CT-2015-003

THE COMPETITION TRIBUNAL

IN THE MATTER OF the *Competition Act*, R.S.C. 1985, c. C-34, as amended;

AND IN THE MATTER OF the proposed acquisition by Parkland Industries Ltd., a wholly-owned subsidiary of Parkland Fuel Corporation, of substantially all of the assets of Pioneer Petroleums Holding Limited Partnership, Pioneer Energy LP, Pioneer Petroleums Transport Inc., Pioneer Energy Inc., Pioneer Fuels Inc., Pioneer Petroleums Holding Inc., Pioneer Energy Management Inc., 668086 N.B. Limited, 3269344 Nova Scotia Limited and 1796745 Ontario Ltd., and

AND IN THE MATTER OF an Application by the Commissioner of Competition for one or more orders pursuant to section 92 of the *Competition Act*.

BETWEEN:

COMMISSIONER OF COMPETITION

Applicant

- and -

PARKLAND INDUSTRIES LTD., PARKLAND FUEL CORPORATION, PIONEER PETROLEUMS HOLDING LIMITED PARTNERSHIP, PIONEER ENERGY LP, PIONEER PETROLEUMS TRANSPORT INC., PIONEER ENERGY INC., PIONEER FUELS INC., PIONEER PETROLEUMS HOLDING INC., PIONEER ENERGY MANAGEMENT INC., 668086 N.B. LIMITED, 3269344 NOVA SCOTIA LIMITED AND 1796745 ONTARIO LTD.

Respondents

RESPONSE OF PARKLAND INDUSTRIES LTD. AND PARKLAND FUEL CORPORATION

OVERVIEW

1. Parkland Industries Ltd. and Parkland Fuel Corporation (together, "**Parkland**") oppose the Commissioner of Competition's ("**Commissioner**") application for an order under section 92 of the *Competition Act* (the "**Application**").

2. Parkland denies that the Commissioner is entitled to any of the relief he seeks on his Application. He has improperly defined the relevant geographic markets and asserted a substantial lessening of competition where there is none.

3. The Commissioner's allegations of unilateral and coordinated effects are exaggerated. Given the proposed remedies Parkland offered before the Commissioner issued this Application, most of the increased market shares and concentration levels asserted in the Application – without any reference to Parkland's proposed remedies – are inaccurate and misleading.

FACTS ADMITTED AND DENIED

4. Except for the allegations in paragraphs 6-8 of the Notice of Application and as otherwise admitted herein, Parkland denies all of the Commissioner's allegations.

STATEMENT OF GROUNDS AND MATERIALS FACTS

Parkland and the Transaction

5. Parkland is an independent marketer of fuel and petroleum products. Parkland offers gasoline, diesel, propane, lubricants, heating oil, and other petroleum products to motorists, businesses, consumers, and wholesale customers in Canada and the United States.

6. The Commissioner's Application relates only to the sale of fuel, directly and indirectly, from gas stations to motorists in certain communities in Ontario and Manitoba. In this regard, Parkland operates retail gas stations ("**Corporate Stations**") and sells fuel on a wholesale basis to gas stations ("**Independent Dealer Stations**") owned and operated by independent, third-party dealers. Parkland controls the decisions of Corporate Stations and, in particular, sets the retail price of fuel at Corporate Stations. The relationship between Parkland and independent third-party dealers is limited to the supply of fuel and ensuring compliance with branding.

Independent dealers control the decisions of Independent Dealer Stations, including, in particular, setting the retail price of fuel.

7. Parkland has deep roots in Western Canada. It identified Pioneer, which operates Corporate Stations and supplies Independent Dealer Stations in Ontario and Manitoba, as an attractive target with complementary business operations. Parkland agreed to purchase Pioneer's 181 Corporate Stations and its 212 supply agreements with Independent Dealer Stations (the "**Transaction**").

8. The Transaction provides Parkland a unique opportunity to, among other things, (i) grow its presence in new regions, including the large Ontario market; (ii) significantly increase its fuel purchases to take advantage of volume discounts offered by supplier refiners; and (iii) achieve supply synergies, efficiencies, and flexibility, driven mainly by improved supply pricing from refiners relating to achieving volume thresholds, estimated reductions in overlapping staff, improved convenience store performance due to lower purchasing costs and offering new products, and the elimination of redundant back-office functions.

9. The Transaction was initially scheduled to close on January 31, 2015 but the outside closing date was extended four times to provide the Commissioner more time to evaluate the Transaction. Although Parkland and Pioneer worked diligently with the Commissioner to assist his review for more than seven months, they could not wait any longer to extend closing. On April 27, 2015, pursuant to their commitment to provide the Commissioner 15-days notice of closing, Parkland and Pioneer advised the Commissioner of their intention to close on May 13, 2015.

10. Two days later on April 29, 2015, although it did not believe that the Transaction was likely to substantially lessen or prevent competition but with the objective of resolving the Commissioner's concerns to permit closing of the Transaction, Parkland advised the Commissioner of its intention following closing to divest four Corporate Stations and six wholesale fuel supply agreements with Independent Dealer Stations (the "**Parkland Divestitures**").

11. On April 30, 2015, the Commissioner issued his Notice of Application and served materials to support his request for an interim hold separate order in respect of 14 communities (the "**Commissioner's Markets**"). None of the Commissioner's materials acknowledged the Parkland Divestitures or their impact on competition.

12. In response to the hold separate order sought by the Commissioner, Parkland affirmed its commitment to complete the Parkland Divestitures and further committed to terminate its wholesale supply agreement with the Independent Dealer Station in Tillsonburg (the "**Tillsonburg Commitment**").

13. On May 29, 2015, the Tribunal released its reasons and order regarding the interim hold separate order. It refused to issue an interim hold separate order for eight of the Commissioner's Markets: Hanover, Port Perry, Gananoque, Welland, Aberfoyle, Innisfil, Allanburg, and Chelmsford/Azilda (the "**Not Held Separate Markets**"). However, the Tribunal granted an interim hold separate order (the "**Hold Separate Order**") in respect of assets in Warren, Lundar, Bancroft, Kapuskasing, Tillsonburg, and Neepawa (the "**Held Separate Markets**").

Closing the Transaction

14. The Transaction is expected to close once the appointments and other arrangements required by the Hold Separate Order are complete.

15. After closing and with the continued objective of resolving the Commissioner's concerns with the Transaction under the *Competition Act*:

(a) With respect to the Held Separate Markets, Parkland proposes to implement the applicable Parkland Divestitures and the Tillsonburg Commitment by entering into an order that contains the types of terms set forth in consent agreements recently registered with the Tribunal in merger matters, and that the Hold Separate Order be replaced with such order on consent.

(b) With respect to the Not Held Separate Markets, Parkland intends to complete the applicable Parkland Divestitures, notwithstanding that the Transaction will not result in a substantial lessening of competition in those communities.

The Geographic Scope of the Relevant Markets is Larger than the Commissioner Alleges

16. The Commissioner has not precisely pleaded nor properly defined the scope of any of the Commissioner's Markets.

17. The Commissioner pleads only one material fact to support his allegation that the relevant geographic markets are as narrow as he alleges: transportation costs constrain the ability of purchasers of retail fuel to cost-effectively source fuel from outside their locality.

18. Geographic boundaries for retail fuel are set by the distance consumers will drive to purchase it. Transportation costs are only one factor influencing the geographic scope of the

relevant markets. Consumers buy fuel not only where they live, but also where they shop, work, and travel. For this reason, retail fuel prices at stations near where consumers work, shop, or travel constrain the retail price at stations near where consumers live.

19. When all relevant factors are considered, the geographic scope of some or all of the Commissioner's Markets is larger than the Commissioner alleges.

The Transaction will not Substantially Lessen Competition

20. Parkland denies that the Transaction creates, enhances, or maintains market power in all of the Commissioner's Markets.

21. Having failed to properly define the geographic scope of the relevant markets, the Commissioner's allegations regarding market share and concentration levels are fundamentally flawed. For example, if gas stations in Guelph, Barrie, and Niagara Falls are included in the market share and concentration level analysis – as they should be – for Aberfoyle, Innisfil, and Allanburg, respectively, post-merger market shares are dramatically lower than the Commissioner alleges and well below the 35% safe harbour threshold set out in the Merger Enforcement Guidelines. Similarly, the number of competitors is dramatically higher than the Commissioner alleges in support of his allegation of potential coordinated effects.

22. Whether or not the Commissioner has properly defined the geographic scope of the relevant markets, Parkland denies the Commissioner's allegations that post-merger market shares and concentration levels will rise as he alleges in all markets.

23. Attributing Independent Dealer Stations to Parkland for analysis of retail market shares and concentration levels in all cases paints an incomplete picture of the actual post-merger competitive landscape at the retail level. Among other things, it either ignores or understates the impact of the dealers in setting the retail price of fuel. Further, increased concentration and market share is not the sole basis for determining whether the Transaction is likely to prevent or lessen competition substantially. Parkland pleads and relies on section 92(2) of the *Competition Act*.

24. Parkland and Pioneer compete directly against one another in the retail sale of fuel in only one of the Commissioner's Markets – Kapuskasing, where each owns a Corporate Station. In 11 of the Commissioner's Markets, Parkland and Pioneer compete in different product markets: one of Parkland and Pioneer sells wholesale fuel to Independent Dealer Stations, while the other owns a Corporate Station and sells fuel at the retail level. In the remaining 2 Commissioner's Markets, neither Parkland nor Pioneer participate in the retail market at all. They only sell wholesale fuel to Independent Dealer Stations.

25. Whether or not the market shares and concentration levels rise as the Commissioner alleges, Parkland denies that the Transaction enables it to exercise greater market power, either unilaterally or on a coordinated basis. Among other things, independent, third-party dealers will continue to set the retail price of fuel at Independent Dealer Stations in 13 of the Commissioner's Markets.

26. In addition, Parkland prices its wholesale fuel to Independent Dealer Stations based on regional price zones. Post-Transaction, were Parkland to increase its wholesale price to a dealer in, for example, Aberfoyle, it would also have to increase its price to dealers in neighbouring

Guelph, which is part of the same regional price zone. Even if Parkland could increase prices in Aberfoyle post-Transaction (which is denied), doing so would cause the volumes sold in Guelph to fall, thus eliminating any benefit to Parkland of increasing the wholesale price in Aberfoyle.

27. Contrary to the Commissioner's bald assertions in paragraph 26:

(a) While consumers may have no alternatives to motor vehicle fuels, alternative providers of retail motor vehicles fuels exist and compete with Parkland. Such alternatives include the Independent Dealer Stations which Parkland supplies, but at which it does not set the retail prices.

(b) Barriers to entry are modest and insufficient to deter entry. In May 2013, a new Ultramar station opened in Aberfoyle. In June 2014, Costco opened a station in Guelph. In May 2015, work began on a new Petro-Canada station in Tillsonburg.

(c) Effective competition remains in each of the Not Held Separate Markets. Effective actual or potential competitors include the large, integrated refiners Imperial Oil, Shell, and Suncor, as well as unintegrated retailers such as CST (Ultramar) and big box stores (e.g., Costco).

(d) The Transaction does not eliminate rivalry between Parkland and Pioneer. In all but one of the Commissioner's Markets (Kapuskasing), Parkland and Pioneer do not compete at the retail level.

28. Whether or not the Transaction substantially lessens competition in the Commissioner's Markets (which is denied), Parkland is not incented to raise prices. Owing to the significant volume discounts available from refiners, Parkland's incentives are to keep prices low to increase

volumes sold so that it can take advantage of the volume discounts across its entire fuel purchases. Moreover, Parkland is not motivated to increase prices at Pioneer-branded Corporate Stations as its analysis predicts such price increases would harm the "Pioneer" brand and therefore would reduce volume sales and lower profitability.

The Transaction's Efficiencies are greater than and offset any alleged Anticompetitive Effects

29. If the Transaction substantially lessens or prevents competition, which is not admitted but denied, the Transaction's efficiencies in the Commissioner's Markets are greater than and offset the effects of any alleged substantial lessening of competition. Such efficiencies include: improved supply pricing relating to achieving volume thresholds, reductions in overlapping staff, improved convenience store performance due to lower purchasing costs and offering new products, and the elimination of redundant back-office functions.

Relief Sought

30. The Commissioner is not entitled to any of the relief he seeks in this Application. With respect to:

(a) **An order prohibiting Parkland from implementing the Transaction (paragraph 27(a)(i))**: The Transaction is expected to close as soon as the appointments and arrangements required by the Hold Separate Order are complete. The Tribunal has no jurisdiction to prohibit implementation of a completed merger. In any event, there is no basis for a permanent prohibition order because the Transaction does not substantially lessen competition.

(b) **An order requiring Parkland to dispose of assets (paragraph 27(a)(ii))**: There is no basis for a divestiture order because the Transaction does not substantially lessen competition. In the alternative, if the Transaction does substantially lessen competition in the Commissioner's Markets, which is not admitted but denied, divesting assets outside of the Commissioner's Markets is not required to remedy any substantial lessening of competition.

(c) **An order requiring Parkland to notify the Commissioner of any future proposed merger where the proposed merger would not otherwise be subject to notification pursuant to the *Competition Act* (paragraph 27(b))**: Even if the Tribunal found that the Transaction substantially lessens competition, it has no jurisdiction to make this order because Parkland does not consent to it, nor would it remedy any substantial lessening of competition in the Commissioner's Markets.

31. Parkland requests that the Tribunal dismiss the Commissioner's Application with costs to Parkland on a substantial indemnity basis.

CONCISE STATEMENT OF ECONOMIC THEORY

32. Parkland's Concise Statement of Economic Theory is attached as Schedule A.

LOCATION AND CONDUCT OF THE HEARING

33. Parkland agrees that the Application be heard in English and held in Ottawa, Ontario.

Dated this 15th day of June, 2015

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SCHEDULE A

CONCISE STATEMENT OF ECONOMIC THEORY

1. This statement of economic theory relates to the eight Not Held Separate Markets. The Held Separate Markets are not considered because the Parkland Divestitures and Tillsonburg Commitment address any potential substantial lessening of competition in those communities.

2. Within the Not Held Separate Markets, Parkland supplies fuel at wholesale to Independent Dealer Stations that have wholesale supply agreements with Parkland. Parkland does not set the retail price for any of these stations. Retail prices are set by each Independent Dealer Station independently of Parkland and independently of any other Parkland Independent Dealer Station. There are either one or two Pioneer Corporate Stations in each of these locations, and in Chelmsford/Azilda there is one Independent Dealer Station supplied by Pioneer and one Pioneer Corporate Station. Pioneer sets the retail prices at its Corporate Stations.

3. The only means that Parkland has to influence the retail prices at Independent Dealer Stations in the Not Held Separate Markets is through the Parkland "rack forward" margin which is the additional margin that Parkland charges its dealers above the rack wholesale price that is set by the refiner. Increasing its rack forward margins by an amount sufficient to have more than a *de minimis* effect on the retail fuel price would not be profitable for Parkland, for the reasons discussed below.

4. Parkland does not set a different wholesale price to each Independent Dealer Station, but instead charges a single common rack forward margin to all dealers within a given Parkland price zone who sell the same retail brand. The Independent Dealer Stations that are part of the Not Held Separate Markets typically do not represent the majority of dealers within any Parkland

price zone to which they belong. The reasons why Parkland has multiple dealers within a given price zone, which are related primarily to minimizing administrative costs, are unaffected by the Transaction, and hence the Transaction will not change Parkland's policy of charging the same rack forward margin to all dealers within a single price zone.

5. If Parkland were to increase its rack forward margins to all of its dealers in the price zones within which the Independent Dealer Stations in the Not Held Separate Markets operate, retail prices would rise if dealers passed on all or part of the higher rack forward margin to customers. Assuming they did so, the retail prices at the Independent Dealer Stations supplied by Parkland would be higher than at competing retail gasoline stations throughout areas that are much larger than the Not Held Separate Markets. This would not be profitable for Parkland after the Transaction, because Parkland would lose too much volume at its Independent Dealer Stations that are within the price zones but not included in the Not Held Separate Markets in addition to losing volumes at the Independent Dealer Stations that are part of the Not Held Separate Markets.

6. Consumers are extremely sensitive to price differences across gasoline stations in a given market. Available estimates of the own-price elasticity of demand for a single station range from -18 to -30. Using these estimates, if a single gasoline retailer were to increase its retail price by 1% and rival stations do not immediately follow, the gasoline retailer with the higher price risks losing 18 to 30% of its volume. This makes it unprofitable to persist in charging a higher price relative to rival stations for any meaningful period of time.

7. The individual Not Held Separate Market communities of Hanover, Port Perry, Gananoque, Welland, Aberfoyle, Innisfil, Allanburg and Chelmsford/Azilda are not properly

defined relevant geographic markets for antitrust purposes. A hypothetical monopolist controlling all retail stations within each of these towns would not find it profitable to impose and sustain a small but significant and non-transitory increase in price ("SSNIP") above levels that would exist in the absence of the Transaction. Most of these towns are connected because of commuting and shopping by its residents to a larger centre, such that competing stations in the larger centre discipline the prices charged by retail stations within the smaller satellite towns. Even without taking the Parkland Divestitures into account, the market share of Pioneer and Parkland Corporate Stations and Independent Dealer Stations supplied by Parkland and Pioneer in properly defined geographic markets is generally low. When account is taken of the Parkland Divestitures, the Transaction following the Parkland Divestitures does not change market concentration materially in any properly defined relevant geographic market. Where there are no Parkland Divestitures, the Parties' post-merger volume share in Guelph/Aberfoyle is 29%,[1] 18% in Niagara Falls/Allanburg and 15% in Barrie/Innisfil.

8. The Parties' low combined volume shares mean Parkland has no incentive or ability to exercise market power unilaterally post-merger. As noted above, Parkland has no incentive to increase the wholesale prices charged to its Independent Dealer Stations in the Not Held Separate Markets. Furthermore, Parkland has no incentive or ability to increase retail fuel prices at Pioneer stations post-merger because the diversion from the Pioneer stations to Parkland's Independent Dealer Stations is too small. Losses to rival stations far exceed any volume losses that would be diverted to Parkland Independent Dealer Stations, for which Parkland would only earn a wholesale margin in any event.

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[1] This volume share reflects the change of Parkland site number 51333 at 352 Elizabeth Street, Guelph, which is no longer a Parkland dealer and is now supplied by a competitor.

9. It is well established in the economics literature that relevant geographic markets for retail gasoline stations are a function of the stations' connectivity along the road network and the direction of traffic flows as well as the distance between station locations. Competition is not localized when consumers can substitute stations far from each other but close to a common commuting path.

10. Within properly defined geographic the Transaction changes market concentration marginally, such that there is unlikely to be any material change in the Parties' incentives or ability to exercise market power through coordinated behaviour with other gasoline retailers within each market. While the Commissioner refers to a number of factors that may facilitate the exercise of coordinated behaviour in the retailing of gasoline the referred-to factors are present in nearly every retail gasoline market in Canada. Yet, we observe competitive pricing for the sale of gasoline throughout Canada. This makes the factors unhelpful for determining when coordination is likely. Instead, the profitability of coordinating compared to the cost should be examined. When this is done for each of the Not Held Separate Markets, the costs to the Parties of any attempts to increase prices with the hope that competitors will follow exceed the potential benefits. As a result, the Transaction will not increase the likelihood of successful and effective coordination post-merger.

CT-2015-003

THE COMPETITION TRIBUNAL

IN THE MATTER OF the *Competition Act*, R.S.C. 1985, c. C-34, as amended;

AND IN THE MATTER OF the proposed acquisition by Parkland Industries Ltd., a wholly-owned subsidiary of Parkland Fuel Corporation, of substantially all of the assets of Pioneer Petroleums Holding Limited Partnership, Pioneer Energy LP, Pioneer Petroleums Transport Inc., Pioneer Energy Inc., Pioneer Fuels Inc., Pioneer Petroleums Holding Inc., Pioneer Energy Management Inc., 668086 N.B. Limited, 3269344 Nova Scotia Limited and 1796745 Ontario Ltd.;

AND IN THE MATTER OF an Application by the Commissioner of Competition for one or more orders pursuant to section 92 of the *Competition Act*.

AND IN THE MATTER OF an Application for an Interim Order pursuant to section 104 of the *Competition Act*.

BETWEEN:

COMMISSIONER OF COMPETITION

Applicant

\- and -

PARKLAND INDUSTRIES LTD., PARKLAND FUEL CORPORATION, PIONEER PETROLEUMS HOLDING LIMITED PARTNERSHIP, PIONEER ENERGY LP, PIONEER PETROLEUMS TRANSPORT INC., PIONEER ENERGY INC., PIONEER FUELS INC., PIONEER PETROLEUMS HOLDING INC., PIONEER ENERGY MANAGEMENT INC., 668086 N.B. LIMITED, 3269344 NOVA SCOTIA LIMITED AND 1796745 ONTARIO LTD.

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RESPONSE OF PARKLAND INDUSTRIES LTD. AND PARKLAND FUEL CORPORATION

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