Tribunal File No. CT-98/2

THE COMPETITION TRIBUNAL

IN THE MATTER OF THE *COMPETITION ACT*, R.S.C. 1985, c.C-34, as amended, and the *Competition Tribunal Rules*, SOR/94-290, as amended (the "*Rules*");

AND IN THE MATTER OF an inquiry pursuant to subsection 10(1)(b) of the *Competition Act* relating to the proposed acquisition of ICG Propane Inc. by Superior Propane Inc.;

AND IN THE MATTER OF an Application by the Director of Investigation and Research for orders pursuant to s.92 and other provisions of the *Competition Act* consequential thereto.

BETWEEN:

THE DIRECTOR OF INVESTIGATION AND RESEARCH

Applicant

- and -

SUPERIOR PROPANE INC., PETRO-CANADA, THE CHANCELLOR HOLDINGS CORPORATION and ICG PROPANE INC.

Respondents

RESPONSE OF SUPERIOR PROPANE INC. AND ICG PROPANE INC.

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PART I ~ SUMMARY OF RESPONSE

1. The respondents Superior Propane Inc. ("Superior") and ICG Propane Inc. ("ICG") oppose the application of the Director of Investigation and Research (the "Director") on the following principal grounds:

(a) The primary motivation for the acquisition by Superior of ICG (the "Acquisition") is to generate efficiencies of $240 to $300 million. These efficiencies promote the express goals in sections 1.1 and 96 of the *Competition Act*, R.S.C. 1985, c.C-34 (the "*Act*"), and can only be realized through the merger.

(b) This merger will not substantially lessen competition in any relevant product market. Propane competes vigorously with natural gas, fuel oil, electricity, wood and other fuels in the traditional (non-automotive) segments, and with gasoline and diesel fuel in the automotive segment (collectively, natural gas, fuel oil, electricity, wood, gasoline, diesel and other fuels are hereinafter referred to as "alternate fuels"). Competition from alternate fuels is responsible for a steady decline in certain key segments of the propane distribution business.

(c) Propane accounts for only 2% of Canadian energy consumption. Alternate fuels supply the remaining 98% of Canadian energy demand, thereby disciplining propane pricing in each end-use. Accordingly, this merger will not result in a substantial lessening or prevention of competition in any relevant market.

(d) Due to his erroneous definition of the relevant market, the Director's market share figures are incorrect.

(e) This industry is characterized by ease of entry and low sunk costs. There is a significant history of actual entry into the propane distribution business. As well, distributors of alternate fuels, and foreign propane and alternate fuel distributors, are potential entrants into this business.

(f) Despite sections 1.1 and 96 of the *Act*, the Director has failed to even address Superior's efficiencies claim in either his review of the Acquisition or in his Application.

PART II ~ ADMISSIONS AND DENIALS

2. Superior and ICG admit the allegations in paragraphs 2, 4 (subject to the clarification that the Acquisition did, in fact, close on December 7, 1998), the second sentence of paragraph 5, and the first, third and fourth sentences of paragraph 10 of the Director's Application.

3. Superior and ICG have no direct knowledge with respect to the allegations in the first sentence of paragraph 5, or those in paragraphs 7, 8 and the first sentence of paragraph 35, and expressly deny the substance of the reports allegedly catalogued in paragraphs 8 and 35 of the Director's Application.

4. Except as otherwise expressly admitted herein, Superior and ICG deny each and every allegation in the Director's Application.

PART III ~ STATEMENT OF GROUNDS AND MATERIAL FACTS UPON WHICH SUPERIOR AND ICG RELY

A. BACKGROUND FACTS

1. THE INDUSTRY CONTEXT

(i) Generally

5. Propane occurs naturally in natural gas and crude oil, and is a byproduct of gas processing and oil refining. There are over 600 gas processing plants across Canada (from which approximately 86% of Canadian propane supply is generated), with Edmonton and Sarnia serving as the current principal regional hubs. With the development of the Sable Island, Nova Scotia natural gas project, which is anticipated by the end of the year, that too will likely become a regional hub. High volume storage facilities are located in Alberta, Saskatchewan, Manitoba and Ontario. Propane is transported from these facilities, as well as from gas processing plants, to distributors and consumers by pipeline, rail or truck, and these supply channels are accessible to any industry participant.

6. Propane is a commodity that is traded freely on North American markets. It is purchased by propane distributors primarily at natural gas plants, oil refineries, and major pipeline supply points, generally at posted commodity prices.

7. Only approximately 40% of Canada's propane supply is consumed in the Canadian market. The balance is exported to the United States.

8. Propane is used in commercial, industrial, residential and agricultural applications (the "traditional" segments), as fuel for water heating, space heating, refrigeration, cooking, stationary engines and other applications. Propane is also used as a fuel for cars and other vehicles (the "automotive" segment). Apart from its use as an energy source, propane is also an important feedstock in the petro-chemical business.

(ii) Key Competitive Factors

9. Propane distribution is a local, relationship-based business, in which propane competes for market share with aggressive low-cost propane retailers and distributors of alternate fuels. Competition from alternate fuels is responsible for a steady decline in certain key segments of the business.

10. There are low barriers to entry into the propane distribution business. It is a business of tanks, trucks and local salespeople; it is not dependent on technology, trade secrets or intellectual property. In fact, all a person needs to enter the business is access to a telephone, a truck and a storage tank, none of which requires an entrant to incur significant sunk costs. As a result, there is frequent entry by new competitors, including suppliers of alternate fuels who see the propane business as a way of expanding their own customer base with a complementary energy offering. The ease of entry into the propane distribution business precludes the likelihood of a profitable, sustained material price increase post-merger, even without significant competition from alternate fuels.

11. Indeed, the Director, in approving Superior's purchase of Premier Propane in 1993, expressly recognized that alternate fuels are substitutes for propane, and that there are low barriers to entry.

2. THE ACQUISITION

(i) Parties to the Acquisition

(a) <u>Superior</u>

12. Superior is a corporation incorporated under the laws of Canada, engaged primarily in the distribution of propane in all 10 Canadian provinces and both territories. All of the outstanding shares of Superior are owned by the Superior Propane Income Fund (the "Fund"), a limited purpose trust established for the purpose of holding the unsecured subordinated notes and equity of Superior. Trust units in the Fund, which are widely held, are listed on the Toronto Stock Exchange.

13. Superior's revenues for the fiscal year ended on December 31, 1997 were approximately $506 million, representing propane sales of approximately 1.435 billion litres and related equipment sales, rentals and service**.**

14. Superior's propane supply is currently sourced from 17 different propane producers in Canada and the United States. On occasion, wholesale propane suppliers demand volume commitments from Superior to reduce their own propane storage costs. In return, the supplier grants small pricing concessions. However, to accommodate such purchase commitments, Superior must arrange for underground storage facilities to inventory excess purchases. Savings from pricing concessions are offset by storage facility costs and inventory carrying costs.

15. Propane, once purchased by Superior, is transported from supply and storage points by cargo liner and rail to Superior's branch locations ("primary distribution"), and then from the branch to the customer by Superior's own fleet of trucks ("secondary distribution"). Superior carries out most of its primary distribution in eastern Canada using its own truck fleet. In western Canada, Superior contracts with third parties for the primary distribution of its propane.

16. The propane distribution business is fundamentally one of local branches, local operations and local competition. Each Superior branch manager sets his or her own prices in response to local market conditions, including competition from other propane retailers and distributors of alternate fuels.

17. Prior to the Acquisition, Superior distributed propane to approximately 200,000 customers, including a relatively small number of high volume, low-margin, customers in Canada and the northeastern United States, from approximately 126 locations (80 branches and 46 satellite or storage locations). Following the integration of 14 non-overlapping ICG locations upon the closing of the Acquisition,

pursuant to the terms of a hold separate arrangement voluntarily undertaken by Superior, and ultimately the subject of a consent order by the Tribunal, Superior now distributes from 140 locations. A list of current Superior locations is attached hereto as Appendix "A". Each Superior branch location markets propane and also sells, installs and services propane equipment (with the exception of the 14 former ICG locations, which do not sell equipment) to all classes of customers.

(b) ICG

18. ICG is a corporation incorporated under the laws of Canada, and is engaged in selling and distributing propane and providing related services to customers in all Canadian provinces and territories except Prince Edward Island, Newfoundland and, to a lesser extent, Nova Scotia. ICG operates through a network of company-owned distribution outlets and independent dealers located throughout its sales and distribution area. In 1990, Petro-Canada acquired ICG and combined Petro-Canada's retail propane operations with ICG's business.

19. ICG's revenues in fiscal 1997 were approximately $311 million, representing propane sales of approximately 1.074 billion litres and related equipment sales, rentals and service.

20. Prior to the Acquisition, ICG distributed propane through a network of approximately 110 locations to about 100,000 customers. Upon closing the Acquisition, and in accordance with the consent order referred to in paragraph 17 above, 14 non-overlapping ICG locations were transferred to Superior. A list of current ICG locations is attached hereto as Appendix "B".

21. ICG's operations are geographically divided into five marketing distribution regions: Eastern, Central, Prairie, Western and Pacific. Its offices are designated as either (i) customer care centres ("C3's"), which are located in Montreal, Toronto, Winnipeg, Calgary and Vancouver and are responsible for the

management of their respective regions, including propane pricing; or (ii) operating centres ("OC's"), which are located in each service area and are responsible for coordinating customer sales, supply and service within their area. Finally, there are several supply, storage and service sites ("S3's") located within each OC service area, typically used for bulk propane storage.

22. ICG obtains its propane through Petro-Canada at competitive market prices, pursuant to a supply agency agreement. Pursuant to this agreement, Petro-Canada also arranges ICG's bulk storage requirements and its primary distribution.

(ii) Acquisition Agreement

23. The Director's description of the Acquisition at paragraphs 3 and 4 of his Application is, in several respects, factually incorrect and, in others, incomplete.

24. Pursuant to an agreement entered into on July 20, 1998, Superior agreed to purchase from The Chancellor Holdings Corporation, a wholly-owned indirect subsidiary of Petro-Canada, all of the issued and outstanding shares of ICG for a net purchase price of $175 million.

25. The purpose of the Acquisition is to realize efficiencies. For a net purchase price of $175 million, Superior expects to realize approximately $500 million of value (ICG's cash flows of $200 million and efficiencies of $240 to 300 million, on a present value basis), none of which is attributable to the exercise of market power by the merged entity. The bulk of the efficiencies would be generated by the rationalization of local operations due to the elimination of approximately 76 overlapping Superior and ICG locations. The balance would be attributable to operational savings arising out of, for example, the re-configuration and coordination of routing and delivery schedules, the rationalization of branch support functions, the integration and reduction of Superior's and ICG's sales staff and the reduction

of corporate office overhead. These efficiencies could not be achieved absent the merger, through cost-cutting or otherwise, and are necessary to preserve and enhance the competitiveness of propane as an energy alternative for Canadian consumers.

PART IV ~ ASSESSMENT OF THE COMPETITIVE IMPLICATIONS OF THE ACQUISITION

A. THE RELEVANT MARKET

1. RELEVANT PRODUCT MARKET

(i) Generally

26. The product market in both the traditional and automotive segments includes propane and the variety of alternate fuels which compete with propane in each end-use. Contrary to the Director's allegations in paragraphs 10 and 11 of his Application, for each end-use there is at least one and, frequently, more than one, alternate fuel that can be used as a substitute.

27. As described in detail in paragraphs 31 to 40 below, the most common alternate fuels in the traditional segments are natural gas, electricity, fuel oil and wood. In the automotive segment, gasoline and diesel fuel are the primary alternates.

28. The clearest indication that alternate fuels are, in fact, close substitutes to propane is that propane has lost a share of the energy market, particularly in certain key segments, as a result of customers switching to these alternate fuels. While there continues to be modest switching into propane, it is clear that the switching out of propane is greater. For example, automotive propane demand, which grew from negligible amounts in 1980 to over 30% of propane consumption in the mid-1990's, has been declining at the rate of 10% to 15% per year since then.

29. The behaviour of Superior and ICG confirms this close substitutability: (i) they set their propane prices by reference to prices of alternate fuels; and (ii) they have identified alternate fuels as their principal competition in their securities filings.

30. Indeed, in 1993, the Director accepted that alternate fuels are substitutes for propane and discipline its pricing; he has not disclosed to the Tribunal, either in his injunction application in December 1998 or here, why his views have changed.

(ii) Alternate Fuels

Natural Gas

31. Natural gas is a significant discipline on propane. In those areas where natural gas becomes available, demand for propane for heating and many other end-uses is supplanted by natural gas due to its convenience and substantial price advantage. As acknowledged by the Director at paragraph 10 of his Application, "[i]n many applications [propane] is subject to displacement by natural gas, where natural gas pipeline networks are available."

32. In 1996, natural gas accounted for 33% of total energy demand in Canada, up from 25% in 1980. It is available in every major urban centre in Canada, excepting the Atlantic provinces. Even there, offshore natural gas is scheduled to be introduced, through initiatives such as the Sable Island project, as early as the end of this year.

33. In rural areas, natural gas becomes available as soon as a sufficient number of potential customers is identified to justify installing pipeline connections. Thus, the influence of natural gas is felt not just in those areas where it becomes available, but also in those nearby areas where it has the potential to expand. The transition to natural gas is facilitated by the fact that propane appliances and

furnaces can be adapted for natural gas use with a few minor adjustments and minimal cost.

Electricity

34. Although electricity is generally more expensive than other energy sources, it commands a significant share of energy consumption in traditional segment end-uses (e.g., 36% of residential and commercial energy consumption, and 32.5% of industrial energy consumption). Consumers in many end-uses have a significant preference for electricity due to its greater convenience in relation to other energy sources. As the electricity industry continues to deregulate in several provinces, gradually introducing market-based pricing, and as new and innovative generating capacities are developed, electricity will become more attractively priced relative to other energy sources. Electricity is widely available throughout all regions of Canada, and accounted for 24% of total energy demand in Canada in 1997, up from 18% in 1980.

Wood

35. Wood is a significant competing energy source to propane in Canada. This is especially the case in rural areas where propane has a significant presence.

36. Major advances in wood-burning technology over the past five years have made wood-burning safer, more efficient and convenient. Furthermore, wood is available in all areas of Canada at reasonable prices. As of the mid-1990's, more than 400,000, or 6% of all single family dwellings in Canada, were using wood as their primary fuel for heating; in addition, over 950,000 single family dwellings, or 14%, were using it as a supplementary heating fuel. Accordingly, wood's share of the residential heating segment is more than three times that enjoyed by propane.

Fuel Oil

37. Fuel oil has always been a significant competing energy source to propane, and that competitiveness is increasing. Fuel oil enjoys a large price advantage over propane for home space and water heating purposes everywhere in Canada except Alberta. (Propane is less expensive in Alberta than elsewhere due to the fact that Alberta is the principal source of propane in Canada.) Fuel oil is available throughout Canada as it is delivered to customers primarily by truck in the same way that propane is distributed.

38. In 1997, fuel oil and other refined petroleum products accounted for 38% of total energy demand in Canada, down from 52% in 1980. In recent years, however, the efficiency levels of fuel-oil furnaces have improved from roughly 60% to approximately 90%, thus matching natural gas and propane furnaces which have been available in the 90% efficiency range for some time. As a result of these improvements in technology, heating oil is today 50% more efficient for home space and water heating than it was just a few years ago. Although fuel oil cannot be used for certain applications (e.g., for cooking and operating appliances like clothes dryers), it can be combined with other sources of energy, particularly electricity which is generally available and used by virtually all energy consumers.

Substitutes for Automotive Propane Use

39. In the automotive segment, propane competes primarily with gasoline, diesel fuel and natural gas. Engine technology, however, has outpaced current propane conversion technology, effectively limiting the ability to convert new vehicles to propane. Moreover, the improved efficiency of gasoline engines and the continuing withdrawal of government subsidies encouraging propane use have eroded the price advantage of propane over gasoline and diesel. As a consequence, demand for automotive propane is (and has been since the mid-1990's) declining at a rate of 10% to 15% per year.

40. The ease with which customers can switch out of automotive propane contributes to this decline. This switching is facilitated by, among other things, the use of dual fuel systems, the ease of conversion and the limited lifespan of, in particular, fleet vehicles.

(iii) Director's Allegations as to Equipment and Service Markets

41. The Director alleges at paragraph 9 of his Application that there are separate markets for propane equipment and accessories and the service of such equipment and accessories. However, these are essentially derivative goods and services within the energy supply and distribution market. Accordingly, while Superior and ICG compete for propane customers, presently they do not generally compete for the supply of equipment and service independently of their competition for propane supply.

42. In any event, equipment sales and related service represent only a small portion of Superior's and ICG's business. In fact, with the exception of Quebec, ICG has been exiting this business in recent years. There are numerous independent suppliers, such as appliance manufacturers, retailers and heating contractors who have a much greater presence than Superior and ICG. The result is a competitive environment within which the merger will not substantially lessen competition.

(iv) Conclusion as to Relevant Product Market

43. In summary, the Director's definition of the relevant product market, being limited to propane, is too narrow. First, it excludes alternate fuels, and therefore disregards the vigorous inter-fuel competition that has resulted in and continues to drive a steady decline in propane demand in certain key segments. Second, it singles out certain end-uses for propane as being unique and not reasonably capable of substitution, which is incorrect. Third, the Director erroneously identifies the equipment and related services "markets" as being

relevant to this case; in any event, the merger would not substantially lessen competition therein.

2. RELEVANT GEOGRAPHIC MARKET

44. Superior and ICG are in the business of distributing propane through their branch locations across Canada. The relevant geographic markets are local, delineated by the area within which each branch location can deliver to customers. Typically, a propane retailer has a service area of approximately 50 to 300 km., beyond which delivery becomes increasingly uneconomical. The range reflects the fact that the larger a shipment for a specific customer, the more economical it is to ship propane further distances as the per litre cost of delivery decreases. Thus, the range of a particular local market depends on features unique to that market, most significantly, the nature of its customer base.

45. While oriented around a particular branch location, the geographic market definition should recognize the competitive impact of other energy retailers who, while not located in the same vicinity, sell in overlapping areas and can easily extend into adjoining areas. Propane and alternate fuel providers who sell into Superior's and ICG's delivery areas from outlets or facilities located outside that radius, discipline the price that can be charged for propane by a particular branch location.

46. Superior and ICG deny that there is a separate geographic market for "major" or "national" account customers, as alleged by the Director at paragraph 12 of his Application. Regardless of whether delivery is made to a customer at one or more location, pricing for major accounts is still determined locally (and in the case of ICG, regionally, with local input) and in competition with local propane distributors and alternate fuel suppliers in each delivery location.

B. NO SUBSTANTIAL LESSENING OF COMPETITION

47. Superior and ICG deny that the Acquisition will substantially lessen or prevent competition.

1. MARKET POWER

48. The merged entity will continue to compete for customers with both alternate fuel suppliers and propane distributors.

49. Alternate fuel providers, who together supply 98% of Canadian energy demand, vigorously compete with propane distributors, and are steadily eroding propane's market share in certain key segments.

50. As to competition with propane distributors, both Superior and ICG have always offered additional service (e.g., guaranteed 24-hour supply, etc.). As a consequence, they have been able to charge a somewhat higher price. However, there is a limit to the premium which can be charged for the additional service, and this premium is disciplined by the prices charged by propane distributors. The prices charged by the merged entity will continue to be disciplined by those competitors as customers can switch to low-priced, low-service propane suppliers.

51. It is also the case that, in order to compete for market share with alternate fuels, the merged entity will have to continue to provide at least the current level of service, at current price levels, or it will lose customers.

52. For the foregoing reasons, the merged entity will not be able to exercise market power by increasing its pre-merger margins or decreasing service quality.

2. MARKET SHARES

53. The market share figures set out in paragraph 19 of the Director's Application are calculated on the basis of propane sales alone, which account for only 2% of overall Canadian energy demand. As a result of ignoring the competition from alternate fuels, the Director's market share figures overstate Superior's and ICG's market power.

54. Further, the Director's estimate of the market shares attributable to "national" or "major" account sales at paragraph 20 of his Application suggests that the merged entity would have market power over these customers. In fact, Superior's and ICG's major account customers have significant countervailing power due to the quantity of their purchases and their concurrent and ready ability to self-supply or to switch to other local propane or alternate fuel distributors. Moreover, most of Superior's, and a significant number of ICG's, major account customers are integrated oil companies (auto propane and oil field services customers) who have sophisticated transport capabilities and ready access to their own propane supply.

55. As for the equipment sales and service markets, the Director does not indicate Superior's and ICG's shares, and baldly concludes at paragraph 21 of his Application that the merged entity would be the "dominant source of supply" in "a significant number of local markets" as a result of the merger. In fact, with the exception of Quebec, ICG has largely exited the equipment and service business. Thus, quite apart from the fact that the Director has incorrectly identified such markets as being relevant to this case, he has overstated Superior's and ICG's influence therein.

3. LOW BARRIERS TO ENTRY

56. Superior and ICG deny the Director's allegation at paragraphs 23 to 25 of his Application that there are significant barriers to entry into the propane business. To the contrary, as was expressly recognized by the Director in approving

Superior's acquisition of Premier Propane in 1993, there are relatively few requirements for entry. As a result, during the last four years alone, approximately 29 new propane marketers (including suppliers of alternate fuels) have entered the propane distribution business.

57. Entry into the propane distribution business, expansion of existing competitors into contiguous service areas, or expansion into propane by alternate fuel suppliers, domestic and foreign, can be accomplished in a timely fashion and without significant sunk costs, for the following three reasons.

58. First, there is ease of access to propane supply throughout Canada at commodity-based prices.

59. Second, entry into the propane distribution business requires only a modest financial investment and few sunk costs are incurred. This is especially the case for current propane retailers expanding into new areas, and for alternate fuel providers seeking to add propane to their product offering.

60. The most significant requirement for entry is access to a bulk propane delivery vehicle. The purchase price for such a vehicle varies depending on size (for example, a 3,500 litre bulk delivery truck, which will deliver approximately 2 million litres per year, costs approximately $120,000). These vehicles are also available for hire.

61. The necessary investment in storage facilities will vary according to the proximity of the potential entrant to major supply points; if the local market is close to a major supply point, the storage facilities required will be minimal as a delivery truck can be filled at the supply point before every run. A new entrant in certain parts of Alberta, Southern and Southwestern Ontario, Montreal and Quebec

City, for example, would require only limited storage facilities (for storing cylinders and other equipment).

62. Accordingly, one could enter the propane distribution business for a total investment of approximately $120,000-$300,000. Few of these costs would be sunk costs as there is a used market for most of these items.

63. Third, there are no onerous licensing or regulatory requirements for entry into the propane distribution industry. There are no price or production quantity regulations in effect anywhere in Canada, except in Prince Edward Island (where the price of propane is regulated). Federal and provincial licensing requirements, which pertain primarily to the handling, transporting and storing of propane (and which, in some cases, are the same as those required for natural gas), can generally be satisfied in one to two months.

64. The Director, in contrast to the foregoing, cites the following specific factors at paragraphs 23 to 25 of his Application as barriers to entry into the propane industry: (i) long-term and short-term restrictive contracts; (ii) the mature nature of the industry and its flat or declining growth; (iii) the time required to obtain necessary permits for storage of propane; (iv) the time required to enlist customers in light of the parties' reputations for reliability; and (v) the disadvantage faced by potential competitors to the merged entity, in light of the merged entity's alleged ability to control the supply of propane and equipment.

65. Superior denies that these factors contribute to a substantial lessening of competition as a result of the merger.

66. First, the fact is that customers switch to alternate fuels and other propane distributors notwithstanding their contractual commitments. Further, Superior has undertaken to eliminate contractual provisions of concern to the

Director, as discussed in paragraph 86 below, in the event that the Tribunal permits the merger.

67. Second, the fact that the propane industry is mature has not prevented numerous small to mid-scale low-cost entrants. These potential entrants could easily operate to capacity on a modest investment. Many competitors already do.

68. Third, Superior and ICG deny that considerable time is required to obtain permits for storage tanks. Indeed, a potential entrant in certain parts of Alberta, Southern and Southwestern Ontario, Montreal and Quebec City would require very limited, if any, storage facilities since a delivery truck could be filled at a major supply point before every run.

69. Fourth, as to reputation being a barrier to entry, two points should be made. First, there is a significant history of entry. Second, Superior's and ICG's reputation does not, and will not, dissuade customers from seeking low-priced, low-service propane supply.

70. Fifth, with respect to propane supply and equipment, Superior and ICG enjoy negligible, if any, buying power. With respect specifically to propane supply, as described above at paragraph 14, Superior receives small discounts for some of its large purchases of propane, but in return it contractually agrees with those suppliers to take the propane when the supplier (i.e., not Superior) demands it. This reduces the suppliers' storage costs, but increases Superior's costs. As for ICG, it obtains its propane supply through Petro-Canada at competitive prices, pursuant to a supply agency agreement.

4. EFFECTIVE COMPETITION REMAINING

71. The merged entity will continue to face vigorous competition from existing propane distributors and suppliers of alternate fuels.

72. Even apart from alternate fuel providers, there are approximately 105 independent propane retailers across Canada, including 11 multi-regional propane marketers and several large regional competitors. Although considerably smaller than either Superior and ICG, these propane retailers exert significant competitive pressure. Even with relatively small capacities, these lower-cost operators can and do undercut Superior and ICG on price. Contrary to the Director's allegations at paragraph 30 of his Application, such low-cost competitors are not price-followers.

73. The propane industry is also characterized by a pattern of new entry, which historically has included ex-Superior and ex-ICG employees. As well, suppliers of alternate fuels, both domestic and foreign, are potential entrants into the propane distribution business.

5. REMOVAL OF VIGOROUS AND EFFECTIVE COMPETITOR

74. The Director asserts at paragraph 32 of his Application that Superior and ICG "recognize that the other is the 'key rival' " and, at paragraph 29, that "Superior and ICG adhere to a general policy of non-competition", which has included acting jointly to rationalize the parties' own market dominance and product offerings through swaps and other transactions. The Director's contradictory pleading, and the inconsistency of this case with his approval in 1993 of Superior's acquisition of Premier Propane, underscores the flawed nature of his Application.

6. CONCLUSION

75. Given the substitutes available for each end-use for propane and the ease of entry into the industry, the merger is not likely to substantially lessen or prevent competition in any relevant market. In the alternative, if the Acquisition does lessen or prevent competition substantially, which is denied, such effects are less than, and would be offset by, the efficiency gains resulting from the Acquisition.

C. EFFICIENCIES

76. The Acquisition is expected to generate substantial efficiencies, in the range of $240 to $300 million (net present value). There are at least seven categories of efficiency gains that would be realized through the Acquisition.

77. First, the merged entity would be in a position to eliminate a significant share of corporate head office overhead and public company costs, due to its ability to eliminate one of the two head offices and to combine corporate functions, including senior management, accounting and finance, human resources, legal, safety, regulatory, information systems, engineering, fleet and marketing functions.

78. Second, efficiency gains would accrue from the elimination of duplicate branch and field locations. Prior to the Acquisition, Superior and ICG operated approximately 126 and 110 field locations, respectively. The Acquisition would permit the combined entity to rationalize approximately two-thirds of ICG's existing network of field locations and associated field support functions, while allowing the merged entity to serve the existing customer base more efficiently.

79. Third, improved routing of delivery vehicles would generate efficiencies. At present, Superior's and ICG's delivery routes overlap in markets where they compete. The rationalization of these routes would allow for the elimination or redeployment of many of the trucks in the two company fleets.

80. Fourth, the merged entity would be able to reduce capital expenditures. This would be realized by the merged entity's ability to optimize its truck utilization rates by combining fleets, rationalize branch locations that would otherwise require annual capital upgrades and reduce expenditures on customer equipment inventory.

81. Fifth, the merged entity would be able to reduce information technology costs. Savings would result from (i) the integration of ICG's and Superior's information systems and the related reduction in maintenance costs; and (ii) reduced computer capital expenditures due to a smaller combined workforce.

82. Sixth, the merged entity would realize a one-time savings, upon integration, as a result of improved asset productivity. Specifically, fewer truck purchases would be required due to the truck fleet rationalization process discussed above, and proceeds would be realized from the sale of surplus properties resulting from the integration of Superior's and ICG's overlapping locations.

83. Finally, the Acquisition would allow the merged entity to yield efficiencies in several, less readily quantified, respects. For example, the merged entity would be better positioned to respond to customer service demands. A larger customer base at individual branch locations would provide the critical mass necessary to redeploy existing staff in a manner that would enhance individual skill levels, generating higher employee satisfaction and operating efficiencies through specialization. By dedicating employees to specialized service roles, the Acquisition would result in heightened responsiveness to customer needs. In addition, the Acquisition would allow, in certain remote areas, for the merger of two operations that, on their own, are not currently economically viable, thereby improving the long term prospects for these operations by exploiting increased economies of scale and lower cost structures. As a result, customers in remote locations would be better assured continuous access to propane and related support services. The augmented value of the business would also, of course, benefit Superior's Canadian unitholders.

84. Such efficiency gains will be lost if the Director is granted the relief sought in the Application. They cannot be achieved through independent rationalization or any other acquisition.

85. If there is a substantial lessening or prevention of competition, which is denied, it is outweighed and offset by the efficiency gains attributable to the merger.

D. VOLUNTARY UNDERTAKINGS

86. Superior has undertaken to implement the following measures in the event that the Tribunal permits the merger:

(i) Contractual Provisions - Superior will commit to the following:

- It will not enforce term provisions in its existing Standard Customer Contracts For Propane Supply (for greater certainty, "Standard Customer Contracts For Propane Supply" do not include contracts that contain specific terms requested by the customer, including contracts entered into pursuant to bids and tenders);

- Subject to the foregoing:

    - it will adopt a standard form propane supply contract terminable by the customer on 30-days notice;

    - it will waive contractual terms calling for liquidated damages, and limit itself to seeking recovery of accounts receivable;

    - it will waive its contractual rights to match lower prices quoted by competitors; and

    - it will waive contractual terms restricting the right of previous customers/agents and contractors to enter into the propane business.

(ii) Employee Non-Compete Covenants - Superior will not enforce non-compete covenants against former Superior or ICG employees nor seek such covenants in the future.

(iii) Arrangements with Equipment Suppliers - Superior will eliminate any exclusivity arrangements presently in place and will not seek any in the future.

(iv) Continuing Support for PGAC - Superior will continue its support for the Propane Gas Association of Canada ("PGAC") (one-member-onevote structure) and, through its membership in the PGAC, will continue to support the Emergency Response capability presently offered to members. Superior will not seek the appointment of its representative as Chair or Vice-Chair of the PGAC.

(v) Facilitating Propane Supply for Competitors - Superior will allow all competitors to have access to supply locations where Superior or ICG have "Keep Dry" arrangements on a "most-favoured nation" basis (i.e., on terms equivalent to Superior's).

(vi) Surplus Equipment - Superior will make available to new entrants and existing competitors surplus equipment (at fair market value) made available by the rationalization following the completion of the merger.

PART V ~ RELIEF SOUGHT

87. Superior and ICG respectfully request that this Application be dismissed and that the relief sought by the Director in paragraph 41 of his Application be denied. In the alternative, if the Tribunal finds that there is a substantial lessening or prevention of competition which is not outweighed and offset by the efficiencies, there should be a hearing to determine the appropriate remedy.

PART VI ~ PROCEDURAL MATTERS

88. Superior and ICG agree to this Application being heard in the City of Calgary, Alberta.

89. Superior and ICG further agree to these proceedings being conducted in English.

DATED this 29th day of January, 1999.

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APPENDIX "A"

SUPERIOR LOCATIONS

British Columbia

1.	Burns Lake
2.	Campbell River
3.	Castlegar
4.	Port Hardy - Satellite
5.	Chetwynd
6.	Coquitlam
7.	Squamish - Satellite
8.	Cranbrook
9.	Radium - Satellite
10.	Fort St. John
11.	Fort Nelson - Satellite
12.	Kamloops
13.	Ashcroft - Satellite
14.	Kelowna
15.	Nanaimo
16.	Victoria - Satellite
17.	Prince George
18.	Terrace
19.	Powell River (former ICG)
20.	Sechelt (former ICG)

Alberta

21.	Calgary
22.	Edmonton
23.	Camrose - Satellite
24.	Thorsby - Satellite
25.	Westlock - Satellite
26.	Edson
27.	Whitecourt - Satellite
28.	Valemont - Satellite
29.	Dryton Valley - Satellite
30.	Fort McMurray
31.	Grande Prairie
32.	Lethbridge
33.	Champion - Satellite
34.	Taber - Satellite
35.	Medicine Hat - Satellite
36.	Peace River
37.	High Level - Satellite

38. Manning - Satellite
39. Red Deer
40. Oyen - Satellite
41. Rocky Mountain House - Satellite
42. Slave Lake
43. Red Earth - Satellite

Saskatchewan / Manitoba

44. Lloydminster
45. Elk Point - Satellite
46. Provost - Satellite
47. Bonnyville - Satellite
48. Prince Albert
49. Buffalo Narrows - Satellite
50. La Ronge - Satellite
51. Meadow Lake - Satellite
52. Tisdale - Satellite
53. Regina
54. Swift Current - Satellite
55. Weyburn - Satellite
56. Yorkton - Satellite
57. Shaunovan - Satellite
58. Saskatoon
59. Winnipeg
60. Virden - Satellite
61. Dryden - Satellite
62. Morden (former ICG)
63. Portage la Prairie (former ICG)
64. Dauphin (former ICG)
65. Swan River (former ICG)
66. The Pas (former ICG)

Northern Ontario

67. Echo Bay
68. Hearst
69. New Liskeard
70. North Bay
71. Ottawa
72. Carleton Place - Satellite
73. Ste. Rose - Satellite
74. Pembroke
75. Porcupine

76. Sudbury
77. Little Current - Satellite
78. Thunder Bay
79. Fort Frances - Satellite
80. Manitouwadge - Satellite

Central Ontario

81. Bala
82. Bancroft
83. Barrie
84. Belleville
85. Fenelon Falls
86. Huntsville
87. Keswick
88. Kingston
89. Peterborough
90. Prescott

Greater Toronto Area (GTA) Region

91. Concord
92. Whitby

Southern Ontario

93. Chatham
94. Simcoe
95. Stratford
96. Strathroy
97. Walkerton
98. Owen Sound - Satellite

Niagara Region

99. Guelph
100. Smithville

Quebec

101. Cap-de-la-Madeleine
102. Drummondville
103. Bromont - Satellite
104. Gatineau

105. Joliette
106. Les Cèdres
107. Rivière-du-Loup
108. Matane - Satellite
109. Edmunston - Satellite
110. St-Romuald
111. La Malbaie - Satellite
112. St-Constant
113. Sept-Îles
114. Thetford Mines
115. Vimont
116. Jonquiere (former ICG)
117. St. Prime - Satellite (former ICG)
118. Arvida - Satellite (former ICG)
119. Val D'Or (former ICG)
120. Mont-Laurier (former ICG)
121. Rouyn-Noranda (former ICG)

<u>New Brunswick</u>

122. Bathurst
123. Fredericton
124. Moncton
125. Saint John

<u>Nova Scotia</u>

126. Bridgewater
127. Digby - Satellite
128. Dartmouth
129. Kentville - Satellite
130. Trenton
131. Sydney
132. Truro

<u>Prince Edward Island</u>

133. Charlottetown

<u>Newfoundland</u>

134. Pasadena
135. St. John's
136. Grand Falls - Satellite

Yukon

137. Watson Lake
138. Whitehorse

Northwest Territories

139. Yellowknife
140. Hay River (former ICG)

APPENDIX "B"

ICG LOCATIONS

British Columbia

1. Abbotsford (incl. Chilliwack)
2. Squamish
3. Burnaby
4. McKenzie
5. Quesnel
6. Williams Lake (incl. Anahim Lake)
7. Prince George
8. Valemount
9. Kelowna
10. Kamloops
11. Salmon Arm (incl. Revelstoke)
12. Smithers
13. Prince Rupert
14. Terrace
15. Victoria
16. Port Alberni
17. Courtenay
18. Port McNeill
19. Nanaimo
20. Surrey

Alberta

21. Lake Louise
22. High River
23. Calgary
24. Fort McMurray
25. Boyle
26. Camrose
27. Wetaskiwin
28. Edmonton
29. Peace River
30. High Prairie
31. Red Earth Creek
32. High Level (incl. Zama)
33. Grand Prairie
34. Bonnyville
35. Vermilion
36. Maidstone (incl. Edam)
37. Elk Point
38. Lloydminster

39. Golden
40. Invermere
41. Castlegar
42. Cranbrook

<u>Sask. / Manitoba / Northern Ont.</u>

43. Kenora
44. Winnipeg
45. Brandon
46. Marathon
47. Ignace
48. Thunder Bay
49. North Battleford
50. Meadow Lake
51. La Ronge (incl. Isle a la Cross)
52. Prince Albert
53. Saskatoon
54. Swift Current
55. Maple Creek
56. Yorkton
57. Estevan
58. Assiniboia
59. Carlyle
60. Regina

<u>Ontario</u>

61. Peterborough
62. Barrie (incl. Hanover)
63. Mid-Ontario and Metro (North York)
64. London
65. Stratford
66. Springfield
67. Windsor
68. Sarnia
69. Kingston
70. St. Andrews
71. Eganville
72. Gatineau
73. Ottawa
74. Timmins
75. Sault Ste. Marie
76. Wawa

77. North Bay
78. Sudbury (incl. Spragge)
79. Moncton

Quebec

80. Prevost
81. Coteau-du-Lac
82. Montreal
83. St-Jean-sur-Richelieu
84. Granby
85. Tracy
86. Ste Catherines
87. Sherbrooke
88. Trois-Rivieres
89. Acton Vale
90. Drummondville
91. St-Georges de Beauce
92. Thetford Mines
93. Quebec
94. Baie-Comeau
95. New Richmond
96. Matane (incl. Ste-Anne-des-Monts, Gaspe)
97. Rimouski
98. Longueuil

Yukon

99. Watson Lake (incl. Dease Lake, BC)
100. Whitehorse (incl. Dawson City)

Northwest Territories

101. Yellowknife