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February 10, 2023

Public Utilities Board
Petroleum Pricing Review
PO Box 21040
Confederation Building
St. Johns, NL
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ppreview@pub.nl.ca

Re: Issues to be addressed in the 2022-2023 Petroleum Products Pricing Review – Phase I

Dear Board Members,

On behalf of North Atlantic, Newfoundland and Labrador's largest fuel supplier, I am pleased to provide comments and a suggested list of items to consider as part of Phase I of the 2022-2023 Petroleum Products Pricing Review.

The Clean Fuels Regulation (CFR)

It is our understanding that the CFR will be addressed via a process outside of the 2022-2023 Petroleum Products Pricing Review. The timelines detailed in the consultation document well exceed those required to address the CFR which has its first obligation period beginning on July 1, 2023. We would like to emphasize that this deadline is quickly approaching, and it is imperative that a mechanism is established well in advance of July 1, 2023, to address the increasing cost of fuel related caused by the CFR and to ensure fuel security to the province.

Wholesale Mark-up (Transportation and Heating Fuels)

The existing mark-up model is not reflective of current costs as our industry has experienced increases in many areas:

1. Increased transportation costs (rates and fuel surcharge) for transporting fuels from the marine terminal to the retail stations or bulk terminals. In fact, at times in 2022 the fuel surcharge exceeded freight costs. This is applicable for both on-island and off-island transportation. All propane continues to be imported from terminals in Nova Scotia and New Brunswick and is subject to these increased costs.

2. The cost of fuel acquisition relative to benchmarks has gone up based on supply and demand.
3. The cost of hedging has increased. Given the extreme volatility in prices, North Atlantic has to hedge the price risk of its inventory.
4. Increases in interest rates and as inventory is priced in USD, we have to finance it in USD, which further increases the financing costs.

Zone Differentials

North Atlantic recommends that a comprehensive review of the zones and differentials be undertaken as this has not be reviewed since price regulation was established. A large percentage of the volume sold in many of the zones in this province are delivered to retail Sites and bulk terminals by bulk hauler from Come By Chance. Delivery rates to these zones from Come By Chance continues to increase, along with fuel surcharges that have been added in recent years by the bulk haulers. The zone differential for these zones should be increased to reflect the incremental cost of transportation vs. the base zone.

Gasoline Grade Mark-ups

With respect to the wholesale mark-up for Mid-grade and Premium gasoline, the current wholesale mark-ups for Mid-grade and Supreme is less than Regular. Typically, wholesalers receive higher margins on higher grade products. We recommend that the wholesale margin for Mid-grade and Supreme be greater than Regular and recommend that a review be completed.

Retail Mark-up Models

As an overarching statement, the existing retail mark-up models for Heating and Transportation fuels are based on 2019 and not inclusive of the increase in costs for the past 3 years which needs to be considered in the review.

Retail Mark-up (Heating Fuels)

Our industry has experienced cost increases for the delivery of Heating Fuels (Oil and Propane) from the bulk terminal to the Home Heat customer through both the company operated and distributor models. The increases include:

1. Insurance
2. Trucks, parts, and maintenance
3. Increased wages and employee retention programs
4. The increased cost of fuel used by delivery vehicles to deliver heating fuels to customers.
5. Increased number of deliveries as customers place smaller orders due to the increased price of heating fuel.

Also, the Home Heat business is under tremendous pressure with the electrification incentives that exist today. The volume decline has already started, and this decline is projected to continue. Increasing costs and decreasing volumes, and thus gross margin dollars, is not a sustainable model making our industry unviable.

Retail Mark-up (Transportation Fuels)

The Retail business has also been impacted with cost increases in many areas (processing fees, labour, insurance, maintenance, etc.), but for the purposes of this review we strongly urge that the focus be on processing fees and labour, as they are the biggest drivers in the overall cost increase. Firstly, the COVID pandemic has accelerated society's transition to contactless payment. The number of customers paying via credit card tap has increased significantly with very few consumers using cash. Additionally, credit card fees charged to merchants are on a percentage basis; therefore, fees have skyrocketed with the increase in the pump price. These two points have resulted in significantly increased credit card fees at the retail level. Secondly, the minimum wage value which was used to develop the existing retail mark-up was based on the 2019 minimum wage of $11.40. The minimum wage is currently $13.70 and will be increased to $15.00 by October 2023. This is a 32% increase in wages which is not currently included in retail mark-ups.

Like the Home Heat business, there has also been a decline in transportation fuel volumes since 2019 and the expectation is that volumes will continue to decline with less commuting due to hybrid working models and as EV adoption increases. As volumes decline, gross margin dollars in turn decline but the costs of operations continue to rise. Consideration must be given to the retail mark-up to ensure the future viability of the independent retailer and to ensure supply security in rural areas of the province.

Extraordinary Adjustments

While notice of extraordinary adjustments is not intended to be publicized, recent months have indicated that this information is challenging to control. Early release of extraordinary adjustment has resulted in the refusal of scheduled deliveries in advance of an expected price decrease and overwhelming requests for fuel delivery prior to expected price increases. In addition to these logistical issues, we are concerned that the adjustments are damaging the reputation of the industry. North Atlantic requests that alternatives to extraordinary price adjustments be considered in the review process and suggest that consideration be given to two scheduled price changes per week (Tuesday and Friday) that could smooth out the volatility.

Establishment of Benchmark Prices

Currently the Public Utilities Board establishes prices based on a 7-day average with Friday's posting carrying over for Saturday and Sunday. Given the volatility experienced since March 2022, a big swing up or down on the Friday value can further exasperate the price swing. North Atlantic recommends that consideration be given to establishing prices based on a 5-day average.

Establishment of a Minimum Price

A minimum fuel price contributes to a diverse supply chain in which retailers, wholesalers and primary suppliers can all benefit. It also helps provide fuel security in circumstances where it might otherwise be at risk. Minimum fuel price requirements are currently included in Nova Scotia, Prince Edward Island and Quebec regulations.

Impacts from the NARL Refinery Closure

The refinery closure has had a significant impact on the cost of providing fuel to the local market that needs to be considered as all suppliers have experienced incremental terminal costs. As an example, all suppliers of propane on the island have had to build additional storage capacity which comes with both capital and operating costs.

Again, we very much appreciate the opportunity to provide comments on the Phase I review and look forward to engaging on future phases. Should you have any questions or wish to discuss further, please feel free to contact me at (709) 570-5640.

Sincerely,

David Button
Chief Executive Officer
NARL Marketing Limited Partnership