

THE COMPETITION TRIBUNAL

IN THE MATTER OF an Application  
by the Director of Investigation  
and Research under sections 92 and  
105 of the Competition Act,  
R.S.C. 1985, c.C-34, as amended;

IN THE MATTER OF the acquisition  
Imperial Oil Limited of the shares  
Texaco Canada Inc.

BY		COMPETITION TRIBUNAL
OF		TRIBUNAL DE LA CONCURRENCE
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OTTAWA, ONT.		# 20 (A)

B E T W E E N:

THE DIRECTOR OF INVESTIGATION  
AND RESEARCH

Applicant

- and -

IMPERIAL OIL LIMITED

Respondents

AFFIDAVIT OF KENNETH G. BROWN

I, Kenneth G. Brown, of the City of Southern Pines  
in the State of North Carolina, in the United States of  
America, MAKE OATH AND SAY AS FOLLOWS:

1. I am a consultant in the field of energy economics  
and petroleum refining with 37 years experience in all phases  
of the petroleum industry and have been retained by the  
Director of

Investigation and Research, Consumer and Corporate Affairs - Canada to provide my opinion on the competitive effects of the acquisition by Imperial Oil Ltd. of Texaco Canada Inc. particularly with respect to the Sarnia and Nanticoke refineries. Now shown to me and attached as Exhibit "A" to this my affidavit is a copy of my Report.

2. The contents of this Report attached as Exhibit "A" to this my affidavit and the opinions expressed therein are true to the best of my knowledge, information and belief.

3. I make this affidavit pursuant to Rules 42(1) of the Competition Tribunal Rules.

SWORN before me at the )  
City of Hull, in the )  
Province of Quebec )  
this 20<sup>th</sup> day of July )  
1989.

  
Kenneth G. Brown

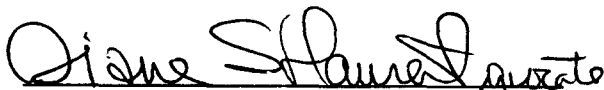
  
Commissioner for taking Oaths

EXHIBIT "A"

Exhibit "A" to the Affidavit  
of Kenneth G. Brown, sworn  
before me this 20<sup>th</sup> day of  
*July* 1989.

*Diane Hament Lavate*

Commissioner for taking Oaths

## REPORT OF KENNETH G. BROWN

In respect of the acquisition of Texaco Canada Inc. by  
Imperial Oil Limited

1. The purpose of this report is to address whether or not, with the implementation of the draft Consent Order, the Imperial/Texaco merger and subsequent operation of Imperial's Sarnia refinery in conjunction with Texaco's Nanticoke refinery is likely to result in a lessening of competition in the refining industry in Canada. My evaluation of this issue is based on my review of the terms of the Draft Consent Order, my experience with the refining industry in Canada, and in the U.S., and a review of other information in this proceeding. While outside of the Atlantic region, the most significant impact of the merger in the refining sector is in the Ontario/Quebec market. It is my opinion, based on these facts and experience, that the Draft Consent Order will result in a situation where operation of the Sarnia refinery in conjunction with Nanticoke refinery should not give rise to concerns about competition in the refinery industry in Canada.

2. The Draft Consent Order accomplishes this through specific requirements and prohibitions on the part of Imperial Oil Ltd. which are addressed below.

(a) First, the draft Consent Order requires the supply assurance by Imperial of motor gasoline to independent resellers for a minimum of 7 years and potential maximum of 10 years from its Sarnia and Nanticoke refineries at Imperial rack supply points in Ontario and Quebec;

(b) Second, the volume of motor gasoline made available shall be 1511 million litres in the first year, adjusted upward thereafter in proportion to the increase in demand;

(c) Third, the volume is not to exceed 26.4% of the gasoline refining capacity from the combined refineries;

(d) Fourth, the sales to independent resellers will be in accordance with reasonable commercial terms (prevailing market conditions); and

(e) Fifth, the term of supply, at the individual purchaser option, may be from one to a maximum of five years.

3. The Draft Consent Order will provide continuity of supply as outlined above and it is my opinion based on the analysis set forth below that the joint operation of the Sarnia and Nanticoke refineries is preferable to divestiture of Nanticoke or to a third party venture with Imperial.

4. The Sarnia (IOL) refinery is a complex refinery with two crude trains, a fluidized catalytic cracking unit, a hydrocracker unit, a fluid coking unit, two reformer units, an HF (hydrofloric acid) alkylation unit, four desulphurization units (hydrofiners), a hydrogen synthesis plant, a sulphur plant, a lube oil plant, and a utility plant. Other facilities include a chemical complex which shares the light ends and utilities with the refinery.

5. The fluid coker unit makes heavy crude oil (usually high sulphur) an attractive feedstock. The ability to accept heavy crude makes Sarnia unique (in Canada) with respect to economics and operating constraints.

6. Nanticoke refinery is a medium conversion refinery and consists of a single crude train (atmospheric/vacuum unit), a fluidized catalytic cracking unit, a catalytic reforming unit, a sulphuric acid alkylation unit and a sulphur plant. Nanticoke is a relatively new refinery with modern facilities, designed to handle mainly light sweet crudes. Nanticoke lacks desulphurization facilities needed to process heavy high sulphur crude oils.

**PAGES 4, 5, 6 CONTAIN CONFIDENTIAL INFORMATION**

11. It is my opinion that the advantages, shown in the foregoing, arise solely from 'joint operation' of the two refineries, and are not possible through separate 'standalone' operations because certain elements are missing.

12. The elements needed to function jointly, that are not available in the 'standalone' situation are:

(a) Timely and detailed information by a single management with the technical skills to 'optimize' both refineries in response to market condition.

(b) The exchange of streams between refineries which take advantage of processing activities to achieve the most efficient use of stream qualities and spare capacity.

(c) A centralized overview of 'joint refinery' economics which ultimately produces products at a combined cost that is less than either refinery could on a standalone basis. This extends into inventory control, coordinated unit shutdowns for maintenance, elimination of duplicate refinery service manpower and improved contingency planning.



13. In my opinion, the clearly identifiable advantages of 'joint operation' are real and will be translated into improved efficiency mainly in reduced cost of producing products; improved refinery utilization; increased gasoline production capability; reduced product purchases (mainly imports); increased export opportunities; reduced refinery inventories; and improved shutdown planning.

14. I consider that the availability of excess gasoline production capacity in Ontario is important to ensure competition in refining. Accordingly, I have examined the issue of excess gasoline production capacity in the Ontario refining industry through use of a model constructed for the purpose and it is my opinion that there exist sufficient gasoline production capacity to satisfy demand up to 1995, without major refinery capacity expansions. Individual refiners may elect to relieve octane stress through equipment additions before 1995.

15. There is also excess refining capacity in Quebec which is adequate to cover anticipated gasoline demand through 1995. In addition, Quebec has more ready access to imports of gasoline from a variety of foreign sources which are less economical for the Ontario market. In fact, based on historical import data, the refining industry and the independent resellers in Quebec have elected to satisfy substantial portion of gasoline demand through imports.

In considering Ontario/Quebec as a single market, it is my opinion that both provinces share similar characteristics, i.e. excess refining capacity and access to imports, neither of which will change as a direct result of the merger. As long as these conditions remain in effect, it is unlikely that competition will be lessened in refining as a result of the merger.

#### CONCLUSION

16. For reasons set out above, it is my opinion that in the Ontario/Quebec gasoline refining market, the merger, taken together with the provisions of the Draft Consent Order, is not likely to lessen competition for the foreseeable future. In the Atlantic Region, any lessening of competition in the refinery sector has been eliminated by the divestitures required by the Draft Consent Order. Lastly, the merger has minimal impact on refining in Western Canada given that Texaco has no refining facilities in the region.