% range (although other elements of that report suggest otherwise). MTA membership data, which involves only some of the market, suggests a figure more like 40%. Hence MTA uses "less than 50% and perhaps as high as 40%" as a broad indicator, for present purposes. But the point here is not the exact figure (which MTA accepts is not clear), but simply that there is a significant independent retailer component in this market.

price/provider relationship at the end of a contract term, so they will be a vulnerable component of the retail market;

9.6.3 market changes that impose price pressure on wholesalers that have their own vertically aligned retail outlets, without ensuring active retailer access to the wholesale market, are likely to result in independent retailers bearing the brunt of any price pressure (with a real prospect of being crowded out of the market by differential supply availability or pricing, even a price squeeze);

(a) price pressure is to be expected, but if retailers (particularly independent retailers) can only be price takers they risk being the meat in the sandwich between wholesalers and consumers;

(b) retailers, particularly smaller independent retailers, are dependent on wholesalers for supply and, even if there are improvements around terms and conditions generally, have limited bargaining power;

(c) vertically integrated retailers will have more certainty around supply/pricing, may be favoured by a parent wholesaler (differential pricing or "raising rival's costs"[22]), and are likely to be better placed to survive pressured retail margins if the available margin is captured at wholesale level (i.e. a price squeeze); and

(d) perversely, that could mean that reforms focussed only on the wholesale market, but not on retailer access to that market, would increase wholesaler numbers but decrease retailer numbers, with independent retailers being the most likely casualties; and

9.6.4 that could concentrate the market further in the hands of wholesalers and retailers that are vertically aligned, reducing the scope for independent retailer participation and competition – as outlined in the following graphic:

[22] See the first full bullet point on page 12 of the MTA's 22 February 2019 submission on the Market Study into Retail Fuel.

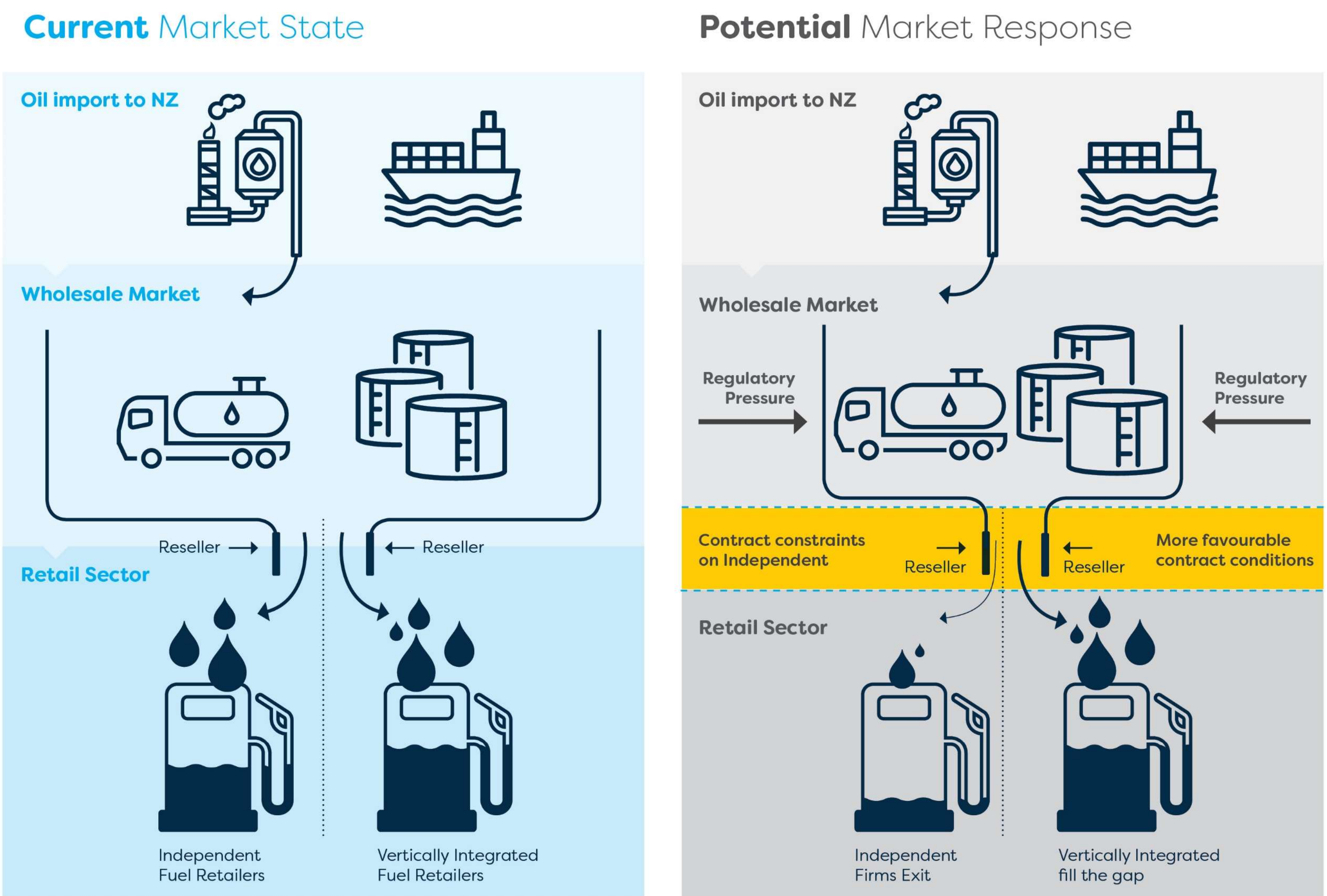

Figure 1 Potential market response to regulation of wholesale market

9.7 The issues impacting on independent retailer participation and competition could also have a similar effect on independent reseller participation, if independent resellers too are not put in a better position to actively access competitive wholesale pricing.

9.8 In that context, any market changes focussed on competition in the wholesale market should also:

9.8.1 deliver better visibility and access to that market for resellers and retailers, including independent resellers and retailers, so that they can actively see and actively seek competitive prices (and are not just operating as price takers);

9.8.2 ensure that any regulatory reforms or other changes to increase wholesale competition do not, perversely:

(a) reduce retailer numbers, particularly independent retailer numbers, and retailer competition; and/or

(b) concentrate retailing among firms that are part of vertically integrated wholesaler arrangements (majors/retailers or reseller/retailers on long term contracts with majors);

What more could be done?

9.9 MTA encourages the Commission to weigh up the following:

9.9.1 Give more specific consideration to what sort of regulatory changes will be necessary to:

(a) free up the contractual constraints, and perhaps other commercial constraints, that are impacting on this market;

(b) improve transparency and visibility of discounting, price boards (including for high octane products) and overall price;

9.9.2 consider more active regulatory intervention to create a (more) liquid wholesale market; and

9.9.3 consider options that that would allow:

(a) wholesaler and reseller participants to offer raw fuel to an available active/liquid market;

(b) reseller and retailer/dealer participants, including independents, to actively participate (not just as price takers) in an active more liquid wholesale market to acquire raw fuel;

(c) participants (including retailers/resellers buying fuel wholesale) to have options to determine:

(i) what proportion of fuel is sold/acquired on contract on fixed or price constrained rates, and what amount is acquired on an essentially live liquid market (e.g. whether some or all buy prices are fixed on longer term/hedged arrangements or acquired on a live market);

(ii) whether they buy their fuel from one or more wholesaler, or through a broker or some form of joint buying process (if those options emerge in the market), or through a wholesale market;

(d) some of the benefits of the existing Borrow and Loan ("B&L") system (or an equivalent system) to be extended to assist to create a more liquid/active engagement by retailers with the wholesale market.

9.9.4 Some specific possible options include:

(a) direct retailer/reseller access to an active liquid wholesale market in which wholesalers/resellers are competing on price to sell fuel (or at least raw fuel) - such a market could be put in place:

(i) by way of a regulated extension of the existing B&L arrangement and/or extended infrastructure sharing arrangements (essentially treating all importer / wholesaler / reseller inputs and outtakes as part of a closed fuel supply system); or

(ii) as a separate regulated wholesale market system; and

(b) regulation to give retailers a statutory right or option to renegotiate their buy price, or access other buy prices, in specified circumstances if their existing delivery arrangements or price are no longer competitive;

(c) some application or extension of the broader regulatory reforms that are happening in respect of unfair contract terms in the "B to b" space – MTA refers to its 28 February 2019 submission to MBIE[23], and the summary of its position that appears on page 6 of that submission; and

[23] MTA submission to MBIE on "Protecting Businesses from Unfair Commercial Practices" (available on request).

(d) regulatory structures (which could range from a regulatory authority to some sort of market body, or even some sort of ombudsman) and/or market/operating rules or guidelines.

10. MTA urges the Commission to take the bull by its horns and address all the identified issues at this point, rather than leave some to be dealt with at some other point through its regulatory role[24].

11. MTA believes the issues have been sufficiently clearly identified for the Commission's final report. The Commission could offer:

11.1 more expansive and comprehensive options to address the identified issues in the wholesale market; and

11.2 options that will ensure that participants in the retail sector too can be more than price takers but can at least have the option to more actively participate in the wholesale market in which they buy fuel.

Next steps?

12. We thank the Commission, again, for the opportunity to participate in this process.

13. Should you require any clarification in respect of any of these comments, please do not hesitate to get in touch.

MTA intends to have representatives present during the Consultation Conference, particularly elements on which MTA has made submissions or provided comment. However, if the Commission anticipates that MTA would be asked to address issues, we would appreciate some warning so that - if we perceive we could contribute usefully - we can ensure that we are in a position to do so.

[24] See the Draft Report, paragraph 8.25, where the Commission notes that the report has not considered the issues from that perspective but retains the ability to do so if any information collected in any context gives the Commission reason to do so.

Schedule 1 – table of responses to Draft Report questions (invited comments)

Paragraph	Page	Question	Response
Chapter 3: Outcomes in regional fuel markets			
3.36	70	High returns on new retail investment could occur in a competitive market if overall growth was strong, but we do not currently consider this is the case for retail fuel. On the contrary, retail capacity has been growing faster than total demand, so the average volume sold at each site is declining. We currently consider that **high returns on investment in new sites is likely to reflect high margins**. We invite comment on this view	There are in effect, two retail markets, one operated under a vertically integrated network by one of the major wholesale fuel suppliers and another being a more independent/dealer network where a wholesaler or reseller supplies a retailer. The data identified in the Draft Report relates to return on investment assessments on the viability of new vertically integrated sites, in the favourable conditions available to a vertically integrated entity retail operation. There is no evidence of independent retailer returns at those levels, and nothing to suggest independent retailers match modelled vertically integrated returns or that any growth in both markets is equal. Returns available to vertically integrated market participants, which may be captured at wholesale level, may simply not be available to independent retailer that are price takers at the end of the supply chain. Our view is that returns on investment in the independent / dealer business operating models are not only lower than the other side of the market, but risks may also be higher.
3.42	72	Values of q above unity are consistent with other analysis in Chapters 4 to 7 of this draft report of ineffective competition, and a range of barriers to entry, deterring new wholesale entry. We currently consider **that ineffective competition is the most plausible explanation for the estimated values of q above unity. This is enabling each of Chevron, Z Energy, and Gull (and potentially other firms) to earn excess profits**. We invite comment on this view.	See comments above.

Paragraph	Page	Question	Response
3.50	74	We currently consider that the **majors and these smaller firms are all benefitting from above competitive levels of retail fuel prices. The cost of this is borne by consumers**. We invite comment on this view.	MTA maintains that the Draft Report findings relate to fuel companies, not independent retailers, for that reason and for the reasons identified above. It appears that any sampling is not sufficient to extrapolate out to other smaller firm resellers, and it cannot be sufficient to extrapolate out to independent resellers operating an entirely different model. The Draft Report records at paragraph 3.43 that these findings relate to an assessment of BP, Chevron (until 2015), GAS, Gull, Mobil, NPD, Shell (until 2010), Waitomo and Z Energy (until 2010). It is then unclear in Figures 3.2 and 3.3 which companies are included in "All NZ fuel companies" and "Gull and smaller NZ fuel companies". If the definition of "smaller firm' is intended to capture the likes of Waitomo and NPD, and perhaps also entities like Allied, then looking at Fig 3.3 it is interesting to see the average ROACE drops dramatically for the 'all NZ fuel companies' suggesting that there is a clear distinction (lower ROACE) between the a) major fuel companies, b) Gull and smaller NZ fuel companies, and c) the independent retail sites.
3.76	84	Premium petrol prices are seldom displayed on price boards. In Chapter 7, we discuss **retail strategies** for premium petrol and why consumers may purchase it. These features **may be contributing to the growing price and margin differentials between regular and premium petrol.** We invite comment on these matters.	MTA agrees and supports the display of all fuel products to be posted on board.

Paragraph	Page	Question	Response
3.100	93	We continue to analyse the **impact of costs on retail prices**. However, our preliminary view is that these costs do not fully explain the differences we observe across locations. This is because there are some locations where the level of retail prices are inconsistent with what we expect if costs were the primary driver of prices. For example, Figure 3.15 below shows that within the Wellington region, retail prices in the Masterton District are lower than those in other territories. This is despite Masterton being more costly to deliver fuel to from Wellington terminals compared to other retail sites in Wellington city. One key difference between it and Wellington city sites is the presence of **Gull in Masterton**. We invite comment on this view.	MTA agrees. The presence of a low-cost fuel supplier in an area may have an impact on bringing pump price down as is clear in the Masterton area example with Gull. However, MTA considers that the Draft Report has correctly identified the broad range of factors that impact on whether, in what way, and to what extent a low-cost market entrant may impact on price in a particular local market. Anecdotally, MTA perceives that the recent entry by Waitomo in the Wellington area: (i) had an initial impact but only in a very limited area and has seen a nearby unmanned site better the Waitomo price by $0.001/litre over a sustained period; and (ii) has not impacted other areas, as service stations outside the 1-2km radius have retained their pump prices between 2-9 cpl greater than the Waitomo price. MTA has no reason to doubt that where competition is strong, vertically integrated retailers (and those for whom the wholesaler determines price) will compete on board prices but where competition is weak, retailers will compete using discounts and loyalty card schemes. But MTA maintains that a complex range of factors impact on whether and to what extent the arrival of new retailers will have an impact on price.

Paragraph	Page	Question	Response
3.112	97	At this point we think it is too early to tell whether there has been a significant improvement in board prices in the South Island. **Gull and Waitomo's planned entry in the South Island may provide downward pressure on board prices in some local markets in the South Island**. We invite comment on this view.	The entry of Gull and Waitomo into the South Island may bring prices down in some areas but: (i) price support within competitor retail operations will continue until competition is widespread in the SI; (ii) a range of other factors already identified by the Draft Report mean there are significant barriers to entry and constraints on competition; and (iii) there is no basis for confidence that Gull and Waitomo, and small numbers of other alternative resellers, would impact significantly on these markets without more extensive regulatory intervention.

Paragraph	Page	Question	Response
3.126	100	We are continuing to consider further systematic analysis of the **impact that the number, composition, and characteristics of new sites have on competition within local regions** and we invite comment on this issue.	This is difficult to assess, particularly in the context of a wholesale market that is not transparent or liquid. There are issues as to the extent to which vertically integrated supply chains are better supporting some retailers/models/sites that others, through cross subsidies or differential pricing. That is evident, for example, from the anecdotal evidence identified in the Draft Report of retailers seeing competitor unmanned sites sell retail fuel for less than another local retailer, under the same brand, can buy it. The Draft Report also identifies how vertically integrated suppliers are cross-subsidising where necessary to prop up competition in other reasons. If vertically integrated oligopoly suppliers are having a significant impact on competitive out-comes then that issue needs to be tackled first. Unmanned pay at the pump sites have lower operating costs (possibly in the range of $250k annually). While not within the scope of this study, the impact on a small community of providing employment opportunities through a full-service retail fuel outlet deserves some recognition. A low-cost unmanned retail fuel outlet may present an attractive consumer option, but it does not provide other community benefits as do full service manned outlets. Ultimately consumers will assess for themselves how they value those community and other benefits.

Paragraph	Page	Question	Response
3.135	102	The **impact of product differentiation on consumers will depend on the extent of competition between retail sites across the full spectrum of price and service levels**. For example, if there is only one unmanned site in a local market, it might exert only weak price pressure on nearby service stations. We invite comment on this issue which is discussed further in Chapter 7.	Product differentiation will also depend on what each consumer needs on a certain day, be it just lowest priced fuel or the ability to purchase a range of convenience goods, hire a trailer or use the toilet facilities. Having a consumer understand and accept the price differential can be challenging.
Chapter 4: Structural and regulatory conditions of entry and expansion			
4.27	113	We invite comment on our analysis of **conditions of entry and expansion at the refinery level** and our view that **entry at this level of the supply chain is unlikely.**	MTA agrees that entry at this level is unlikely due to current refinery capacity and the prohibitive cost of refinery upgrades to increase capacity. In that context, MTA welcomes the Draft Report's focus on access to infrastructure.
4.49	120	**Importer entry appears most feasible at ports able to serve large areas of demand, where there is greater chance of obtaining sufficient market share to support import cargoes of efficient size**. It appears to us that none of the challenges listed above are likely to be insurmountable, and they are faced by both the majors and other independent importers. We invite comment on our assessment of the potential for entry at the importer level.	In theory, entry into the market in NZ would appear feasible. But the uncertainty around access to a viable retail network with volumes that provide an acceptable return on any investment appears to present a significant barrier to entry. The issues identified in the Draft Report (with much of the retail market locked in to long term contracts and other market factors limiting access to existing or viable new sites) suggests that there are substantial challenges for alternative importers/wholesalers in terms of gaining access to bring fuel into the market and gaining outlets to which to sell fuel. Those issues too need to be addressed.

Paragraph	Page	Question	Response
4.113	133	We currently consider that entrants at the **importer level are likely to face a transport cost disadvantage when looking to supply smaller provincial areas, due to relatively high trucking costs**. Therefore, it is likely to be challenging for a new terminal operator to establish competitive nationwide fuel supply without obtaining lower cost distribution, for example, through participation in the borrow and loan system or wholesale supply from a major. We invite comment on our assessment of conditions of entry and expansion faced at the distribution level of the supply chain.	This is not an area of expertise held by MTA so it can only offer limited comment. But with an expanded B&L system along with new importers entering the market, there may be an opportunity for fuel transporters to improve their efficiencies by backloading product supplying a range of retail outlets. Obviously that will be more difficult for smaller new entrants working their way into the market. MTA understands that the biggest inefficiency in fuel transport occurs when a tanker has delivered its load and must return empty to the bulk terminal to collect a new load. If an expanded B&L system and additional storage facilities existed in advantageous locations, transport costs could be managed more efficiently. MTA has been advised that a more efficient fuel transport system along similar lines may be in place with the movement of fuel for Gull stations and some parts of the Waitomo network. But, to be clear, MTA sees this as *a* factor and not a magic bullet solution to all of the issues the Draft Report has identified.
Chapter 5: Infrastructure sharing arrangements			
5.6	142	In this chapter we describe our current view of the effect that the infrastructure sharing arrangements have on competition. We are continuing to consider **ways in which they might better contribute to the outcomes we would expect to see in a workably competitive market**. We invite comment on our assessment of these issues.	As above (B&L). In addition, MTA refers to and repeats its comments in paragraphs 9 of its covering letter to the Commission of today's date about opportunities to expand the B&L arrangements further in order to seek to offer a more active liquid wholesale market. That could extend to infrastructure sharing, at some level too. MTA perceives that could open up a wholesale raw fuel market in which resellers and retailers (particularly independents) are not just price takers but can participate actively (directly or otherwise) in seeking competitive prices from the wholesaler participants in the market. See paragraphs 9.9.3(d) and 9.9.4(a)(i) of the MTA covering letter of today's date

Paragraph	Page	Question	Response
5.30	147	First, duplication of terminal assets is avoided. This view is also held by industry participants. For instance, Mobil considers that the borrow and loan arrangements enable the majors to enhance efficiencies across the supply chain by avoiding unnecessary duplication of terminal capacity in relatively low volume and geographically dispersed markets. BP has expressed similar sentiments. Second, the sharing of the existing terminal infrastructure likely allows existing terminal capacity to be used more efficiently. However, as we discuss further, it appears that **terminal capacity is insufficient in some areas**. We invite further comment on our assessment of this issue.	Expanding the B&L system to optimise the current terminal capacity would require an industry agreed set of rules that ensures all parties contribute to the supply of volume that ensures product availability in all areas. But both of the factors identified suggest that extending infrastructure sharing would be beneficial, and that there is no reason to confine the benefit of those efficiencies to the majors and/or to fuel supply through the majors. Other markets, such as gas and electricity, share infrastructure for the benefit of the market as a whole.
5.37	148	We invite comment on our analysis of the **effect of the infrastructure sharing arrangements and the terms of access provided by the majors.** We are continuing to consider ways in which the barrier to entry that we currently identify could be mitigated.	Refer to our responses above in this section, and section 9 of MTA submission
5.48	150	We invite further comment on the **potential for access to the infrastructure sharing arrangements and methods by which this might most effectively and efficiently be facilitated**.	Refer to our responses above in this section, and section 9 of MTA submission
5.52	151	We invite further comment on the **potential for access to the infrastructure sharing arrangements and methods by which this might most effectively and efficiently be facilitated**.	Refer to our responses above in this section, and section 9 of MTA submission
5.89	161	We invite comments on our view of these likely effects on competition at the wholesale and retail levels.	Refer to our responses above in this section, and section 9 of MTA submission
5.100	162	We invite comments on the **means by which industry participants consider that pressure on storage capacity and supply could be relieved, as well as ways in which greater import competition could be facilitated**.	Refer to our responses above in this section, and section 9 of MTA submission

Paragraph	Page	Question	Response
5.114	166	It appears that it could be possible to design and implement a refinery allocation mechanism that enables a major to increase supply of domestically refined fuel over a shorter time period while retaining the planning benefits. We invite further comment on **whether such an alternative refinery mechanism is achievable**.	Refer to our responses above in this section, and section 9 of MTA submission
5.123	168	We consider that **the risk of the exchange of information through the Technical Committee unnecessarily affecting competition could be eliminated by restricting each major to verifying their own data for the capacity allocation process**. We invite further comment on whether this change would unduly affect the refinery's efficient operation.	Refer to our responses above in this section, and section 9 of MTA submission
5.125	168	We consider that there may be **low cost ways to reduce the current level of data sharing without significantly impacting the services that COLL provides** and we invite comment on the extent of data exchange currently occurring.	Refer to our responses above in this section, and section 9 of MTA submission
5.139	171	We invite further comment on the **role that information exchange plays in managing COLL's operations** and whether current information sharing arrangements could be modified without unduly affecting COLL's operations.	Refer to our responses above in this section, and section 9 of MTA submission
Chapter 6: Wholesale supply arrangements			
6.38	182	We seek feedback on the degree to which the importance of access to fuel card offers may affect decisions regarding wholesale supply by distributors, and the extent to which this may be harming wholesale competition.	**The acceptance of fuel cards by a retailer is a significant influencer in terms of decisions to align with a wholesaler and being brand specific, do tend to strengthen consumer buying behaviour toward the particular brand.**

Paragraph	Page	Question	Response
6.7	173	We are continuing to assess the effect of these relationships – both contractual and non-contractual – on competition in the wholesale and retail markets. We invite comment on our analysis and **the feasibility of less restrictive contractual arrangements that industry participants could adopt to stimulate competition in both the wholesale and retail markets.**	MTA considers that the contractual issues are significant and that addressing those issues is critical, and feasible. Releasing those contractual constraints will likely require some level of regulatory intervention, unless the culture of reseller/retailer constraint by contract is to be addressed by enforcement processes by reference to existing competition law principles. Addressing the non-contractual issues and constraints is also very important, but remaining non-contractual constraints should be more readily addressed once the contractual issues have been dealt with. See MTA letter paragraph 9
6.85	192	There are at least two instances of a distributor not being permitted to operate outside of an assigned territory without prior approval of the major. Such restrictions may have avoided hold-up problems for distributors when these commercial businesses were first divested by majors. They may have protected relationship-specific investments that distributors made at that time and encouraged expansion of distributors in particular territories. Exclusive territories are widely used in a range of different commercial contexts, and often have a procompetitive purpose and effect. Nevertheless, we have **not identified compelling justifications for the use of exclusive territories in current distribution networks** and we invite further comment on their use. We note that a major previously removed all geographic limitations on its distributors, to the benefit of competition.	On the other hand, MTA are aware of situations where the fuel supplier has set up a competing (unmanned) retail fuel outlet in proximity with a similarly branded existing site that has had a direct impact on the viability of the existing site. Again, this suggests a market controlled by a vertically integrated oligopoly, which can in at least some cases (and perhaps in many cases) impose exclusive territories on downstream providers (resellers or retailers) or introduce own brand (vertically integrated) local competitors, depending on which suits its purposes. These are difficult issues when a vertically integrated provider is both a wholesaler/supplier and a retailer in the same market(s). While there may be scope for legitimate collaborative activity that might allow market allocation it appears that the vertically integrated oligopoly is in some instances dictating when there will be geographical constraints downstream and when it will introduce its own competing entity; that appears to differ from actual collaborative activity with the price taker downstream entities. As per our previous suggestions, the restrictive and unbalanced fuel supply agreements need further investigation.

Paragraph	Page	Question	Response
6.91	193	We are concerned that NPU covenants create a barrier to retail competition. A key criterion for investment in retail fuel sites is finding a property with suitable characteristics at as low a cost as possible. By placing restrictive covenants on sites that have already proven to have many of the characteristics necessary, entry is potentially made costlier and more difficult. We seek feedback on whether the use of these covenants is likely to restrict competition and, if so, whether there are other less restrictive methods for achieving any efficiencies that these covenants may be generating.	MTA agrees that NPU covenants should not be used to restrict retail competition in an area. However, if there are particular environmental (ground water) contamination concerns then in some circumstances it may be appropriate to use the NPU covenant on the property title. MTA is not aware of any other less restrictive alternatives for addressing these issues.
6.110	198	We invite comment on the **methods of wholesale price determination** used throughout the industry and on our consideration of the use of cost-plus pricing formulas or published TGPs as an appropriate alternative approach.	There appears to be merit in establishing an open liquid wholesale fuel market. There also appears to be some merit in that involving publicly posted TGPs indicate prices. This would at least create a degree of transparency in terms of determining what the retail price at the pump should be. MTA refers to its submission in its letter of today's date, in paragraph 9 (9.1-9.9(4)(d), and to its initial submission dated 22 February 2019, Part III, at pages 14-17. as to further options to establish a more active liquid wholesale market.

Paragraph	Page	Question	Response
6.111	198	We consider that our **concerns about how the wholesale relationships are operating in the market** are reinforced by some of the outcomes we have observed in the wholesale market during the study. We invite comment on the observations we describe below	Having at least the opportunity to switch wholesale suppliers at shorter periods might to some extent impact on the power imbalance in the relationship between wholesaler and retailer. For some retailers, long term contracts are seen as security for their business; for others, they are seen as ties that restrict them from growing their business. MTA maintains that a more expansive market solution is required, to give retailers and resellers at least some control over how they engage with the wholesale market, and whether that involves some or all supply on longer term contracts and/or accessed through a more active/shorter term wholesale market. See MTA submission para 9.7.3 (c)
Chapter 7: The retail price and product offer			
7.23	208	We are continuing to consider **whether the relationship we observe between discounting and margins is best seen as a means to avoid direct price competition**. If so, discounting is a symptom of high margins. A similar hypothesis applies to service level differentiation. We invite comment on these issues. However, we note that we are not currently considering any measures to directly limit these activities. Rather, our focus is on promoting wholesale competition so as to increase retail price competition.	MTA agrees that discounting does mask the true price at the pump and can disadvantage some consumers who either don't have the necessary supermarket discount voucher or are members of a loyalty (discount) card scheme. MTA has been made aware that in some cases the level of discounting is born in part by the retailer and reduces their effective margin. The findings in the Draft Report include indications that retail markets served only by the majors are likely to see discounting rather than price board competition. That reinforces concerns that discounting is obfuscating price, and a poor substitute for competition.

Paragraph	Page	Question	Response
7.39	215	**Some fuel retailers are introducing new price signs that display post-discount prices along with minimum and maximum purchase terms**. These initiatives could make it easier for consumers to compare post-discount prices from competing retailers. However, they could also mislead some consumers if they choose a retail site based on the listed discounted price but do not have the necessary docket, loyalty programme membership or card to hand to receive the discount. We are currently considering whether consumers are likely to be able to make better comparisons if board prices showed undiscounted prices that are available to all consumers, or discounted prices that are only available to participants in the retailer's discount and loyalty programme. We invite comment on the **potential impacts for resellers and consumers of a change in practice of this nature**.	As above- This is going to be a tricky one to address as consumers have strong loyalty to some cards where they perceive they get more than discounted fuel (Airpoints, Fly Buys , Goody Card rewards etc). A recent consumer survey commissioned by MTA found that 51% of respondents were loyal to a particular brand and that in 77% of those cases the loyalty was tied to a brand card or discount voucher. In some respects this is a Fair Trading Act issue too. But ultimately transparency, and clarity, appear to be appropriate.
7.50	218	We recognise that it is **difficult to distinguish between discounting that is good for consumers and competition, and that which is harmfu**l. Discounting obviously does provide benefits to some consumers and we have not been able to compare those benefits with the costs of managing and participating in the programmes. However, those who do not participate pay higher prices and discounting has not been associated with reduced margins overall. We invite **further evidence and comment on the impact of the rise of discount and loyalty programmes on the competition outcomes produced in the retail fuel market** as we continue to assess this issue.	As above-

Paragraph	Page	Question	Response
7.60	221	We invite comment on our analysis of the potential effect that **product and service differentiation** may be having on retail competition.	Product and service differentiation across some of the major fuel brands have been developed over time in response to consumer demand - whether that demand is for more convenience goods or a fully comprehensive service. MTA presumes that it is not being suggested that fuel retailers should not develop their business to offer these additional goods and services but just lower their fuel prices. The increased development of unmanned pay at the pump facilities needs to be understood in terms of these consumer experiences and preferences. Some retailers will choose to offer lower priced fuel due to lower overheads and operating costs. But the unmanned service station experience does not suit all consumers. These outlets may not be accessible to those consumers who don't have credit cards or if they do, have a minimum balance on that card of around $150 for the bank to place a hold on while completing the fuel purchase. Similarly, if the consumer does need some help refuelling their car then the unmanned option may not suit them. Ultimately, consumers will decide what suits them. But MTA maintains that it is critical that the other issues that have been identified in the market are tackled, including ensuring that vertically integrated unmanned sites are not receiving preferential pricing, to ensure that market participants are on a level playing field when they engage with the wholesale market.

Paragraph	Page	Question	Response
7.63	221	Our current view is that uninformed consumers and the lack of board pricing for premium petrol may explain the trends we observe in margins on premium petrol. We seek comments on the distinctions drawn in the industry between premium and regular petrol, any evidence of the factors influencing consumer choice on the type of petrol they use and steps that could be taken to better inform consumers of the different characteristics and uses for premium and regular petrol.	MTA supports the display of all fuel product prices on the price board so that consumers can more easily compare prices before they pull on to the retail site.
Chapter 8: Options for recommendations			
8.5	233	We invite comment on the options we have set out, and also welcome suggestions of other options for recommendations we may make that could improve competition. Like the preliminary views expressed throughout the draft report, the options are subject to our further consultation process, further analysis and deliberation, and we may alter or remove any option when we finalise our recommendations.	MTA supports the focus on improvements made to increase competition at the wholesale level but maintain that any changes need to go further than just providing for better alternative importer/wholesaler access to the market and infrastructure, and ensuring that the issues regarding fuel supply contracts between wholesaler and retailer/reseller are addressed. Refer to paragraph 9 (9.1-9.9(4)(d)) of MTA's covering letter of today's date, and the pictogram it contains which identifies possible unintended consequences if only limited changes are made.
8.12	234	We invite comment on the options below, and on others that might better promote competition for the long-term benefit of consumers in New Zealand.	MTA supports the options identified by the Draft Report, focussed on contractual issues and supply side infrastructure access, but says the Commission should go further: see paragraph 9.9 of MTA's letter of today's date.

Paragraph	Page	Question	Response
8.19	235	We invite comment on the role that these **contractual provisions and the current access arrangements for shared infrastructure** have on competition and our current view of the impact that their modification or removal may have, including any impacts that we have not identified.	On the surface it may appear that competition would be improved if issues with the contractual provisions were addressed and access to shared infrastructure was opened up, but MTA maintains that those are important parts of a solution but that on their own they are unlikely to be sufficient and could have a perverse anticompetitive impact by effectively squeezing out independent retailers: see paragraph 9.6 of MTA's letter of today's date.
8.45	239	We invite comment on the likely effectiveness of each of these options in meeting the competition concerns that we have identified and welcome additional suggestions for measures that may improve competition in wholesale markets.	See paragraph 9 (9.1-9.9(4)(d)) of MTA's letter of today's date. MTA considers the response should go further, and has suggested some options. The establishment of a more competitive wholesale market where transparency of pricing is published (TGP), along with the introduction of an 'oil code' (which could draw on the code in place in Australia) could have some merit.

8.61	242	We invite comment on the likely effectiveness of each of these measures in meeting the competition concerns that we have identified and welcome additional suggestions for measures that may improve incentives for competition or diminish the potential to for coordination.	See paragraph 9 (9.1-9.9(4)(d)) of MTA's letter of today's date. Again, MTA considers the response should go further, and has suggested some options. MTA does not support the publishing of retail prices across the range of fuel suppliers as there are examples of where this has been introduced overseas only to have it used by retailers to align their process with other retailers. There are sufficient fuel price monitoring tools around that consumers already access when shopping around for the best price. Ultimately, the retail fuel market is a volume game where retailers seek to sell as much fuel as possible and a key factor in achieving this is to price the fuel to make it attractive to consumers.

Paragraph	Page	Question	Response
Attachment B: Our approach to assessing profitability			
B57	261	Each of these areas is discussed in turn below and in separate attachments to this report (refers to key steps in assessment of profitability). We invite comment and further evidence on each area.	Of the three steps, application of B56.1 and B56.2 use data that are not representative of retail fuel businesses, but rather vertically integrated oligopolies spanning wholesale and retail markets. Hence step B56.3 cannot yield representative indications of excessiveness of profit of firms in the retail market, and in particular of independent retail firms. On further evidence: MTA understands that retail fuel firms are unwilling, in part due to contractual confidentiality provisions from releasing firm level data, by which such firm level analysis could be undertaken. MTA maintains that there is sufficient evidence already of issues in the wholesale market, and that addressing those issues, including how retailers can better engage with the wholesale market, has to be the focus.
Attachment D: Measures of the profitability of firms in the New Zealand retail fuel sector			
D200	335	At this stage of our study, we have not undertaken this analysis (refers to potentially seeking to estimate an IRR for Gull over its business life from entry in 1998 until it was acquired by Caltex in 2017). We invite comments from submitters on whether we should try to undertake such an analysis for our final report (and whether other sources of information may be available).	MTA does not recommend such analysis. It considers that the information to hand already establishes that there are issues in terms of the wholesale fuel market, which in some respects are support by the findings regarding Gull's impact on the market. It considers that the focus should be on options to address the issues that have been identified already, to enable the market to move towards more workable competition, rather than a focus on an exceptional case of an integrated firm to seek to drill into its margins further.

Paragraph	Page	Question	Response
Attachment F: Econometric and empirical analysis			
F149	416	We invite comment on matters that might be relevant to the further analysis we intend to carry out.	There are different price setting mechanisms for the different types of fuel retailers, depending in part on the level of control by a major of the price or retail margin. Hence, further analysis would usefully account for these systematic influences before making broad inferences about price setting responses.

NATIONAL CONTACT DETAILS

Physical address
Level 12,
Nokia House
13–27 Manners
Street Te Aro,
Wellington 6011

Postal address
PO Box 9244
Marion Square
Wellington 6141

Phone
04 385 8859

Members toll free phone
0800 001 144

Mediation Line
0508 682 633

Fax
0800 000 695

Email
mta@mta.org.nz

Website
mta.org.nz