PUBLIC

Proposed acquisition of Esso's wholesale road fuel supply business by Roberts Garages Ltd
Case M1034J

Decision

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Jersey Competition Regulatory Authority
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Summary

1. Roberts Garages Limited is proposing to acquire ten wholesale contracts from the Esso Petroleum Company for the supply of road fuel to Esso's ten branded fuel forecourts. Three of these forecourts are owned by Roberts. This acquisition has been duly notified to the Jersey Competition Regulatory Authority for approval under Articles 20 and 21 of the *Competition (Jersey) Law* 2005.

2. The JCRA has assessed the proposed acquisition and has given conditional approval. The condition ensures transparency in the wholesale prices charged by Roberts to all ten forecourts and that it will continue to be set on the same basis as at present by Esso. Furthermore, movement in wholesale prices will be linked to publicly referenced global input prices, ensuring changes in prices are transparently justified.

The Notified Transaction

3. The Jersey Competition Regulatory Authority (**JCRA**) registered an application (the **Application**) for approval under Articles 20 and 21 of the *Competition (Jersey) Law* 2005 (the **Law**) on 30 July 2014. Roberts Garages Limited (**Purchaser**) is proposing to acquire ten wholesale contracts from the Esso Petroleum Company (**Seller**) for the supply of road fuel to Esso's ten branded fuel forecourts.

4. The JCRA invited comments and received seven submissions (**Submissions**) opposing the merger. The JCRA also held discussions with some of the objectors. A summary of their comments and key points in the Submissions are reported in section 20.

The Parties

Roberts Garages Limited (Purchaser)

5. Roberts Garages Limited, the Purchaser, is a company incorporated in Jersey and is ultimately owned by MRH (GB) Limited, incorporated in England and Wales.

6. The Purchaser is involved in the retail sale of motor fuel in Jersey. The group of companies owned by its ultimate parent company – MRH (GB) Ltd – is involved in the retail sale of motor fuels in Great Britain and the wholesale storage and distribution of liquid fuel products in the Isle of Wight.

Esso Petroleum Company (Seller)

7. The Esso Petroleum Company, the Seller, is ultimately owned by Exxon Mobil Corporation. Its core activities in Jersey, up to now, include the wholesale supply of road fuels and of packaged lubricants for resale.

Acquisition

8. The Seller has exclusive contracts with ten Esso-branded forecourts for the wholesale supply of road fuels. The proposal is that these ten contracts would be novated to the Purchaser.

9. It is estimated that these contracts account for [REDACTED]% of the total retail market for road fuel (estimated by the JCRA in 2011 to consist of 43 million litres per annum) or [REDACTED] million litres. This amount includes [REDACTED] million litres supplied to Roberts' three forecourts ([REDACTED]% of the total market).

Requirement for JCRA Approval

10. According to Article 20(1) of the Law, a person must not execute certain mergers or acquisitions except with and in accordance with the approval of the JCRA. According to Article 2(1)(b) of the Law, a merger or acquisition occurs for the purposes of the Law if a person who controls an undertaking acquires direct or indirect control of the whole or part of another undertaking.

11. Moreover, a merger or acquisition is subject to Article 2(1)(b) of the Law if it satisfies a relevant condition in the Competition (Mergers and Acquisitions) (Jersey) Order 2010 (**Order**) applicable to the specific merger or acquisition under consideration. CICRA's Guideline 6 on Mergers and Acquisitions provides definitions of the three main types of mergers: "Mergers can be categorised as horizontal, vertical or conglomerate. Horizontal mergers involve a merger between parties at the same level in the supply chain; for example, between two retailers, or several producers of the same good or service in the same geographic market. Vertical mergers typically involve either a merger between a business and its supplier or a business and its customer. Conglomerate mergers cover all other types of mergers."

12. The Acquisition is a vertical acquisition as the Purchaser, which is active at the retail level in the provision of road fuel through its forecourts, is acquiring a wholesale business that is also concerned with the provision of road fuel and which, in particular, supplies its retail business.

13. According to the Order, a vertical acquisition is of the type to which Article 20(1) of the Law applies if, in the specific case here:

- One of the undertakings has an existing share of 25% or more of the supply of goods supplied to persons in Jersey; and
- Another undertaking involved in the acquisition is active in the supply of goods that are upstream or downstream of the goods in which the 25% share is held.

14. As the Seller has a share of the wholesale supply of road fuel of more than 25% and as the Purchaser is active in the retail supply of road fuel, an activity that is downstream of the wholesale supply of road fuel, the Acquisition satisfies the condition in Article 3 of the Order. Therefore, the Acquisition is of a type to which Article 20(1) of the Law applies and the JCRA's approval is required before the Acquisition is executed.

Market definition

15. Under Article 22(4) of the Law, the JCRA must determine if the Acquisition would substantially lessen competition in Jersey or in any part of Jersey. To this end, the JCRA needs to identify the markets which are likely to be affected by the Acquisition and, in a second stage, to assess whether competition in these markets will be substantially lessened. The relevant markets for the Acquisition are identified in this section. The impact on competition is assessed in the next.

16. The process of identifying markets is essential to the JCRA's analysis because, by identifying where customers purchase the goods and services they need, the analysis assesses whether customers have an appropriate range of alternatives over which to exercise their choice. In particular, it assesses whether substitutes exist and customers are more or less restricted in the alternatives (price, quality, quantity, etc.) available to them. It is customers' ability to exercise their choice that ensures that markets function well and encourage innovation and 'best endeavour' on the part of suppliers.

17. In the case of a vertical merger, the customers immediately affected by the acquisition may not only be the end customers – those who buy fuel for their individual cars at forecourts – but the forecourts themselves, who buy fuel from a wholesale supplier. The JCRA's assessment is that there are two relevant markets: one in which forecourts negotiate contracts for the provision of road fuel to their premises, namely the wholesale market for road fuel, and another market where forecourts sell road fuels to end customers and compete with other forecourts for business, namely the retail market for road fuel.

Geographic scope of the markets

18. In previous decisions, the JCRA has established the relevant geographical market in such road fuel transactions is the whole of Jersey. There is no evidence in this case to alter this conclusion.

Assessment of Relevant Markets

19. Under Article 22(4) of the Law, the JCRA must determine if the Acquisition would substantially lessen competition in Jersey or in any part of Jersey. While the Acquisition would not change the number of wholesalers operating in the wholesale market, since Esso would simply be replaced by the Purchaser, the Acquisition may lead to a substantial lessening of competition in one or both of the retail and wholesale markets by virtue of the vertical integration it entails.

20. The JCRA received a number of responses to its consultation. They came from stakeholders involved in the supply of road fuel. The main points made in these responses were:

- The acquisition could drive some of the independent forecourts out of business and generally, substantially reduce competition to the detriment of customers. The Purchaser has proved willing in the past to give substantial discounts to customers to win their business.
- A prominent retailer should not hold a wholesale supply business.
- The acquisition gives a prominent retailer visibility of its competitors' margins and volumes.
- Since wholesale supplies will be in the hands of a competitor, a retailer will not be able to determine whether the wholesale price (including rebates, etc.) it is charged is fair, in view of price volatility on the global oil market. The JCRA will not be able to verify the Purchaser' non-discriminatory pricing commitments.
- If supplies are short, the Purchaser as a wholesaler will give priority to its own retail outlets.
- A further party in the supply chain will inevitably mean that prices will rise.
- The Purchaser' forecourt business will have an unfair advantage over other retailers because it will be vertically integrated, reducing costs compared to retailers that have to pay a wholesaler's margin and putting the wholesalers other than the Purchaser at a disadvantage.
- The deal will irreparably damage a competing retailer's ability to negotiate competitive supply arrangements.
- Esso should have given the opportunity to buy its wholesale business to parties other than the Purchaser

- The novation to the Purchaser is detrimental to retailers generally because the Purchaser does not have Esso's financial resources and its expertise in supporting forecourts.

21. Having considered these comments and its statutory duty, the JCRA came to the conclusion there were two main issues at stake:

    - Should vertical integration be automatically ruled out when a wholesaler has a retail business that competes with some of the clients of its wholesale arm?
    - If such vertical integration is not automatically ruled out, does it substantially lessen competition in the relevant retail or the wholesale markets and can the risks to competition be sufficiently reduced by imposing behavioural restrictions on the vertically-integrated entity?

    In deciding these two issues according to the CICRA Guideline on Mergers and Acquisitions, the JCRA focussed on 'assessing whether the merged entity would have the ability or incentive to foreclose the market to competitors, either by denying access to important inputs upstream, or by denying access to "routes to market" downstream.'

22. On the question of whether vertical mergers should be automatically ruled out, the European Union Guidelines on the assessment of non-horizontal mergers (2008/C 265/07) note that a vertical merger does not entail the loss of direct competition between merging firms, as would be the case with a horizontal merger. While a vertical merger may strengthen the position of the merged entity, which may lead to dominance and an abuse of this dominance, a vertical merger may also have positive outcomes for customers by providing scope for efficiencies and reducing transaction costs. These improvements may then put competitive pressure on competitors in the markets in which the merger entity operates, which may further benefit customers.

23. The JCRA does not consider it should refuse approval of a vertical merger in principle and assesses the Acquisition on its specific merits. To do so, the JCRA needed to compare the situation that would prevail in Jersey if the Acquisition did not go ahead with that which would result from the Acquisition.

24. The JCRA believes that, if it did not approve the Acquisition, the more probable counterfactual is that the Seller would let the contracts it has with its forecourts progressively lapse – they are all of short-term duration. As a result, the number of wholesalers in Jersey would be reduced from three to two. An alternative counterfactual is that the Seller would sell its supply business to another company. However the JCRA has no evidence that the

Seller would do so and, in fact, one of the respondents has complained to the JCRA that it was denied the opportunity to purchase the contracts even though it was well known to the Seller. The JCRA has no power to mandate to whom the Seller should sell.

25. The JCRA agrees that the Acquisition increases the risk of significant lessening of competition. The JCRA therefore assessed the risk that the Purchaser could engage in some form of input or customer foreclosure – when access by an actual or potential rival to supplies (input) or markets (customer) is hampered or eliminated as a result of the Acquisition. The JCRA also considered whether such a foreclosure risk could be sufficiently reduced by imposing conditions on the Purchaser before the JCRA could approve the Acquisition.

26. Customer foreclosure would arise if, post-Acquisition, the Purchaser was able to prevent other fuel wholesalers from contracting with the forecourts it would be supplying under the proposed contract novation. The JCRA concluded customer foreclosure would not arise because forecourts would be free to contract with other wholesalers at the end of their current exclusive contracts many of which, as noted, are of relatively short duration.

27. The risk of input foreclosure is that the Purchaser may refuse to supply rival forecourts. However, the current contracts it is acquiring commit it to supply these forecourts. It would therefore be in breach of these contracts if it did not supply rival forecourts. If it refused to renew these contracts at their expiry, the affected forecourts would negotiate with the other two wholesale suppliers, a situation in which they would be no worse off than if the Acquisition had not gone ahead.

28. The risk of input foreclosure is also that the Purchaser may charge forecourts a higher price than they have contracted to pay to the Seller – or provides lower quality fuel to competing forecourts, which the JCRA considers analogous to a price rise. At the moment, the wholesale price which the Seller charges all the forecourts it has contracted to supply is not a fixed common price for all forecourts but a price that can be different for forecourts by contract, which moves on a weekly basis by reference to the Seller's base wholesale prices (referred to as a weekly schedule price). The price changes are communicated to forecourts by means of a weekly e-mail from the Seller. The Purchaser has indicated its intention to continue this practice.

29. However, the JCRA has concluded that the base wholesale prices that the Purchaser will communicate on a weekly basis need to be linked in a transparent way to public reference prices. Without this transparency,

forecourts would have no means of verifying changes in the base wholesale prices match changes in reference prices and, in particular, they are not disadvantaged relative to a rival forecourt owned by the Purchaser. The JCRA understands the authoritative record of wholesale prices for a range of fuels is published by Platts (McGraw Hill Financial)[1]. The JCRA therefore sought and obtained the following undertaking from the Purchaser:

Undertaking: **Roberts Garages and MRH will provide a weekly schedule price distributed to Esso branded forecourts, as currently provided by Esso. The weekly schedule price will be directly linked to changes in the Platts price as published by McGraw Hill Financial.**

In this way each forecourt will have assurance that the only movement in the schedule price provided by Roberts Garages and used to determine its charges to Roberts is fully explained by movements in the average Platts price per litre.

30. The JCRA is satisfied that this level of transparency will enable forecourts supplied by the Seller to verify they are charged on a transparent basis and are set by reference to movements in a publicly referable price, ensuring the Purchaser maintains its commitment made when the JCRA approved the Acquisition.

Conclusion

31. The JCRA has determined that the Acquisition is a case of vertical integration that will not cause a substantial lessening of competition in the fuel wholesale or retail markets provided the Purchaser agrees the commitment stated in section 29 above. On this basis the JCRA approves the Acquisition.

December 2014 **By Order of the JCRA Board**

1 For use in Jersey, Fuel Prices Online is licensed by Platts to provide weekly average prices and convert them from dollars to pound sterling.