REPORT ON ANTI-COMPETITIVE CONCERNS IN OREGON GASOLINE PRICES

Submitted to the United States Department of Justice and the Federal Trade Commission

By U.S. Senator Ron Wyden

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Summary:

Earlier this year, the price of gasoline in Oregon rose at a faster rate than ever before. From an average price of $1.09 per gallon in December 1998, the price went over $1.60 per gallon in April. In the course of investigating whether these unprecedented price increases were the result of market conditions or possible anti-competitive practices, I have acquired information about certain oil company practices affecting competition in retail gasoline markets in Oregon.

I am providing this information to supplement my initial request to Assistant Attorney General Joel Klein for an investigation of gas pricing practices. Along with this information, I am forwarding, on a confidential basis, the names of interested parties in Oregon who are willing to provide detailed information about gasoline pricing practices.

Investigative Findings:

Oregon consumers, gasoline dealers and other interested parties describe a process by which major oil companies affect the retail price of gasoline available to Oregon consumers via several methods:

1) oil companies charge different prices for the same quality petroleum products;
2) oil companies alter the price of gasoline they sell to service stations based on a practice known as zone pricing; and
3) oil companies artificially affect prices in each zone by inserting company-operated stations. In addition to these current practices, proposed mergers raise competitive concerns for Oregon gasoline markets.

During the course of extensive interviews conducted by my staff, dealers asserted that the oil companies with which they are affiliated do not talk openly about zone pricing, or any procedures used to control prices, and will deny the process if asked to comment.

Finding 1: Oil companies are charging vastly different prices for the same product.

Oil companies in Oregon have charged substantially higher wholesale prices for branded gasoline as compared to unbranded gasoline sold by the same company. On April 21, after gasoline prices peaked, The Oregonian reported that Oregon distributors were starting to see a reduction in wholesale prices with the price of wholesale generic gasoline reportedly coming down 30 cents per gallon as compared to an 8 cent reduction on brand-name fuels. The U.S. Supreme Court has ruled that an oil company engaged in illegal price discrimination in violation of the Robinson-Patman Act by selling the same grade and quality of gasoline at different prices to different buyers. Texaco, Inc. v. Hasbrouck, 496 U.S. 543 (1990). The major oil companies refine and sell both generic and brand-name gasoline in Oregon. If they are selling the same product to their own branded dealer stations at a substantially higher price than they charge distributors (jobbers) for branded and unbranded fuel, this practice could violate the Robinson-Patman Act.

Finding 2: Oil companies are manipulating the Oregon gas market by discriminating against small businesses that are similarly situated.

Isolating prices by zones occurs when oil companies base prices on the most effective way to maximize profit for the oil company in arbitrary geographic areas or "zones." In some cases, this involves lowering prices in order to capture high volume, while at other times it may involve increasing prices. For example, oil company delivery trucks may carry dealer tank wagon (DTW) gas to dealer stations in Portland and Salem. They may charge dealers in Salem more than dealers in Portland, not because of the cost of transport, but because gas is selling at higher prices in the Salem zone.

Federal courts have found the practice of charging different prices for gasoline to two similarly situated purchasers to violate the Robinson-Patman Price Discrimination Act when the two purchasers are in "practical competition" even if the buyers are in different states. Ingram v. Phillips Petroleum Co., 259 F. Supp. 176 (D. N.M. 1966). Dealers in Oregon have reported instances where oil companies' zone pricing has resulted in their paying higher prices and losing business to nearby service stations selling the same brand of gasoline. This information suggests that the dealers are in practical competition with other stations that are charged a lower price for the same brand of gasoline, which could constitute price discrimination in violation of the Robinson-Patman Act.

Some oil companies regularly dispatch representatives to go out on the street and survey gas prices in each zone. This information helps the oil company to ultimately determine how much they should charge for gas they sell to their dealers in that zone. When gas prices at the pump shot up by 50 cents in Oregon, oil companies were doing daily surveys.

Finding 3: Oil companies may be using predatory pricing to maximize their share of the gasoline market at the expense of Oregon small businesses.

Finally, dealers have reported instances of company owned and operated stations selling gasoline to motorists at retail prices lower then the wholesale price the dealers paid for the same brand of gasoline. In order for a company owned and operated station to sell gasoline at a lower retail price than the company is selling its gasoline wholesale, the oil company would either have to be charging its dealers a wholesale price substantially higher than the gasoline costs to produce or else the company owned and operated stations would have to be selling gasoline at prices below their cost.

It seems unlikely that the operating costs of maintaining a company owned and operated station are low enough for company owned and operated station retail prices to be lower than dealers' wholesale prices. If the oil companies are in fact charging prices below their costs, such practices could constitute predatory pricing in violation of anti-trust laws.

Consumers are drawn by lower prices without realizing that one branded station is run by an Oregon small business person while the other is wholly owned and operated by a major oil company outside of Oregon. While the consumer may see some small savings in the short-run while buying the lower priced gasoline from the oil company's station, the consumer may see higher prices in the long-run if the Oregon dealer operated station cannot compete and goes out of business.

Proposed oil company mergers raise competitive concerns for Oregon gasoline markets:

Further concerns about gas pricing could be raised by several pending mergers of gas companies. At this time, Arco and British Petroleum have proposed merging, and news reports have indicated a possible merger between Chevron and Texaco. The biggest gasoline marketers operating in Oregon at this time rely heavily on Alaskan crude oil for their supplies. Right now, there are two primary sellers of Alaskan crude -- BP and Arco. If those two companies merge, the oil refineries that use Alaskan crude and the dealers who buy from them will have only one place to buy their oil from -- the merged BP/Arco corporation. Oil Daily recently reported that one of these refiners has already registered objections with the Federal Trade Commission to the BP-Arco merger, and is seeking long-term supply agreements to ensure that the merged company does not engage in price gouging.

Even without such practices from a merged BP/Arco company, the merger would raise concerns for consumers. Refineries are set up to process a particular type of crude oil. Converting to process oil from a different source is a costly process. If this merger is approved, the marketers operating in Oregon will be faced with the choice of purchasing from a monopoly seller, or spending considerable sums to retrofit their refineries to handle crude from another source. The higher costs will inevitably be passed on to the consumer.

Key Features of Gasoline Pricing:

There are two categories by which gas can be purchased by a station before it makes its way to the consumer: rack or dealer tank wagon (DTW). The method by which gas is purchased is determined by whether one is "jobber" (a distributor who owns a tanks truck) or a dealer.

SOURCE OF GAS	SUPPLIER	BUYER
Unbranded rack	Major oil companies	"Jobber" -- owns a tanker truck and sells to various users, such as large companies with high volume gas needs, and in some cases sells to stations.
Branded rack	Major oil companies	Jobber sells to station with an oil company contract allowing it to sell under that oil company brand.
Dealer Tank Wagon (DTW)	Major oil companies	Dealer who has an agreement with an oil company and is required to buy DTW from said company. Dealer may own or lease station property.