



February 10, 2023

Ms. Cheryl Blundon
Director of Corporate Services and Board Secretary
Newfoundland & Labrador Board of Commissioners of Public Utilities
PO Box 21040
St. John's, NL A1A 5B2

Via email: ppreview@pub.nl.ca

Dear Ms. Blundon:

Subject: Petroleum pricing review issues list

The Convenience Industry Council of Canada (CICC) is a national, not-for-profit trade organization representing retail owners, operators and suppliers in Canada's convenience channel. In Newfoundland and Labrador, convenience stores are the largest retailer of motor fuels.

The CICC welcomes the opportunity to provide input into your issues list for the petroleum pricing review that is being undertaken. The CICC's input is specific to retail motor fuel but may have overlap and applicability to wholesale motor fuel.

Our issues list for consideration is as follows:

1. Should there be an increase in the maximum retail mark-up for self-service gasoline and diesel based on changes in operating costs since the last benchmark year of 2019? If so, by what amount?

A review of the maximum retail mark-up is fundamental to the price review process. The last retail mark-up used 2019 as the end year for operating cost change analysis and mark-up adjustment. Given the timing of the retail portion of the pricing review, a comparison of operating cost changes between 2019 and 2022 would be appropriate.

2. Is there a need to change the methodology for establishing the benchmark premium unleaded price? If so, what should that methodology be?

Since regulation was introduced, a fixed 6.0 cents per litre has been added to the established regular unleaded benchmark to derive the premium unleaded benchmark. Global marketplace volatility in 2022 resulted in extended periods where the actual differential cost of premium unleaded well-exceeded the fixed 6.0 cpl differential. This issue is currently under review by Nova Scotia and New Brunswick.

3. Is there a need to change the ‘interrupter clause’ provisions to better minimize the impact of marketplace volatility on regulated motor fuel pricing? If so, what changes should be made?

Several individual and concurrent global marketplace conditions in 2022 resulted in extreme volatility in the pricing of motor fuel products, resulting in numerous instances of the triggering of the interrupter mechanism. While the mechanism is intended to smooth volatility, frequent use of the interrupter can have a detrimental effect on retail mark-ups realized to the point where product could be selling at a loss.

4. Is there a need for the addition of a market adjuster component to the pricing formula? If so, what should the methodology be?

Historically, any adjustment in the retail motor fuel mark-up has been based on changes in operating costs between two review periods. Over time, decisions to adjust have been based on: a) a general assessment of marketplace changes; b) surveying of retailers; and c) an index-based model.

Decisions to adjust the retail mark-up lag the actual market given the time between ‘reviews,’ and the time to conduct a review. A case in point is this review itself which was initiated in 2022 and where any retail mark-up adjustment decision would not take effect until 2024.

Retailer experiences in recent years have highlighted material increases in major operating cost components compared to the end-year of the last review. With no mechanism for relief, retailers are forced to absorb these increases, resulting in material erosion of what should be a reasonable and consistent maximum retail market-up.

Nova Scotia has investigated and implemented a market adjuster component that currently addresses and adjusts the retail mark-up accordingly to reflect changes in the cost of merchant card fees paid by retailers compared to the most recent mark-up review end year. Any adjustments will then be reconciled as part of the next retail mark-up review. New Brunswick is currently in the process of introducing a market adjuster component and establishing what the methodology should be.

5. Is there a need to change the process for changes to the mark-ups and differentials? If so, how?

As per the Board’s issues list, mark-up reviews are infrequent. And though they are critically important, they are lengthy and time consuming when initiated. It is notable that the New Brunswick Energy and Utilities Board has made efforts to shorten the period between reviews and initiates reviews themselves rather than waiting for an application by a retailer. In the other Atlantic provinces, a retailer must submit an application for adjustment and a Board then typically initiates an industry-wide review.

It is well worth considering a change in process that may include the introduction of a market adjuster component that addresses material changes in operating cost components between formal mark-up reviews.



6. Should consideration be given to establishing minimum mark-ups?

The retail motor fuel industry has long maintained that a minimum/maximum model does not adversely impact motorists overall while contributing in a meaningful way to financial stability and continuity of supply among retailers, especially independent rural retailers. In Nova Scotia and Prince Edward Island, a minimum is significantly important in the ability of a retailer to successfully secure reasonable financing, be it lines of credit or loans for capital expenditures, for day-to-day operational needs and/or infrastructure upgrades.

7. Is continuity of supply being impacted? If so, what measures can be taken to mitigate this?

For many motor fuel retailers, particularly those supporting rural communities, motor fuel profitability and financial stability are declining as volume throughput and gross margins are not keeping pace with increases in operating costs and capital investment requirements. With respect to capital investment, it is becoming increasingly difficult to cost justify investments in major capital expenditures, such as underground tank replacement. Without these investments, a retail outlet would have no option but to close at a time when motor fuel marketplace coverage in many rural areas is already 'bare bones.'

8. How does the current retail mark-up review methodology motivate independent retailers to participate?

In the previous two retail mark-up reviews, the PUB utilized an index-based model of cost indicators. For this review, the consultant is utilizing a survey-based methodology. The survey instrument developed is the most complex of any that CICC staff have seen in more than 10 years of being actively involved in retail mark-up reviews in Atlantic Canada.

Adequate retailer participation in an operating cost survey has always been a major issue, particularly among independent retailers. The CICC is concerned that the level of detail being asked for will be a considerable dis-incentive to survey participation. This presents the obvious risk of the sample not being reasonably representative of the population of retailers in Newfoundland and Labrador, but still being submitted as the prime piece of evidence for retail mark-up adjustment decision making.

The CICC also notes that the survey instrument asks for a percentage allocation of operating costs reported to "motorist fuel sales." This appears to be a step backwards in survey methodology as there have been numerous discussions and rulings rendered over the years in other regulated jurisdictions as to the ability of retailers to reliably delineate between 'gas' and 'non-gas' operating costs along with the risk of bias with self-declared cost splits. In the absence of processes to reliably capture the gas/non-gas split, rulings in other jurisdictions state that total site operating expenses are to be used.

Thank you for consideration of these comments and please don't hesitate to reach out with any questions.

Sincerely,



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