Anticipated acquisition by DCC plc of CPL Petroleum Limited

The OFT's decision on reference under section 33(1) given on 24 August 2007. Full text of decision published on 4 September 2007.

Please note that square brackets indicate figures or text which have been deleted or replaced with a range at the request of the parties for reasons of commercial confidentiality.

PARTIES

1. **DCC plc** (DCC) is a procurement, sales, marketing, distribution and business support services group. DCC has five core businesses: DCC Energy, DCC SerCom, DCC Healthcare, DCC Food and Beverage and DCC Environmental. DCC Energy distributes liquefied petroleum gas (LPG) and oil products in Great Britain & Ireland. GB Oils Limited (GB Oils) is DCC's oil distribution business in Great Britain. It distributes oil products to domestic, commercial, industrial and agricultural customers in GB.

2. **CPL Petroleum Ltd** (CPL) is a distributor of oil products and is wholly owned by CPL Industries Holdings Ltd, a privately owned company. The turnover of CPL for the financial year ending 31 March 2007 was £418 million.

TRANSACTION

3. DCC proposes to acquire 100 per cent of the issues share capital of CPL for a consideration of £50 million on a debt free/cash free basis. The transaction was notified by way of a merger notice on 27 July 2007. The statutory deadline expires on 24 August 2007.

JURISDICTION

4. As a result of this transaction DCC and CPL will cease to be distinct. The UK turnover of CPL exceeds £70 million, so the turnover test in section 23(1)(b) of the Enterprise Act 2002 (the Act) is satisfied. The OFT therefore believes that it is or may be the case that arrangements are in progress or in contemplation which, if carried into effect, will result in the creation of a relevant merger situation.

FRAME OF REFERENCE

Product market

5. Both parties distribute heating oils and transport fuels to domestic, commercial, industrial and agricultural customers. There are five basic oil products supplied by GB Oils and CPL: diesel; gas oil; kerosene; fuel and petrol.[1]

6. The parties assert that there is no meaningful distinction between heating oils and transport fuels. For example, while gas oil and heavy fuel oil are generally used as heating oils, gas oil is also used by some customers as a transport fuel and heavy fuel oil is used as a transport fuel for maritime purposes.

7. We found little evidence of demand-side substitution. Customers were unlikely to switch to a different product in response to a rise in price as there are no directly substitutable products for many applications, without undertaking significant engineering changes.

8. On the supply side however, there is the potential for significant substitution in the distribution of fuels. The parties stated that almost all tankers have separate compartments to allow simultaneous transport of fuels and in practice, the majority of distributors supply both heating oil and transport fuel. In general, third parties felt that switching costs for suppliers were low. However, we were told by one third party that once a tanker had been used to carry heavy fuel oil it couldn't then be used for anything else as it leaves a heavier residue than other oils.

9. Therefore, on this basis, we consider the distribution of heating oils and transport fuels to be the appropriate product frame of reference. There is limited evidence, as outlined above, that heavy fuel oil may constitute a separate frame of reference if it restricts the type of fuel that can be distributed in tankers. However it is not necessary to conclude on this point as considering heavy fuel oil separately does not substantially change the competitive assessment.

Geographic market

10. The parties assert that the typical catchment area for a depot is on average 30-50 miles. The overlapping catchment area between the parties' depots may suggest a wider frame of reference. The parties argue that this chain of substitution effect supports a national, or at least regional, geographic frame of reference. Based on the information provided by the parties on the specific depot locations in this case, no competition concerns arose on any

[1] DCC also distribute Liquefied Petroleum Gas (LPG).

geographic frame of reference. No third parties suggested that the market should be wider than GB.

11. It was put to us that the Highlands and Islands in Scotland form a separate geographic market as the limited road network and fewer customers make it more expensive to supply. We therefore also considered Scotland and the Highlands and Islands separately.

12. However, it was not necessary to reach a definitive conclusion on this point as this transaction does not raise competition concerns, regardless of the geographic frame of reference considered.

HORIZONTAL ISSUES

Market shares

13. The parties estimate that post transaction, their combined share of supply (by volume) for the distribution of heating and transport oils in GB will [not exceed 10 per cent]. With regard to the four areas of Scotland, the North, the South West and the South East, the parties' combined share of supply, following the transaction, will not exceed 22 per cent in any area.

14. Both parties operate across England and Wales and named six other large national/regional suppliers. Data provided by the parties on depot locations shows that the parties will continue to face competition from at least five large suppliers in each broad area of the North, the South West and the South East. [2]

15. In addition, the parties stated that there were over 250 smaller regional and local suppliers that compete with the parties in specific areas. All customer comments supported the parties' assertions that local and regional suppliers compete effectively with national providers and that national customers are happy to split contracts into a number of local or regional contracts and in some cases even prefer to use a range of suppliers.

16. With regard to Scotland, DCC is the largest player with 24 depots, compared to CPL with three. As such the increment from the transaction will be relatively small. Post merger DCC will continue to face a competitive constraint from three large regional players, three firms of similar size to CPL in Scotland, and a large number of smaller local suppliers.

17. We considered the Highlands & Islands separately and focused on Inverness where CPL has its only highlands depot. In addition to DCC, we identified at least three key competitors with depots at Inverness.

[2] The boundaries of what is considered North, South East and South West vary slightly from competitor to competitor.

Therefore, at worst, the merger could be considered as a five to four reduction in larger (multi site) suppliers that could provide an effective competitive constraint in this market. Furthermore, smaller local suppliers also operate within this geographical area. The parties assert that there are, in fact, nine distributors with depots in Inverness.

Barriers to entry and expansion

18. The parties consider the cost of entry to be low, with the only significant cost being the purchase and operation of a tanker, which they estimate to cost in the region of £60,000 per annum. The parties consider most new entrants would enter the market in a specific geographic location rather than on a national scale. DCC itself entered the market in 2001 and has grown to its current position through a combination of organic growth and acquisition. It was reported that a number of competitors have also recently expanded.

19. Third party comments were more mixed, however, and some considered that while barriers were still relatively low, they were increasing.

20. As the merger does not give rise to competition concerns it was not necessary to conclude in this case on the extent of barriers to entry and expansion.

Buyer power

21. The parties consider that there is significant buyer power amongst both spot and contract customers. Contract customers are usually large, sophisticated buyers, who can decide which suppliers they want to invite to tender from a large number of possible distributors. Spot customers can and do switch suppliers regularly – often on a weekly basis – to the lowest cost provider.

22. All competitors who commented on buyer power considered that there were a number of buyer groups, particularly for domestic and agricultural customers, able to negotiate discounts based on volumes. In addition, one competitor stated that there were a number of large commercial customers able to negotiate discounts.

23. Customer comments were more mixed although the majority felt that they were able to negotiate, to some extent on price, based on volumes purchased. Only two customers considered that the merger would reduce their ability to negotiate.

24. As the merger does not give rise to competition concerns it was not necessary to conclude in this case on the extent of buyer power.

VERTICAL ISSUES

25. The merger does not raise any vertical concerns.

THIRD PARTY VIEWS

26. We contacted several competitors located across England and Wales and the majority that responded stated that customers can and do switch regularly if prices increase and that there would be no cost to switching supplier. Similarly, the majority of customers in England and Wales considered switching to be relatively easy.

27. The vast majority of customers and competitors considered that local and regional suppliers compete effectively with national providers and that national customers can and regularly do split their contracts between a number of suppliers.

28. We also contacted competitors and customers in Scotland. No competitors raised concerns in relation to Scotland including the Highlands & Islands. Of those serving central and southern Scotland, one stated that customers regularly switch supplier for as little as a 0.1 per cent differential in price.

29. Customer comments in relation to Scotland were more mixed, however, and two customers raised concerns. They considered that if prices increased they would switch suppliers but were concerned that the market is already quite small and the merger would limit competition further. Whilst they considered that switching suppliers was an option, it would be costly in terms of time spent conducting a tender exercise and that the merger would reduce their ability to negotiate. In contrast, the other customers we spoke to had no concerns and considered there to be lots of independents they could use.

ASSESSMENT

30. The parties overlap in the supply of heating oils and transport fuels in GB. Their combined share of supply will not exceed 10 per cent on a national level and 22 per cent in any of the four areas identified. No competitors raised concerns in relation to the acquisition generally or in relation to any specific localities within England & Wales. The few concerns raised by consumers in relation to competition in Scotland, and specifically the Highlands & Islands, were considered but analysis found that post-merger a number of strong competitors will remain. The OFT does not, therefore, believe that the merger will result in a substantial lessening of competition in any market in Scotland.

31. On the basis of the number of other suppliers, the ease of switching and the lack of third party concerns, the OFT does not believe that it is or may

be the case that the merger may be expected to result in a substantial lessening of competition within a market or markets in the United Kingdom.

DECISION

32. This merger will therefore not be referred to the Competition Commission under section 33(1) of the Act.