

New Brunswick Energy & Utilities Board
IN THE MATTER OF a review of the maximum margins, maximum
delivery costs and the 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)

Held at the Delta Hotel, Fredericton, N.B., on October 6th,
2008

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2 delivery costs and the maximum full service charge conducted
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7th 2008

5
BEFORE: Raymond Gorman, Q.C. - Chairman
6 Cyril Johnston - Vice-Chairman
Edward McLean - Member
7 Robert Radford - Member
Steve Toner - Member

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N.B. Energy and Utilities Board - Counsel - Ms. Ellen Desmond
9 - Staff - Doug Goss
- Dave Keenan
10 - Dave Young

11 Secretary of the Board - Ms. Lorraine Légère
12

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14 CHAIRMAN: Good morning everyone. Today's hearing of the
15 EUB is being conducted in order to review the maximum
16 margins, maximum delivery costs and the maximum full
17 service charge currently authorized under the Petroleum
18 Products Pricing Act to ensure that they are justified.
19 This review is being conducted under Section 14 of the
20 PPPA.

21 Today's Panel consists of Robert Radford, Edward
22 McLean, Steve Toner, Cyril Johnston and myself, Raymond
23 Gorman.

24 You may have noticed when you come in that
25 simultaneous translation devices are available throughout

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the proceedings. These listening devices are available at the back of the room in order to allow everyone to hear the presentation in either English or French.

Accordingly, I would encourage everyone present today to participate in the official language of their choice.

At this time I am going to ask the Vice-Chair, Cyril Johnston to deliver the same message in the other official language.

VICE-CHAIRMAN: Bonjour tout l'monde et eh bienvenue à cette audience de la Commission de L'Énergie et des Services Publics N.-B.

Eh, cette audience est dans l'affaire d'une révision des marges bénéficiaires maximales des placements des coûts de livraisons et des plafonds des frais de services complets.

Eh, selon la loi sur la fixation des prix des produits pétroliers. Comme le président vient de dire en anglais, nous avons la traduction simultanée ici aujourd'hui et ça va continuer durant toute l'audience. Alors, eh, nous sommes eh prêts eh à attendre des soumissions dans les deux langues officielles et nous vous encourageons de, de participer dans la langue de votre choix.

Nous prévoyons avoir deux témoins, Monsieur Gardner et Monsieur Irvine. Ces deux témoins ont présenté des

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2 rapports qui sont disponibles en anglais et en français
3 sur notre site web et peut-être ici dans la salle, je
4 l'sais pas.

5 Eh, ces témoins vont témoigner dans la langue anglaise
6 mais vous avez certainement la droit, le droit de, de
7 poser vos questions dans la langue officielle de votre
8 choix. Merci.

9 CHAIRMAN: At this time I'm going to take the appearances.

10 And I believe we have 24 Intervenors who have pre-
11 registered. So I'm going to go through the list of
12 Intervenors and ask the parties to identify themselves as
13 to who they are as representing each party.

14 And as well perhaps if you could identify for me where
15 you are sitting. Some of the people that are
16 participating today may not be people that have appeared
17 before the Board in the past. So I may not recognize you.
18 So when it is your turn, if you could stick your hand up
19 so the court reporter and I could locate you.

20 And also to benefit the court reporter I would ask
21 that you spell your full name when you identify yourself.
22 So these are listed alphabetically. These are the
23 Intervenors who have pre-registered.

24 Accommodation Victoria Enr. et Les Immeubles ROBO.
25 Anybody present?

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And could I ask you to say your name and spell it please?

MR. BOSSE: Benoit Bossé.

VICE-CHAIRMAN: Oui, juste à côté-là.

MR. BOSSE : Mon nom est Benoit Bossé. Je représente eh Accommodation Victoria Enr. Et Les Immeubles ROBO Ltée. d'Edmundston, Nouveau-Brunswick. My name is Benoit Bossé. I represent Accommodation Victoria Enr. et Les Immeubles ROBO Ltee., Edmundston, New Brunswick.

CHAIRMAN: Okay. And I'm going to check with each of the Intervenors at this point as well as to whether or not you will be cross examining the witnesses or making presentation or both.

MR. BOSSE: À ce stage ici, je n'suis pas prêts à faire une présentation et j'suis pas familier tellement à la façon que vous allez procéder donc eh j'aimerais me familiariser un peu plus avant de faire un « inaudible » de faire la présentation.

CHAIRMAN: Thank you. Canadian Federation of Independent Business? Nobody here.

Okay. I do believe they filed a written submission. It was my belief that they would probably be here. So we will see. Perhaps they may show up later.

Canadian Independent Petroleum Marketers Association?

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MS. SAVAGE: My name is Jane Savage, President of Canadian
Independent Petroleum Marketers Association. And I will
be making a presentation here today.

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CHAIRMAN: And will you be doing any cross examining?

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MS. SAVAGE: No.

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CHAIRMAN: Thank you.

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MS. SAVAGE: Thank you.

9

CHAIRMAN: Canadian Oil Heat Association and Canadian Oil
Heat Association/Clark Oil?

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11

MR. GOULD: William Gould, Canadian Oil Heat Association.

12

And I would like to make a short presentation.

13

CHAIRMAN: Thank you, Mr. Gould.

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MR. CLARK: Peter Clark, Canadian Oil Heat Association. And
I will be making a presentation.

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16

CHAIRMAN: Thank you. Cooke's Quik Mart? Nobody here.
Co-op Atlantic?

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MR. ZED: Yes, Mr. Chairman. Peter Zed representing Co-op
Atlantic. And I'm joined by Stephen Davies, V-P Real
Estate and Energy Division and Mr. Daniel Chaisson, the
Director of Wholesale and Development.

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CHAIRMAN: Mr. Zed, will you be both cross examining and
making a presentation?

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MR. ZED: Yes.

25

CHAIRMAN: Thank you. Department of Energy?

1 MR. P. ERVIN: Patrick Ervin of the Department of Energy.

2 With me are Alain Bilodeau with the Department of Energy
3 and Michael Ervin, President of M.J. Ervin & Associates.

4 CHAIRMAN: And Mr. Ervin, you will be both cross examining
5 and making a presentation?
6

7 MR. P. ERVIN: We would like to reserve that option, yes,
8 Mr. Chairman.

9 CHAIRMAN: Thank you. Everett's Car Care? Nobody here.

10 Oh, sorry. I guess if we had a few more microphones it
11 might be easier. But I guess we will have to share.

12 MR. M. EVERETT: Mr. Matthew Everett. Just to observe.

13 CHAIRMAN: Mr. Everett, will you be cross examining or
14 making a presentation or both?

15 MR. M. EVERETT: No.

16 CHAIRMAN: You will be making neither? You don't wish to
17 make a presentation?

18 MR. M. EVERETT: No.

19 CHAIRMAN: Thank you. Gabriel Hache Ltee.? Anybody here
20 from Gabriel Hache Ltee.? Global Fuels Inc.?

21 MR. MADDOCK: Gary Maddock, Vice-president, Global Fuels
22 Inc. and Guy Gaudet, Territory Manager for Global Fuels
23 Inc. will neither be making a presentation or cross
24 examining.

25 CHAIRMAN: Thank you, Mr. Maddock. Greenwood Enterprises

1
2 Ltd.? Nobody here from Greenwood Enterprises Ltd.

3 Hunter's One Stop? No one here?

4 MR. HUNTER: Eldon Hunter from Hunter's One Stop. I will
5 making a brief presentation.

6 CHAIRMAN: Thank you, Mr. Hunter. Irving Oil Marketing
7 Limited?

8 MR. HOYT: Len Hoyt for Irving Oil Marketing Limited. I'm
9 joined by Matt Holland who is the Petroleum Manager for
10 Irving Oil Marketing Limited.

11 CHAIRMAN: Mr. Hoyt, will you be both cross examining and
12 making a presentation?

13 MR. HOYT: Yes, we will.

14 CHAIRMAN: Thank you. Magnetic Hill Esso? Nobody here from
15 Magnetic Hill Esso? Michaud Petroleum Inc.?

16 MR. MICHAUD: Hermel Michaud, Michaud Petroleum. I will
17 just appear for observation.

18 CHAIRMAN: Thank you, Mr. Michaud. Murray's Esso?

19 MR. GRANT: You can probably hear me.

20 CHAIRMAN: Well, I think for purposes of the court reporter
21 we would ask you to speak into the microphone anyway.

22 MR. GRANT: Not a problem. Calvin Grant from Murray's Esso.
23 We will be here for observation but would like to reserve
24 the right to cross examine.

25 CHAIRMAN: Thank you, Mr. Grant. Notre-Dame Express? No

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2 one here from Notre-Dame Express? Richard Service Station
3 and Richibucto Corner Store Ltd.?

4 MR. G. RICHARD: Gabriel Richard, Richard Service Station
5 and Richibucto Corner Store. We will have a little
6 presentation to be done.

7 CHAIRMAN: Thank you, Mr. Richard. Salisbury Road Gas and
8 Convenience?

9 MR. NICHOLSON: My name is Ted Nicholson. I'm here
10 representing some independent dealers from Moncton. I
11 will be here as an observer. But I would reserve the
12 right to cross examine.

13 CHAIRMAN: Thank you, Mr. Nicholson. Scholten's Group?

14 MR. C. SCHOLTEN: I'm Chris Scholten representing the
15 Scholten's Group. And I'm here joined with Jerry Scholten
16 as well. We will not be making a presentation. But we
17 reserve the right to cross examine.

18 CHAIRMAN: Thank you, Mr. Scholten. Ultramar Ltd.?

19 MR. MAYNARD: I'm Warren Maynard from Ultramar Ltd. We will
20 not be making a presentation. However, we would like to
21 reserve the right to cross examine.

22 CHAIRMAN: Thank you, Mr. Maynard. Voice of Real Poverty
23 Inc. I understand from Board Staff that Bethany Thorne-
24 Dykstra has contacted Board Staff to indicate that she
25 will be in attendance at a later time today or tomorrow.

1
2 Westmount Esso & Service Center 1992 Ltd.?

3 MR. ROY: My name is Ronald Roy. I'm representing Westmount
4 Esso. And I'm just here to observe.

5 CHAIRMAN: Thank you, Mr. Roy. XTR Energy Company Limited?

6 MR. WOOTTON: Ken Wootton of XTR Energy Company Limited.

7 Will not be making a presentation but would like to cross
8 examine.

9 CHAIRMAN: Thank you, Mr. Wootton. New Brunswick Energy and
10 Utilities Board?

11 MS. DESMOND: Ellen Desmond, Mr. Chair and from Board Staff,
12 Douglas Goss, David Keenan and Dave Young.

13 CHAIRMAN: Thank you, Ms. Desmond.

14 I appreciate that many of the persons present today
15 have never appeared before the EUB. And therefore before
16 hearing from witnesses I'm going to take a moment to
17 explain the purpose of today's hearing and the procedure
18 that we are going to follow.

19 The New Brunswick Energy and Utilities Board is the
20 body responsible for setting maximum wholesale and retail
21 prices for heating and motor fuels within the province of
22 New Brunswick.

23 The Board has initiated a review of the maximum
24 margins, maximum delivery costs and maximum full service
25 charges currently authorized under the PPPA to ensure that

1
2 they are justified. The PPPA gives that jurisdiction to
3 the Board under Section 14.

4 The Energy and Utilities Board Act specifically gives
5 the Board the ability to engage the services of experts or
6 other persons to advise it in any matter that the Board
7 considers appropriate.

8 To assist with this review the Board engaged the
9 services of Gardner Pinfold Consulting Economists Limited
10 to provide the Board with an analysis of the New Brunswick
11 petroleum market since the setting of the margins,
12 delivery costs and full service charges in 2006.

13 In particular the review was to provide the Board with
14 the basis for determining whether the current amounts for
15 the margins and costs were justified, and if not if they
16 should be adjusted.

17 The objectives of this engagement were to carry out an
18 analysis of the heating and motor fuel wholesale and
19 retail margins, maximum delivery costs and the full
20 service charge for motor fuel, to produce a report drawing
21 on industry data to document whether the amounts are
22 justified or not with reasons and to provide guidance to
23 the Board on the justification of various factors as set
24 out in the Act.

25 Gardner Pinfold has filed its report to the Board.

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2 And the report has been published in both official
3 languages on the Board website. The report represents the
4 recommendations of the consultant and not the opinions of
5 the Board. It is subject to cross examination and
6 argument by the parties and is not intended to establish
7 the margins referred to under the Act. That is the
8 function of this Board throughout the hearing process.

9 With respect to procedure the Board outlined the
10 process to be used in connection with this review which
11 provided an opportunity to registered participants to
12 submit written questions, provide evidence and/or provide
13 written submissions.

14 The only party to file evidence with the Board was the
15 Department of Energy which filed a report prepared by
16 M.J. Ervin & Associates. All parties were also given an
17 opportunity to submit questions to the author of that
18 report.

19 In addition to the above, Intervenors were given a
20 choice to submit their remarks in writing prior to the
21 hearing or to participate in the hearing occurring here in
22 Fredericton over the next three days.

23 For those who have indicated that they wish to
24 participate as full participants in the hearing, the
25 following procedure is going to apply.

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2 First, Michael Gardner of Gardner Pinfold will be made
3 available for cross examination with respect to the report
4 that he filed with the Board. The parties will proceed in
5 alphabetical order with cross examination with the
6 exception of Board Counsel who will proceed last in order
7 to complete the record.

8 Michael Ervin of M.J. Ervin & Associates will be
9 subject to direct examination by the party that filed the
10 report, namely the Department of Energy. Following direct
11 examination he will be made available for cross
12 examination. And the same order of proceeding will apply.

13 Following the evidentiary portion of the hearing, each
14 of the parties will be given an opportunity to make a
15 closing argument to the Board whether or not they
16 participated in the oral questioning of the witnesses.
17 The same order of proceeding will be used with the
18 exception of Board Counsel who will not make submissions
19 as to what the outcome of these proceedings should be.

20 Does anybody have any questions or issues with respect
21 to the process or procedure that we are going to follow
22 today?

23 I think at this time then we can mark some exhibits.
24 There are a number of documents that have been prefiled.
25 And we are going to mark them as exhibits at this time.

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The first document was the publication of the Notice and Hearing. And that is going to become exhibit number 1.

The next document was the report prepared by Gardner Pinfold entitled "Review of Regulated Fuel Margins, Costs and Full Service Charges in New Brunswick" dated August 22nd 2008. And that will become exhibit number 2.

Thirdly, we have questions posed to Gardner Pinfold dated September 3rd 2008 in connection with the August 22nd 2008 report from the following participants. Number 1) Co-op Atlantic; 2) New Brunswick Department of Energy; 3) Irving Oil Marketing Limited; 4) the New Brunswick Energy and Utilities Board and 5) Scholten's Convenience Stores. Those questions will become exhibit number 3.

The next exhibit are the responses of Gardner Pinfold dated September the 10th 2008 including the statement of W. Stephen Cannon to questions from Co-op Atlantic, the New Brunswick Department of Energy, Irving Oil Marketing Limited, the New Brunswick Energy and Utilities Board and Scholten's Convenience Stores. And that document will become exhibit number 4.

The next document is a report from Gardner Pinfold entitled "Review of Regulated Fuel Margins, Costs and Full Service Charges in New Brunswick, Addendum re Propane"

1
2 dated September 10th 2008. And that will be marked as
3 exhibit number 5.

4 The next document is M.J. Ervin & Associates Project
5 Report dated September the 15th 2008 submitted under cover
6 dated September 17th 2008 from Alain Bilodeau of
7 N.B. Department of Energy. That will be exhibit number 6.

8 And the next document are the responses of M. J. Ervin
9 & Associates to questions from the NBEUB submitted under
10 cover of e-mail dated September 29th 2008 from Alain
11 Bilodeau of the New Brunswick Department of Energy. And
12 that will become exhibit number 7.

13 Those are all of the documents that the Board has to
14 mark as exhibits at this time. Does anybody have any
15 other documents that they believe should be marked?

16 Ms. Desmond, does that complete the record as far as
17 you are concerned?

18 MS. DESMOND: Yes, Mr. Chair.

19 CHAIRMAN: Thank you. Does anybody have any preliminary
20 matters or questions or issues to raise prior to us
21 bringing Mr. Gardner forward for cross examination?

22 MR. P. ERVIN: Just one item, Mr. Chairman. Mr. Ervin is
23 here for today and tomorrow. I discussed this with Board
24 Staff previously. And he has a flight out on Wednesday
25 morning from Saint John.

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2 So I'm hopeful that we can get his portion completed
3 by today or tomorrow and just wanted to make that clear at
4 the outset.

5 CHAIRMAN: Okay. Well one way or another we will do our
6 best to accommodate that request, Mr. Ervin.

7 All right. My understanding is that Mr. Gardner is
8 not present yet but will be here shortly. So we are going
9 to take a short adjournment. And I would expect that we
10 should be able to reconvene about 10:30. Ms. Desmond,
11 does that sound about right?

12 MS. DESMOND: Yes.

13 CHAIRMAN: Okay. So we will take an adjournment till 10:30.

14 (Recess - 10:00 a.m. - 10:30 a.m.)

15 CHAIRMAN: Good morning, Mr. Gardner.

16 MR. GARDNER: Good morning.

17 CHAIRMAN: We now have Mr. Gardner available for cross
18 examination by the parties. But prior to cross
19 examination we will ask Mr. Gardner to identify himself
20 for the record. And if you wish to make any introductory
21 comments, this would be the time to do that.

22 And Ms. Desmond, perhaps you might come forward and we
23 will swear him in.

24 (Michael Gardner sworn)

25 CHAIRMAN: Mr. Gardner has been sworn. And so if you have

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2 an opening statement or anything of that nature, Mr.
3 Gardner, this would be the time.

4 MR. GARDNER: Thank you. First I would like to apologize
5 for arriving late. I had an opportunity to see some of
6 the New Brunswick countryside. But it was inadvertent.
7 So I apologize for the time that I have taken. And I will
8 try to compensate by keeping my answers short.

9 Opening remarks, in brief the gasoline marketing end
10 of the industry in Canada generally has faced rising
11 costs, as has much of the rest of the economy over the
12 past few years.

13 The effect in the case of the marketing branch of
14 petroleums has been to reduce the net margins available
15 through the industry with which to operate. And as a
16 consequence this has tended to undermine the viability of
17 this sector.

18 So the report examines a number of these cost factors
19 and concludes that some adjustments to the margins and
20 costs is justified. And these are summarized. I won't go
21 into that detail at this point.

22 In reaching this conclusion or these conclusions we
23 relied on a variety of sources of information. We had
24 hoped to base our analysis and conclusions on industry
25 data. We had engaged in extensive interviews with the

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2 major integrated refiner marketers, the wholesaling
3 companies, with smaller wholesalers, resellers of both
4 gasoline and heating oil, heating oil retailers. And as
5 well we surveyed over 400 retail gasoline outlets in the
6 province and conducted interviews with just under 30 of
7 those to round out our information base.

8 Regrettably, the quality of the information that we
9 obtained didn't allow us to generate results based
10 exclusively on industry data. The results I think, and it
11 is fair to say, would not I guess pass a test of
12 statistical significance.

13 So we have relied or we tended to rely more heavily on
14 published information and some of the data that was
15 provided by the industry, which is admittedly in an
16 anecdotal form.

17 The legislation asks I guess the Board to look at
18 several factors, several relevant factors including
19 transportation, capital costs, volumes, inventory
20 turnover, levies and other factors.

21 And the other factors that the Board is invited to
22 examine are not expressed in any detail. So it was left
23 up to the consultant in this case to determine or try to
24 determine what those other factors, those other relevant
25 factors may have been.

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2 And we did examine those and concluded that there were
3 a couple of factors that were certainly key to the
4 industry, again based largely on information provided by
5 the industry. And these formed the basis for the
6 adjustments that are laid out in the report.

7 I would conclude by observing that in the unregulated
8 parts of Canada prices and the marketing margin has
9 increased relative to those in New Brunswick and in the
10 other regulated provinces in Atlantic Canada.

11 So the adjustments that are laid out in the report are
12 not simply based on the information that has been provided
13 to us by the industry and published information. But also
14 looking at the industry elsewhere in Canada we see that
15 prices have risen relative to New Brunswick and also that
16 the marketing margin has risen relative to New Brunswick,
17 which would support the argument that a combination of
18 competitive factors and cost drivers have been at work
19 elsewhere to the benefit of the industry elsewhere.

20 So with those opening remarks I would invite
21 questions.

22 CHAIRMAN: Thank you, Mr. Gardner. And from my initial
23 taking of appearances this morning I understood perhaps
24 the first person that had an interest in asking questions
25 or doing cross examination is Mr. Zed on behalf of Co-op

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Atlantic.

Anybody who I guess appeared before Co-op Atlantic alphabetically, am I correct none of you wish to cross examine?

Okay. Mr. Zed, proceed.

MR. ZED: Thank you, Mr. Chairman.

CROSS EXAMINATION BY MR. ZED:

Q.1 - Welcome to Saint John North, Mr. Gardner. Mr. Gardner, if you would just please -- I'm going to refer for some time to your report. So if you could just turn to the first page.

The third paragraph from the bottom you talk about the challenge facing the regulator is to design a pricing model that balances the interests of consumers, retailers and wholesalers.

A. Yes.

Q.2 - Would you agree with me that the current regulation under which you undertook your report really balances the interest of the consumer moreso than the interests of business?

It is more directed to effect a favorable result for the consumer moreso than it is directed to a favorable result for business?

A. I'm not sure if I guess grasp the scope of the

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2 question. I think the legislation -- the mandate of the
3 Board is it attempts to balance the interests of
4 consumers, at least as I read the Act, by suggesting that
5 the margins and costs should, well, balance the interests
6 of consumers, that they not pay too much, but at the same
7 time that supply of petroleum products to consumers not be
8 constrained.

9 So there is an attempt to balance there. But the
10 difficulty is that finding a test or a standard which
11 balances those interests is the more difficult one.

12 Q.3 - The following paragraph you talk about -- the operative
13 word here is "average". I mean, we could go through and
14 will go through your report in more detail. But this
15 concept of averaging keeps coming up.

16 And then you make a statement individual wholesalers
17 and retailers could become either better or worse off
18 depending on their starting position compared with the
19 margins allowed under regulation.

20 Isn't this just a tacit admission that with respect to
21 averaging there is somebody above and somebody below the
22 line?

23 A. Yes.

24 Q.4 - And because you are doing averaging -- and I think it is
25 fair to say we all agree that oil prices, petroleum prices

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have risen dramatically in the last few years --

A. Yes.

Q.5 - -- the time period of your report?

A. Yes.

Q.6 - And that if you are experiencing averaging you are always in a period of catch-up?

A. Given the way the regulation is structured in particular, yes, it is an attempt to catch up to the previous week, the previous two weeks as the case may be.

Q.7 - So the wholesalers and retailers are the ones bearing the burden of that catch-up?

A. That's correct.

Q.8 - And in a rising market the other factor that would come into play are costs? I think you have indicated that costs have been rising --

A. Yes.

Q.9 - -- in that same period?

A. Yes.

Q.10 - So it is fair to say that for the past two-year period the burden of the system has fallen on the business side as opposed to consumer side?

A. Yes. That would be true.

Q.11 - Okay. If we go to page 2 you talk about your four key price points. And the first of your price points is

1
2 benchmark price. And you refer to the New York Harbour
3 price as being a commodity price with the greatest direct
4 influence on fuel prices in New Brunswick.

5 Now what about Saint John Rack? Where does that come
6 into play? And how does it relate to New York Harbour in
7 terms of its effect on what portion of the province and
8 what type of business?

9 A. Well, the New York Harbour price essentially is what
10 in a regulated regime is used as the benchmark. And it is
11 used as the benchmark for a good reason. And that is
12 because it is a substantial market in eastern Canada, the
13 largest -- well, probably the largest market, petroleum
14 market in North America. It is transparent. It is highly
15 competitive. And so it serves as a good guide to what is
16 going on in the petroleum market, not just in North
17 America but globally.

18 The Saint John Rack price is a price that follows the
19 New York Harbour movements very, very closely. I mean, it
20 historically is in roughly the range of three cents over
21 New York Harbour. And it serves as a guide for smaller
22 wholesalers and resellers in New Brunswick who are buying
23 from major refiner marketers.

24 It serves as a guide price. It is a posted price in
25 the same way that a mortgage rate might be posted by a

1
2 bank. You can come in and negotiate a better deal if you
3 have the -- I guess the capacity or the ability to do
4 that.

5 So the New York Harbour price serves as a reference
6 price for major traders, the major marketer refiners. The
7 Saint John Rack price serves as a guide for smaller
8 wholesalers and retailers who are buying in the province
9 and serving retail customers.

10 Q.12 - And to the extent that that price is higher, which you
11 have indicated it is, in the range of about three cents --

12 A. Right.

13 Q.13 - -- then the cost of doing business for those people who
14 are bound to buy by the Saint John Rack price is three
15 cents higher?

16 A. That's correct.

17 Q.14 - Thank you. Now the next page 3. And first paragraph,
18 prices are adjusted every week.

19 And my question really -- and I think you may have
20 already answered it. But in a volatile market isn't it
21 true that the average may never be the right number? It
22 may never reflect the true price?

23 A. I'm sorry, the average?

24 Q.15 - The average cost?

25 A. You mean the average that the Board takes into

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consideration?

Q.16 - If we do an average on a weekly basis which is the process --

A. Yes.

Q.17 - -- and the price is changing on a daily basis --

A. Yes.

Q.18 - -- isn't it true that that average price may never be the same as the actual price?

A. It would be coincidence if it were. But in a steadily rising market the regulated price is always going to be trying to catch up because it is based on an average of the previous week, and conversely in a declining market.

Q.19 - And so that is just a catch-up that we are playing that you refer to in your opening --

A. That's right. Yes.

Q.20 - -- responding to the first question? Thank you.

I would like you to turn to page 5. And we are talking about then industry structure. And I may just have a couple of general questions.

In general would you categorize the New Brunswick market as competitive? And perhaps, you know, compare it to other jurisdictions. I mean, is it competitive compared to Nova Scotia? Is it competitive compared to Ontario?

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2 A. Yes. It is competitive. It is competitive compared
3 with markets generally across the country. If one
4 considers the structure of the industry as an indicator of
5 competitiveness, there are a number of competitors at the
6 major wholesale integrated refiner level, five or six, 20,
7 30, 40 smaller wholesalers in both motor oil and motor
8 gasoline and heating oil, and several hundred retailers.

9 So taken collectively there is a competitive structure
10 at work there.

11 Q.21 - And basic economic theory is that if there is a
12 competitive market then prices will not rise arbitrarily?

13 A. Prices wouldn't rise arbitrarily. They would
14 presumably respond to supply and demand conditions in the
15 market, yes.

16 Q.22 - And I guess really this is just kind of a very general
17 question. But without regulation would prices necessarily
18 be any different than they are today?

19 A. Well, prices may be lower than they are today. They
20 could be higher than they are today. But if we look at
21 what has happened in the rest of Canada in other -- in
22 nonregulated markets, prices in western Canada for example
23 are 2, 3, 4 cents on average higher than they were prior
24 to -- well, prior to July 1st 2006. Prices in other parts
25 of the country and margins in other parts of the country

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2 have risen relative to the Atlantic Provinces and New
3 Brunswick in particular.

4 So the competitive circumstances are responsive to
5 global conditions. But they are also responsive to cost
6 factors as well. And we can see that I think in the way
7 prices have moved elsewhere in the country.

8 Q.23 - So -- and barring any sort of weekly price wars and
9 that kind of thing, over time businesses have to collect
10 their costs before profit, and that if businesses don't
11 collect enough to cover their costs, that businesses will
12 no longer be, I mean, over time in the long run. Is that
13 a fair statement?

14 A. Well, that is a fair statement. And we have -- I
15 think we have seen that throughout Canada, throughout the
16 Atlantic Provinces in the decline and the number of both
17 wholesalers and retailers. It's a fact of life that costs
18 are rising and margins have been declining and business is
19 no longer viable.

20 Q.24 - I'm just going to ask you a question from page 8. And
21 this -- you may not be able to answer this. But your
22 third paragraph you talk about 20 percent of New Brunswick
23 homes use oil for heating.

24 And I guess -- how does that compare to other
25 jurisdictions, in the Maritimes in particular?

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2 A. It is relatively low by comparison. So for example
3 Nova Scotia would be in the order of 70 percent heating
4 with oil. And Newfoundland somewhere between but closer
5 to the 70 percent mark.

6 Q.25 - Do you know why that is?

7 A. Well, in large measure because alternative heating
8 sources are relatively attractive in price compared with
9 other jurisdictions.

10 So for example electricity in New Brunswick is
11 competitive whereas in Nova Scotia it isn't. Natural gas
12 is competitive and becoming increasingly so.

13 Q.26 - Do you see any problem in dealing with or administering
14 a regulation that would recognize the Saint John Rack
15 price for retailers or resellers as opposed to New York
16 Harbour, in other words a split calculation? Isn't it
17 just more paperwork?

18 A. Well, I'm not sure it's more paperwork. Ultimately
19 the end point is going to be the consumer who is buying
20 the petroleum product whether it is gasoline or heating
21 oil. So in a sense it doesn't make a great deal of
22 difference where you start.

23 Ultimately the market is going to determine what the
24 consumer, the price consumer faces. So if you start with
25 New York Harbour, a number of larger companies trade at

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2 that price point or that reference point. It is a more
3 challenging environment for smaller wholesalers who are
4 buying at the rack or near the rack price.

5 But whether you use one or the other, yes, it is a
6 more complex calculation. At times -- even though there
7 is an average of three cents, at times the spread goes to
8 two cents or to four or five cents. And so the margin can
9 be squeezed.

10 But presumably in setting the original margins the
11 regulator would have been sensitive to those swings and
12 set it at an average that recognized I guess the
13 complexity of the market.

14 If that is not the case then trading at New York
15 Harbour would tend to benefit those in the industry who
16 buy and sell at that and to some extent compromise those
17 who are buying at the rack, because they are all selling
18 into the same market and realizing the same selling price.

19 So, yes, it is a more complex calculation. The end
20 point would not be any different. You have got a single
21 market price simply because you are selling with a lower
22 margin or lower -- a higher buying point or acquisition
23 point doesn't mean you would be able to sell at a higher
24 price.

25 Q.27 - But it would afford those dealers an opportunity to

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2 raise the price if the market permitted in order to cover
3 their increased costs?

4 A. Well, if the market permitted -- if by that you mean
5 that currently they are trading below the maximum, then
6 sure there would be room to move, if -- you know, again it
7 is not so much dependent on where they start as where they
8 end at the retail end.

9 Q.28 - Thank you. If you would turn to page 11 please, the
10 last paragraph before figure 2.4. It talks about the
11 average spread between New York Harbour spot price and the
12 Saint John pump price excluding tax was fairly stable, in
13 the 11 to 12 cent range between January -- now -- and then
14 it says, the average spread presumably form the basis for
15 the regulated margin of 11 cents plus transportation.

16 So 11 cents was chosen even though the range was 11 to
17 12 cents. Do you have any idea of what that extra one
18 cent would represent the terms of profit or revenue for
19 the average dealer?

20 A. Well, one cent on five cents is 20 percent. But again
21 the reason why this is framed in fairly general terms is
22 because it's not very clear to the industry on what basis
23 the original margin was set.

24 The response to the question how was it set was well,
25 it seems to have been set based on the experience during

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2 the two or so years prior to, and coupled with a look at
3 what was going on in the other Maritime Provinces as a
4 guide for what might be an acceptable margin.

5 Q.29 - But you would agree, according to your paragraph, that
6 it was set at the low end of the range?

7 A. Well, it was set at low end of the range, yes.

8 Q.30 - Thank you. Next page, middle of the page 12, the
9 paragraph beginning the point is that only looking at the
10 margin or comparing margins and changes in margin without
11 knowing more about the full extent of the financial
12 arrangements is unlikely to provide a reliable basis for
13 assessing the respective financial positions of
14 wholesalers and retailers. What else should be looked at
15 in a perfect world?

16 A. Well, in a perfect world I think the text describes
17 the complexity of the arrangement between wholesalers and
18 retailers. And it's unlikely that the same deal applies
19 between any of the wholesalers and any of the retailers
20 that that wholesaler supplies.

21 There are differences in volume, differences in
22 location, differences in characteristics, in credit
23 rating, a whole range of issues that make this a complex
24 set of arrangements.

25 The point of this though is that if the regulatory

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2 framework had specified that five cents must be the retail
3 margin and six cents must be the wholesale margin, then it
4 would have made a mess I guess of the marketing
5 arrangements between wholesalers and retailers.

6 But because there is the out provided that you can
7 continue with your existing arrangements, that the five
8 cents and the six cents don't mean very much. The 11
9 cents means something, the overall marketing margin in
10 this case.

11 So I think your point would be well taken if there was
12 some rigidity in how that overall margin were to be
13 divided. But because of the flexibility provided it
14 allows retailers and wholesalers to work out their
15 arrangements in a way that presumably works to the benefit
16 of both parties.

17 Q.31 - Thank you. Turn to page 17. Your very last paragraph
18 on the page you make a statement regulation is generally a
19 blunt instrument when used to address disparate economic
20 objectives.

21 A. Right.

22 Q.32 - I just wanted to read that into the record to make sure
23 everybody -- but my question really is wouldn't you agree
24 that there are other ways to regulate the industry than
25 the current system?

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A. Well, there may be many other ways to regulate. This is the one that I was asked to look at.

Q.33 - I understand that.

A. So -- yes.

Q.34 - I understand that. But really what about a zero based cost, looking at zero based cost? Have you ever had any experience with looking at that kind of a system?

A. Well, I think the line you quoted is a blunt instrument. What I'm driving at there is that it essentially treats the industry as a collection of homogeneous entities or enterprises, which it manifestly isn't.

As a consequence, some better than others, moving back to your point about the average, the circumstances each of these enterprises faces is -- can differ substantially from the high end to the low end.

But regulation doesn't necessarily capture the nuance. Let's put it that way. It allows the parties to work out their arrangements but within that 11 cent range or whatever the particular fuel and the margin, you know, under consideration.

So it doesn't allow more flexibility than the nature of the arrangements. You are still restricted to when prices change. You are restricted to I guess the ups and

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2 downs and the vagaries of when you buy your fuel in
3 relation to when the price was set and whether it is going
4 up or down and so on. So I think it is a tough one to try
5 to grapple with. But the -- and then again it depends on
6 what your objectives are.

7 If the simple objective is to maintain price stability
8 then this regime can do that. But if at the other end of
9 it you are also trying to maintain a level of supply, the
10 objective of the change in stability may compromise your
11 ability to maintain levels of supply, particularly when
12 they are operating through resellers with narrow margins
13 or you are operating through retailers who are in remote
14 or rural areas of the province where costs are higher and
15 volumes are lower.

16 But the regulatory system, I guess ignores those
17 nuances. It is a blunt instrument.

18 Q.35 - Thank you. I think you answered my first question of
19 the day as to which way the balance was shifting under
20 this regulation.

21 The next question I have for you is on page 20. And
22 the lead-in to that is the bottom of page 19. But you are
23 talking about the regulator in New Brunswick having no
24 such discretion.

25 And that is with respect to "Weekly adjustments are

1
2 made according to a strict application formula with no
3 accommodation to ensure wholesalers and retailers are no
4 worse off or better off than they would have been had
5 market conditions prevailed."

6 Would such a discretion be a good thing?

7 A. Well, I think such a discretion could be a good thing
8 simply because it allows the regulator a bit more
9 flexibility, in times of -- let's say in times of rising
10 prices to ensure that the wholesale sector is left whole.
11 But at the same time, during times of declining prices
12 that, you know, excessive margins aren't being earned.

13 So -- and that challenge is borne largely by the --
14 you know, by the smaller wholesalers and the smaller
15 resellers because they are starting with a narrower
16 margin. They are relying on -- in an unregulated market
17 they rely on their nimbleness, their buying and selling
18 ability, their ability to adjust rapidly to changing
19 conditions in order to survive.

20 And by introducing the rigidity of a one-week change
21 and not allowing the regulator to either compensate or to
22 diminish the margin, as the case may be, it can leave the
23 supplier, the wholesaler in particular, in a very
24 difficult position, if you are looking at an extended
25 period of rising prices.

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2 Q.36 - And aren't the businesses that are in that position,
3 and affected negatively in that position, the most
4 vulnerable?

5 A. Well, they are the most vulnerable because they start
6 out with lower margins, yes.

7 Q.37 - The next paragraph after figure 4.1 you are talking
8 about rising prices. "During all but a few months since
9 regulation was introduced wholesalers have been buying
10 fairly consistently above the benchmark price."

11 I take it obvious that that means they absorb the cost
12 of that?

13 A. That's right. In this type of regulatory environment
14 it is the wholesaler that is the shock absorber.

15 Q.38 - And I think you in conclusion on page 22, that section,
16 "To conclude, the marketing margin in New Brunswick has
17 declined since regulation was introduced. This has
18 occurred over a period when the average marketing margin
19 in Canada has increased."

20 A. Yes.

21 Q.39 - That goes back to your earlier --

22 A. Yes.

23 Q.40 - -- statement?

24 A. That is right.

25 Q.41 - Thank you. Take you to page 26, Mr. Gardner, the

1
2 second paragraph, the last sentence of that paragraph.

3 "Anecdotal evidence suggests there has been some decrease
4 in the number of retailers and also in the number of
5 resellers over the past two years, though accurate data on
6 the number, their capacity and the volume they account for
7 are not available."

8 So on what basis did you -- you know, what is your
9 anecdotal evidence that you are relying on to make that
10 statement?

11 A. Well, I'm access to the list of wholesalers and
12 retailers in the province that are licenced to sell. The
13 difficulty with the files is they are not necessarily up
14 to date. Some people may hold licences and not actually
15 operate. Or since the licence was issued they have ceased
16 operating, gone out of business.

17 Volumetric information tends to be collected perhaps
18 on an annual basis. And it is not always up to date. So
19 in other words it was difficult to do any fine analysis on
20 volumes and on averages because the data weren't
21 necessarily up to date.

22 But anecdote -- well, the best anecdote was the number
23 of, not at this address, no longer in business and so on
24 we received when we sent out the dealer survey. So I
25 don't know how many of those we would have received, 30 --

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perhaps in excess of 30. That was using the most up-to-date list that was provided by the Province.

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Q.42 - So subject to all of those qualifications you really believe this statement to be true?

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A. I'm sorry?

7

Q.43 - I mean, subject to all of those qualifications about the lack of solid information, you believe that statement to be true, notwithstanding that it is anecdotal?

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A. That the numbers have declined?

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Q.44 - Yes.

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A. Yes.

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Q.45 - I think that is about it for your report. If we could just turn to some of the IR's. Do you have the IR's --

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A. Yes.

16

Q.46 - -- handy?

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I'm going to take you first to the EUB IR's. Question 3 when you get there.

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A. Yes.

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Q.47 - And you may have already answered this in your opening remarks. But first of all do you view the responses that you received as being statistically significant?

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A. To make sure I have the right question, these are the Department of Energy's questions?

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Q.48 - No. EUB.

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A. I'm sorry.

Q.49 - EUB, Question 3.

A. Okay.

Q.50 - The question re survey questionnaires.

A. Right. I see the question now. And so your question on that?

Q.51 - Your answer indicates that 12 percent of the survey questionnaires were returned, 27 gasoline retailers were interviewed, 12 wholesalers, 9 heating oil dealers. And you attach a list.

And my question to you is do you see the number of responses you received as being statistically significant?

A. No.

Q.52 - And what numbers would you have needed to make statistically significant findings?

A. Well, I guess it would have varied depending on the information we were looking for. But for example on cost data, which was one of the main objectives of our survey, we would have been looking for I think in the order of a 25, perhaps 30 percent response rate in order to obtain, you know, reliable information. Or even, if not statistically valid, at least representative information.

So it was -- on the cost side we had to look to other areas in order to -- other sources of information in order

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to come up with the impact of rising costs on the industry.

Q.53 - And when you say cost side, what costs in particular were you interested in looking at?

A. Well, we were looking -- interested in looking at for example the impact of credit card costs, the impact of labour costs, the impact of utilities, municipal taxes, cost of storage, the factors that the Board has laid out in the legislation.

Q.54 - I understand that. So you weren't looking for a rate of return or return on investment or any of those kinds of numbers because they are not -- they are not really relevant to the current regulation?

A. It's not a test, no.

Q.55 - Now are you satisfied that the information you received, because you also indicated that you went to outside sources, that the information you received is consistent with all other outside sources?

A. The admittedly anecdotal evidence that we did obtain from the industry, for example on credit card usage or on credit card rates charged by the companies, those values are consistent with ones that are available in the published literature. And that's certainly a key one.

On labour costs, again the proportion of costs that is

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2 accounted for by labour is consistent with statistical
3 information from other sources that we were able to
4 obtain.

5 Q.56 - Short of getting a bigger response from the business --
6 from the businesses that you surveyed, is there any other
7 way that you could have verified the numbers other than
8 what you did?

9 A. Well, for example, with the credit card -- the fees,
10 it may have been possible to contact -- it would have been
11 possible to contact the credit card companies. But
12 whether we would have received information that would have
13 been of any value is open to question.

14 It is clear that when it comes to credit card, the
15 Visa and Mastercard in particular, the arrangements they
16 make with individual companies are just that. And they
17 will have a range of arrangements depending on volume,
18 depending on revenue, depending on the number of
19 transactions, a whole range of things.

20 So -- and we would have been told that it varies
21 between 1.75 and 2.3 or 2.4 percent for the major cards.
22 And that's -- there are published sources of information
23 that provide just that. And that is what the dealer has
24 told us as well. And that is what the major wholesalers
25 told us.

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2 So when you hear numbers like that often enough and in
3 the same range you tend to accept them as having some
4 validity.

5 Q.57 - So you are really comfortable with the methodology you
6 employed. And in practical terms there was really not
7 much else you could do?

8 A. No. In practical terms there was very little we could
9 do. Because the industry, simply for a variety of
10 reasons, wasn't forthcoming with the data that were
11 needed.

12 Q.58 - Okay. Just give me a minute, Mr. Gardner. I may be
13 very close to the end.

14 Okay. That does it for that. Now I just have a very
15 general question for you.

16 You are familiar with utility pricing models like cost
17 of service?

18 A. Yes.

19 Q.59 - In a perfect world and in a world other than the one we
20 live in, is there any reason why a cost of service model
21 could not be adopted as a regulatory -- part of a
22 regulatory mechanism for petroleum pricing? Is there not
23 a way you could do that?

24 A. Well, I'm sure there is a way. But whether it would
25 be administratively straightforward or efficient is

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2 certainly open to question. Every single enterprise is
3 different. So there is no utility in the purse sense.

4 Q.60 - Okay. No. I understand that. And there isn't a
5 utility. But is there anything to prevent for example
6 stakeholders getting together with proper supervision from
7 the Board, in a stakeholders group, and developing in
8 effect a proxy model for costs?

9 And there may be a formula for small retailers. There
10 may be a second formula for wholesalers. There may be two
11 or three formulae.

12 But is there any reason why a group could not get
13 together to put together actual cost, a cost model that
14 could be employed in these calculations?

15 A. Well, you could employ a cost model, sure. But your
16 original question went to a rate of return and again in
17 the regulated utility sense.

18 And the difficulty I think the Board would have or a
19 regulator would have in those circumstances is the lack of
20 homogeneity of the enterprises. They vary so much that a
21 single rate of return or an acceptable rate of return for
22 one may be, you know, substantially higher or much too low
23 for another.

24 Q.61 - No. I understand that.

25 A. Yes.

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Q.62 - But is there anything -- if a group could get together and agree to those figures, in other words, the industry would agree on a cost model for -- and maybe not across the board. There may be two or three little deviations here or there given size or market or whatever else.

But if the industry could agree on such a cost that would take into account actual cost from the business side, okay, is there any reason that could not be administered if the formula were agreed to and allowed under the regulation?

A. Sure. A cost model like that could work if its output were to measure I guess the change in costs over a period rather than a rate of return needed to support those costs. So if you just look at the cost side of things, sure, there are --

Q.63 - The rate of return might be built into the actual cost. But that wouldn't be what would be tried to capture by rate of return. You wouldn't try to capture a rate of return?

A. Right.

Q.64 - You would try to capture increased costs --

A. Sure.

Q.65 - -- in real time. And on the other side of the equation --

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A. Yes. Of course you could do that.

Q.66 - Of course.

A. Yes.

Q.67 - And isn't there -- aren't there better models than the current model to increase -- or sorry, to capture actual pricing as opposed to average pricing?

A. Well, right now there is -- I don't think there is a model. I mean, that's part of the challenge here, is that the Act and the regulations don't provide a great deal of guidance. They list a number of factors. But those aren't, you know, necessarily the most important factors.

Q.68 - But we are reinventing that now. We are reinventing that.

A. Yes.

Q.69 - So isn't it possible that you could have such a regulation that will have closely captured price on one side, wholesale price on one side and, to go back to a couple of minutes ago, actual cost increases on the other?

A. Of course. I mean, if you were to simply take what might be a typical statement of expenses for a retail outlet, there may be 10 to 12 items on that cost sheet. And you could track those over time, sure.

MR. ZED: I have no further questions. Thank you,
Mr. Gardner.

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2 CHAIRMAN: Thank you, Mr. Zed.

3 The Department of Energy. Mr. Ervin?

4 MR. ERVIN: Thank you, Mr. Chairman. Just a couple of quick
5 questions.

6 CROSS EXAMINATION BY MR. ERVIN:

7 Q.70 - I think, Mr. Gardner, on page 22, and Mr. Zed referred
8 to this, in unregulated areas of Canada prices and
9 marketing margins have increased as of late.

10 Was there an actual study or data that you referred to
11 in making that statement?

12 A. Yes. The figures 4.3 and 4.4. on page 21 and 22 of
13 the report.

14 Q.71 - I guess my question is where does that come from, just
15 briefly? Where does the data -- that conclusion come
16 from?

17 A. Well, if you look at figure 4.3 for example, comparing
18 the pre and current regulatory margin changes, the
19 marketing margin, preregulation and disregulation at that
20 time period, we see that the marketing margin in 4.3,
21 figure 4.3 has declined in Saint John.

22 When we look at other centres in Canada over those
23 periods, the relative changes have, with the exception of
24 Toronto and Halifax, have increased.

25 Q.72 - Okay.

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2 A. And similarly in the other part of the equation I
3 suppose is the relative price changes. And if we look at
4 figure 4.4 comparing major centres across Canada, there
5 have been substantial increases relative to Saint John,
6 New Brunswick and western Canada and even in central
7 Canada. The differences between New Brunswick and
8 Toronto, Sudbury, Montreal, what have you, have declined,
9 had been larger prior to this.

10 So what these figures show is that relative to New
11 Brunswick margins have expanded and prices have increased
12 relatively more quickly.

13 Q.73 - You also made reference, Mr. Gardner, to the anecdotal
14 evidence that there have been market exits from retailers
15 in New Brunswick.

16 Are you aware of any new establishments that have
17 established in the past two years? Or did you -- or was
18 the length of service any part of your study to determine
19 whether any of the respondents were in fact new entrants?

20 A. No. It wasn't a factor or an indicator that featured
21 directly in the computations other than looking at changes
22 in volume. And it's true there have been additions to the
23 retail network in New Brunswick.

24 Again we have gone to each of the major wholesalers to
25 -- individual refiner marketers to ask them about their

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2 site counts, how many additions, how many closures and so
3 on.

4 We didn't get information from all of them. But the
5 information we did receive indicated that there were a few
6 new stations to offset some of those. But the exits
7 exceeded the additions.

8 Q.74 - And in your survey I think you mentioned that you had
9 surveyed the wholesalers, retailers in relation to what
10 their costs were. And you got information back from that
11 and I would imagine from your face-to-face interviews.

12 Were those just related to you? Or were you able to
13 verify them or have them audited in any way?

14 A. No. This is the -- what we had asked for,
15 particularly from retailers, what were their actual
16 financial statements for four years. And most indicated
17 they would not be prepared to share financial information.

18 We asked for it in two ways, one on the questionnaire
19 itself itemizing the costs that we were looking for and
20 would they, you know, fill in the numbers.

21 But there was another question asking whether they
22 would agree to release their financial statements to us so
23 that we could validate the information and have just a
24 more accurate set of numbers.

25 And with very few exceptions the retailers and

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2 certainly the wholesalers and the integrated companies did
3 not wish to share any of their financial information.

4 So what we ended up with were several returns with
5 detailed information on a variety of costs, but not enough
6 of those to be able to say anything about the statistical
7 significance of what we were looking at.

8 Q.75 - And Mr. Zed examined or explored I guess the
9 possibility of setting up some kind of a cost of service
10 regulatory model.

11 And are you aware of any such model existing in North
12 America at this time?

13 A. No.

14 MR. ERVIN: That is all I have. Thank you, Mr. Chairman.

15 CHAIRMAN: Thank you, Mr. Ervin.

16 I believe the next person that indicated they wanted
17 to cross examine was Mr. Maddock on behalf of Global
18 Fuels.

19 MR. MADDOCK: No. No questions right now. Thank you.

20 CHAIRMAN: Thank you, Mr. Maddock.

21 And I think the next person after that was Mr. Hoyt on
22 behalf of Irving Oil Marketing Limited.

23 CROSS EXAMINATION BY MR. HOYT:

24 MR. HOYT: Mr. Zed has covered some of the ground. So it
25 will save us some time. I will try just to deal with some

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new issues.

Q.76 - Can you describe, Mr. Gardner, how Gardner Pinfold came to be retained by the Energy and Utilities Board in this proceeding?

A. Yes. We received an invitation to submit a proposal on the terms of reference. We responded. And our firm was selected.

Q.77 - And do you know who else participated in that process?

A. I'm aware of only one other company who participated in the process. But I have that again anecdotally. There may have been more. But I'm only aware of one other.

Q.78 - Could you share that anecdote, who that other party is?

A. I believe it was M. J. Ervin.

Q.79 - Can you describe any other relevant experience you have in relation to petroleum products legislation?

A. Well, my firm conducted a review of the petroleum marketing industry in Nova Scotia two years -- three years ago. And then we were subsequently retained by the Province to review the regulatory -- well, the extent to which regulation was achieving its objectives in Nova Scotia a year and a half ago.

Prior to that I was an expert witness in the early 1990's during regulatory proceedings in Nova Scotia. That was I think the last year in 1991 that petroleum was

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2 regulated.

3 Otherwise I started my career as an economist with a
4 utility, the hydro utility. And we have been retained in
5 the past on regulatory matters related to natural gas as
6 well in franchise applications. If that provides some
7 background.

8 Q.80 - So it would be fair to say in the last couple of years
9 you monitor what is going on with petroleum pricing
10 regulation in the Atlantic Provinces?

11 A. Yes.

12 Q.81 - And I can assume that you have no vested interest in
13 the motor fuel or heating fuel industries in New
14 Brunswick?

15 A. None whatsoever.

16 Q.82 - Can you describe the process that you undertook in
17 preparing your report please?

18 A. Yes. We drafted -- initially started by drafting
19 questionnaires and survey instruments to circulate to the
20 retail sector and to the wholesale sector both motor fuels
21 and heating oil. We contacted the major integrated
22 refiners and major wholesalers requesting interviews.

23 And these were face-to-face interviews. And all but
24 one -- all agreed to those meetings. But we were unable
25 to find a convenient time for one of them. So we did have

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2 meetings with all the major wholesalers. We met with
3 several of the resellers of petroleum products.

4 We met with several of the heating oil companies, two
5 of the major propane distributors. As well we met with I
6 think just under 30 of the retail gasoline dealers in the
7 province.

8 So this formed the basis of our attempt to gather the
9 information that we needed in order to meet the objectives
10 of the analysis.

11 Q.83 - And over what period of time did those consultations
12 take place?

13 A. Those consultations took place between mid June and
14 mid July roughly. Sorry, it would have been mid June
15 toward the end of July.

16 Q.84 - And Mr. Zed referred to the EUB Question 3. I will
17 just -- I will cite the relevant portion of it, where you
18 had indicated that Gardner Pinfold interviewed 27 gasoline
19 retailers, 12 wholesalers and 9 heating oil dealers. And
20 then, as you pointed out, you attached a table 2 which
21 sets out the names of the parties that you consulted.

22 Would you describe the gasoline retailers, wholesalers
23 and heating oil dealers interviewed as a good sample of
24 the industry in New Brunswick?

25 A. Yes.

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2 Q.85 - And did you receive a good level of cooperation from
3 those that you interviewed?

4 A. With the exception of providing us with the detailed
5 costs we were looking for, the cooperation was excellent.

6 Q.86 - And you had an opportunity to speak with a
7 representative of my client Irving Oil as part of that
8 process?

9 A. Yes, I did.

10 Q.87 - I would like to refer to page 11 of your report. And
11 Mr. Zed referred you to this statement. I want to refer
12 to it in a bit different way.

13 And it states that "The average spread between the New
14 York Harbour spot price and the Saint John pump price
15 excluding tax was fairly stable, in the 11 to 12 cent per
16 litre range between January 2003 and July 2006. This
17 average spread presumably formed the basis for the
18 regulated margin of 11 cents per litre plus transportation
19 currently in place in New Brunswick."

20 Do you see that statement?

21 A. Yes.

22 Q.88 - And so am I right that you believe that is likely how
23 the original total maximum margin of 11 cents was
24 originally established?

25 A. Yes.

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2 Q.89 - And do you believe that the Province of New Brunswick
3 gave any consideration to non-petroleum revenues in
4 setting the initial motor fuel margins under petroleum
5 products pricing legislation?

6 A. I'm not aware of any consideration.

7 Q.90 - Can you refer to page 30 of your report? And I would
8 just ask you to read the conclusion at the bottom of the
9 page.

10 A. Conclusion, the maximum margin should increase by two-
11 tenths of a cent per litre to compensate wholesalers and
12 retailers for general price inflation since regulation was
13 introduced.

14 Q.91 - So could you confirm that your calculation of that .2
15 cent per litre increase was in recognition of a general
16 price inflation that has affected both wholesalers and
17 retailers since July 2006?

18 A. Right. Yes.

19 Q.92 - Could you refer to the summary page which I believe is
20 at the beginning of your report?

21 And I note, just looking at the chart, that there is a
22 recommendation that there be a one cent per litre increase
23 in delivery cost for wholesale heating fuels.

24 Do you see that?

25 A. Yes.

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2 Q.93 - And could you confirm what you are proposing is that
3 the one cent per litre increase be available to be shared
4 between the wholesaler and retailer of heating fuel?

5 A. That is correct.

6 Q.94 - So it is not just to be on the wholesale side. The
7 idea is that that would be shared?

8 A. The idea is that the current two cents, as it is laid
9 out in the price schedule, be increased to three cents.
10 However, that is shared between wholesalers and retailers.

11 Q.95 - All right. In your view, Mr. Gardner, how often should
12 the maximum margin and delivery costs under the petroleum
13 products pricing legislation be reviewed?

14 A. I would think at least once a year.

15 Q.96 - And is there a better way to do it than the process
16 that we are in the midst of?

17 A. I think the process that we are in the midst of should
18 result in, at the very least, identification of the most
19 significant heads of cost that underpin the structure of
20 the industry, both the wholesale and retail level.

21 It should identify the data sources that might be
22 available to support an analysis of those costs. And
23 ideally it would provide a methodology that allows the
24 Board and the industry to make the adjustments in a more
25 expeditious way.

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2 In other words, when I look at the sources of
3 information that ultimately we are left to rely on, they
4 are all in the public domain with some minor exceptions.
5 And I think those areas of exception could easily be
6 addressed in a more I guess mechanical way.

7 Let's take credit cards, for example. The major swing
8 factor there is price and usage. Both those values would
9 be well known to the industry and could be verified by the
10 Board by collecting information, by extending the
11 collection of information for example that the Board now
12 compiles from industry.

13 Transportation costs, again the main swing factor is
14 the price of fuel, the fuel adjustment charge. Again it
15 is a factor that could I think easily be rendered through
16 a formula. I mean, the industry uses a formula to arrive
17 at the fuel adjustment charge. It results in a price.

18 Again the Board could obtain that information I
19 believe under the current legislation in order to effect
20 the changes in a more automated way.

21 Q.97 - So then to kind of summarize that then, it would be
22 possible to develop a fairly transparent formula that
23 would track and recognize wholesalers' and retailers'
24 increasing costs?

25 A. I believe so, yes.

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2 MR. HOYT: That is all the questions that I have.

3 CHAIRMAN: Thank you, Mr. Hoyt.

4 I believe the next person indicated they would have
5 questions or might have questions was Mr. Grant with
6 Murray's Esso.

7 MR. GRANT: No questions at this time.

8 CHAIRMAN: Thank you, Mr. Grant.

9 The next individual was Mr. Nicholson with Salisbury
10 Road Gas and Convenience. Okay. We will come back to
11 him.

12 Mr. Chris Scholten of Scholten's.

13 MR. SCHOLTEN: No questions at this time.

14 CHAIRMAN: Thank you, Mr. Scholten. Mr. Maynard of Ultramar
15 Ltd.

16 CROSS EXAMINATION BY MR. MAYNARD:

17 Q.98 - I just have a question regarding your opinion on how
18 the distribution costs are addressed in the New Brunswick
19 regulations.

20 They differ quite a bit from other jurisdictions in
21 that there is a provincial price set. And then market
22 participants are asked to justify their distribution cost.

23 The industry has a need for infrastructure. If we all
24 pull from one product source of course there is not a
25 whole lot of flexibility in the system.

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2 Do you feel that the method in which the New Brunswick
3 regulations govern that threaten the level of
4 infrastructure in the industry?

5 A. Well, at this point, as I understand the industry,
6 there are let's say two, three major supply points for
7 product, petroleum product in New Brunswick.

8 Let's take gasoline diesel, the Irving refinery, the
9 Ultramar refinery through its Chatham storage facility and
10 from the Imperial refinery in Dartmouth. Product is
11 supplied from each of those sources depending on relative
12 costs and logistical considerations.

13 Under current regulation the wholesaler is permitted
14 to charge the retailer the actual costs of delivering to
15 the point of distribution or the retail outlet whether it
16 is a gas station, a bulk plant, what have you.

17 What this has done is to change the competitive
18 dynamic in the province. So that at this point the
19 retailer in a market area that is supplied through the
20 least cost method essentially determines the market price
21 in that area. Because they are not permitted to charge
22 any more than the actual transportation cost.

23 So what has happened is that -- in the past the price
24 in a given market would have been determined by a number
25 of factors including price leadership in a particular

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market, a different set of dynamics.

But now the distribution costs, the transportation cost is the primary force and the most efficient, either -- the most efficient retailer in terms of its transportation costs is going to set the lowest price.

Now what does that mean? Well, it means that if you are operating a large storage facility, as Ultramar does in Chatham, that your ability to supply the market and to meet the costs of that distribution facility are now driven by a province-wide set of distribution costs that may be different than those that are applied before regulation was introduced.

Whether or not a dealer wishing to purchase from Ultramar can get product to the outlet, the retail outlet or to its own bulk plant in the case of heating oil, in a way that it could prior to regulation, at least in a way -- you could get it in a way, but whether you can get it at a least cost point I guess is open to question.

Because running that plant up in Chatham is costing the operator and it is costing each of the purchasers from that plant. Whether that price is now competitive with the actual distribution cost that is allowed to be passed through is I guess the factor that is going to determine in the long run whether or not you are able to sustain

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2 that facility.

3 So without knowing more about the details, I don't
4 think that you can say in the abstract that this is a good
5 thing or a bad thing. But it changes the competitive
6 environment. I think that is the key.

7 And given the cost structure and given that regulatory
8 environment governing transportation costs, it could well
9 undermine the viability of that plant.

10 Q.99 - Moreso than the manner in which other jurisdictions
11 handle distribution costs?

12 A. Well, yes. The two other jurisdictions, Newfoundland
13 and Nova Scotia divide the province into essentially
14 subjurisdictions where allowed costs are permitted to be
15 passed forward.

16 So it's not a single market from a distribution
17 standpoint. That creates its own set of challenges for
18 operators within each of those areas, those market areas.

19 But the average cost in that area is one that is known
20 and permitted to be passed through, subject to the minimum
21 price in each of those -- in each of those areas. So it
22 is not necessarily the least cost supplier that is running
23 or driving the market, unlike the case in New Brunswick.

24 One of the factors that would be affected of course is
25 the volume of sales. Because if you suddenly shifted to a

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2 least cost supplier or a retailer in an area, that
3 retailer sets the price.

4 If that price, you know, is set at a level where
5 another retailer or other retailers in that market area
6 cannot match it in the long term, they go out of business.

7 And so the volume that another, for example Ultramar
8 would have had in that region would be adversely affected.
9 The same could be said for supplies from Imperial in
10 Dartmouth into southeast New Brunswick.

11 Q.100 - I guess as a consultant for the Province in this
12 process can you comment about the amount of infrastructure
13 that has been removed from the industry over the last 10,
14 20 years?

15 A. In this province or generally?

16 Q.101 - Well, generally, yes.

17 A. Well, generally, I mean, the number of retailers in
18 Canada generally and in the Atlantic Provinces has
19 probably dropped by 50 percent in the last 15 to 20 years.
20 The number of wholesalers has declined. The number of
21 bulk plants has declined. And the number of refineries in
22 Canada has dropped significantly. The storage capacity
23 has declined.

24 A lot of this has been facilitated by product exchange
25 agreements between the refiners, that they will supply

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2 from different points. And not everybody has to maintain
3 storage facilities or even have a refinery in a market
4 area.

5 But all of which has also served to -- I guess to
6 shorten the supply capacity in the event of a shortage.
7 And it contributes, as we have seen in North America
8 generally to, you know, quite sharp price spikes, if there
9 is a problem with one of these facilities, whether it is a
10 refinery or a storage centre.

11 Q.102 - So I guess in summation you would agree that the
12 methodology that is being used by the Province really
13 creates a market condition where there is the lowest
14 common denominator.

15 The participant that has the lowest distribution cost
16 will basically set the price in a particular area of the
17 province?

18 A. Yes. That is what is happening. That is right.

19 MR. MAYNARD: No further questions.

20 CHAIRMAN: Thank you, Mr. Maynard.

21 We are going to take a break. I guess it is 12:00
22 o'clock. So I think we will break for lunch at this point
23 in time. When we come back I think Mr. Wootton of XTR
24 Energy may have some questions, he indicated earlier.

25 As well Mr. Nicholson I think was out of the room when

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2 we called upon him. And then Board Counsel will have an
3 opportunity to ask questions.

4 So we will break until 1:15.

5 (Recess - 12:00 p.m.- 1:15 p.m.)

6 CHAIRMAN: Good afternoon. I understand there may be a
7 couple of people here this afternoon that may not have
8 been in attendance this morning when I did the
9 appearances.

10 So is there anybody that is currently a registered
11 Intervenor is now in attendance and we should take note of
12 their attendance?

13 MR. MCDOWELL: My name is Jim McDowell from Notre-Dame
14 Express in Moncton. I just checked in.

15 CHAIRMAN: I guess you missed that part of it this morning.
16 We asked everybody to speak into the microphone.

17 MR. MCDOWELL: So I talked with Lorraine (Mrs. Légère) just
18 moments ago. I do not really have any questions at the
19 moment. Thank you.

20 CHAIRMAN: Thank you, Mr. McDowell.

21 Is there anybody else in attendance that we would not
22 have taken note of this morning?

23 All right. Well, in continuing with cross
24 examination, I think we had indicated we had missed
25 Mr. Nicholson. Is he in the room?

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2 All right. Mr. Wootton?

3 MR. WOOTTON: Thank you. Just a couple of questions for
4 Mr. Gardner.

5 CROSS EXAMINATION BY MR. WOOTTON:

6 Q.103 - One of the factors that significantly impacts the New
7 Brunswick marketplace are the privately-owned retail
8 petroleum workers. They represent the lion's share of the
9 rural fabric that really holds the province together and
10 provides petroleum services to the community at large.

11 It is really critical that the legislation, as
12 everybody has talked about, continues with equitable
13 solutions for all the stakeholders. And oftentimes they
14 are not as vocal as some of the rest of us.

15 So I wanted to ask you a few questions from their
16 perspective in how this legislation affects them.

17 These folks privately invest in their facilities and
18 all are the entrepreneurs out there in the marketplace.
19 They provide the essential services to the rural markets.
20 and under the legislation today there is only established
21 a maximum selling price, no minimum selling price.

22 Did you investigate, as part of establishing and
23 looking at this legislation, did you investigate the
24 opportunity to establish a minimum selling price to
25 provide these independent owners and operators some

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protection from aggressive pricing strategies of integrated natures or the large big box stores?

A. The legislation doesn't provide for a minimum price. And we didn't direct our attention to determining whether or not there was a case for a minimum price. It is not one of the listed relevant factors.

But in the course of meeting with the dealers in the province and in selecting the dealers we have been able to speak with, we identified what I think was a good representative sample across the spectrum of suppliers as well as geographically, but focusing on the independence rather than the integrated, which we have dealt with indirectly through the meetings with the wholesalers.

And I think there was little question that the independents in rural and remote areas feel particularly vulnerable under regulation, in part because their costs tend to be higher, in part because their volumes tend to be lower and in part because their opportunities to generate revenues from activities or services other than petroleum are more limited.

And many of them did come out and ask, you know, why can't we have a minimum price like they do in Nova Scotia, like they do in Prince Edward Island. And I mean, the response is simple, that it is just not provided for in

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2 the Act.

3 And it does affect the smaller dealers, the regulatory
4 structure, because of the change that occurred, and we
5 discussed this earlier, in the way transportation affects
6 the competitive environment, driving price to the lowest
7 cost supplier within a market area.

8 So that is one factor in some of the smaller stations
9 that have either taken delivery from a tandem rather than,
10 you know, a B-train or one of the larger trucks.

11 They also face a competitive dilemma of trying to
12 price and retain some margin against the -- particularly
13 the integrated refiner outlets, and particularly if they
14 operate in close proximity to one of the integrated
15 refiner outlets. Because the bigger companies have got
16 deeper pockets and can drive down price to a level where
17 it is very difficult for some of these smaller dealers to
18 compete.

19 That is the reality in the rural and remote areas.
20 They face competition. They face pricing strategies that
21 are, if not intended to, you know, make it a nonviable
22 operation. That is unfortunately from their perspective
23 the result they see. So it is a tough business.

24 Q.104 - You had mentioned some of the other regulated markets.

25 Some of those regulated markets, in fact most of the ones

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2 we operate in, do provide that downside protection for
3 this very important group of stakeholders, and therefore
4 establish a minimum price in the marketplace to provide
5 them at least a level from which they can go to their
6 bankers and to other investors into their business and
7 provide at least a level of comfort that the risk isn't
8 zero margin.

9 Is there any downside protection for this important
10 group within the current legislation?

11 A. No. There is no minimum margin.

12 Q.105 - And could a minimum price structure be easily
13 implemented and established within the context of this
14 legislation?

15 A. I think the legislation would probably have to be
16 amended in order to provide for it. But I mean, there is
17 nothing to stop that.

18 Q.106 - Okay. In your experience would you suggest or agree
19 that this particular group would be served well with the
20 introduction of minimum pricing?

21 A. Well, in some markets they would be. I think one
22 would have to go and look at the actual pricing behavior.
23 And again it can be deceiving.

24 Because if you look at where in major locations, the
25 major urban centres where pricing information tends to be

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2 available, you will see that in most areas the price is
3 fairly close to the maximum, on average, week to week.

4 There are some exceptions. But those areas are not
5 the areas that are necessarily influenced by -- or where
6 the rural and remote dealers would be influenced by those
7 pricing strategies.

8 So coupled with the higher costs they face and coupled
9 with the specific pricing activity that occurs in those
10 areas -- and you know, I will give you a concrete example
11 of one, when we were going around.

12 And I spoke with a -- in fact it was an XTR station in
13 one of the smaller communities in the center of the
14 province. The owner, who happened to be, you know, a
15 couple of doors down from a larger station run by one of
16 the integrated refiners, or at least owned by, said that
17 she is facing, you know, the closure of her station
18 because she is finding it impossible to compete.

19 And the pricing strategy that is going on in that
20 market, which will never appear in the official
21 statistics, she is a full serve and the station is a self-
22 serve. And as soon as she tries to move her price within
23 a cent of the self-serve, they drop their price.

24 So that there is a two cent spread. Knowing that
25 people in the community, even though they may be

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2 supportive of her, are not going to stand for, you know, a
3 two cent difference. They will go to the lower price. So
4 she has been forced to keep her two cent spread in order
5 to sell any gas at all.

6 So it is that kind of environment that people are
7 trying to survive in. And in that case and in many of the
8 other cases you ask the owner and say, well -- and she has
9 got, you know, a small store as well. But she will close
10 when she retires. Because she can't imagine being able to
11 sell the business.

12 But I asked her how much she earned. Because this
13 business is open, you know, 16 hours a day and so on,
14 five, six days a week, seven days a week. She takes home
15 about \$25,000 after all things are said and done. And
16 there is no -- there is nothing else left over. There is
17 no contribution to anything else. 25,000 bucks.

18 And this is the state of things in rural parts, not
19 just in New Brunswick but in Nova Scotia, P.E.I. and
20 Newfoundland as well. People in rural areas running
21 stations, marketing a service don't take a whole lot home.
22 And they work very long hours.

23 Q.107 - So in the example you use, they are being allowed
24 today to enjoy a two cent -- or they are being allowed to
25 price two cents above that competitor in that particular

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market?

A. That's right. Where the preference would be to price one cent above in order to maintain volumes.

Q.108 - And today it is two cents. And tomorrow they may decide that they want it to be 3 or 4. Under the current legislation there is nothing that would prevent them?

A. Well, as long as the -- as long as the price doesn't exceed the maximum.

Q.109 - Yes, correct. Under the current legislation and the application of it as it relates to this important group, would you expect that you would see an increase in the number of people entering the petroleum marketplace as private rural retail petroleum facilities? Or do you think that their numbers will decline?

A. Well, I think the history is one of declining numbers again in this province and elsewhere. New highways are terrific. And I just drove down through New Brunswick, you know, from Montreal. And I think at one time or another I visited, you know, each one of these stations.

And it's great to have the on and off-ramps. But for every one on the off-ramp there is probably one just a few kilometers down the road that is -- or two or three that are going out of business.

So the size of the margin is ultimately going to

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2 determine the level, the location and the quality of
3 service. I mean, that is the decision. That is the
4 tradeoff.

5 And to the extent that the margin is reduced to
6 benefit consumers, and we all want lower gasoline prices,
7 you are effectively saying this is the level of service or
8 the location of service that we are trying to achieve,
9 that we are happy to have. And there is a tradeoff there.
10 There is no question.

11 Q.110 - Thank you. On to haulage for just a minute. Under
12 the current legislation the maximum haulage recovery rate
13 is two cents per litre.

14 Would you agree that the haulage costs that are in
15 excess of two cents a litre to deliver to some of the
16 rural facilities reduces the overall margin -- as you
17 refer to it, as 11 cents.

18 So if it is -- if the haulage into a site is say three
19 cents, then the net available margin for the wholesaler
20 and the retailer to share is then reduced from 11 down to
21 10?

22 A. Depending on which market you are in, 11 would be the
23 outside limit. But in some of these remote rural areas
24 the outer limit may be let's say 12 cents. Where you are
25 up against the least cost competitor your costs are going

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to be higher, your transportation costs to a small station.

That money has to come from somewhere. And it is going to come from the margin that the market will tolerate in that area, as driven by the most efficient supplier into that area.

Q.111 - Sure.

A. I mean, the notion that -- and we hear this a lot, the notion that somehow transportation is outside the margin. I mean, it isn't. It forms part of the difference between the purchase price and the selling price.

And it could be utilities. It could be labour. It could be a number of other things. All of that has to come out of the marketing margin.

Q.112 - Throughout this year we saw huge increases in diesel costs which directly resulted in higher than traditional haulage costs and in some cases for deliveries to the smaller sites taking split loads, for example. Their haulage rates have gone far in excess of the two cent maximum provided for under the legislation.

We have seen a slight decline in that, thank goodness, over the last couple of months. But we still have a variety of sites which have excessive haulage rates over and above the maximum.

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2 As part of the review process that you did for haulage
3 rates specifically, did you look at creating a haulage
4 rate structure that would be variable driven by the
5 movement of diesel?

6 A. Well, it would be I think a straightforward matter to
7 design one and build it into the weekly margin setting.
8 The industry uses a formula in a nutshell. For every cent
9 increase you are looking at a .5 percent increase in the
10 fuel adjustment charge.

11 So it is just a matter of applying that to the
12 starting point, whether it is -- I can't remember -- let's
13 say 90 cents on the diesel, something like that. And
14 there you get your formula.

15 So it could be formula based in the same way that
16 dealing with credit cards could be formula based. Because
17 both are sensitive to the price of fuel which is a fairly
18 transparent -- it is a known quantity.

19 MR. WOOTTON: Thank you. Those are my questions.

20 CHAIRMAN: Thank you, Mr. Wootton.

21 Before I ask Ms. Desmond whether or not she has any
22 questions, is there any party present that I didn't call
23 upon for cross examination that wishes to cross examine
24 Mr. Gardner?

25 Well, it doesn't appear that there is anybody then

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that has any further questions other than Ms. Desmond. So Ms. Desmond?

MS. DESMOND: Thank you, Mr. Chair.

CROSS EXAMINATION BY MS. DESMOND:

Q.113 - Mr. Gardner, could you turn to page 7 of your report and specifically to paragraph above the chart. There is a reference to stations selling approximately as an average 200,000 litres of gasoline annually.

Are your recommendations that are included in your report based on that average volume?

A. No. You are referring to the smallest size stations of 200,000 litre? Or the 2,000,000?

Q.114 - Sorry. I mean to say 2,000,000. Is that the average on which your recommendations are based?

A. Well, that is the average in the province. And I think the recommendations are based on the average values for the key recommendations based on average values for the stations as we see them. And that 2,000,000 is just about where the arithmetic average is. So yes.

Q.115 - And given that some retailers sell a lot less than that 2,000,000 litres, are your recommendations appropriate then for those smaller vendors?

A. They are appropriate in the sense that they apply equally on a -- given the way the legislation is framed.

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2 It is not going to -- you know, it is going to make a
3 difference to a smaller retailer who has low volumes. But
4 the actual amount of income that is generated is still
5 relatively small.

6 So for a station selling 200,000 litres annually, a
7 cent increase, you know, amounts to what, to a thousand
8 dollars? I mean, it is not that great. But it does make
9 a difference. So it is appropriate in that sense.

10 The difficulty -- and I guess we get back to the blunt
11 instrument that that regulation is, that when you allow a
12 cent that one of those smaller low volume dealers
13 desperately needs, we are also providing the market and
14 the multimillion litre station with that same margin,
15 whereas that station may not be as desperately in need as
16 the smaller one.

17 Q.116 - Recognizing though that certain costs don't vary with
18 volume, how should those factors be taken into
19 consideration?

20 A. The cost or the factors that we have looked at, I'm
21 trying to think of one that doesn't vary with volume.
22 Labour costs tend to.

23 Although there is, you know, there is -- again the
24 average of about 50 percent of the costs of running a
25 station are accounted for by labour. And there is some

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2 variation although it is not much from the smallest to the
3 largest. Credit card, that is simply a function of price.

4 Transportation is largely a function of price although
5 the nature of the station is also going to be a factor
6 there, whether it can take deliveries from, you know, an
7 efficient tanker or it is going to take deliveries from a
8 smaller tandem with the attendant higher costs that that
9 entails.

10 And if you could give me an example of a cost that is
11 insensitive to volume and how that might apply, that might
12 make it a little bit easier to respond.

13 Q.117 - I think just one that comes to mind is municipal
14 taxes. They wouldn't -- that wouldn't necessarily be
15 sensitive to volume.

16 A. No. Except that higher volume stations are going to,
17 you know, have a higher assessment. Now whether that is
18 proportionate to volume or not, I guess it would vary from
19 station to station.

20 In the course of looking at that as an issue, we did
21 obtain from Service New Brunswick a listing of all the
22 stations and the levy and the assessment. And they tended
23 to vary, rural and urban as far as the levy was concerned.

24 It was impossible to determine, particularly without
25 volume information, whether the assessment or whether the

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levy was then sensitive to volume. There was just no way of knowing that.

Q.118 - Okay. I have a question with reference to page 11 of your report. And at the bottom of that page there is a reference to marketing margins?

A. Yes.

Q.119 - Now as I understand it, Mr. Gardner, a lot of resellers or secondary wholesalers are paying less than the rack price, is that correct?

A. The ones we have talked to would be paying at rack and some slightly below. We are talking a tenth or so or slight above. But the rack tended to be a good guide to what the resellers are paying except in the case of -- well, I'm just saying the very large ones.

But the very large ones in a sense aren't resellers, they are wholesalers. But even in that case, if they are as much as a cent below rack they would be doing well.

Q.120 - And can you identify the type of reseller that would purchase motor fuel at or above the rack price?

A. The type? Well, these are resellers who supply almost exclusively retailers in rural and remote areas.

Q.121 - And for those retailers then the rack prices were only a guideline, is that correct?

A. Well, it's a starting point. And the actual price

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they pay would depend on the volume they draw and ultimately the kind of deal they can strike with the supplier. That's usually a function of volume, credit rating, you know, factors like that.

Q.122 - So the actual margin then flows to the wholesaler, retailer. And it depends whether or not they pay, not necessarily on the rack price?

A. Well, that is right. It is the acquisition cost that is going to determine their margin, yes, at the buying end.

Q.123 - And for heating fuel retailers what would be the differential there from the posted rack price and what would normally be paid?

A. Well, again it is going to vary. The best -- the best deal what we heard was I think a tenth or so below rack. And then you could be up to two, three cents above rack depending.

Like some of the smaller heating oil retailers are buying from regional resellers. So it is going through two hands and a bulk plant before it gets onto their truck. So they are down the chain of it.

Q.124 - Mr. Gardner, on page 12. And you indicate a number of factors that should be considered when you are assessing the accuracy of the retail margins. And some of those

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2 factors include whether there is fuel sold on consignment,
3 which party is responsible for the investment in the
4 physical assets.

5 But isn't it the total concept matter, not the
6 financial arrangements between the wholesaler and the
7 retailer?

8 A. I think the discussion you refer to on page 12 is I
9 think a kind of a reminder to somebody looking at this
10 industry that the margin does not always reflect the sum
11 of the relationship between the buyer and the seller.

12 So that someone receiving -- let's say a retailer is
13 given a five cent margin, it may not be comparable to a
14 retailer who is getting a 3.5 cent margin. Because a 3.5
15 cent margin retailer is perhaps selling on consignment, so
16 doesn't bear the carrying cost, doesn't bear the risks of,
17 you know, the ups and downs depending on when it is
18 purchased.

19 So I think your point is accurate. At the end of the
20 year what that dealer is looking at is how much revenue
21 did I earn, what were my costs, did I make a profit this
22 year? And if you wanted to, you could divide that by your
23 volume and say, here is my actual margin.

24 But this discussion is not directed toward trying to
25 design a system or trying to specify a margin. It is

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simply to point out that the relationship between wholesalers and retailers is complex, not just because everybody gets a different deal on the margin but because of the different costs that each bears in the relationship or can bear in the relationship.

Q.125 - And if I understand that, there is risk that both parties are able to share that risk to some extent. But really who pays is not an issue. It is whether the total margin should be adjusted.

Do you agree with that?

A. Well, who pays is certainly an issue from, you know, a retailer's standpoint who is trying to stay in business. And presumably if the wholesaler wants that dealer to stay in business they will make an adjustment in the relationship that ends up with that retailer getting more margin.

But yes, I mean, at the end of the day it is the overall margin that has to cover the cost of marketing. And that is what is important, sure.

Q.126 - Okay. And the lack of knowledge as to the specific financial arrangements between the different wholesalers and the different retailers, that doesn't in any way inhibit the Board from setting an appropriate margin during the course of this hearing?

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2 A. No. Because given the latitude that the Act provides
3 for wholesalers and retailers to work out their own
4 arrangements, unless, you know, you happened to, you know,
5 strike a retailer who has got -- that was living by the
6 letter of the regulation as far as margin is concerned --
7 that may occur.

8 But broadly, I mean, virtually all arrangements are
9 carried over from the preregulation days. And very, very,
10 very few dealers or wholesalers that we talked to are
11 living according to, you know, the 6 and 5. They are
12 carrying through their original arrangements.

13 Q.127 - Next on page 27 of your report. Table 4.1 And I'm
14 looking at the line where you have got price and then
15 there is gasoline, diesel and heating fuel. And then
16 price -- should those numbers -- are they wholesale or
17 retail prices that you have indicated there?

18 A. These are retail prices.

19 Q.128 - Why is it you list a retail price there? And how did
20 you come to that?

21 A. Well, the retail prices are -- let's call it
22 indicative prices looking -- based on recent months on the
23 assumption that the recent past is going to be a better
24 guide to the future than the distant past.

25 And by distant I mean prior to, you know, 2000' and

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2 early 2008. So retail prices were used because they
3 approximate what the retailer is paying the wholesaler.

4 I mean, it's subject to the margin, yes, and HST. But
5 as an indicative guide to what the carrying charges would
6 be, in my view it reflects a basis for making this
7 computation.

8 Q.129 - Wouldn't it be fair to suggest that the retailer is
9 paying the wholesaler maximum price but that would be sort
10 of the maximum cost to the retailer, the wholesaler
11 maximum?

12 A. That price includes road tax. It includes
13 provincial -- sorry, the federal excise tax. So the only
14 thing that is excluded is the retail margin plus the HST
15 on the margin. That is right.

16 Q.130 - What would be the normal terms of payment between a
17 heating fuel retailer and your wholesaler?

18 A. Again, normal. We have heard everything from three
19 days, 10 days. It does vary. We view seven days as a
20 guide for motor fuel.

21 And 40 days -- the 30 days for heating oil refers not
22 to the payment terms to the wholesaler but the payment
23 terms from the customer to the heating oil company. So it
24 is that carrying charge that is reflected here.

25 And again it varies. It varies. Some of the dealers,

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2 particularly the dealers in the more remote and rural
3 areas, pointed to, you know, 45 and 60 day terms, that
4 this was how long it was taking to get their money. But
5 we use 30 days as a guide.

6 Q.131 - Recognizing that that is going to depend on the
7 circumstances and recognizing a 30 day carrying charge
8 from the retailer to the customer and a seven day carrying
9 charge from the wholesaler to the retailer --

10 A. Right.

11 Q.132 - -- should there not be sort of an adjustment for those
12 carrying charges, say a net carrying cost of 23 days?

13 A. Well, we are talking about heating oil versus diesel
14 and gasoline, the motor fuels. The carrying charge for
15 gasoline and diesel that is included in the analysis here
16 is from the retailer paying the wholesaler. The retailer
17 gets the money. It is a cash transaction.

18 In the case of heating oil we are looking at the
19 carrying costs to the retailer rather than the retailer to
20 the wholesaler, okay. And that is what I'm reflecting
21 here.

22 So there wouldn't -- there wouldn't necessarily be a
23 net 23. It is a question of what the industry is
24 carrying. And the carrying costs are different in the
25 case of motor fuel compared with heating oil.

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Q.133 - So if there are -- with the heating oil customers, if cash is paid by the customer, is the 30-day carrying cost appropriate? Is that what you are suggesting?

A. Well, what I'm suggesting is that what the heating oil companies, the retailers we spoke with, were telling us that their customers are taking up to 60 days to pay their costs, okay, the cost of fuel, that 30 days is the norm, 45 to 60 is not unusual.

Some pay by credit card. And it is simply taken on or averaged over the year. It varies widely. We use 30 days as an indicative term based on what we are told.

Q.134 - Just looking to July of 2006. And you have got a price of 1.05 for gasoline?

A. Right.

Q.135 - How did you calculate that figure?

A. I can give you the data sheets for all of those values if you wish. I mean, if you are asking -- are you going to go through each of these prices?

Q.136 - Actually I have a sheet that maybe we could circulate and have a look at and see how that compares with your data, if I have the permission of the Chairman to do that.

CHAIRMAN: Certainly. Before we proceed, the Board didn't receive a copy of those.

MS. DESMOND: I believe Mr. Young went to make a few extra

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copies of the price sheet. I could come back to this.
CHAIRMAN: Look, as long as we had one more we can probably share.

Okay. Any time you are ready, Ms. Desmond.

MS. DESMOND: Sorry about that.

Q.137 - If I could just -- Mr. Gardner, the information we just circulated, for the benefit of other participants, is the maximum posted prices by the Energy and Utilities Board.

And I just wanted to provide that to you so we had that as a source of reference and wondered how you came to your prices for July '06 and July 2008?

A. Okay. The -- I have to apologize right off the top here. Because the '06 price is an average for the year rather than the month. And it is for diesel as well as gasoline.

Q.138 - Recognizing that the first six months of 2006 would not have been regulated prices --

A. That is right.

Q.139 - -- would you need to make an adjustment now to this table to reflect that?

A. If you were going to use this method I would make an adjustment, basing it on the average for those last six months.

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The reason I framed that as a conditional is because the net effect, when you run the calculations, is so small that the conclusion was that this could be rolled into the, you know, inflationary value rather than computed on this basis.

Q.140 - I think that is the case for motor fuel. But what about heating fuel for July 2006?

A. Heating fuel, I think it is substantial enough that it would warrant -- yes, again it is the annual average that is used there which is roughly 85 cents. So if you want to use it you would use six months.

Q.141 - Are you prepared, Mr. Gardner, to perhaps redo that table?

A. Sure. Yes.

Q.142 - For July of 2008, in those three columns, can you confirm to the Board how that number was calculated?

A. Sure. Again it is not specifically July. My apologies again. The -- I think for this type of calculation, because it is intended to be forward-looking -- in other words, we are not simply trying to compensate dealers for what happened six months ago or over the past two years, but rather to look ahead to ensure that the base of the margin reflects what is likely to occur, I used the -- used prices from April to

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September of this past year as a guide to what is more likely to occur than an annual average or even a two-year average.

So in other words, it is looking at crude prices as they were and fuel prices as they were during the April to September period rather than in a specific -- a specific month or a longer term average as a guide to what is likely to occur in the future.

Q.143 - Did you say April to --

A. April to September.

Q.144 - -- September? Or would that have been perhaps August?

Because I believe the report was submitted in September.

A. Well, sorry. The price sheet I'm looking at includes September. So you are right. It would have been August.

Q.145 - So just for clarity purposes, I guess, you have got it labeled July. But it is really not representative of that month?

A. No. That is an error in that. That shouldn't have read July.

Q.146 - It is representative of April to August?

A. In 2008.

Q.147 - And is that the same in each of those three columns, gasoline, diesel and heating oil?

A. Yes.

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2 Q.148 - Okay. And just on that point, if I could reference
3 you as well to table 4.2. This is on page 28. It is just
4 the next page. And in the table there you have a
5 reference to 2006 and then May of 2008.

6 So I'm wondering if you could explain what those
7 entries represent and if they are consistent with the
8 entries that you used in table 4.1?

9 A. Right. The 2006 value is an average. And I -- if you
10 look at the response to the Co-op IR it essentially takes
11 the two-year period from 2004 to 2006 as the basis for
12 that computation. And I can -- I can give you the
13 detailed data sheet that supports that table.

14 So it is essentially taking not just 2006 but the
15 period from July '04 to June '06, the two years prior to
16 the introduction of regulation that gets you to that 98
17 cent average price. And that is a volume weighted
18 average.

19 The price in 2008 is for the month of June. Again I
20 think one of the IR's had questioned that. And it was an
21 error on my part. It should be June, not May.

22 Q.149 - Yes. And I think that was an IR from the Department
23 of Energy?

24 A. Right.

25 Q.150 - But if you could just back up to the 2006 entry, I

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think you said that was an average of --

A. That is average of 2004 to 2006, from July '04 to end of June '06.

Q.151 - And is that January 1, 2004 to the end of --

A. July '04 to --

Q.152 - July '04?

A. -- June '06. Yes. Two years.

Q.153 - Is there some rationale for why you took those -- that particular time frame as opposed to the period of time just prior to regulation or maybe May of 2006?

What was the rationale for picking those months?

A. Well, the rationale for pricing the period leading up to regulation was that it, as I understand it, formed the basis for the margin that was applied in July of 2006. In other words, these values would have been consistent with the cost base over that same period, okay, that this price applied to credit cards.

The use of June '08 rather than a long-term average in my view would make more sense, since it is the more likely price going forward than a long-term average. In other words, it is more likely you will see prices in the \$1.25, \$1.35, \$1.40 range looking ahead than you will see prices in the -- you know, in the 90, 95 cent range.

So again, the computation I believe for the

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contribution to the margin should reflect as closely as possible current circumstances.

Now the difficulty of course this presents is that if this is done on an annual or a biannual basis, given the way prices fluctuate, it could rapidly become dated, either too high or too low.

So I guess it is another example, going back to some earlier questions, of a variable that has a substantial effect on the net margin over which the dealer has really no control, that could I think easily be computed to form part of, you know, the week to week margin setting, since it is a function of price.

Q.154 - But this though -- this is an important factor for the Board. Because it has a significant impact on the total recommended change.

A. Right.

Q.155 - So that entry for 2006, I think wants to be as reflective as possible of the differential in the two years since regulation.

So is it still your view that the two-year average is appropriate? Or would a figure from June of 2006 perhaps be more appropriate?

A. Well, my view is that the margin, the 11 cent margin that was selected, as I understand it, was based on

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2 conditions in the two years leading up to the introduction
3 of regulation. And so this is the cost base that would be
4 consistent with that period, 98 plus cents.

5 If you used a month -- I mean, take your pick. They
6 range from 96 cents to \$1.12 in the six months leading up
7 to the introduction of regulation. So there is
8 considerable variation there.

9 But I think the key point is to try to make the base
10 upon which, you know, the comparison is made as consistent
11 as possible with the base that determined the margin to
12 begin with, which is the two years, as I understand it.

13 Q.156 - You indicated that in table 4.1 it was an April to
14 August entry for July of 2006?

15 A. On table 4.1, yes.

16 Q.157 - 4.1?

17 A. Yes.

18 Q.158 - Why did you not use that same rationale then for table
19 4.2?

20 A. In the case of -- in the case of credit cards, this is
21 a factor that -- to which the margin is highly sensitive.
22 I mean, it varies literally from day to day.

23 So I think the ideal from my perspective would not be
24 to tie the future setting for a year at a time or two
25 years at a time, but rather to have it fluctuate with

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2 prices.

3 So the more flexible or the more -- yes, the more
4 flexible that that setting can be, I think the better off
5 it is for, you know, for retailers who are facing these
6 costs.

7 In the case of carrying charges, the carrying charges
8 are not going to fluctuate. They are not driven by a
9 variable that is as sensitive to market conditions as is
10 the price of fuel. And so it seems to me entirely
11 consistent to use a price which is indicative of future
12 levels rather than a longer term price.

13 CHAIRMAN: Ms. Desmond, before you leave that line of
14 questioning, one of the questions I think that you put to
15 Mr. Gardner with respect to table 4.1 I believe was "Can
16 you redo that?" And I believe he said yes.

17 Was that intended to be an undertaking?

18 MS. DESMOND: Yes, it was, Mr. Chair. And perhaps if
19 Mr. Gardner might indicate how quickly --

20 CHAIRMAN: That was my question, if that was intended as an
21 undertaking.

22 Mr. Gardner, could you perhaps let us know how long
23 that would take to do that calculation and to provide us
24 with the amended table 4.1?

25 I don't expect that you will do it sitting there,

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but --

WITNESS: I mean, I do have my -- I don't have a printer here. But the computation itself could be done fairly readily.

CHAIRMAN: Is that something that if for example your testimony were completed today that you could work on and provide potentially by tonight or tomorrow?

WITNESS: Yes.

CHAIRMAN: And that was, as I understand it, Ms. Desmond, the single undertaking, was to redo table 4.1, is that correct?

MS. DESMOND: Yes. That is correct, Mr. Chair.

CHAIRMAN: Thank you.

Q.159 - And with respect to credit card costs -- and I know there has been some reference to anecdotal information. And I believe that is the case with credit card usage. You reference an increase in credit card usage. And I have got, you know, sort of a collection of information that was provided to you.

How comfortable are you, Mr. Gardner, that that is a reliable estimate?

A. I'm comfortable that the current level of usage is in the 40 to 45 percent range. Whether it started from 30 percent or 35 percent or 25 percent, I'm less confident.

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2 Because we asked the question of -- in the questionnaire
3 we asked the dealers we were dealing with. We asked the
4 wholesalers, the major wholesalers, the integrated refiner
5 marketers the same questions. How much has this changed?
6 What was it four years ago or an average of two to three
7 years ago? What is it now?

8 This represents I guess our best assessment of what
9 those numbers look like. And it is anecdotal. It is
10 important. But you know, I'm afraid that is the best we
11 could do with the information we had available.

12 In the course of discussing this with the major
13 wholesalers who would have I think a better -- would have
14 better systems to track this kind of information, I did
15 ask them specifically if it would be possible for them to
16 document this.

17 Because putting 30 and 45 percent in, even though it
18 is based on a number of -- or input from a number of
19 people, doesn't carry the evidentiary weight that
20 something that is generated based on actual information --
21 you know, it wouldn't carry the same evidentiary weight.
22 But we didn't get that information.

23 Q.160 - I do see that you referenced testimony from the
24 States. I think it is the Cannon testimony?

25 A. That is right. Yes.

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2 Q.161 - And I believe that at page 4 of that document he talks
3 about a percentage increase to 40 percent, that that was
4 the increased usage of credit cards?

5 A. Yes.

6 Q.162 - And I'm just wondering why, if that is a document you
7 have relied upon, why you have suggested 45 as opposed to
8 40 percent?

9 A. Well, again Mr. Cannon actually said over 40 percent.
10 If I can read the -- just for the benefit -- I don't know
11 if everybody has read this.

12 But the document we are referring to is a statement by
13 counsel for an organization called the Merchants Payments
14 Coalition pursuant to an antitrust inquiry in the U.S.
15 Congress specifically dealing with credit card companies,
16 Mastercard and Visa.

17 And the testimony walks through how the business is
18 conducted and indicates the -- well, in their view that
19 the practice of Visa and Mastercard in particular in
20 establishing these interchange fees is noncompetitive
21 because they collude with the banks in setting these
22 rates.

23 In the course of his testimony he indicates the
24 amounts of money that are -- that are in question. And
25 they are in the billions of dollars, tied up in just the

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2 interchange fees.

3 On page 4 that counsel just referred to the heading is
4 Merchants Must Accept Visa and Mastercard Brands of Credit
5 and Debit Cards. In 2006 the dollar value of all U.S.
6 general purpose payment card transactions exceeded \$2.7
7 trillion. This represents more than 38,000,000,000 credit
8 card and debit card transactions in the United States
9 alone which account for more than 40 percent of all
10 transactions between merchants and consumers.

11 So the support for the statement in looking for some
12 support for this statement at 45 percent, I came across
13 this document. And it seemed, because it was on point
14 with respect to credit cards, seemed to provide at least,
15 you know, a ball park for the value that retailers and
16 wholesalers in this province have provided us with for the
17 proportion of transactions.

18 On the question of -- which you may be going to, the
19 percentages, we were given a range of percentages by --
20 this is a percentage, the interchange fee, the
21 transactions fee. The lowest was 1.75 in current
22 transaction fees all the way up to 2.3 percent. And this
23 is just for Mastercard and Visa.

24 And those fees vary depending on the number of
25 transactions, the value. And it depends again on the deal

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2 that that particular station negotiates with the credit
3 card companies. And from there the fees go up. So that
4 if anybody is accepting American Express that might be the
5 3 to 3.5 percent range.

6 So what that means is that on -- you know, if gasoline
7 is one dollar, 2 percent of that price goes to the
8 company, comes off the top of the retailer's 5 cent margin
9 or whatever the margin is.

10 As price goes up, the percentage -- I mean, if it goes
11 up to say \$1.50, the price of gasoline, then it is 3 cents
12 off the top. So the margin goes from 5 to 2 cents.

13 A question had arisen in one of the IR's about where
14 is the support for the fee, the size of the fee. And
15 again everyone to whom that question was put, the
16 wholesalers and retailers, the lower bound of the fee was
17 1.75 and the upper bound was 2.3 for the generally
18 accepted cards, Mastercard and Visa. So just to provide
19 in this case a conservative estimate, we used the 1.75
20 percent.

21 The discussion on the size of the fee, if you read on
22 in that document, is on page 13, 14 and 15.

23 Q.163 - I take from your testimony, Mr. Gardner, then that you
24 have used a conservative number for the credit card fee,
25 that perhaps the 45 would not be as conservative a figure?

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A. Yes. It's more difficult to say whether that's conservative or liberal. It represents what many of the people who spoke to that issue used, that the number is -- and some of them are up in the 50, 60 and 70 percent range. So it's probably at the middle.

But as I say, it is anecdotal. And it is unfortunate that the companies in whose interest this number operates weren't more forthcoming in the -- with the details.

Q.164 - I just have one further question on credit card cost. And you might have suggested that in table 4.1 the better approach was to use an April to August average for the July 2008 entry.

Could I ask you to take that same methodology, and using April to August 2008, apply that average to table 4.2?

A. Okay.

Q.165 - Are you able to do that calculation, sir?

A. Yes.

CHAIRMAN: That would be undertaking number 2.

Q.166 - Mr. Gardner, have you ever made changes to the maximum margins that have been made in other regulated jurisdictions since July 2006?

A. Yes.

Q.167 - Can you just provide a brief summary of what those

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changes were and why the changes were made?

A. I just hope I have my dates right. But in Prince Edward Island the Gasoline Dealers Association formally applied for an increase in the margin. And I have a copy of the application document.

The Board there agreed to an increase of one cent that was phased in January 1st. I'm trying to recall whether that was -- I believe it was 2008, in June of 2008, two 5 cent increments.

Newfoundland more recently has introduced a 1.5 cent increase which seemed to be preemptive in the sense that there was no -- at least to my understanding no formal application or no process that heard an application, but rather the Board recognizing that costs had increased and informally, hearing pressure from the retail sector, had directed an interim increase of 1.5 cents.

Q.168 - If you could turn to page 29 please of your report.

In table 4.3 you reference the wage share of margins. Is that a statistical term used by Statistics Canada? Or is that your own term? And what would that incorporate?

A. The wage share -- I guess using it that way it is my term. The basis for that 50 percent share is an analysis, a financial analysis of gasoline stations in New Brunswick compiled by Statistics Canada based on Revenue Canada

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2 information. I have a copy of the financial statement
3 which I would be happy to submit.

4 And essentially what Statistics Canada has done is
5 introduce a service, and it is online, it is web-based,
6 where it provides almost as a guide I suppose to small
7 business, an ability to determine what the financial
8 position of other businesses in your industry is and
9 divides it into, you know, quartiles and so on. And you
10 can go and you can see how well you are doing. You can
11 essentially benchmark.

12 So this analysis for New Brunswick focuses on gasoline
13 stations both incorporated and unincorporated. There are
14 just over 300 in the sample. And it is based on the
15 financial returns to Revenue Canada. So it lays out in
16 some detail the cost structure of the industry.

17 The wage share of operating costs is 49.98 I think
18 percent which we rounded up to 50 percent. We have used
19 the term wage share of margin because the industry
20 essentially operates at something very close to zero
21 profit in the aggregate.

22 So in other words, the entire margin is needed to
23 cover the operating costs, okay. Just to extend that,
24 that analysis shows that 50 percent -- sorry, 51.6 percent
25 of the gasoline stations incorporated -- 306 I think there

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2 are in the sample. 51.6 percent are profitable. So 48.4
3 per cent are unprofitable. And the amount of profit is
4 literally about \$2,000.

5 And this is based on 2004 data. And that analysis
6 will be available for 2006 I think in another month or
7 two.

8 Q.169 - So when you talk about 50 percent of the operating
9 costs and then 50 percent of the wage share of the margin,
10 it is just coincidental that they are both 50 percent. Is
11 that what I'm hearing you say?

12 That the operating cost, 50 percent of that goes to
13 wages and salaries, but that there is a margin and that
14 half of that margin is used just for those operating
15 costs?

16 A. Okay. Because we don't have actual data from the
17 gasoline stations in New Brunswick to form the basis for
18 the analysis, we were I think fortunate to find this
19 source of data. Because for the industry it provides a
20 rich database.

21 It shows and it breaks out several different elements
22 of cost, operating cost. And wages and salaries is one of
23 them. Wages and salaries account for 50 percent of total
24 operating costs.

25 Then the question is how do you apply that or relate

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that to the margin?

And in our approach to this we reasoned that since the industry is only just breaking even, it means that the entire margin is used to cover operating costs, with a negligible amount for profit. So it is reasonable to assign 50 percent of the margin, the 5 cents, to cover operating costs.

Q.170 - Okay. And that has been very helpful.

We do have -- I think what you are referring to is your source document. And perhaps with the permission of the panel we could circulate that.

And you could just maybe walk the panel through those numbers to demonstrate how you got that 50 percent?

A. Certainly.

CHAIRMAN: You have our permission to circulate that provided you give us copies this time.

MS. DESMOND: We also have by way of information the source document that supports the 40 percent in table 4.4. So we will circulate that now as well.

CHAIRMAN: Thank you. Okay. Everybody appears to have both of those documents.

Q.171 - So Mr. Gardner, is this the same document you referenced? I think we tried to find your number 1, Statistics Canada?

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2 A. Yes.

3 Q.172 - Okay. And can you explain how you got to that 50
4 percent based on the source data?

5 A. Sure. If you go to the line Operating Expenses, it
6 shows 177,000 as the average.

7 Q.173 - Just for the benefit of other people in the room, we
8 are talking about the gas stations 2004?

9 A. That's right.

10 Q.174 - Thank you.

11 A. So looking at line 1, 2, 3, 4, 5, 6, 7, Operating
12 Expenses, it is the third line in bold, it shows an
13 average of \$177,000 for the industry as a whole. That is
14 per station.

15 And directly under that, labour and commissions is
16 \$88.4 thousand. That is where the 50 percent came from.

17 Q.175 - I think when we were looking at this source document
18 there is an entry for wages and benefits, right under
19 "Cost of Sales".

20 I'm wondering how you account for that now based on --
21 I guess how does that fit into your 50 percent?

22 A. Well, I think that relates to the acquisition of fuel
23 which is the primary product, and possibly other items
24 that the gasoline station may sell. But that's related to
25 purchasing the inputs rather than selling the outputs.

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2 Q.176 - And on the next page and your reference to 40 percent
3 of the wage share of margin for heating oil -- could you
4 perhaps -- it is the document entitled "Petroleum Product
5 Wholesaler Distributors, 2004."

6 A. Right.

7 Q.177 - Are you able to maybe just walk us through how you got
8 to that 40 percent?

9 A. Sorry. I'm just going to -- yes. This one I used the
10 same -- the same basis, the 116/261, but adjusted it
11 downward. Again to -- in this case to reflect -- so that
12 computation works to 44 percent. I got it down to 40
13 percent based on the input from the industry, and also in
14 part because this was as close as we could get, you know,
15 to heating oil.

16 It is not exactly the same business. It is
17 wholesalers and distributors. And even though we are only
18 talking four percentage points, just based on the
19 information we got from people in the business, it seemed
20 that 40 percent might be a more accurate picture of the
21 labour cost.

22 Q.178 - Just a minute ago you referenced the profitability of
23 different retail service stations and the difficulty that
24 businesses were having in their operations.

25 When you talk about profitability does that refer just

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to motor fuel sales? Or are you including the profitability of all business loans including all petroleum operations?

A. I'm referring to the profitability of the gasoline stations as they are configured in the province. Now clearly some are more profitable than others. But the reference includes all lines of business.

Q.179 - And that is the 2004 Statistics Canada study?

A. That's right. The --

Q.180 - I was just going to ask if you might make a copy of that available as an undertaking?

A. Sorry. When you say that --

Q.181 - It was a reference to the 2004 StatsCanada study?

A. Well, so we are talking about the same thing, I mean, we retrieved this from the StatsCan website, okay. So it is the same document, yes.

The version I have breaks it down by size of firm into quartiles. So there is I guess a richer analysis available there.

But your question I think goes to whether or not in this case non-petroleum revenues are included. And they are. This represents all gas stations, independent gas stations in the province.

Q.182 - Given that statistic of the level of businesses that

1
2 are struggling, why is it that we have so many retail
3 operations still continuing to operate in New Brunswick?

4 A. I think until the capital completely runs out, in many
5 cases it is less expensive to stay in business than it is
6 to get out. There are substantial costs associated with
7 exiting the industry, associated with environmental
8 cleanup, pulling out tanks and so on.

9 Why people do it -- if you look at this statistic
10 where 51.6 are profitable -- 51.6 percent are profitable
11 and 48.4 percent are unprofitable, that is not a snapshot.
12 I mean, if you go back and look at this in 2002, 2000 the
13 same proportions are there. So people are just getting
14 by.

15 But when you look at what is critical for a company,
16 particularly an independent retailer in a rural or remote
17 area, there is no capital to reinvest. There is no
18 capital to expend.

19 In Michael Ervin's report he talks about non-petroleum
20 revenues. And believe me, I mean, there are many, many
21 stations in New Brunswick in rural and remote areas who
22 would love to have a C-store or a car wash. But there are
23 two impediments. (1) they don't have the capital and (2)
24 they are not in the right location.

25 And so the notion that non-petroleum revenues are

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2 somehow going to rescue the industry I think is misguided.
3 It cannot happen. It happens in certain locations for
4 certain well-capitalized companies. But generally it is
5 problematic.

6 Now just before I leave that point, unfortunately in
7 the case of New Brunswick this StatsCan or Industry Canada
8 small business profile breaks down the gasoline industry
9 into two parts, incorporated and unincorporated.

10 If we look at Nova Scotia, whether the question was
11 asked a little differently or whether the results were
12 submitted a little differently, the report breaks down the
13 industry into two parts as well, gasoline stations with
14 convenience stores and those without, another category.

15 The number of businesses with convenience stores
16 number 100. 52 percent are profitable. 48 percent are
17 unprofitable. In the gasoline stations without
18 convenience stores, the data show -- and there are 248 of
19 those -- the data show that 77.5 percent are profitable.

20 Now it is difficult to know what kind of inferences to
21 draw from that. But I guess if I were getting into the
22 business, I'm not convinced that unless the location were
23 ideal, I would put in a convenience store.

24 Because it is not axiomatic that this makes a business
25 more profitable, judging from the data from Nova Scotia.

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2 And I think those stations are broadly similar to the ones
3 we would find in New Brunswick.

4 Q.183 - But should not at least some of the costs that would
5 be related to non-petroleum sales be -- shouldn't those
6 costs be attributed to those other parts of the business?
7

8 Is there some fashion or mechanism by which you can
9 make that analysis?

10 A. Well, again we asked that question on the survey. And
11 we didn't get enough response to make a difference. But
12 ideally, sure, you would want to have a breakdown of both
13 where the revenues come from and where the costs go.

14 But in the absence of that detailed breakdown, if you
15 make the assumption that 50 percent of those costs would
16 be attributable to the back store and 50 percent to the
17 pumps, you are still looking at 50/50.

18 And I think 50 percent is not unreasonable, again
19 given the limited information we have from the industry,
20 coupled with what we see for, you know, the business or
21 the gasoline stations without convenience stores. It is
22 still in that range.

23 Q.184 - I wanted to just reference then -- there was an IR
24 from the Department of Energy. I'm sorry. It was a
25 report from the Department of Energy in the report of M.

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J. Ervin.

And he has a table, table 3, if you could just maybe turn to that.

Now I stand corrected. I'm told it is in an IR response that was posed by the Board to M. J. Ervin. I'm sorry about that. But it is table 3, if you are able to find that reference. It is in the IR's to Mr. Ervin.

A. Yes. If you have a copy of that somewhere, but -- thank you. Yes.

Q.185 - And I'm just actually comparing your report, page 29, right under "Minimum Wage", where you suggest that the minimum wage in New Brunswick has risen by 19 percent. And then his response to an IR, table 3. And he has significantly different percentages of wage increases.

And I'm wondering if you might want to comment on the data that has been provided in table 3?

A. Our survey of the retail gasoline dealers indicated that virtually all the pump attendants and workers, other than skilled mechanics, worked essentially for minimum wage.

Since July 1st of 2006 the minimum wage in New Brunswick has gone up by 19 percent. And those statistics are available from -- I think it was \$6.30 to 7.75 over that period.

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2 Q.186 - Yes. I think that you have in your report at page 29?

3 A. Right.

4 Q.187 - 6.50 to 7.75?

5 A. Yes. And so applying that to the wage bill, you know,
6 suggests that the industry is facing a major cost crunch.
7 I don't know how you would compare an industry-specific
8 statistic, the sector specific in the case of gasoline,
9 with one that covers the entire retail trade industry.

10 And to suggest that weekly earnings in the retail
11 trade rose by only 3.6 percent from '06 to '08, you know,
12 if that is what the stats show, that is what the stats
13 show. I don't know.

14 But many people in the retail trades also work,
15 broadly speaking, in convenience stores, in grocery
16 stores, in department stores, in shopping malls, you name
17 at, work at minimum wage.

18 How they either escape the law or misreporting is not
19 clear. But for wage earners only in that industry it is
20 surprising that we have only seen a 3.6 percent increase.
21 I can't explain the difference.

22 Q.188 - My next question is with respect to full service
23 charge. And I believe in an IR response you did provide
24 information about the full service charges in other
25 Atlantic markets.

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2 Based on the information that you have provided to the
3 Board in your report in the IR responses, do you have a
4 recommendation for the Board as to what an appropriate
5 charge would be for full service?

6 A. Well, I understand that the Board can't simply by
7 regulation lift the cap. But based on what we have
8 observed in Nova Scotia, where again there was a
9 recommendation or a report a year or so ago that said lift
10 the cap, and they were similarly constrained, they didn't
11 lift the cap. They set it at \$999 I think or something
12 like that. So there is an abstract cap which is never
13 achieved.

14 But the analysis that the regulator in the province
15 has conducted weekly surveys by zone in the province of
16 many of the full-serve and split-serve dealers that would
17 have been affected by the removal of the cap, and they
18 found that on average the dealers increased their prices
19 by a cent or so. And it varied between rural and urban.

20 But at the outer limit, the more remote stations, in
21 most zones -- now I can find the actual table here -- in
22 most zones the maximum went to one to two cents over the
23 full-serve.

24 Q.189 - Mr. Gardner, perhaps I could have panel members turn
25 to that document. Because I believe you did provide it as

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a response to an IR. And it was a response to an EUB IR.

A. IR number 1 I believe.

Q.190 - Number 1? Thank you.

A. And there is a table at the back of the IR's that summarizes the month-by-month changes in six zones in the province.

So essentially what the dealers are subject to is the competitive environment. So they are free to raise their full-serve charge to what the market will bear. And what the market bears depends on how far the next station is away, whether it is full-serve or split-serve, a number of those kinds of competitive factors.

And in only one zone had dealers in the rural part raised their prices into the 4 to 5 cent range above the full-serve price.

In most zones the shift falls in the 1 to 2 cent range, 2 cent per litre range. And that is above regulated full-serve.

So lifting the cap hasn't meant that most dealers are able to raise prices indiscriminately. They are still governed by the competitive environment.

If there were a number you had to pick -- and this is based on the outside limit in Nova Scotia in rural areas - - it is somewhere in the 4 to 5 cent range.

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2 But as I say, in most cases, in rural areas there is
3 very limited latitude to price above the -- significantly
4 above the self-serve limit.

5 Q.191 - I appreciate that you are looking at Nova Scotia
6 information. But would you make that same type of
7 recommendation here in New Brunswick?

8 A. Well, the recommendation in the report was to lift the
9 cap and let the market settle where it may. And I
10 understand that there is a regulatory problem with doing
11 that.

12 So you know, limiting the increase, you know, to 10
13 cents over self-serve would probably see in some areas as
14 much as 3, 4 or 5 cents over. But at least it would give
15 the retailer the opportunity to -- or a greater
16 opportunity to realize a margin that worked.

17 But again, the dealers in New Brunswick who provided
18 specific comment on the margin suggested that a margin in
19 the 4 to 5 cent range, these were rural dealers, would be
20 more appropriate in their circumstances. And they felt
21 that they could charge those kinds of prices.

22 Q.192 - Okay. Our next line of questioning is to delivery
23 costs.

24 CHAIRMAN: I'm just wondering how much longer your cross
25 examination might be. Because it was our intention to

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have an afternoon break.

MS. DESMOND: Perhaps we should have a break now. I'm going to be probably another 20 minutes or so.

CHAIRMAN: Okay. We will take a 15-minute break then.

(Recess - 3:00 p.m. - 3:15 p.m.)

CHAIRMAN: Ms. Desmond, before you proceed it has been brought to my attention -- and perhaps it is partly because of the fact that Mr. Gardner is unrepresented, but is here as a result of having been retained by the Board.

But the Board didn't actually qualify him as an expert. And I suspect that maybe Mr. Ervin might ask -- or his counsel may ask to have him qualified as an expert.

Does anybody here have any objection to the Board qualifying Mr. Gardner as an expert?

Mr. Zed, I see you with your hand on the microphone.

MR. ZED: I have probably known Mr. Gardner for about 40 years. And I certainly would have no objection of him being qualified as an expert.

CHAIRMAN: And Mr. Hoyt quite frankly asked the type of questions that one might ask leading up to it. But if there is any objections -- does anybody wishes to ask any questions on that?

MR. HOYT: I certainly have no objection.

CHAIRMAN: Okay.

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2 MS. DESMOND: Mr. Chair, can I suggest that Mr. Gardner be
3 declared an expert, I guess as an energy economist with an
4 expertise in petroleum products, if that is an appropriate
5 area of expertise.

6 CHAIRMAN: I think that would do it. And again is everybody
7 okay with that?

8 All right. He is so declared as an expert. So you
9 can proceed, Ms. Desmond.

10 Q.193 - Mr. Gardner, our next -- a few questions related to
11 delivery costs.

12 And with respect to motor fuel could you please
13 explain how you arrived at a 3 cents per litre as an
14 appropriate maximum delivery cost?

15 A. We asked the wholesale companies for delivery costs to
16 each of their stations. We reviewed data that the
17 companies had supplied to the Board on delivery charges.

18 We -- I met with one of the transportation companies
19 to review their method of charging for fuel delivery. We
20 asked retailers throughout the province what they were
21 paying to wholesalers for delivery costs.

22 On the basis of that, the number that sort of popped
23 out of the analysis was something between 2 and 3 cents at
24 the outer limits in areas in northeast, northwest of New
25 Brunswick.

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So recognizing that this isn't a specific value but rather an up to amount, that 3 cents in the current and anticipated price environment, seemed to capture the outer range of what was likely to occur within the next year or so.

Q.194 - Perhaps without identifying any particular community, could you indicate what the highest delivery cost is that you found in the course of your review?

A. I think I have a table here somewhere that sets out that information. If I can just remember who asked the question.

Q.195 - I believe it was IOL number 14.

A. Yes. Table 2 in the IOL response. This is I guess a sample of charges we included in table 2. And I see Caraquet, Edmundston.

There are two areas, two locations where we withheld the name because it would have been so specific I think to identify the retailer and the supplier and Pointe-Sapin as well. So there are five listed here that are 3 cents or more. And all the rest are in the 2 plus cent range.

So even at 3 cents there are two here that exceed that amount or at least did exceed that amount during I guess what we would call the peak that was realized in the July period.

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2 Q.196 - Are there any communities in New Brunswick where there
3 is only one petroleum retailer?

4 A. Well, I'm sure there are many. But we haven't visited
5 them all. So I'm not sure how to answer the question.
6 But I'm sure there are.

7 Q.197 - Moving then to heating fuel at the bottom of page 33,
8 you have got a recommendation I believe, increasing the
9 maximum delivery cost by one cent per litre?

10 A. Yes.

11 Q.198 - But if I read the bullet point just at the bottom of
12 that page, there is a reference to what that one cent per
13 litre includes. And it includes the 0.75 cents per litre
14 for the actual increase in fuel cost.

15 And I believe the 0.25 cents is for anticipated or
16 future cost, is that correct?

17 A. Well, it is -- it is one cent. It is not adding
18 anything to it. It is one cent based on the 15 percent
19 increase in costs. But the allowance -- it would provide
20 an allowance for future price increases.

21 Q.199 - And I guess that is the distinction I'm trying to
22 make. You have got a piece there for actual costs plus a
23 percentage for future cost increases, is that correct?

24 A. Well, I'm suggesting that the one cent per litre would
25 cover the increase in cost and at the same time provide an

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2 allowance for future increases, in other words, that going
3 to 3 cents would provide for costs in the -- let's say
4 2.2, 2.3, 2.4 and in anticipation of future increases up
5 to the 3 cents.

6 So it is not adding anything to the one cent. It is
7 simply anticipating it.

8 Q.200 - I believe the delivery on heating fuel though is 5
9 cents?

10 A. Well, but the -- I guess the point I'm making is that
11 this one cent, following the same logic as the gasoline
12 and diesel, it is the same trucks, it is the same range of
13 destinations, that one cent would increase, would provide
14 enough ground for the delivery at least to the bulk
15 plants.

16 I have made a distinction in the analysis that heating
17 oil companies are essentially transportation companies.
18 They are storage and transportation companies. And as
19 such their operating costs capture. And in some cases
20 that 13 cent per litre margin is made up largely of
21 transportation costs.

22 So it is kind of -- the way the margin is broken down
23 is artificial, let's put it that way, in the regulations,
24 that it doesn't reflect accurately how the businesses or
25 the diversity in the businesses and their cost structures.

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2 As I think the note -- there are a couple of heating
3 oil dealers I spoke with. Their distribution costs, that
4 is before the fuel gets to them -- sorry, after the fuel
5 gets to them, their distribution from their bulk plants to
6 their customers is in the 10 cent per litre range, out of
7 the margin of 13 cents.

8 Q.201 - How did you arrive at that 15 percent increase in cost
9 for delivery on heating fuel?

10 A. Using the same approach as for gasoline and diesel
11 fuel. When I looked at the change, you know, in the pre
12 and post regulatory period, the increase at the start, I
13 think the fuel adjustment -- or the delivery cost plus
14 fuel adjustment was something in the order of 1.2 and it
15 had risen to 1.45 cents per litre on average.

16 So it worked out to about a 15 percent change. But it
17 was the same -- the same figure as for gasoline and
18 heating oil.

19 Q.202 - If you could still look at that table 2 which we just
20 referred to. Can you perhaps just explain the indicative
21 freight rates including fuel surcharge that you reference
22 at the bottom of that page?

23 A. Sure. These rates were provided by -- it is an
24 amalgam of two or three wholesale companies who provided
25 these rates. And for specific locations the actual rate

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had increased.

Because what I had asked each of the wholesalers to provide us with was a buildup over a period of months from the start of regulation to -- at the time we did the survey it was in June, July of 2008 -- was to ask them for specific rates in those months. And they had provided that or at least some of them provided that before I met with the transportation company.

And what the transportation company provided was the formula to actually compute the fuel adjustment charge, which at this point I wasn't aware of yet.

So what this reflects is for specific locations the actual transportation cost including the fuel adjustment charge. So you can see the buildup of how that occurred. And this kind of buildup would have occurred for a variety of stations around the province.

Q.203 - I don't see any reference to what the first line of data is versus the second line of data?

A. These are two locations, okay. And I had left them off deliberately. Because the source wanted this to remain confidential.

Q.204 - You have created that chart I guess with the data from two companies. Is that representative of --

A. Yes. The rates -- the rates that the companies charge

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2 vary very slightly to -- you know, there can be a slight
3 difference in the fuel adjustment charge. There may be a
4 slight difference in the fixed component of the charge.

5 But at the end of the day, at current levels, you
6 could probably reliably say that for extended hauls you
7 are looking at 6/10 of a cent per hundred or 7/10 of a
8 cent per hundred kilometers.

9 I mean, there are different rules of thumb, \$75 an
10 hour depending on the type of truck to \$85 an hour of
11 delivery time is another way of looking at it.

12 And you can look at the total litres, 50,000 litres
13 and work out over a three or four-hour haul what the per
14 unit is. But I think using 6/10 to 7/10 of a cent would
15 capture the range.

16 Q.205 - In the recommendations you have differentiated between
17 the increase for wholesalers and the recommended increase
18 for retailers. I think it is one cent per litre for
19 wholesalers and 0.2 cents for retailers.

20 Can you explain why you have presented it in that way?

21 A. Well, I presented it that way because there are a
22 couple of components there. One is the delivery from the
23 refinery or the storage to the heating oil bulk plant
24 which is captured by the 5 -- notionally captured at least
25 by the 5 cents.

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2 The .2 cents per litre is meant to reflect the fuel --
3 just the fuel cost share of total operating costs, which
4 based again on information provided came to about 10
5 percent of the operating costs of the retail heating oil
6 dealer.

7 And so applying the increase in operating cost, the 15
8 percent against the 10 percent share against the 13 cent
9 per litre margin gets you to 2/10 of a cent.

10 Q.206 - It just would appear to me that that 0.2 cent is
11 really not an operating cost --

12 A. It is --

13 Q.207 - -- it is a delivery cost?

14 A. It is an operating cost. But it is the estimate of
15 the delivery component of operating costs. It is a way of
16 getting at what these companies really do. They are
17 transportation companies.

18 And as I said in the introductory remarks, it is just
19 a bit artificial to have this 5 cents out there when the
20 13 cents is really capturing what the companies do. And
21 that is to deliver fuel.

22 Q.208 - Mr. Gardner, I just want to look at your addendum, the
23 propane addendum that was filed separately from your
24 original report. And I'm looking at page 2 of that
25 report.

1
2 And you have got two sort of tables on page 2. And
3 I'm wondering if you might explain how you arrived at the
4 18 percent and 82 percent that you have got documented on
5 those two tables?

6 A. Well, this is -- propane is about the most opaque
7 segment of the energy industry in the province. There are
8 no published prices other than for transportation. So
9 heating fuel, unless you are a buyer yourself, going to
10 the company and asking for price data, is going to not be
11 very rewarding.

12 Because I did ask that of two of the major companies.
13 And that was too sensitive. So I didn't get that
14 information. The propane rack price I obtained from
15 Shell, who were quite happy to provide it on request.

16 But in order to get some kind of history of the
17 margin, the 50 cents that is allowed in the legislation,
18 it is difficult to find, impossible to find a series that
19 would go back a period of years to be able to determine
20 where that 50 cent per litre came from.

21 So without having a clear sense of where the 50 cents
22 came from, I understand -- I presume that when the
23 original margin was set that the regulator had input from
24 industry.

25 Although neither of the companies that I met with, you

1
2 know, was prepared to allow, you know, where that number
3 might have come from. But both agreed that it seemed a
4 reasonable guide to the margin prior to regulation.

5 Now when it comes to the delivery costs, I asked the
6 companies what does it cost to move product from Sarnia to
7 Moncton. And again I did get information on a cents per
8 litre basis, that to make sense of producing a table that
9 was consistent with the approach used in the rest of the
10 report, I rendered as a percentage of the overall margin,
11 since that is what has to cover that transportation cost.
12 There is no wholesale segment in this industry to speak
13 of. It is primarily retail.

14 So the retailers essentially occupy that 50 cent
15 marketing margin. And the amount of the cost, or the cost
16 two years ago, was approximately 18 percent of the 50
17 cents, okay, 9 cents.

18 And I was given the end point. Taking the 15 percent
19 used as a guide to the increase in transportation costs,
20 it implies an impact on a gross margin of 1.35 cents per
21 litre.

22 So it was industry information on the cost of delivery
23 from Sarnia to Moncton that provided the basis for this 18
24 percent, okay.

25 Q.209 - I note that you have a note "Subject to verification."

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What does that mean?

A. Well, it means that I didn't receive a document that laid out prices the way I did for gasoline and for heating fuel in discussions with retailers.

The industry is -- propane industry is very, very sensitive about its information. There are limited numbers involved. And giving one source effectively gives the other the competitive information it needs.

So it was very difficult to extract useful information, let's put it that way, in this industry. And this is about the best I could do.

Q.210 - Could you also explain, when you look at the increase in freight cost -- first there is the increase in operating cost -- how did you arrive at that breakdown of 15 percent and 6 percent?

A. Again the 15 percent reflects the same percentage used for gasoline and diesel fuels and heating oil in the province. So it is as simple as that. I just used that as a guide.

And the basis for that is essentially in the increase in diesel fuel costs, since that reflects the fuel adjustment charge and it reflects what a large user like CN would be using, okay.

Q.211 - And perhaps you could just identify, where you have a

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2 delivery allowance on page 3 of your report, what is the
3 distinction then between that delivery allowance on page 3
4 and your transportation information on page 2?

5 A. The delivery allowance is from the bulk plant to the
6 customer, okay. So it reflects the delivery allowance in
7 the last column on the price sheet that the Board
8 circulates, okay, that 10 cents.

9 And again it reflects the cost or the increased cost
10 of fuel, diesel fuel over the period, 15 percent.

11 Q.212 - I don't think you addressed the 6 percent at the
12 bottom of page 2. I'm not sure that I heard that
13 explanation.

14 A. That is based on the GDP deflator, for lack of a
15 better term. You have a 6 percent annual -- sorry, 3
16 percent annual increase over two years. It is a 6 percent
17 increase. That is a StatsCan inflation figure.

18 Q.213 - Mr. Gardner, I see in your report that you also have
19 allowed an increase for the levy fee based on the
20 regulated levy fee --

21 A. Right.

22 Q.214 - -- that must be paid?

23 Now the levy fee arguably was understood to be part of
24 the legislative regulatory scheme. The legislation was
25 put in place in 2006.

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2 Would you agree that perhaps when the government
3 introduced this legislation in the regulations that that
4 was anticipated, that that levy fee would be a necessary
5 piece of what would have to be paid, and as such set the
6 margins accordingly?

7 A. Well, I have no specific information about what the
8 regulator might have incorporated into the original margin
9 when it was set.

10 Q.215 - Or when the government introduced the legislation?

11 A. Right. Yes. I don't know. If that is the case then
12 perhaps it shouldn't be there.

13 Q.216 - And Mr. Gardner, you are aware that there was changes
14 to the legislation in 2007. And I don't believe there
15 were changes to the levy or how changes -- how the level
16 was to be recouped at that particular point in time?

17 A. Right.

18 Q.217 - So is it fair to say that the intent of the
19 legislation is that perhaps the wholesalers are
20 responsible for that levy and not the consumers?

21 A. Well, if it was intended to be part of the margin then
22 consumers are responsible. If it's not intended to be
23 part of the margin then wholesalers would be responsible,
24 recouping it out of costs somewhere. But I don't think
25 you can have it both ways.

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2 MS. DESMOND: Thank you, Mr. Gardner. Those are all my
3 questions.

4 CHAIRMAN: Thank you, Ms. Desmond.

5 Any questions from members of the panel? Mr. Radford?

6 MR. RADFORD: No, Mr. Chairman. That is fine.

7 CHAIRMAN: Mr. McLean?

8 MR. MCLEAN: No.

9 CHAIRMAN: Mr. Toner?

10 BY MR. TONER:

11 Q.218 - I have a few questions now that you are deemed an
12 expert I guess.

13 My question relates to volume of litres. Because you
14 make reference to the retailers in the province. There
15 are different types of volume, as small as 200,000 litres.

16 A. Mmmm.

17 Q.219 - Can you give me a breakdown of the number, of the 470
18 dealers? Like are they broken up into three categories
19 and what those categories are for? Or is a breakdown --
20 is there such a breakdown?

21 A. There may be such a breakdown, but -- and I had hoped
22 to use Board data to try to determine what categories
23 dealers might fall in.

24 But it is incomplete, let's put it that way. The
25 information that has been provided to the Board doesn't

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allow for that kind of calculation.

Q.220 - So when you talk about a rural dealer and an Irving dealer -- I'm going to give you an example, like the Irving Big Stop in Salisbury is a high volume?

A. It is a big Big Stop.

Q.221 - Is it a rural dealer? Or is that an urban dealer?

A. That is a rural dealer in an urban environment.

That's a -- you know, that's a multimillion litre a year operation.

But it is -- in my view it is an urban dealer that happens to be in a rural area. But it is on the main highway. I stop there frequently.

Q.222 - So I take it that it is an urban dealer?

A. Well, I mean, it is an urban capacity, let's put it that way. I mean, the volumes are such that it would conform to what you would expect to see in a major urban centre.

Q.223 - Yes. In the report in relation to the credit card fees, because I'm going back down that road, you talk about -- in the report that you gathered here, you are talking about 40 percent. But credit card fees and debit card fees aren't the same?

A. No, they are not.

Q.224 - And they are quite a bit different?

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2 A. Yes.

3 Q.225 - So when you have reflected in this report that you
4 took your data from, which is from the U. S., when it
5 states -- it states that this represents more than
6 38,000,000,000 credit card and debit card transactions,
7 represents more than 40 percent of the transactions.

8 I find that this conflicts with your 45 percent that
9 you are using. I'm having difficulty with your 45 percent
10 average --

11 A. Mmmm.

12 Q.226 - -- to be honest with you. And because it makes such a
13 big impact on the 58 cents that you are suggesting.

14 And I find that a lot of the data that is gathered to
15 get there is very difficult for me to accept. So I would
16 like you to run down that again. Because if we are going
17 to use this 45 -- I believe there is a cost, let's put it
18 that way, I just don't understand how the real impact is.

19 Because there is no math. It seems to me it is a very
20 easy mathematical calculation for the retailer to give
21 that data. So I guess --

22 A. Yes. Sure. None of the dealers we asked pulled out a
23 record of transactions and said, here it is. None of the
24 companies we asked pulled out a record and said, here is
25 the percentage.

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2 The dealers we spoke with vary in terms of the level
3 of sophistication and running a business. Some of them
4 are -- you know, they could run, you know, substantial
5 enterprises in a number of different disciplines. Others,
6 they are just not that sophisticated.

7 This is more anecdote. But one dealer we met with who
8 was very small, maybe a couple of hundred thousand litres,
9 maybe less, she had no idea of why she wasn't making any
10 money, no idea.

11 And she offered some invoices. And they happened to
12 be records where credit card transactions were kept, all
13 right. They showed up because of the transactions with
14 her supplier. Virtually all her margin was gobbled up by
15 the transaction fee, by the credit card fee. And I
16 pointed this out to her. It was pretty obvious. She
17 wasn't sophisticated enough to pick up the nuance.

18 She was surprised. And she wondered why her
19 accountant had never brought this to her attention. But
20 she in the final analysis was thinking that she was going
21 to get out of the gasoline business altogether because it
22 just didn't pay.

23 So when we go to see people to ask them for
24 information, there are one or two people, usually the
25 owner. And he is trying to run the station. And he is

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2 doing this, he is doing that and he is distracted. Ask
3 him to fill out forms, it takes time.

4 So the long and short of it is that trying to gather
5 this kind of information in the space of a month or two
6 that we had to do the analysis proved to be very, very
7 difficult. So we accepted at face value the information
8 that people provided us with.

9 And many, many, many of the dealers said, I'm using --
10 I'm getting, you know, 40, 50 percent of my transactions
11 are with credit cards. Because it is costing 70 to \$100
12 to fill the tank.

13 Most people don't have that kind of cash or they don't
14 keep that kind of cash in their pockets. They are now
15 using credit cards whereas before they would have used
16 cash. Yes. No question. Debit cards are in there.

17 But that 40 percent in that report is not what we
18 relied on. What we relied on was the information we
19 obtained from the dealers. And they indicated that it had
20 gone up from 30 percent, 40, 45 percent.

21 And what I had tried to find was some evidence that
22 would corroborate that in a published form. And this was
23 as close as we could get to something that was specific to
24 retail transactions, including gasoline.

25 So I think you are right. And I'm, you know, I guess

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2 a victim of the inability or the unwillingness of people
3 to provide or do the work that it requires to provide that
4 kind of information.

5 But I -- you know, a number of the major companies
6 said that that is not -- you know, it is not a trivial
7 exercise to go back and recreate those files and to
8 document that stuff, so --

9 Q.227 - That it is not trivial?

10 A. It is not trivial.

11 Q.228 - Yes.

12 A. And it is not -- it is certainly not trivial for the
13 individual dealers to go back and do that. It is time-
14 consuming.

15 And they, with all due respect, believe that they
16 have, you know, other things, and some of them would even
17 think better things to do with their time than talk to
18 consultants who are prying about their financial
19 information.

20 Q.229 - Now -- and if you took it now from a number of
21 stations -- because I think like there is 470 stations,
22 but there is a billion dollars of volume -- a billion
23 litres of volume. What -- if we were to get a true -- if
24 we were to go and say, let's get a true number, like let's
25 take the time, let's say take a year and figure that out,

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2 how many -- what percentage of litres would be required in
3 your opinion to give us an accurate figure of this number,
4 to give us an idea of what real percentages of people that
5 use credit card versus --

6 A. Well, I guess if I were, you know, empowered to get
7 that information, I wouldn't -- I don't think I would go
8 to the individual dealers. But I would deal directly with
9 the major wholesalers who end up processing a lot of this
10 information.

11 And if you look at the proportion of gasoline that
12 flows through the integrated refiner outlets, I think you
13 would get a very good idea of the proportion overall in
14 the province.

15 But to ask -- you know, if you have got between 450
16 and 500 dealers or 550 dealers in the province, I think
17 you would want to get at least, you know, 25 percent. And
18 in order to get a good weighted average you would want to
19 have rural and urban and so on and make sure those volumes
20 captured, you know, the industry as a whole.

21 So it is -- I mean, with some thought I think you
22 could probably work out something that is statistically
23 reliable, given the kind of information you are looking
24 at.

25 But off the top I would think you would be -- you

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2 would probably be in the 25, 30 percent of volume that you
3 would want to be looking for.

4 MR. TONER: Okay. Thank you.

5 CHAIRMAN: Thank you, Mr. Toner. Mr. Johnston?

6 VICE CHAIRMAN: Thank you.

7 BY VICE-CHAIRMAN:

8 Q.230 - Mr. Gardner, could you turn to page 21 of your report.

9 This page contains data relating to the marketing margin
10 in Saint John and across the country.

11 What is the source of this data? Did you compile this
12 yourself or your firm?

13 A. No.

14 Q.231 - How did this come about?

15 A. No. The data -- and maybe the print is small, but --
16 my apologies to Mike Ervin there. This information is
17 available on public -- publicly accessible websites. And
18 in this case I relied on M. J. Ervin's website for this
19 information.

20 Q.232 - Okay. On the charts it makes reference to Gardner
21 Pinfold. Is that --

22 A. Just prepared by, just pulling in the data and
23 creating the chart. The data itself comes from M. J.
24 Ervin.

25 Q.233 - All right. Now my next question is with respect to

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2 the margins in cities outside New Brunswick, and
3 particularly western cities, I understand that what we
4 refer to as the marketing margin with respect to Saint
5 John and the upper graph is the pump price as compared to
6 New York Harbour, is that correct?

7 A. That's right.

8 Q.234 - With respect to other cities, let's pick Vancouver, is
9 it -- are we using another base line apart from New York
10 Harbour?

11 A. Yes. In strict terms the marketing margin is defined
12 as, you know, the rack to retail price. So all of these
13 prices are from the local rack price in that city to the
14 retail price in that city.

15 Q.235 - Okay. So these two charts are showing separate things
16 then. Because the upper chart, which is figure 4.2, that
17 is showing rack to retail and New York Harbour to retail?

18 A. That's right.

19 Q.236 - And the bottom chart is showing rack to retail only?

20 A. That's right.

21 Q.237 - Okay. So this is showing in the western cities the
22 growth in the margin between rack and retail and then the
23 reduction. Okay.

24 So these are showing slightly different things?

25 A. Well, yes, they are. Though because -- the lower

1
2 chart is a comparison of relatives. The upper chart is
3 taking Saint John only and showing, you know, how the
4 effective margin, New York Harbour to retail, as well as
5 the marketing margin rack to retail have moved over the
6 last eight years.

7 It is showing the distinction between an integrated
8 refiner, what the acquisition cost to the pump price would
9 be versus let's say a reseller purchasing at the rack
10 price.

11 Q.238 - Okay. Now in the last bullet point above the lower
12 graph it says "The average margin in Canada has increased
13 by just over .6 cents per litre."

14 Can you tell me anything about what that means,
15 "average margin"? Are we dealing with that on a volume
16 basis? Or how is that being handled?

17 A. Yes. That is done on a volume basis. So that is
18 taking the average across all the points where data is
19 collected across Canada.

20 And I can't remember the total number of stations or
21 the total number of cities. It is in the order of 12 or
22 so. And I think they may all be here, where there is a
23 rack price quoted and reflected in a marketing margin.

24 Q.239 - So just so that I'm clear on this, we have in the
25 southern Ontario market where the margins have in fact

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declined?

A. Right.

Q.240 - Because that would be a very large volume area, that is going to pull the Canadian average down?

A. Yes.

Q.241 - Okay. Now there was a conversation that -- well, there was a question and answer this morning with the gentleman from Ultramar regarding delivery charges and the bulk plant situation.

And I'm just wondering if you could elaborate a little bit on that and how the structure of delivery charges under our legislation affects wholesalers who are operating bulk plants.

I'm not sure if I fully understood the difficulties that that was posing.

A. That is probably a question that is best directed to the operator of the bulk plant in question. But in this case Ultramar. But if Mr. Maynard is not going to appear on the stand I will try to take a crack at it.

They charge a fee for deliveries taken from that bulk plant. And I don't know if it is a public number. But in any event there is a fee associated with that. And I have been given a number. Although I have been given a number by a number of different people. So perhaps I can say

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2 what it is.

3 But in any event let's say it is in the range of, I
4 don't know, a cent or so, okay. So from Chatham to the
5 market they serve they are trying to recover their one
6 cent or so per litre.

7 Now their ability to realize that amount depends on
8 the relative cost, delivered cost of fuel from the
9 refinery in Saint John and to some extent the refinery in
10 Halifax or Dartmouth.

11 And the transportation costs of course are going to
12 vary with distance. But in the area served by the Chatham
13 facility, it starts off charging a cent or so for
14 deliveries taken from that plant.

15 So in effect it is competing with deliveries that are
16 taken from the refinery let's say in Saint John. At some
17 point there is -- before regulation there was a break-even
18 point. However the company sorted out their cost or their
19 delivered costs.

20 In this environment, in the regulated environment, the
21 delivered cost becomes an explicit part of the final
22 product price in the sense that the wholesaler has to or
23 is supposed to show it as a distinct segment of the price,
24 so that the retailer knows how much he or she is allowed
25 to add to get at the maximum or the total rather retail

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2 selling price.

3 So exchange the competitive dynamic. Because now,
4 depending on where you -- from whom you are buying your
5 fuel and how far it goes, and depending on competitive
6 conditions in that market, you are either able to or not
7 able to pass along the full cost of delivery.

8 So if the wholesaler purchasing from the refinery in
9 Saint John is saying right, that has cost you 2 cents, so
10 here is -- your all-up cost is now 13 cents -- say it is
11 in a northern community -- if you want to buy from
12 Ultramar or, you know, you may have a better price from
13 Ultramar for your fuel, but the cost of operating that
14 facility plus the delivery cost may leave you in a
15 disadvantageous position.

16 So you either have to, you know, roll back your
17 selling price, including the distribution -- or the
18 storage charge, or lose the customer.

19 And I think what has been happening in some of these
20 markets is that because the market price is now driven by
21 the lowest cost supply into that market, it has become
22 more difficult for companies with storage to compete.

23 Before, the price was not necessarily driven by that
24 least cost distribution. It was driven by market forces.
25 Transportation was in there somewhere. But there wasn't

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2 an explicit limit that said you may only charge this much.
3 Now -- at least that is my sense of it.

4 One of the difficulties -- and we went to a number of
5 retailers and asked them what is your transportation cost
6 to get the fuel here? They couldn't tell. Because it was
7 rolled up into the price. Or how are you determining what
8 your maximum price is? They said well, we priced it off
9 the station down the road.

10 So I think we have got a sense of how regulation is
11 supposed to work. But how it is actually working, not
12 just in the rural areas but out there, I think retailers,
13 many of them don't have a very clear sense of how it is
14 supposed to work.

15 They are behaving the way they used to behave. Maybe
16 they have got an explicit transportation cost that they
17 can show to the Board and maybe they don't. But many of
18 them said, we don't know, okay.

19 So the dynamic -- in a nutshell the dynamic has
20 changed because the price in any given market is now set
21 by the station that has got the lowest cost delivery. And
22 before, that wasn't necessarily the case.

23 And so you had -- competition was, you know, the final
24 selling price, where this variable transportation formed
25 part of that. And now it is explicit. It is taken out.

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It is shown or it should be shown.

And it is more difficult I think for some companies to realize the costs or to recover the costs that they had prior to regulation been able to recover.

Q.242 - So in a nutshell, prior to regulation you had a series of variables that you could compete on. And now the only variable is transportation?

A. Well, it is not the only variable. But it has become an explicit variable. And as a consequence, and because regulation says you may not charge any more than your maximum retail price plus transportation, it has driven the market to the lowest cost -- well, the retailer that has the lowest cost delivery.

Q.243 - Just one final point. Do you have -- have you formed any opinion as to what would be the effect on the continuity of supply if the margins were not increased?

A. Well, I think that -- I think that retailers, some retailers -- you know, the high cost, so the less competitive retailers out there, particularly in rural and remote areas, that we will see further attrition from the industry. Some of that is going to occur anyway.

But I think that not increasing margins could accelerate that. It is a difficult argument in those markets where prices are not now at the maximum, you know.

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2 Why should they increase?

3 And I think the purpose of the legislation is to
4 provide a framework for competition to occur in that
5 allows the industry to move up to a maximum margin as
6 competitive conditions warrant.

7 So I know in some markets, the more competitive
8 markets, particularly in the southern part of the
9 province, the pricing below, you know, the maximum. But
10 those are competitive conditions in that market.

11 We know that circumstances have changed between say
12 Saint John and Moncton because of transportation, that
13 Moncton used to be a lower cost environment but now it is
14 higher cost. Those kind of relative changes have occurred
15 across the province. And you can see that by looking and
16 tracing price changes before and after regulation was
17 introduced.

18 But to go back to your general point, I think that
19 establishing -- or failing to increase the margin is going
20 to compromise the ability of a number of retailers to stay
21 in business, not just retail gasoline but heating oil as
22 well.

23 The sense I get from talking to retailers is a number
24 of them, the first question they ask when you come into
25 the room is, do you want to buy a business? Because a

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2 number of them are in pretty rough shape.

3 But not necessarily because markets -- but margins are
4 limited, that is a factor -- but because of competitive
5 pressures in that industry. There are lots of things at
6 work.

7 VICE CHAIRMAN: Thank you very much. Those are my
8 questions.

9 BY THE CHAIRMAN:

10 Q.244 - Mr. Gardner, it has been a long day. So I won't ask
11 you very many questions many questions.

12 But I am going to take you to the end of page 21. And
13 that would be figure 4.3 which is the change in the
14 average marketing margins. And I think Saint John in that
15 chart is probably -- and I assume that is representative
16 of New Brunswick -- is essentially the only market that
17 shows any significant decline in the margins.

18 And I think from listening to you today, that would be
19 an advantage to the consumer, I think is what you would
20 say and in a situation like that, is that correct?

21 A. Yes. That is correct.

22 Q.245 - Okay. And the converse would be true then. So if the
23 margins had increased that would be an advantage to
24 industry?

25 A. Yes.

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2 Q.246 - And the note on the side of figure 4.3 says that the
3 decline in Saint John is due mainly to the adjustment lag
4 in a rising market.

5 Well, we currently seem to be in a declining market.
6 So would the converse be true? Would that in fact then
7 drive the margins in the other direction?

8 A. Yes. That tends to be the case.

9 Q.247 - This morning in a response to -- I think it was a
10 question from Mr. Zed, you said something to the effect
11 that industry is not very forthcoming with data. I find
12 that somewhat intriguing given that industry has not filed
13 any evidence with us here today.

14 Do you have any explanation? Did anybody explain to
15 you why they were not forthcoming with data?

16 I'm not suggesting names. But what was the rationale
17 is really what I'm wondering about. Particularly whereas
18 I say we don't really have evidence from industry at all.
19 What we have is your evidence and Mr. Ervin's evidence and
20 of course the cross examination and what we will get in
21 argument.

22 Did you get -- were there reasons put forth for that
23 position?

24 A. Well, the main reason I think is that the industry,
25 particularly the refiner marketers, do not want to reveal

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2 commercially sensitive information.

3 And I would be very surprised -- and this is not just
4 New Brunswick. This is -- you know, Nova Scotia as well
5 there was a hearing a couple of years ago. None of the
6 participants in the industry put forward evidence to
7 support a position or another position.

8 I think that they are simply unwilling to risk
9 revealing the kind of commercially sensitive information
10 or subject that information to cross examination.

11 Q.248 - Is that your supposition or was that -- is that the
12 kind of explanation that you got? Or is that what you
13 just imagined must be a good reason --

14 A. Well, that is partly what I have been told. Another
15 reason is that, for some of the larger companies,
16 depending on where they are, the information that is
17 necessary to address some of these issues is consolidated
18 over wide areas. And it would not be again a trivial
19 matter to try to isolate New Brunswick from those
20 operations.

21 So that there is a -- I guess there is a data issue.
22 And there is also -- I think as well there is a cost issue
23 of actually doing the work.

24 Q.249 - Did anybody explore with you the possibility of
25 providing information on a confidential basis such as is

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allowed under the EUB Act?

A. No.

CHAIRMAN: Well, thank you, Mr. Gardner. As I say, it has been a long day for you for sure. And we thank you for your attendance here today.

WITNESS: Thank you.

CHAIRMAN: I guess normally that would take us to our second witness. But it is 4:30.

My understanding, Mr. Ervin, is that you would prefer that the cross examination of your witness occur essentially all at the same time. You don't want to really split it between today and tomorrow.

Is that a fair --

MR. ERVIN: That is correct, Mr. Chairman.

CHAIRMAN: Okay. All right then. Did I understand that there may be one party that has indicated that they would like to make a submission today, if it were relatively short?

Ms. Desmond, is that correct? There was -- for somebody that couldn't be here tomorrow that wanted to make a submission today that had approached you?

MS. DESMOND: I believe there may be more than one. But that is the case, yes.

CHAIRMAN: Okay. Because what I was going to say is if we

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2 had one person and everybody was in agreement to have it
3 sort of done out of order and it was relatively short, we
4 might consider doing that.

5 But I don't really want to get into hearing
6 submissions before we have heard all of the evidence.

7 MS. DESMOND: I believe it was Ms. Savage. She had
8 expressed an interest if it was possible to do her and her
9 submission this afternoon.

10 CHAIRMAN: Okay. I understand Ms. Savage has filed the
11 submission with us?

12 MS. DESMOND: Yes.

13 CHAIRMAN: I'm just wondering. How long would it take you
14 to make that submission? It is not possible for you to be
15 here tomorrow I take it is your problem?

16 MS. SAVAGE: I apologize. That is right. It would probably
17 take me about 10 minutes I'm expecting to make the
18 submission.

19 CHAIRMAN: Well, the only qualification I'm going to put on
20 that is that I really don't really want to start taking
21 submissions today.

22 And I don't want to take them out of order, if the
23 parties have any problem with that, in the sense that
24 normally we would hear the evidence first of course and we
25 still have evidence yet to come.

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Who knows? Maybe your submission would change after you heard the other witness. I don't know.

But if you say it would take about 10 minutes, does anybody here have a problem with Ms. Savage presenting her argument today out of order?

MR. ERVIN: Speaking for the Department, Mr. Chairman, we would have no objection to that.

CHAIRMAN: If anybody has a problem just put your hand up and I will hear you. All right.

Well, even though it is fairly late in the day we will -- if you want to come forward, Ms. Savage, we will hear your submission now.

MS. DESMOND: Mr. Chair, I'm sorry, I wasn't clear on the undertakings Mr. Gardner had provided to the Board, what his claim was for.

CHAIRMAN: I understood when I questioned about it that he was going to prepare the responses to them and would have it done today or tonight. I guess he has been here all day. So I'm assuming he didn't get much chance to work on them.

So my understanding is that they would be done this evening. He is nodding his head affirmatively, so tonight. And once we have those they can be circulated by way of e-mail to all of the parties who have registered.

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2 MS. DESMOND: I just wonder, Mr. Chair -- and I haven't seen
3 of course his new material. But if there were questions
4 arising from the new data.

5 CHAIRMAN: Mr. Gardner, you plan to be here tomorrow anyway,
6 I think in the original scheme of things. So you can be
7 available tomorrow for additional questions if necessary?

8 MR. GARDNER: Yes.

9 CHAIRMAN: Thank you.

10 VICE-CHAIRMAN: Just before you begin, Ms. Savage. Monsieur
11 est-ce que vous avez quelque chose que vous voulez dire?

12 MR. BOSSE: « inaudible »

13 VICE-CHAIRMAN: Vous voulez parler au micro?

14 MR. BOSSE : J'ai préparé un document pour eh, une entrevue
15 que j'ai eu avec Radio-Canada. Eh, il y en a des copies
16 pour tout le monde, si on peut les distribuer puis
17 « inaudible ».

18 VICE-CHAIRMAN: Alors c'est, essentiellement une soumission
19 par écrit?

20 MR. BOSSE: Une soumission par écrit.

21 VICE-CHAIRMAN: Pour la Commission?

22 MR. BOSSE: Pour la Commission.

23 VICE-CHAIRMAN: O.K. À la fin d'la journée, madame la
24 secrétaire va prendre votre soumission, va donner des
25 copies à tous les membres de la Commission ainsi que eh

1
2 tout le monde dans la salle.

3 MR. BOSSE: Merci.

4 CHAIRMAN: Okay, Ms. Savage.

5 MS. SAVAGE: Thank you very much for the opportunity to do
6 this early and out of order. It is very much appreciated.

7 In general, we would like to thank the New Brunswick
8 Energy and Utilities Board for the opportunity to present
9 our views.

10 My name is Jane Savage and I am the President of the
11 Canadian Independent Petroleum Marketers Associate,
12 acronym is (CIPMA). CIPMA is a national not-for-profit
13 trade association, based in Toronto, representing the
14 independent sector of the Canadian Fuel marketing
15 Industry. "Independent" in our industry just to clarify
16 means non-refiner and non-integrated oil companies.
17 Independents in this context, are industry participants
18 who buy rather than refine their fuel for distribution and
19 sale to Canadian consumers. Our members market fuel
20 products in all provinces of the country. CIPMA members
21 represent about 15 percent of the retail gasolines sites
22 in Canada, while about 30 percent are owned and operated
23 by refiners or fully integrated oil companies. The
24 balance are independently owned or dealer-owned sites. In
25 New Brunswick, our members are Co-op Atlantic, Wilson Fuel

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2 Co. Ltd., Bluewave Energy and Canadian Tire Petroleum.
3 These companies comprise a significant share of both the
4 retail heating oil and retail gasoline markets.

5 My background is in the refining and marketing segment
6 of the Canadian oil industry where I have been for almost
7 30 years. I am a professional engineer registered in
8 Ontario and a graduate of Queen's University with a
9 Masters of Business Administration from McGill University.
10 My background includes refinery design and operation,
11 commodity futures trading in crude oil and petroleum
12 products, international petroleum products, cargo trading,
13 supply economics and marketing in all petroleum products.
14 I feel I bring a knowledge of the workings of global and
15 Canadian petroleum markets to CIPMA and to government and
16 I am a regular commentator on gasoline prices.

17 As a general statement on price regulation, CIPMA
18 recommends against the regulation of petroleum products
19 prices in all circumstances except where there has been a
20 failure in the federal competition laws (or application of
21 these laws) to prevent anticompetitive activities.
22 Consumers will enjoy the lowest possible price for fuel
23 products if there is strong competition.

24 The New Brunswick government opted to regulate
25 gasoline prices in July '06 for another purpose to

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2 stabilize prices for New Brunswick consumers and not
3 because in our view of a failure of competition laws or
4 their application. In CIPMA's opinion, compared to other
5 parts of the country at the time, New Brunswickers were
6 not only enjoying competitive markets, but relatively
7 stable pricing. Nonetheless we fully accept the will of
8 the people of New Brunswick and are honoured to be part of
9 this process.

10 At this juncture, CIPMA advocates that the Board
11 recommend that the government engage in the development of
12 broad objectives of the regulation.

13 To regulate an industry, in our view, means to marry
14 the needs of consumers with the needs of the industry to
15 deliver against certain expectations. It is only when
16 these inputs have been established transparently can a
17 regime function effectively into the future with a minimum
18 of unexpected consequences including interrupted supply,
19 lack of capital input, closure of sites or companies and
20 possibly disenfranchised consumers, as examples of
21 unexpected consequences.

22 Since this Board has taken this approach with other
23 regulated utilities, and since the New Brunswick
24 government decided two years ago to make petroleum
25 retailing a utility, these inputs along with robust models

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2 that normally accompanies regulated entities we feel is
3 required.

4 So, we recommend first that the service level expected
5 from the industry to ensure consumers are well served by
6 the regulated industry be established. Then a rate of
7 return must be established using zero-based costing, from
8 which flows margins and pricing. This should all be done
9 in a consultative approach with the key stakeholders in
10 the process with the end result being a model we can all
11 live with.

12 Because this essential analysis has been omitted, in
13 our view, thus far from the regulatory process, it renders
14 it difficult at best to objectively assess the adequacy of
15 the prices and margins. By choosing the wrong margins or
16 pricing in the absence of robust agreed to models with
17 zero-based costing, could result in adverse consequences.

18 At this point, our members are concerned that costs
19 have increased without a commensurated increase in margin.
20 Costs such as credit card fees, minimum wage costs,
21 working capital costs and electricity rates are all
22 contributing to a reduction in return, in particular,
23 smaller, lower volume retail operations are becoming more
24 marginal.

25 As with other regulated utilities, once objectives are

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2 defined, a rigorous and transparent application and review
3 process must ensue. It is well documented that capital
4 investment will not occur in a jurisdiction where economic
5 outcome is subject to political whim. So CIPMA advocates
6 that the Board recommend a rigorous zero-based approach or
7 model and if the regime's objectives need to be altered,
8 updated or changed according to changing conditions --
9 political or economic, it is recommended that this be
10 undertaken with input from all stakeholders.

11 As a final point, an important change has been taking
12 place in New Brunswick and other jurisdictions in North
13 America which CIPMA would like to emphasize for this Board
14 so that this can be emphasized in the Board's final
15 report.

16 This change is the devolution of integrated oil
17 companies from the marketing segment of the industry and
18 their replacement by independent fuel marketers. This is
19 happening because these regional, often family-owned or
20 cooperatively owned businesses have intimate knowledge of
21 their markets and can serve them more efficiently, that is
22 more cost effectively. They are in the business of
23 distributing and marketing fuel products directly to
24 consumers in rural and urban markets. It is important to
25 note that unlike the major integrated oil companies who

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2 profit from rising crude oil prices or rising refining
3 margins -- both of which are demonstrably the key drivers
4 behind consumer price, independents' profits do not
5 increase with rising prices. Instead, they are seeking
6 ways to decrease consumer prices by fighting against
7 rising credit card fees and calling for higher levels of
8 oversight in the crude oil futures markets to reduce
9 speculation. Both of these latter two initiatives, CIPMA
10 is actively involved in.

11 In other words, the folks from whom most New
12 Brunswickers buy their heating oil and gasoline are on
13 their side and are not profiting from consumer price
14 increases.

15 With this in mind, we invite this Board and indeed all
16 New Brunswickers to avoid strategies with regard to price
17 regulation which is underpinned by the belief that
18 windfall profits are being made by the companies selling
19 petroleum -- sorry, the companies selling petroleum to the
20 consumer. This is not the case.

21 In summary, I would like to thank you for your
22 attention and opportunity to present our views.

23 Petroleum retailing companies in New Brunswick expect
24 to be treated as any other business that is regulated by
25 the province. We believe it is in the public interest to

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do so.

We encourage the Board, with full consultation with stakeholders, to take the same zero-based approach to establishing the desired service levels and appropriate rates of return for the regulated petroleum retailing industry in New Brunswick as they have with other utilities. Only then will defensible margins and prices, which should be reviewed regularly in an open and transparent process.

Thank you again for your time. And thank you again for letting me intervene earlier.

CHAIRMAN: Thank you, Ms. Savage. Does anybody on the Board have any questions? Mr. Radford?

MR. RADFORD: Mr. Chair, I am sorry, Ms. Savage is rushing off, because she has raised a couple of points that I would like to think about further. But you did mention just so I can clarify it, you did mention that you represent, for example, Canadian Tire?

MS. SAVAGE: That's right. Yes.

MR. RADFORD: But Canadian Tire does cross merchandising?

MS. SAVAGE: Yes.

MR. RADFORD: They have their own, and they have their own credit card, right?

MS. SAVAGE: Yes.

1 MR. RADFORD: And when I listened to Mr. Gardner, he says
2 about 1.75 goes towards credit card. Your client has also
3 got not only the 5 -- got it at 1.75 for themselves, don't
4 they?

5 MS. SAVAGE: Right. And I will just clarify Canadian Tire
6 Petroleum is a unique member of our association because
7 they have their own credit cards, and so take a -- call it
8 an agnostic position on the subject of credit card fees.

9 MR. RADFORD: Thank you.

10 CHAIRMAN: Mr. McLean, anything? Mr. Toner?

11 MR. TONER: No.

12 CHAIRMAN: Mr. Johnston? And I don't have any questions.

13 Thank you very much for taking the time to make that
14 presentation today.

15 MS. SAVAGE; Thank you very much.

16 CHAIRMAN: We appreciate the effort that you put into it.


17 And I guess we just -- we are going to hear as well from
18 Mr. Bosse?

19 (Off the record)

20 CHAIRMAN: We will adjourn until tomorrow at 9:30 a.m.

21 (Adjourned)

22 Certified to be a true transcript of the
23 proceedings of this hearing as recorded by me, to
24 the best of my ability.

25 
Reporter

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