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EVIDENCE

Wednesday, August 27, 2008

Chair

Mr. James Rajotte

Subcommittee on Oil and Gas and Other Energy Prices

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● (1000)

[*English*]

Ms. Erica Pereira (Procedural Clerk): Honourable members of the committee, I see a quorum. We can now proceed to the election of the chair. I am ready to receive motions to that effect.

Hon. Dan McTeague (Pickering—Scarborough East, Lib.): Madam Clerk, thank you very much for this. I'm honoured to nominate Mr. James Rajotte, who I understand will get an increase in pay if we nominate him today as subcommittee chair—and of course we'll extend to this committee free lunches.

[*Translation*]

Ms. Erica Pereira: Mr. Dan McTeague moves that Mr. James Rajotte do take the chair of the subcommittee. Are there any other motions?

[*English*]

Is it the pleasure of the committee to adopt the motion?

Some hon. members: Agreed.

Ms. Erica Pereira: I declare the motion carried and James Rajotte the duly elected chair of the subcommittee.

Some hon. members: Hear, hear!

Ms. Erica Pereira: Before inviting Monsieur Rajotte to take the chair, if the committee wishes, we will now proceed to the election of vice-chairs.

[*Translation*]

I am now ready to receive motions for the position of First Vice-Chair.

[*English*]

Mr. Bruce Stanton (Simcoe North, CPC): I propose Dan McTeague as first vice-chair.

Ms. Erica Pereira: It has been moved by Bruce Stanton that Dan McTeague be elected as first vice-chair of the subcommittee. Are there any further motions?

Is it the pleasure of the committee to adopt the motion?

Some hon. members: Agreed.

[*Translation*]

I declare the motion adopted and that Mr. Dan McTeague is duly elected First Vice-Chair of the subcommittee.

[*English*]

I am now prepared to receive motions for the second vice-chair.

[*Translation*]

Hon. Dan McTeague: I have the great honour to move that Mr. Robert Vincent be elected Second Vice-Chair of the subcommittee.

[*English*]

Ms. Erica Pereira: It has been moved by Dan McTeague that Robert Vincent be elected as second vice-chair of the committee. Are there any further motions?

Is it the pleasure of the committee to adopt the motion?

Some hon. members: Agreed.

Ms. Erica Pereira: I declare the motion carried and Robert Vincent duly elected as the second vice-chair of the committee.

[*Translation*]

I now invite Mr. James Rajotte to take the chair.

[*English*]

The Chair (Mr. James Rajotte (Edmonton—Leduc, CPC)): Well, good morning, ladies and gentlemen. Welcome back to Parliament.

The media can now stop writing about the election because it's happened.

I thought we'd all be in much better humour this morning. I'm sorry, that was a bad joke.

Welcome back, and congratulations to Mr. McTeague; and *monsieur Vincent, félicitations*.

We do have two motions before we start with the witnesses. The first deals with routine motions. Everyone should have a copy. These are the motions that the industry, science and technology committee operates under. There are three pages. These are the same motions as we adopted for the industry committee. You'll note on page three that the rounds of questions are the same rounds of questions we operate with in the normal industry, science and technology committee.

Mr. McTeague.

● (1005)

Hon. Dan McTeague: I propose that all motions be allowed to stand and that they be adopted by this committee.

The Chair: Thank you.

(Motions agreed to)

The Chair: We are going to suspend for two minutes, because this committee is televised. So we will suspend and allow the committee to be televised. We'll also ask the witnesses for the first two-hour session to come to the table.

● _____ (Pause) _____

●

The Chair: Would members please take their seats, please? I remind members and witnesses that we are being televised for both the two-hour session this morning and the two-hour session this afternoon.

I want to read, for the benefit of members and witnesses and for the general public, the motion that was adopted:

> That the Standing Committee on Industry, Science and Technology strike a subcommittee whose membership be composed of all 12 members of the standing committee to hold approximately three meetings during the late summer or early fall to hear from representatives of the oil and gas industry, pension fund managers, institutional investors involved with global electronic exchanges, and relevant witnesses to explain the reason for the increases in the price of oil and gas.

That is the formal motion that was adopted. That's the reason for this subcommittee, and we have two sessions here today.

From 10 a.m. until noon, we have three witnesses. First of all, from the Canadian Petroleum Products Institute, we have Mr. Peter Boag, president. Welcome.

Secondly, we have Mr. Warren MacLean as an individual. Welcome.

Thirdly, from the Canadian Independent Petroleum Marketers Association, we have Ms. Jane Savage, president and CEO. Welcome.

We will start with Mr. Boag and work our way down. You have up to five minutes for an opening presentation and then we will go to questions from members.

Mr. Boag.

● (1010)

Mr. Peter Boag (President, Canadian Petroleum Products Institute): Good morning.

Thank you, Mr. Chair. I very much appreciate the opportunity to be here today to contribute to your deliberations on a very topical and important issue for Canadian consumers.

Far too often, when we contemplate the workings of the marketplace, there's a tendency to discount the role information plays in ensuring that consumers are well armed to make choices about how to allocate their hard-earned dollars. So your work and that of CPPI is important in ensuring that Canadians can make the best choices for themselves and their families.

As many of you know, the members of the Canadian Petroleum Products Institute are the major refiners and marketers of petroleum products in Canada. Collectively, they operate 16 refineries and supply the bulk of transportation fuel choices across Canada. Their presence, products, and services are a daily necessity for Canadians. At the very root of their existence, my members are intensely competitive companies that strive to provide high-quality, affordable products. No other industry interfaces with the consuming public with a street-level, transparent display of product prices and signs as large as you and I are.

Three markets influence the cost of fuels at these stations—markets that are driven by the economic fundamentals of supply and demand. The first two are international commodity and financial markets.

First is the global market for crude oil. Thousands of daily transactions are executed by traders around the world. I believe it's well recognized today that increasing global demand, especially from Asia and the Middle East, is fundamentally driving increases in crude prices. Just look at how many people are coming out of poverty in Asia, in particular, and upward pressure on crude prices should be no surprise.

Second is the North American market for wholesale fuels. There is no unique Canadian fuels market. Wholesale prices in Canada are driven by product supply and demand balances across North America.

The third market is the local retail market—the decisions of individual retailers in any given community at any given time. As of December 31, 2006—the most recent retail survey of Canada—there were 13,772 retail gasoline stations operating in Canada. With only about 30% of those retail outlets under the ownership of major refiners, there are more than 9,500 decision-makers involved in setting the posted price of fuel at gas stations across Canada.

In the Atlantic provinces and Quebec there is also an overlay of provincial legislation and regulation that limits competition. In the Atlantic provinces, they set a maximum pump price either weekly or twice a month. In Quebec, the Régie de l'énergie sets a weekly floor price.

All three of these markets—global, North American, and local—have shown considerable volatility in the last year, with Canadian pump prices reaching all-time highs in July.

Crude oil is by far the single largest component of the pump price. Data prepared by Natural Resources Canada shows that at the current average Canadian pump price for regular unleaded gasoline—as of earlier in August, that was $1.30 a litre—crude accounts for roughly 82¢ of that cost, or just under 65% of the pump price.

Pump price changes in Canada over the past months closely track changes in crude prices set in the global market. There are a couple of charts in my presentation that show how the price components break out across Canada and how the crude oil and gasoline prices correlate over the past number of months.

This same data shows that taxes are the second largest component of pump prices—on average 34¢ per litre across Canada, or about 26% of that average $1.30 a litre pump price. Finally, the data shows that refining and marketing operations account for the smallest component of pump prices. In early August it was about 14.5¢ a litre, or about 11% of the pump price.

Refining margins are substantially lower today than they were one year ago. I stress that margins do not equal profits. Refining margin is the difference between the price of crude entering the refinery and the wholesale price of fuel leaving the refinery. Profits, if any, exist only after all costs are paid. Refining margins in early August were hovering under 8¢ per litre, at about the same level as the national average marketing margin—the difference between the wholesale price exiting the refinery and the pump price consumers pay.

● (1015)

Refiners have been squeezed by the significant increase in crude prices over the past few months. According to data from NRCan: "For the four week period ending August 12th, refiner margins were below 8 cents per litre at the national level and trailed last year's levels by more than 9 cents."

Weakening U.S. demand has exerted downward pressure on North American wholesale gasoline prices. The most recent data available from NRCan—this is in early August—shows that on a national level wholesale prices in the United States and Canada were within 1¢ of each other.

While it may be of little consolation to Canadians, the volatility we have recently witnessed is not unique to Canada. What is unique to Canada is that, notwithstanding this turbulence, Canadians pay the second lowest price in the western world for petroleum fuels. This is a function of a competitive marketplace with a very efficient refining sector.

We acknowledge the important role that the federal government plays in ensuring our competitive marketplace, and in particular we congratulate this committee for the important work it has done over the years with its review of the Competition Act. In conjunction with a very professional and knowledgeable Competition Bureau, Canadians can have confidence in a marketplace framework that truly defends the rights of consumers. As the federal government looks to further improvements in the Competition Act, CPPI will be a responsible partner with government in keeping marketplace laws modern.

For the moment, I would like to bring to your attention and that of Canadians some of the factors that affect the cost of fuel produced and sold in Canada, factors that are unrelated to increasing the amount of fuel produced. Some of these considerations are justified by environmental considerations, but they are costs nonetheless. The decision to desulphurize fuel resulted in environmental expenditures of about $5 billion by the Canadian refining sector. In April of this year, the government eliminated the federal excise tax exemption on the blending of renewable fuels.

In conclusion, we understand Canadians' concerns and frustrations with fuel price volatility. At the same time, this is the best evidence of a marketplace delivering a choice of quality products at the lowest cost possible. Global supply and demand factors are the principal drivers of fuel prices, and while CPPI does not study all international dimensions, it is clear that the demand for fuel products is likely to rise in regions like Asia, where people are buying their first cars.

Taxes are the second largest component of pump prices, and while it is not the role of CPPI to evaluate taxation levels, this component is the single largest discretionary element in the cost Canadians pay. There are other government policies that are driving costs, some supported by sound scientific reasons for environmental improvement.

Our industry is committed to providing Canadians with quality fuels at the lowest possible cost, from safe and reliable facilities. We can also provide you with conservation tips to stretch your hard-earned dollar. At the end of the day, Canadians are best served by a competitive marketplace. Today they pay the second-lowest prices in the western world.

Thank you.

The Chair: Thank you, Mr. Boag.

Mr. MacLean.

Mr. Warren MacLean (As an Individual): I thought I'd start out by giving you a brief CV of my background. I graduated from McMaster University with a Bachelor of Chemical Engineering degree and a Master of Business Administration. I have worked in the petroleum industry for 32 years, 10 with Gulf Canada and 22 with Suncor. I've worked in both the upstream and downstream segments of the industry, including refining, supply, trading, wholesale marketing, crude marketing and logistics, strategic planning, and mergers and acquisition-type activities. I recently retired, on June 30, 2008, and the last position I held was vice-president, supply, distribution, and biofuels.

As for the purpose of the committee today, there have been significant concerns and questions recently that the run-up in price of crude and the associate products, gasoline and diesel, has been the result of speculation and not due to market fundamentals. I cannot answer the question around how much of the price rise is due to speculation and how much is due to fundamentals of supply and demand. I can try to help you understand various markets, price discovery and price-setting processes, and how they interact. My own personal belief is that it would be extremely difficult for speculators to drive the price against market fundamentals due to the size of the market, market liquidity, number of market players, and the complexity of the market, including such things as multiple locations, quality factors, refining configurations, and substitution effects.

So what I was planning to do is just walk through each of those sections, beginning with markets.

Crude oil is traded on a worldwide basis, whereas petroleum products tend to be traded more regionally. Major refining centres tend to be price-setting markets. Those include northwest Europe, the U.S. gulf coast, and the Far East, the Far East being represented usually by Singapore but may be switching to India as refining capacity in India grows. Prices for products tend to trade at the marginal cost of the high-cost refiner. Crude oil easily arbitrages between the three markets, whereas products usually are limited to trade in the Atlantic basin and the Pacific basin, logistics being the primary driver for the market segmentation.

In terms of price discovery, generally there are three means of price discovery: the futures markets in New York and London, what's termed the swap markets, and then the physical or cash markets.

Futures markets provide the highest level of price transparency limited to single highly liquid commodities with standard terms and conditions. Buyers and sellers put up margin and are protected by the exchange against default by counterparties. Markets are regulated.

Swaps are similar to futures but are not regulated and are usually between large highly sophisticated players. Risk of default is managed through the creditworthiness of the counterparties.

In physical markets, or cash markets, price discovery is limited somewhat to the major refining centres, such as the gulf coast. Buyers and sellers complete transactions on a daily basis and report these transactions to various industry publications such as Platts, Reuters, Opus, etc. These media then publish a list of crude and product prices for a range of qualities and different market locations. Contractual arrangements often use these publications to set transaction prices on a daily basis.

In terms of price setting, the price in any market is a function of the local supply and demand structure and the transportation cost to the major refining centre. In a supply-short market, price will be set at a transportation-plus basis. In other words, you take the price in the major refining centre and add the cost of transportation. In a supply-long market, price will be set on a transportation-minus basis, which is the reverse of the short market.

● (1020)

Added complexities include interactions between regional markets; regulatory requirements affecting quality; something I think you've probably heard, termed "boutique fuels"; structural product movements, where a company may own a pipeline to a particular market and will include the sunk cost of that pipeline in the pricing of their products—I would call that a structural product movement—and logistics barriers, such as the St. Lawrence Seaway being closed in the winter. All of these inhibit truck price transparency. Any of these factors make the price less transparent in that particular market.

To conclude, again I'll say that market size, complexity, and diversity all contribute to the unlikelihood of speculators driving prices contrary to fundamentals.

Thank you.

The Chair: Thank you very much, Mr. MacLean.

We'll go to Ms. Savage.

Mrs. Jane Savage (President and Chief Executive Officer, Canadian Independent Petroleum Marketers Association): Thank you for enabling CIPMA, the Canadian Independent Petroleum Marketers Association, to address this committee on the subject of oil, gas, and other energy pricing.

CIPMA represents the larger independent fuel marketers in Canada. What defines "independent" in the downstream sector, which is the refining and marketing sector of the oil industry, is companies that buy rather than refine the petroleum products they sell. Independents' profitability on gasoline is therefore tied closely to the retail margin, which is the difference between the price you and I pay at the pump and the cost at the wholesale level.

Of the 13,800 gas stations in Canada, as Mr. Boag mentioned earlier, about 70% are owned by independents, with the balance being owned by refiners. CIPMA has 15 member companies that own or have some level of control of about 15% of the retail sites in Canada; the balance are not represented by a trade association.

The subject of today's committee meeting is to understand more about the rising price of petroleum. Specifically, there are two aspects I would like to address: who is benefiting from this rising price of gasoline, and the speculative component of the crude oil markets.

We would like to contribute as best we can to that understanding, first by discussing the broad sectors within the Canadian oil industry, and specifically the relative profitability of the independent sector. We will do this in the context of gasoline. Second, we'll request that the committee take action to limit the speculative interests in the crude oil futures markets. We'll explain why this is important to the independent sector of the Canadian oil industry as well as Canadians.

Who is benefiting from the price increases at the pumps? The simple answer to that is crude oil producers. I've taken a long-term view of prices, and we see that crude oil has gone up 46¢ a litre of the total of 47¢ a litre in the past five years. There have been some cost changes. All sectors of the oil industry have seen cost increases, but we can safely say that most of the profit from higher gasoline prices is accruing to crude oil producers in this country, not to independents.

To simplify this complex industry—again, my colleagues have addressed this somewhat—there are three broad sectors in the oil industry. There are crude oil producers, which is traditionally called the upstream of the industry. And in the downstream there are two sectors: refiners and refiner marketers, and independent fuel distributors and marketers.

All three sectors work within the economic limit of a market-based margin that is given or determined by the market. As Mr. Boag pointed out, this does not necessarily reflect profit, but it reflects the available margin to each of these sectors. Refiners work with the difference between the market price of crude oil and the wholesale price of fuel products. Independent distributors and marketers work with the difference between the wholesale price of fuel products and the retail price that consumers pay.

Again, in the last five and a half years, we have seen an increase of about 47¢ a litre at the pump, and the vast majority of that has been in the sector known as crude oil production.

Contrary to what most Canadians think, almost 10,000 of the 14,000 gas stations, i.e., those owned by independent business people, have seen their available margin increase by a tiny amount, but net profit has been declining. That is simply because credit card costs increase as a percentage of the cost of fuel at the pump. Seventy percent of the gas stations in Canada actually see reduced profits as prices rise. The independent sector is in fact financially motivated for lower prices, contrary to what many Canadians believe, which is that it is the gas station making the money.

● (1025)

I'd like to turn now to the subject of speculation in the crude oil futures markets. Whatever the root causes driving crude oil markets higher may be, there is no debating that the volume of trading by non-oil or speculative interests in crude oil futures and indeed all energy commodity markets has increased. A recent article in the *Washington Post* has revealed that a full 81% of the oil contracts on the New York Mercantile Exchange, a far bigger share than had been previously stated by the Commodity Futures Trading Commission, comes about through speculative interest.

I want to define "speculative interest" because I think there's some confusion about it. Fundamentally, speculative interest on the crude oil markets are those interests that don't have any physical crude oil or crude oil-related products to buy or sell. So these are folks who are in the markets to invest and make money.

Up until recently, speculative interest in the volatile commodity oil markets has been naturally limited by the high risk associated with this volatility in commodity oil markets. But recently, reports of declining supply and rising world demand, together with ever-increasing forecasts of higher prices by investment banks, have led to the worldwide belief that crude oil markets cannot go anywhere but up. This has increasingly caused investors to ignore the traditional and increasing inherent risks of commodity oil markets. Of significant concern for this committee and for Canada is, for example, the increasing percentage of Canadians' retirement income that is at risk in the most volatile crude oil market seen in decades.

U.S. regulators have put forward a number of possible interventions in the trading of crude oil markets. These vary from relatively inconsequential measures to eliminating the speculative component altogether, which would be a huge intervention. We respectfully call on the political leadership in Canada to acknowledge this risk and support U.S. regulators to increase market oversight, which would be a key change to the CFTC at this point. Also, stepping back for a moment, equity markets—that is where most of us have our retirement investments—are extremely well regulated. One could argue that the same level of regulation does not exist in the oil market.

I'd like to conclude by emphasizing that at least 70% of Canada's gas stations see no benefit from rising prices. Rather, profits are declining as a result of increased credit card costs. We also ask this committee to look very carefully at the speculative component of crude oil markets.

Thank you.

● (1030)

The Chair: Thank you, Ms. Savage.

We'll go to questions from members.

I'll remind witnesses that members have very limited time for questions. The first round will be six minutes. Members may choose to put questions to one or all three of you. If you are not asked a question and you would like to respond, please so indicate to me, and I will try to ensure that you get some time. But there is very limited time, so we ask you to be short in your answers.

We'll start with Mr. McTeague.

Hon. Dan McTeague: Thank you, Chairman, and my thanks to all committee members for making this day happen. I think it's extremely important for Canadians.

We had determined as a committee to look into the impact of the markets on the unprecedented rising in the cost of energy prices, together with the impacts on futures commodities in general. We assume the prices will continue to go up. That in itself is a concern, but we also recognize that the recent rundown in commodity prices, in particular with respect to crude, does not necessarily mean lower prices for consumers, as one would have expected, given what we've seen in the past.

I have three questions. I will ask one of each witness, if you don't mind, Chair.

Ms. Savage had referred to the *Washington Post* article.

[*Translation*]

Unfortunately, I have not had a chance to have this article, which I found on the Bloomberg.com website, translated. But with the committee's permission, I will distribute it. It may be difficult to have it translated because of the copyright.

[*English*]

The Chair: Mr. McTeague is asking for consent. There's a *Washington Post* article that unfortunately has not been translated yet. He's asking consent of the committee to distribute it.

D'accord?

Hon. Dan McTeague: Thank you, Mr. Chair. Thank you, committee members.

It's a bit of an illustration here and perhaps provides the basis for my first question to Mr. MacLean.

Thank you very much, sir, for being here today. I appreciate it. Your years of experience will certainly come in handy.

This article points out that one particular company, Vitol, a Swiss company, was able to activate almost 11% of all the actual shares of crude oil on a particular day, June 6, which saw crude rise by $11 in a given day to $138.54, unprecedented, certainly, for market analysts concerned.

Mr. MacLean, you didn't touch on the issue of contango. It's terminology that is not familiar to most, but it really deals with the fact that supply and demand fundamentals can be set aside in favour of this constant belief that prices will rise, obviously predicated on what's happening in the BRIC countries, the Brazils, the Russias, the Indias, and the Chinas.

I'm wondering, given the recent changes to the rules by which people can trade on NYMEX—basically and essentially over-the-counter trades in the evening, intraday, whenever they wish—and with respect to the changes that have been allowed to take place at the request of companies, such as Enron in the past, do you not believe, sir, that there is a large, more preponderant activity that has never been seen before that may have had an undue interest or influence on driving these prices up to where they are today?

● (1035)

Mr. Warren MacLean: What I tried to present was that there are three different segments in the marketplace—the futures market, or NYMEX, being only one of them.

You referred to over-the-counter, which I would call the swaps market, an independent market not regulated like the NYMEX is, and I think that's what you're referring to as having the Enron effect. I believe that in Enron's heyday they were given credit for convincing the U.S. federal government not to regulate that swaps market.

I was trying to distinguish between the cash market, or the physical market, and the futures market. People may be able to play with the futures market but they can't play with the cash market, because they cannot control all of the physical supply of oil. There's simply not enough capability to do that. They are linked, there's no doubt about it. There's a fairly strong correlation. I spend my career looking at differentials between various markets, and they do move around quite a bit.

Hon. Dan McTeague: The article here suggests that Vitol was able, on that given day.... Its contracts amounted to 57.7 million barrels of oil, about three times the amount the United States consumes daily.

Given the revelation of this particular piece of information, does it not change your view that there are in fact several groups—perhaps smaller groups, very powerful groups—who, on a 5% margin, can possibly implement or change the market fundamentals, notwithstanding all the players? The fact is that there seems to be demonstration here of a handful of players who have tremendous market power and are doing enormous damage to the economies of the world, including Canada's.

Mr. Warren MacLean: I think I said that I can't answer the question about how much is speculation and how much is not, but I gave you my personal perspective. I could be wrong. You're right, I could be wrong.

Hon. Dan McTeague: Thank you for that, Mr. MacLean.

Mr. Boag, I have a simple question. I always thought the industry operated on a first in and last out principle; that is, when crude prices go up, the price is immediately reflected the next day at the pumps. And thanks to you folks, I'm able to get those prices at about the same time as you do and pass them on to consumers.

One thing I find interesting in my region, the Toronto market, is that wholesale prices on average in the past four weeks, as crude has dropped, are today anywhere from 2.5¢ to 4.5¢ more expensive than in Kingston, Ottawa, and Montreal. Considering transportation in a short or long type of market and considering that you're integrated companies that make a lot of money at crude, notwithstanding the reasons for the speculation, can you explain to me how it's possible that some regions of this country—I think of Calgary and Edmonton, for instance, which are 15¢ a litre above the NYMEX benchmark—and respecting the fact that it isn't the only market, how is that justified, sir? How do you justify 2.5¢ when your industry is selling some 65 billion litres of gasoline every year?

Mr. Peter Boag: I think what it reflects are differences between local and regional markets with supply and demand to balance each side. Clearly, across Canada we operate in a number of different local regional markets, and the supply and demand dynamics within those markets do differ. Clearly, we've seen a tremendous amount of volatility in fuel prices over the last number of months.

I can't talk to the specifics of what's happening in your constituency or in your city, Mr. McTeague, on the basis of an individual observation over a short period of time. Certainly we'd have to look at the longer-term volatility overall and longer-term shifts. But clearly, from our position, it really reflects the local supply and demand dynamics, which are not the same in every region of the country.

● (1040)

The Chair: Thank you, Mr. Boag.

Thank you, Mr. McTeague.

We'll go to Monsieur Vincent.

[*Translation*]

Mr. Robert Vincent (Shefford, BQ): Thank you. I am going to give the floor to Mr. Bouchard.

Mr. Robert Bouchard (Chicoutimi—Le Fjord, BQ): Thank you, Mr. Chair.

Welcome, and thank you for coming to testify before us about the price of oil.

My first question goes to Mr. Boag. In your text, we read: "In the Atlantic Provinces and Quebec, there is also an overlay of provincial legislation and regulation that limit competition."

Have these measures in Quebec and Atlantic Canada provided consumers with lower prices, or have they actually helped prices to rise compared with those in other parts of Canada?

[*English*]

Mr. Peter Boag: Thank you for the question, Monsieur Bouchard.

Our observation—and certainly the research that we have seen on regulated markets suggests this—is that regulated markets do have an influence in reducing price volatility. But at the end of the day, consumers pay more for fuel in a regulated market than they do in a market that operates under market principles.

[*Translation*]

Mr. Robert Bouchard: Thank you very much.

We know that Canada is an oil-producing country. Are there other oil-producing countries where consumers pay less that the world price and less than in Canada? Perhaps Mr. MacLean can answer that question.

[*English*]

Mr. Warren MacLean: I think the answer is yes. The countries that come to my mind are Nigeria, Venezuela, and probably Saudi Arabia. A lot of the producing countries do subsidize the price of their products to their citizens.

[*Translation*]

Mr. Robert Bouchard: Very good. I have another question.

In Canada, has the price of oil ever been lower than the world price? If so, by what means was that lower price achieved?

[*English*]

Mr. Warren MacLean: Is that question for me?

[*Translation*]

Mr. Robert Bouchard: Mr. MacLean.

[*English*]

Mr. Warren MacLean: Actually, when I started in the business, Canadian prices were kept below world prices. I started in the industry in 1976, and I believe the prices stayed regulated until about the early nineties, and then went to world pricing after that—at the end of the NEP, I think.

The way that was accomplished was that there was a cap put on the domestic production of oil, and then when a company such as Gulf Canada, which I was working for at the time, imported crude, it would pay the world price and the Canadian government would pay it the difference between the capped price on Canadian oil and the world price. At first, I believe, the Canadian taxpayer swallowed the difference between the two, but as the differential became larger and larger, the government funded that program—which we call a compensation program—through a refinery gate tax. In essence, that was passed through to the consumer.

● (1045)

[*Translation*]

The Chair:

You have a minute left.

Mr. Robert Bouchard: My last question goes to Ms. Savage.

You said that the price of crude can only go up. You also spoke about distributors, but you said very little about refiners. In some places—I come from Saguenay—Lac-Saint-Jean—like the region around Quebec City, retailers are supplied by a single refiner. Does it seem right to you that a single refiner is able to provide refined petroleum products to all the retailers in several regions, not just for one company, but for all? Could that lead to higher prices?

[*English*]

The Chair: Mrs. Savage.

Mrs. Jane Savage: Thank you.

There's no question that the concentration of refineries or refiners in Canada is quite high; in other words, there are very few refiners in Canada, just a handful. I think it's nine, if I have that number right. It's in that area anyway.

Because of this, if one espouses the belief that the more the number of competitors, the lower the price, one could assume that with this high concentration of refiners in Canada, we are paying a higher price at the wholesale level for our fuel. And we can only look at the evidence of that.

Certainly I don't believe there's any collusion, or anything of that nature, between refiners, but I would suggest that because of this high concentration, there is an oligopoly of some sort that enables price parallelism. So parallel prices are set. For example, in Toronto we see the rack prices or wholesale prices move daily, and all refiners move in the same way every single day.

There is a little more price competition in the province of Quebec, partly because of the independent import terminals that operate in Quebec City—which provide competition to the Ultramar refinery in Quebec City and Saint-Romuald—and in Montreal, where Norcan has a facility. So these facilities help to add to the competition.

The Chair: Thank you.

Merci, Monsieur Bouchard.

We'll go to Mr. Carrie, please.

Mr. Colin Carrie (Oshawa, CPC): Thank you very much, Mr. Chair.

I want to thank the experts for being here today.

I have a question for the panel.

I've been back in my constituency of Oshawa all summer, and one of the most common questions I've been getting is, why are these prices so high? What I'd like to know is, are speculators actually fuelling the price of gas? Do you have any evidence of this? If they are, are they doing anything illegal? And if so, should provincial security regulators step in? Or is this even an argument, that we should have a common security regulator?

I'd like to ask that across the panel.

Mr. Warren MacLean: Canada is a price-taker. As I've tried to say, these major refining centres tend to be the price-setting marketplaces. So other markets besides them take their prices from these major refining centres for both crude oil and crude oil end products. That's the first point.

Are speculators having an impact? They may very well be having an impact. Are they doing it legally? I think time will tell. I think the U.S. is actively trying to find a bogeyman. Will they find one? My sense is no, but they may. I mean, I was surprised by Vitol's position in the NYMEX, but I don't think that is conclusive about anything.

Again, I'll try to make this point: these are separate markets; nobody is controlling the physical market. Crude is bought and sold via hundreds of thousands of transactions a day, and nobody has enough storage to be able to control it to really move the market. So somebody may be playing with the futures market, which may be having some impact on the physical market, but I don't think it's appreciable.

● (1050)

The Chair: Mr. Boag, do you want to comment?

Mr. Peter Boag: I certainly would echo Mr. MacLean's remark that because we're operating in the context of a North American fuels market, of which Canada comprises approximately 10%, we're ultimately price takers with respect to the price of wholesale fuels.

The rise in fuel prices paid by Canadians this past few months has clearly been driven by the increase in crude prices. That has had an impact on refiners, in that refining margins have decreased significantly from where they have been in the past year, as demand in the U.S. in particular has begun to ease. Retail margins have been consistent for some time. So as far as speculation in crude markets goes, I would echo Mr. MacLean's remarks.

Mr. Colin Carrie: Madame Savage.

Mrs. Jane Savage: We are absolutely price takers; that is, we operate in a global pricing environment.

I take issue with just one thing Mr. MacLean has said about the physical markets—the question of speculation and how much speculation impacts the actual price we're paying at the pump. The physical markets are, without question, actual trades of crude oil or gasoline in large volume. However, most of them are priced off the NYMEX. So if I go out as a trader to buy a cargo of gasoline, I'm usually buying it as a number related to the NYMEX. The price discovery mechanism—say, Platts or Reuters—uses the NYMEX as a guideline for prices. So there is that component. Then it goes back to the question of how much the speculative component is affecting price in these things.

In Canada, we don't have jurisdiction over that because the trading happens in New York. The Commodity Futures Trading Commission in the United States oversees the futures markets. So it is not a provincial jurisdiction. We can only bring pressure to the United States' regulators to move this forward to understand fully what's going on in the speculative component.

The Chair: Mr. Carrie, you have about a minute and a half left.

Mr. Colin Carrie: I know consumers are really concerned about the price of gasoline, and they want to know what goes into the price they pay for gasoline. My understanding is that there are four components. It's the cost to locate and get crude oil out of the ground, which I believe takes a lot of energy; the cost to change the crude oil into gasoline, the refining margin; the cost to operate the local station, the transportation charges; and the taxes of the provincial, federal, and municipal governments.

In your opinion, what would a carbon tax do to the price of gas? If we put a tax on carbon, would people want to keep the price of gasoline down?

The Chair: Does anyone wish to answer?

Ms. Savage.

Mrs. Jane Savage: Presumably a carbon tax would increase the price of gasoline at the pump. I'm certainly not going to comment here on whether that would be a favourable or unfavourable thing to do.

Mr. Colin Carrie: Okay. I just wanted an overall opinion.

Mr. Warren MacLean: I agree it would raise the price.

May I just rebut one thing Ms. Savage said?

An example of the disconnect that can occur between the physical market and the futures market happened some time in 2007. The New York Mercantile Exchange trades a crude called WTI, West Texas Intermediate—the commodity crude—and it is physically produced in Texas. It's used in refineries in and around that area. There were major problems with a couple of refineries in that area, and that crude could not escape that particular market so it couldn't get out. There was tremendous pressure downward on that crude.

Another crude is Brent, which is produced in the North Sea. The typical spread is $2 in WTI's favour. It went to $8 to $10 in Brent's favour. So if there were speculators playing with it, they would have kept WTI up and the rest would have gone up with it.

● (1055)

The Chair: Thank you, Mr. Carrie.

We'll go to Ms. Nash. I will gently remind our witnesses to be briefer, if they can. We are running over time here. It's a very good discussion, but we are running over time.

Ms. Nash, you have six minutes.

Ms. Peggy Nash (Parkdale—High Park, NDP): Thank you, Mr. Chair.

I'd like to thank my fellow committee members for supporting my motion and agreeing to be here in Ottawa before the House resumes to attend to this important issue of oil and gas prices. It's something, clearly, that we've all heard about from our constituents over the past several months. I believe these are important hearings.

It's a complicated subject. I'd like to thank our witnesses for being here to help us understand what goes into the price of gas at the pump and what the various factors are that are involved in price increases.

I was struck by an article earlier this summer, based on a report by an economist at the Bank of Montreal, that said—this is before things started to moderate somewhat—that oil prices had passed the tipping point and were a drag on the Canadian economy. He called the price a “heavy anchor” undercutting consumer confidence and leading to higher inflation, and he said that the prices were now burning up about 7% of Canadians' disposable income, a record high. Clearly we have all heard that from people in our communities.

What is frustrating for a lot of people is that we are the second largest oil supplier in the world. Consumers, I think, are rightly frustrated by an inability to understand why it is we are paying so much for oil and gas.

Mr. Boag, we heard you talk about supply and demand. But what is also frustrating for people is that we see prices fluctuate. They tend to go up before the summer. They tend to go up before a long weekend. They can even fluctuate during the day—they seem to go down in the evening and up during the day.

If these are world markets and it's supply and demand, why do the prices change over the course of a day?

Mr. Peter Boag: Ms. Nash, thank you for the question.

Yes, there's no question that there's a significant degree of volatility in gas prices. I think everyone would agree that this can be very distressing for consumers.

I would just reiterate that ultimately the price paid at the pump is a function of three markets. One is that there are, yes, global implications in terms of setting the price of crude, which is the most significant component of the price of gasoline at the pump. There are North American markets, and we've had a significant discussion already this morning around the North American wholesale market for fuels. Then ultimately there's the retail market; that is, across Canada, thousands of individual decisions by retailers, who set the price at the pumps based on local market conditions and the assumptions they make and the information they have with respect ultimately to supply and demand conditions within their local market.

As they respond to that level of information and the information that's relevant to their market, they're going to adjust prices as they see fit to meet their business objectives, recognizing that this is an industry—the only one, to my knowledge—that posts prices at the street level on signs as large as you and I are. Consumers in Canada and around most parts of the world are very sensitive to those price differences. A tenth or two-tenths of a cent per litre difference will cause a consumer to change behaviour and choice of service station. As various retailers look at that and decide they're not going to lose market share to a competitor and can see that price change across the street, they're going to respond as they see fit, based on their business model.

● (1100)

Ms. Peggy Nash: Thank you, Mr. Boag.

Ms. Savage, I'll ask you, then, why prices go up before a long weekend.

Mrs. Jane Savage: I don't think they do, necessarily. I think that's a perception that is out there with consumers.

Ms. Peggy Nash: You see me smiling.

Mrs. Jane Savage: I know. I really don't think they do on a consistent basis. Competition is really the reason that prices fluctuate as much as they do. In some markets they don't fluctuate as much; in some markets they fluctuate ten times a day.

Ms. Peggy Nash: These are really the retailers deciding what they're going to do before a long weekend or in the course of a day, and this is their fluctuation.

Mrs. Jane Savage: Keep in mind that there are hundreds and hundreds of retailers in this market. Using economic theory, the competition at the retail level is very high. I would suggest that at the wholesale level those prices underpin retail and that there is much less competition at the wholesale level.

Ms. Peggy Nash: Thank you.

Let me go back to the change in prices. It seems to me that sometimes events such as a refining fire in the southern U.S. or political tensions between countries on the other side of the world can suddenly cause crude prices to go up. Is that an excuse for oil pricing to take advantage before there is a legitimate justification for price increases? Why does that kind of fluctuation occur?

Mr. Peter Boag: In answer to your question, I would say no. I think what you're seeing is ultimately people's perceptions on how an individual event, whether it's a hurricane or something else, is going to affect the supply of crude and how that's going to ultimately reflect—

Ms. Peggy Nash: Is that just the market speculating?

Mr. Peter Boag: It's not the market speculating; it's the market responding to a perceived change in the supply and demand balance.

I want to come back to the question you posed to Ms. Savage about gas prices going up before a long weekend. I share her view that, although there are perceptions to that effect, there's no empirical evidence for them. In fact, an extensive report done by the Conference Board of Canada several years ago came to the conclusion that there was no evidence that prices went up before long weekends.

We will generally see some seasonal differences in prices. As the summer driving season arrives, there is a much increased demand for gasoline, and the supply and demand balance changes. We generally see an increase in the price in the summer.

The Chair: Thank you, Mr. Boag.

Thank you, Ms. Nash.

We'll have another round of questions if we have time.

Mr. Alghabra.

Mr. Omar Alghabra (Mississauga—Erindale, Lib.): Thank you, Mr. Chair.

Good morning, everybody. Thank you all for being here.

Ms. Savage, I want to start with you. You touched upon the lack of competition at the refinery and distribution level. Perhaps that's understandable, given the barriers to entry and the high capital requirement for such a thing. What do you think a government role could be in ensuring that there is at least some fair competition in that market?

Mrs. Jane Savage: I think transparency is the key thing. One thing we have talked about regularly is having information beyond price available in the public domain. The amount of fuel that's available at any particular time—gasoline inventories and heating oil inventories, for example—is not in the public domain in Canada. It is in the United States.

I think inventory levels have quite an effect on price. Access to them would help the entire industry, as well as Canadians in general, to understand some of the price moves in Canada a little better. I am talking about an inventory monitoring system that would simply aggregate all the inventories in Canada and put them out there on the Internet for everybody to see. That would be one suggestion.

Mr. Omar Alghabra: Thank you.

Mr. Boag, I would ask you to respond to that. Why don't we have such a mechanism? Would the industry be open to it?

● (1105)

Mr. Peter Boag: First of all, let's put this into context.

Yes, over the last number of years we've seen a significant rationalization in the number of refineries in Canada. Notwithstanding, we've actually seen an increase in refinery capacity. As we've reduced the number of refineries, remaining refineries have expanded significantly. Today we produce more refined petroleum products than we did many years ago, and with fewer refineries. That has been done as refineries have striven to achieve greater levels of efficiency, to respond to productivity, and to achieve economies of scale. This helps Canadian consumers by keeping product prices down, because the production costs are lower.

As to a government role, given the high capital costs associated with building a new refinery—several billions of dollars—the role of government is really to create economic conditions conducive to investment in that kind of capacity. This adds value to Canadian natural resources. It's the investment climate that makes Canada attractive to billion-dollar investments that have extremely long amortization and pay-back periods.

Mr. Omar Alghabra: Thank you, Mr. Boag, but I'm still curious as to your response to my question. Would the industry be open to publicizing or publishing their inventory level and having some kind of monitoring occur?

Mr. Peter Boag: I think in the past the industry has been supportive of having a monitoring agency. We think that in the end that information is useful to Canadians. Certainly we'd be willing to discuss how that might work and what might ultimately be of use to Canadians.

Mr. Omar Alghabra: With the previous government, wasn't there an agency created to monitor inventory levels and gas prices?

Mr. Peter Boag: Yes, I believe there was.

Mr. Omar Alghabra: Where is it now?

Mr. Peter Boag: I don't think anything came of that. I'll have to take a bit of a pass on this because I am relatively new to this industry. While I'm clearly very focused on the issues of today, on past government actions too far back I'd have to get some better information for you.

Mr. Omar Alghabra: My understanding is that it was cancelled by Conservative Prime Minister—

Mr. Peter Boag: My understanding is that it did not come into effect, yes.

Mr. Omar Alghabra: Okay. But the industry would not be reluctant to have those inventory levels published.

Mr. Peter Boag: I think we'd have to look at the specifics of what was being published. Certainly the concept of information is not something we're opposed to, but I think we'd need to have a broader discussion on the specifics of what that information might be.

Mr. Omar Alghabra: Thank you.

The Chair: Thank you, Mr. Alghabra.

We'll go to Mr. Stanton, please.

Mr. Bruce Stanton: Thank you, Mr. Chair.

Thank you to our panellists here this morning. It's a very intriguing topic, of course, and it's on the minds of many folks particularly through this past summer, going back to early July.

Mr. Boag, returning to the theme you were discussing with Ms. Nash's question, I want to come back to that briefly, the notion that shocks in the supply—and I think back to Hurricane Katrina—instantly show up at retail. I know I get the question regularly from constituents in my riding, who ask, how is it that it shows up literally the same day when there's an event that causes that?

Could you explain that?

Mr. Peter Boag: I think what really is behind that is the sensitivity of markets to those kinds of shocks. Those events are instantly read in the markets and ultimately have an instant impact on the kinds of markets that Mr. MacLean has been talking about trading. They do actually happen that fast, as the market responds and prices change.

Mr. Bruce Stanton: But clearly the gas that's in the tank at the local retailer was purchased at a lower price, so they don't necessarily have to charge a higher price for that.

Mr. Warren MacLean: Could I try to answer this one?

Mr. Bruce Stanton: Please.

Mr. Warren MacLean: That's true, there is an amount of inventory that's always in place. The problem is that when you take one out, you have to replace it. What do you replace it with? You replace with what you paid for it that day. So that answers the question why, even though there's inventory in place, you still get the current price on the current day.

In terms of why Katrina translates immediately, it is because it's such a liquid market and so transparent. If I'm a wholesaler and my choice is to sell to market A or B, and market A just went through a hurricane and needs product and is willing to pay for it, why would I sell to market B at a lower price? It's simply the way the price translates through the marketplace.

● (1110)

Mr. Bruce Stanton: So it's an anticipation of the fact that we're going to have to purchase—

Mr. Warren MacLean: It's an arbitrage process.

Mr. Bruce Stanton: Okay. And that's why it's instant, is what you're saying.

Mr. Warren MacLean: That's right.

Mr. Bruce Stanton: Mr. Boag, going back to the question Mr. Carrie posed in regard to this additional taxation, it has been speculated about or proposed that this carbon tax could be upwards of $40 a tonne. Even though the policy suggestion is that it won't be put on gasoline, I think you nodded your head to indicate that it would show up. Could you clarify?

Mr. Peter Boag: It would clearly depend on the specifics of the policy initiative. I can't speculate on what a policy initiative might be and what the impacts on the industry would be.

Mr. Bruce Stanton: Would it get passed along, though? What would happen?

Mr. Peter Boag: Again, I can't speculate and can't forecast how a specific policy initiative that's hypothetical at this point may ultimately impact prices.

Mr. Bruce Stanton: Thank you very much.

Mr. MacLean, going back to this situation, a couple of you witnesses have referred to this “driving” of the price of oil, and Ms. Savage referred to it as well.

In the reading that I did just ahead of today's meeting, from the interim report that the inter-agency task force came out with in early July, they indicated that really only 2% of the oil futures—and I think this referred to the cash transactions, that is, 2% of the contracts—actually resulted in physical delivery of product. In a case like that, I'm trying to imagine what kind of conditions....

Perhaps I'll ask Mr. MacLean first. What kind of conditions might you see if in fact there was this other speculation going on about those prices? In other words, if the trading drives the prices up, as has been suggested, what kind of circumstances might we see in the market that would give weight to that argument? For example, it has been suggested here that if that was in fact happening, inventories would be higher. But in fact, inventories have not really risen at all with this recent spike in trading.

Could you comment on that? I say this particularly because people would be interested to know that the price they're paying for gas isn't being artificially bumped up by overabundance of trading.

Mr. Warren MacLean: The first thing I'd say is that there is a role for what we're calling “speculators” in the market. They do provide a huge amount of liquidity to the marketplace. And the reason that—

Mr. Bruce Stanton: What do you mean by liquidity?

Mr. Warren MacLean: Liquidity allows buyers and sellers to transact at a given price. Without speculators, there would be less transaction. Something like the bid-asked differential would rise, there would be less activity in the marketplace, and it would stagnate. There would be no transparency in the marketplace. So they do have a valuable position.

I think what you're thinking of is if speculators are manipulating the market. That's a different situation.

Mr. Bruce Stanton: How would you tell that?

The Chair: I'm sorry, Mr. Stanton—

Mr. Warren MacLean: I don't know how you'd tell. I can't answer that myself.

The Chair: Thank you, Mr. Stanton.

We'll go to Monsieur Vincent.

[*Translation*]

Mr. Robert Vincent: Thank you, Mr. Chair.

Welcome to the committee. There is one question on everyone's lips: why do crude oil producers not have inventory on hand to accommodate any eventuality? Prices go up when there is a mere gust of wind in any oil-producing country. If there was inventory on hand, the price would remain the same even with that gust of wind. Why do crude oil producers not have inventory on hand to take care of those situations?

Is this artificial scarcity not the reason why the price of a barrel of oil goes up?

[*English*]

Mr. Warren MacLean: I don't think inventory is the answer here. There are situations.... There are stores of inventory. The U.S. has the strategic petroleum reserve, which is a store of inventory for emergency purposes. It generally is not used to regulate pricing.

What producers are trying to do, I would say, is maximize the value of their resource. Holding excess inventory is going to decrease the value. I really don't know why a producer would hold inventory.

● (1115)

[*Translation*]

Mr. Robert Vincent: The price at the pump is high because producers are creating an artificial shortage so that they can keep putting money into their pockets.

Mr. Boag said earlier that he could not understand why prices are going up. Well, when you have a long weekend or are on holiday, you use more gas. So they put up the price and make more money. Does that make any sense to you?

[*English*]

Mr. Peter Boag: I would repeat my earlier remark, that certainly there are seasonal fluctuations given to supply and demand that have some impact on prices, but—

[*Translation*]

Mr. Robert Vincent: Could you answer my question, please?

[*English*]

Mr. Peter Boag: —there is no empirical evidence, to our knowledge, that would support the assertion that gas prices traditionally go up at the beginning of long weekends.

[*Translation*]

Mr. Robert Vincent: You work in this area; how come you do not know why the price of oil goes up? Consumers can tell that the price will go up by two or three cents a litre the day before a holiday. Do consumers have more experience than the people who work in the industry and who are in a position to know when prices will increase?

You say that you do not understand why prices go up, so how is it that consumers do?

[*English*]

Mr. Peter Boag: Mr. Chair, speaking through you to the committee, we're here today to try to explain what is a very complex situation driven by a number of factors, both globally, in the context of a continental North American market, and in the context of thousands of decisions being made by retailers to set prices.

I'm certainly not able, here today, to predict where prices are going to go tomorrow, next week, or next year on a reliable basis. If I could predict the price of crude oil on a reliable basis, I think I'd be doing something else by this time in my career.

Yes, price volatility is clearly a difficult situation, and we understand Canadians' concerns with price volatility. But we're here today to try to contribute to knowledge of the complexity and the factors that ultimately drive prices and drive that volatility.

The Chair: Ms. Savage wanted to comment.

Mrs. Jane Savage: This is just to address your question of inventories.

I can't speak on the crude oil side, but on the product side, this is part of the reason we would like to see a monitoring program in place for product inventories—that is, inventories of gasoline, heating oil, and diesel, the key products that Canadians use.

We have been in a period of declining inventories, and we're finding that because companies are financially motivated to reduce inventories, our vulnerable areas of Canada are more vulnerable—to supply outages, to a refinery shortfall, to a pipeline problem, to ice in the St. Lawrence River, to very cold weather. All these things contribute to vulnerability of supply. As a very minimum, I feel we should have some inventory monitoring in place to reduce that.

The Chair: Monsieur Vincent, you're right out of time, but do you have a very short question?

[*Translation*]

Mr. Robert Vincent: Mr. Boag, when you answered a question from Mr. Stanton, you said that when the price goes up at the pump... why does the price go up at the pump? It is the same gas that was bought at a lower price, but as soon as the price per barrel goes up, the price at the pump goes up too. It does not work the same the other way round. When the price of crude drops, the price at the pump stays the same. Why?

● (1120)

[*English*]

The Chair: Please be brief, Mr. Boag.

Mr. Peter Boag: I would dispute that. I think the prices go both up and down very quickly, almost instantaneously, in response to the price of crude. What I also would reiterate is that throughout all this, and notwithstanding the volatility, Canadians still pay the second lowest price for gasoline in the western world. I would certainly pose to Monsieur Vincent the question, where does he think the price should go? What does he think the price should be?

The Chair: Thank you. *Merci.*

We'll go to Mr. Van Kesteren, please.

Mr. Dave Van Kesteren (Chatham-Kent—Essex, CPC): Thank you, Mr. Chair.

Thank you, witnesses, for coming here. It's fascinating.

I wanted to touch on something Ms. Savage said. I'm not trying to correct you, but I think you were implying that at your level it's pretty much transparent and there seems to be a pretty regular flux in price, but that it's at the well that there is more of the profit.

Is it safe to say it's at some wells? I would assume that if you're pumping it out of Saudi Arabia, where there's a lot of just pumping, rather than out of some offshore drilling or something that's more expensive.... Is it safe to say that at some wells the profits are higher than at other wells?

I don't want a long answer to that. Is it safe to say that?

Mrs. Jane Savage: Sure, yes.

Mr. Dave Van Kesteren: I think that needs to be cleared up too, because this thought occurred to me, and correct me if I'm way off in left field. We know that supply and demand dictate where the price is going to be. We know there's a theory out there about peak oil: whether the peak oil is something that's going to happen shortly or whether it's somewhere in the near future, it's safe to assume that when that happens the price is going to skyrocket. Is the high price of oil keeping our price of oil down? If the high price of oil encourages some of the exploration and if the earth has *x* amount of oil, but if we're approaching the point where we're going to be extracting that, then is the high price encouraging exploration and subsequently producing enough oil that we don't get to that point yet?

Do you understand what I'm saying?

Mr. Warren MacLean: I think that is one of the concerns people see in the industry: the high prices of crude oil have not resulted in an increase in reserves. That plays into the peak oil theory. If you look at the major producers, their production levels are flat to declining. Some of the independents in the U.S. are seeing some growth in production. There are some pockets of growth. Saskatchewan has a particularly good pocket of growth in production. On a general perspective, that's why you see the big debate in the U.S. about access to land to drill more. They're just not seeing the growth in reserve additions with the higher prices. I think that's adding to the concern and probably reinforcing the price increase.

Mr. Dave Van Kesteren: Mr. Boag, I want you to jump in on this.

What I'm suggesting is the possibility that if we didn't have the price we have, the exploration wouldn't be there, we'd have less oil, and the price would just take off.

Mr. Peter Boag: Certainly the high prices for crude act as an incentive to explore and particularly look for crude in what would previously have been uneconomic areas and uneconomic reserves. So yes, I would agree with Mr. MacLean that high prices do act as an incentive to find more, particularly to explore those opportunities that may have been uneconomical at lower crude prices.

Mr. Dave Van Kesteren: The logical conclusion to that would be that if we are successful in some of our exploration we may see... maybe not a glut, but certainly a level that would cause prices to drop.

Mr. Peter Boag: You're talking only about the supply side of what is a complex supply and demand equation. Clearly the demand side is ultimately going to have a significant impact on what that supply-demand balance is that ultimately is a fundamental behind prices.

Mr. Dave Van Kesteren: We won't get into that.

Maybe you could touch very quickly on why we see such a variance in the price between gas and diesel. I'm a member of the trucking caucus; I'm the chairperson, actually. I know that is a real concern. I know truckers are very concerned about the price. Why is there such a price disparity between the two?

● (1125)

Mr. Peter Boag: I think what you're seeing there is an even tighter supply-demand situation on middle distillates, including diesel, than there is on gasoline. I think that's particularly tight in the Atlantic basin. Europe has a huge demand and thirst for diesel these days because of its significant and rapid dieselization of its automobile fleet. The demand profile in Europe is quite different from what it is here in North America, in that diesel is much higher in demand than gasoline. Also, we've seen significant economic growth throughout the world over the last number of years, and diesel is largely driven by demand. It's largely driven by economic growth. So it's a combination of factors that ultimately have created a very tight supply and demand situation for diesel that has driven diesel prices up proportionately higher than gasoline in the last few months.

The Chair: Just very briefly, then.

Mr. Warren MacLean: I'd agree with that as well. The only thing I'd add is that the industry has to produce ultra-low-sulphur diesel, which is added to the cost. It probably costs more to produce diesel now.

My belief is that diesel is the cause of the run-up in crude prices. It's not crude prices that are driving the market; it's diesel prices worldwide.

The Chair: Thank you, Mr. Van Kesteren.

We'll go to Ms. Nash, please.

Ms. Peggy Nash: Thank you, Mr. Chair.

On the issue of the cause of gas prices, we're hearing that Canada's price is relatively low. Some would argue that the price should even be higher. I think the difference is that rather than having a higher price, which some countries do, and having that money invested in green solutions—alternative energy sources and other things, to offer alternatives to people—the price here is set privately and the profits are going to private interests. We are the second largest supplier in the world, and the impact is huge on all aspects of our economy.

I was quite struck recently to learn that an airline, Jazz, is going to abandon having life jackets on their flights because of the cost of fuel. So if there's an emergency, “hang on to your seat ” is basically their message.

So there's a real concern about the total impact of these prices on the economy, and a fear and a sense by consumers that they are getting gouged.

Prices pretty much track crude costs, normal refining costs, marketing margins, taxes, etc. But every so often there are periods when prices spike. One study I read said that every additional penny per litre above the normal costs of marketing, etc., generates $1 million for the industry from gasoline sales alone. Sometimes it can go up to tens of millions of dollars a day, just from the price of gasoline.

Mr. Boag, are oil companies gouging Canadians by having prices higher than the costs that could be attributed to crude, refining, taxes, and normal marketing and profit costs?

Mr. Peter Boag: My unequivocal answer is absolutely not.

Ms. Peggy Nash: But how do you account for that difference, when over and above these costs there are price increases that clearly go to the oil companies?

Mr. Peter Boag: I'm not sure I understand your question. Could you be a little more specific on what you're trying to ask?

Ms. Peggy Nash: I'd like to know why there are periods when the price of gasoline, for example, is higher than the cost of crude plus taxes and normal marketing and mark-up costs. Where does that differential go?

● (1130)

Mr. Peter Boag: We're talking about a hypothetical situation, and I'm having a hard time understanding when that hypothetical situation actually exists.

Ms. Peggy Nash: Take this summer, for example.

Mr. Peter Boag: I don't believe that was the case this summer. In fact, when we look at the various components that comprise the price of gasoline for Canadians today and this summer, the change has largely been driven by the price of crude—

Ms. Peggy Nash: But when crude goes up, even a slight extra differential in the pricing here in Canada means big profits for the oil industry.

Mr. Peter Boag: It doesn't mean big profits for the refining sector, because I can tell you today that refining margins, which are a relatively small component of the difference between the price of the crude that refiners pay and the wholesale price they get when they sell, are now 8¢ to 9¢ below where they were a year ago. They're running around 18%—

Ms. Peggy Nash: The oil company profits are up significantly this year. Do you not think there's any correlation between the large increases in oil company profits and the price that people are paying at the pump?

Mr. Peter Boag: No, I think oil company profits today are largely being driven by the exploration and production side of their businesses and the high global price for crude, which isn't set in Canada.

Ms. Peggy Nash: So there's no correlation between the increase in profits in the oil companies and the increase in price that Canadians are paying at the pumps.

Mr. Peter Boag: Without looking specifically at individual financial reports of publicly traded companies, I think there's a pretty good correlation between profits and the price of crude.

The Chair: One brief question, Ms. Nash.

Ms. Peggy Nash: Do you think there's justification, Ms. Savage, for an increase in the price of crude not just being passed on, but additional prices being tacked on that consumers pay at the pumps?

Mrs. Jane Savage: No. The world price of crude oil determines the cost that a refiner pays for that crude oil and so determines a refiner's cost, and then at the wholesale level it is the world price of gasoline, for example, that sets those rack prices where most retailers buy. I think that's fairly transparent. For example, the chart in my presentation shows each of those components as this builds up.

Ms. Peggy Nash: How do you track the additional—

Mrs. Jane Savage: It's from crude oil, no question.

The Chair: Thank you, Ms. Nash.

We'll go to Mr. Eyking, please.

Hon. Mark Eyking (Sydney—Victoria, Lib.): Thank you, Mr. Chair.

From looking at the presentations so far this morning, it would seem to me that the oil producers who are drilling the oil and the oil-producing countries are making all the money, and the refineries and everybody down the line aren't, and that the refinery capacity is not going to increase any time soon because there's capital outlay and there's not enough return. That's my assessment here.

I'd like to talk about inventories, and inventories in regions. We have a big country, we have remote regions, and we have only a few players.

I'll tell you what happened in our region last year. We ran out of furnace oil for a couple of weeks. We live on an island. There's only one storage facility. There are different retailers who draw from it, but at the end of the day there is one storage facility.

You talk about keeping inventories low or even moving inventories around. So if you have a big company and they see a better market somewhere, that could be happening. But at the end of the day, you have a region that's without furnace oil, and if there are ice conditions around or ships not available....

Now, provincial governments are asking how they can avoid this happening or how they can interfere with it. How do you see us dealing with this? Can you penalize these people for not having oil available, because technically they have a monopoly, or do you encourage them by helping them with their inventories? How do you see us overcoming this, with a big country like ours, few players, and remote areas that could be without furnace oil if they're moving their inventories around?

That's for Mr. MacLean or whoever wants to answer the question.

Mr. Warren MacLean: Again, it's back to inventory. I think you're putting too much importance on the ability of inventory to solve all problems. It will only solve the problem for the duration that you have the inventory. That may work at times; it may not work at other times.

In my experience, I was in one situation in my total career where there was a supply situation in Ontario. There was maybe anecdotal evidence of run-outs by customers, but I don't think consumers didn't get the product they needed; they actually got the product they needed, and I think the industry has done a very good job.

As to an earlier question about Quebec, with one refiner, I think the industry has rationalized the infrastructure, which has lowered the cost to the consumer, because the cost to the industry has gone down.

So if you want to add cost to the industry and see prices go up, mandate inventories.

● (1135)

Hon. Mark Eyking: You said they did a good job. Well, they didn't do a good job in our region, because we didn't have furnace oil. And of course we don't want to pay more than we should, for other regions—

Mr. Warren MacLean: Did any houses run out?

Hon. Mark Eyking: Yes, they did.

Mrs. Jane Savage: If I can add to that—

Hon. Mark Eyking: Just very briefly, because I'd like to split my questions.

Mrs. Jane Savage: Sure.

Just quickly, there are areas in Canada that are very vulnerable to inventory run-outs, there's no question. With the concentration of refiners, with running at low inventories, and with limited infrastructure to bring imported product in, especially in the winter, there is a deep concern on our members' part for exactly what you speak of.

The Chair: Mr. McTeague, you have a minute.

Hon. Dan McTeague: Mr. MacLean, you mentioned earlier that Canada is a price taker. I think you all agreed with that. I'm wondering, however—given that the United States every week provides, through its Energy Information Administration, a *Weekly Petroleum Status Report* very similar to the one that the Liberals had proposed and that was scrapped when the Harper government took over—how you would categorize the current situation in the United States, in which Canada plays a very important role, whether it be for crude or for natural gas.

We have here every week at the same time, and it should happen at around one o'clock—in fact, it's probably out already—an inventory report that gives accurate information. It shows that for the past five years our numbers, whether for distillates, diesel, gasoline, or residuals—take your pick—are pretty much within the same area. In other words, the inventory reflects supply and demand and it reflects the amount of actual inventory that's out there.

How is it possible, if we're still with what we've been doing for the past five years, that we would see prices double, using your theory that this is very much a function of supply and demand? How can you say that, when you know that the inventory numbers haven't changed a whole lot? Supply is where it should be, and demand is where it should be, and yet prices are almost double where they were two years ago.

Mr. Warren MacLean: Inventory is only one piece of the equation. Production is the other piece. Production goes up and down with demand.

Hon. Dan McTeague: Excuse me, Mr. MacLean. The inventory report includes every week the amount of production and the amount of demand. The inventory is the final analysis.

Mr. Warren MacLean: I don't understand the question, then.

Hon. Dan McTeague: In the United States, which consumes 52% of all of the transportation fuels in the world, inventory right now is at a maximum level. It's not low, it's not high; it's within the five-year bandwidth. And yet the prices for commodities such as crude have doubled. Your proposition is that there's no problem with supply and demand. I submit to you that if inventory is where it should be—that is, supply and demand, inventory and production, are exactly where they've been over the past five years, within the bandwidth.... Why have prices doubled?

I'm sorry, Chair. Go ahead.

The Chair: Mr. McTeague, you will have another spot coming up.

Mr. MacLean, do you want to respond to that briefly?

Mr. Warren MacLean: The price has gone up because the demand for crude has gone up. You're only seeing one piece of the puzzle by looking at U.S. statistics.

The Chair: We'll come back to this.

We'll go to Monsieur Arthur.

[*Translation*]

Mr. André Arthur (Portneuf—Jacques-Cartier, Ind.): Thank you, Mr. Chair.

Our three guests are giving clear answers to the questions they are being asked. But sometimes, they are not very much help because the law of supply and demand is a big concept that can explain any number of things. But, when my colleague Mr. Carrie asked you a specific question, you started to mutter an answer that I did not understand. I even had to turn to this young grandfather to my left so that he could repeat what the muttering was about.

Ms. Savage, what would be the effect of a carbon tax on oil prices in Canada? I would like a clear answer that I can hear.

● (1140)

[*English*]

Mrs. Jane Savage: As I said earlier, a carbon tax applied directly to gasoline at the pump would result in an increase in price. Anything other than that is unclear; that's all I can say. Without understanding exactly how it would play out, I can't forecast. If it's applied somewhere else or to other commodities—for example, to crude oil only.... It depends on the circuit and how it goes through. I can't answer that question until we know specifically.

[*Translation*]

Mr. André Arthur: Thank you.

Mr. MacLean.

[*English*]

Mr. Warren MacLean: My answer is that it's going to cause the price to go up. I don't care where you put it on or how you do it; if it's a tax, it has to be reflected eventually in the price. That's my personal perspective.

[*Translation*]

Mr. André Arthur: Mr. Boag.

[*English*]

Mr. Peter Boag: My answer would be closer to Madam Savage's. It really depends on the implementation details of that tax and what products it's imposed on. Talking about a carbon tax in general, the devil is always going to be in the details, if one is to comment specifically on what the impacts on price would be.

Mr. André Arthur: We talked a lot about speculators, who are somewhat to the petroleum market what scalpers are to show business; they buy a thing in advance and then sell when it's needed. We know there are some huge concerns, such as in Switzerland, that are busy putting huge amounts of money into petroleum stocks all over the world. Vitol seems to be quite a discovery.

How could we make sure those foreign concerns are not investing Canadian money, be it from Power Corporation, the teachers, or la Caisse de dépôt et placement du Québec? How can we make sure there is no Canadian money behind those scalpers?

Mrs. Jane Savage: In my opinion, I think you have to ask them.

Mr. André Arthur: They won't say.

Mr. Warren MacLean: I think that's a question for the guys this afternoon.

The Chair: You have two minutes.

[*Translation*]

Mr. André Arthur: The price of gas at the pump hits Canadians directly when they fill up their cars. They pay, they suffer and they move on. They grumble, they hate you, but that is your problem.

The price of diesel hits everyone, because it has an impact on public transportation and on the cost of goods that have to be transported. This impact is more insidious and much more long-term than the price of ordinary unleaded gas. Naively, I always imagined that it cost much less to refine diesel than to refine gasoline because, for diesel, the processing is shorter and it uses things that you do not have to remove, except sulphur now.

Can you help a simple soul like me to understand why a product that costs less to refine costs more to buy?

[*English*]

Mr. Peter Boag: The principal reason really comes down to supply and demand balances. There has been a much greater demand, and growth in demand, for diesel over the last number of years than there has been for gasoline. So the supply and demand situation for diesel, not just in Canada but in North America and throughout the Atlantic basin, is much tighter. As a result of that tightness in supply and demand, diesel prices are higher, and diesel prices have risen higher than gas prices.

Mr. André Arthur: So if supply and demand operated normally, an honest market—seeing a bigger demand for diesel—would simply refine more diesel and less gasoline. They don't do that. They jack up the price. Is there something wrong there?

Mr. Peter Boag: Because it's very difficult.... Our Canadian refineries are configured in what has traditionally been the split between gasoline and diesel demand. So those refineries are configured to produce a certain proportion of diesel and a certain proportion of gasoline. That can't change overnight. You can't just turn a switch and all of a sudden say we—

● (1145)

Mr. André Arthur: Overnight is the last two years, sir.

The Chair: Okay, Monsieur Arthur.

Mr. Peter Boag: You're talking about a period of years of investment through a number of different cycles of refinery investment to be able to make a configuration change of the magnitude that would allow you to significantly change the proportion of diesel to refinery produced in a Canadian refinery.

The Chair: Thank you.

We'll go to Mr. McTeague.

Hon. Dan McTeague: I'm just receiving information from the Department of Energy in the United States—it's too bad we can't get it from here—that crude is down to its lowest level of consumption since 1998, and yet we may see crude actually increasing today. Again, there is this opposite effect: demand is down, prices are up, and consumers are very frustrated.

Mr. Boag, I want to ask you a question about the Toronto market, but it may also play into other markets as well.

Ms. Savage, you may also want to respond to this as best you can.

In May, retail margins in Toronto—and I include Clarington, Oshawa, Ajax, Pickering, Mississauga, Etobicoke, all the way to Burlington—were in the average of 5¢ a litre, almost without exception. Over the past 10-week period, that retail margin has gone from 5¢ to 6.5¢ uniformly and in lockstep. Furthermore, diesel wholesale prices relative to gasoline and premium relative to gasoline on the order wholesale of 4¢ to 5¢ a litre—facts that your association and its members kindly offer at 3 o'clock in the morning—is self-evident.

Mr. Boag, can you explain to me why your members, who have such a preponderance in my market in the GTA, covering some four million to five million Canadian motorists, are able to get exactly the identical price higher than it has been certainly in the past month and a half? And how do you explain the 4¢ or 5¢ differential from where you were just a few months ago?

Mr. Peter Boag: That's ultimately driven by the supply and demand conditions within the market. And those are the decisions of the hundreds of individual retailers, who can look across the street to see what their competitor is charging, and they're based on the fact that they want to retain their business and not see their business go to their competitor.

Hon. Dan McTeague: Wouldn't your business be better off if the price was lower, rather than charging a higher price that's identical to the competitor across the street, who may also happen to be your supplier?

Mr. Peter Boag: I can't comment on the decisions of individual retailers, but that's the nature of a competitive market.

Hon. Dan McTeague: When the APPI presented itself before the U.S. Congress, it pointed out that there was variance in pricing at the retail level. It would appear that your retail margins in Toronto, in the GTA, are absolutely identical. I'm not going to suggest why that is, because I think in 1998 it made a number of recommendations to avert that.

But I wanted to ask whether you believe someone has an enormous amount of market power in order to make the price exactly one-tenth of a cent within a 150-kilometre radius, which makes my job of predicting prices the next day much easier. It's something I'm not exactly pleased with.

Mr. Peter Boag: To answer your question, no, I would say that's a reflection of a highly competitive market where retailers are competing to get market share and are not prepared to see their competitors take their share from them.

Hon. Dan McTeague: Does anybody else want to comment on this?

Mrs. Jane Savage: I'll just comment on the wholesale prices that underpin retail prices.

Certainly in Toronto we've seen an increase in the spread between Toronto and Montreal on the wholesale level. Traditionally, Toronto runs at about 0.8¢ to a penny higher than Montreal does, and that reflects that the incremental barrel is coming from Montreal and costs about a penny to get into that market. Recently that spread has blown out to as much as 3.5¢ a litre.

Again, the market control by the folks who are setting those prices is high, and we've spoken to that before. The concentration of refining interests in Ontario and the land-locked nature of Ontario enable refiners to price whatever they want, really, at the wholesale level.

Hon. Dan McTeague: Let me ask you about the Toronto picture. It's my understanding, with the ethanol regulations in Ontario, that what in fact happens to meet that particular 5% standard is that you have 10% ethanol content in most GTA, Toronto, gas tanks. This means you have, in effect, perhaps as little as one supplier coming from Petro-Canada in Montreal providing product to Bronte, which provides product pretty much to the entire city. In fact, when you drive up to any station and you see someone dropping off a load in a no-name tank truck, you'll see that the product usually comes from one supplier, often Petro-Canada.

Is this how the market is best characterized—one supplier, one price, and with an absolute four players who don't compete against each other at wholesale—and the reason why one can explain why prices move up and down in lockstep fashion? What would be the impact on independence if they decided to, say, challenge that 6.5¢ margin for regular unleaded or that 12¢ margin for premium? What would happen in that scenario?

● (1150)

Mrs. Jane Savage: I think the scenario you paint is correct, with perhaps one exception, and that is that the incremental supply of fuel in Ontario is from Petro-Canada in Montreal via the pipeline that runs between Montreal and Toronto. The last barrel, if you will, comes in from Montreal. There are four refineries in Ontario that refine and blend product, including ethanol-blended product in Ontario. So with that exception, I would say that what you're painting there is correct as far as the scene goes.

Mr. Warren MacLean: I think he said that Petro-Canada was supplying all of the GTA, and I don't think that's correct at all. There are pipelines coming from Sarnia on which both Shell and Suncor have product coming into Toronto. There's product coming from Esso Nanticoke on a pipeline. Petro-Canada brings it in by pipeline, but so does Ultramar.

Hon. Dan McTeague: Mr. Chair, I wonder if it would be possible for the researchers to reflect what Mr. MacLean has said. For instance, the Nanticoke refinery does not have reformulated gasoline —ethanol. Therefore, it cannot supply the Toronto market. This is part of my concern.

Thank you.

The Chair: Thank you, Mr. McTeague.

As the chair, I'm going to take the next spot.

Members and witnesses, we started about 10 minutes after 10, so perhaps I can ask the witnesses this. I know we asked you to stay until noon. If you have to go, you have to go. But perhaps we could impose upon you for a few more minutes, if that's okay.

I just wanted to drill down, Mr. MacLean, to some of the understanding, especially with respect to the price of crude. That seems to be where the main concern is. Crude is, as you've all mentioned, the primary determinant in terms of the price of gasoline. There is a concern, and Mr. McTeague has provided a very good article in terms of speculation.

In terms of the price of crude, we have the physical market, also known as the cash market, where we have the commercial participants. Then we have the futures market, and people are saying this is where the speculators are taking their action.

Can you drill down for the committee what percent...? Is there a way of telling, if the price of crude is a certain amount today, what amount is due to the cash market, what amount is due to what people may describe as more legitimate trading versus how much is due to the actual futures market, which is people not actually buying the product but buying to hold for future gain? Is there a way of drilling down to find out how much is due to the futures and how much is due to the actual physical market?

Mr. Warren MacLean: I think people over time, people a lot more knowledgeable than I am, have spent time trying to exactly figure that out. It's not only speculators; it's what the security premium in the market is. In other words, is what's driving the price higher the Iranian nuclear program, the Middle East situation? People are always trying to parse the price of crude by various factors that they have, in my opinion, no way of ever figuring out.

I get back to this: if speculators are manipulating the market, that's another question. I think that's what's under investigation. The whole situation with Vitol having 11% of the open interest on the NYMEX, I think, is going to...if it's true, because I'm not even sure that's true. That's what's reported, but those are the things that I think the U.S. is trying to figure out right now. But again, it's due to manipulation. I don't think anybody can parse the price of crude by the various factors,

The Chair: It was interesting that in your last response to Mr. Van Kesteren, I think, you mentioned that in your view diesel is actually driving up the price of crude. Am I correct that you said that? If so, can you explain that?

Mr. Warren MacLean: Sure.

Nobody consumes crude oil—nobody. Consumers consume gasoline, diesel, and various other products. But at times the market will be driven by various parts of the market. If there's a shortage of crude and crude prices run up, if it's really crude-driven you'll see a shrinking in the refining margin because refiners are trying to outbid each other for crude that's scarce.

What I think you've seen in the last number of years is a shortage of diesel in China primarily, but also in India. If you want to look at a refining margin, look at the refining margin for diesel. It has blown out tremendously. There was a run-up after 2005, and then again toward the end of 2007-08. If you trace that back, you can see that demand in China for diesel was tremendous. In 2005, I believe they had some hydro-electricity problems and their electricity system was very suspect, so people had their own diesel generators and were out buying diesel from the marketplace.

Again, it happened after the earthquakes in China, where they shut down about 30 coal mines. They didn't have coal available to run power plants, so individual consumers were out buying diesel to generate their own electricity.

● (1155)

The Chair: My final question—and I'm sorry I don't have more time—may be more for the afternoon panel.

The U.S. lawmakers, the ones who are concerned about the role of speculation, are saying there's two factors. One is that there were regulators in the past who put limits on the amount, in terms of how much they could have in terms of a commodity exchange, so you would limit the amount that happened, say, in a futures market over commodities like the price of crude. Second is the allowing of what are called private electronic platforms. So the U.S. lawmakers are saying these two things are causing the role of speculators to increase, driving up the price for their benefit, not to actually reflect market price.

I don't know whether you can touch on that. It may be a question for the afternoon panel, but do you want to touch on those two things, whether those two developments are perhaps things we ought to look at?

Mr. Warren MacLean: I think those two things do make sense, that if there is an issue and you want to solve it, those would be the mechanisms through which to solve it. One would be to really decide who a speculator is and who is a commercial player and then to put limits on them in the futures market. The other would be—and I think they're headed for it anyway—to regulate the over-the-counter market or the swaps market.

The Chair: Thank you.

Members, Monsieur Vincent has one more question, so what I'm proposing we do is allow each party one more spot. If we can limit it to one question per party, we can then have a brief response to the members.

We are going over time right now, so I'll start with Monsieur Vincent, then Mr. Alghabra, and then a Conservative, then Ms. Nash.

Monsieur Vincent.

[*Translation*]

Mr. Robert Vincent: I cannot ask you just one question as it comes in three parts.

Mr. Boag, you started your presentation by saying that you represent 16 refineries. First, do the refineries, or the refiners, influence the price at the pump?

Second, in recent years, can the cost of refining go up and down?

Third, why does every refining company have the same per litre rate?

Please be assured that I will have a supplementary question after you answer.

● (1200)

[*English*]

The Chair: Mr. Boag.

Mr. Peter Boag: As I indicated in my initial remarks, there are a number of components, ultimately, of that price. There's the crude price of crude, there are taxes, and there are ultimately the refining and retail margins. So I guess to that extent, yes, refiners do have an impact and do have a role in the price.

Around the issue of setting the price, ultimately the wholesale price, the price that refiners get for their product, is determined in the context of a North American market, and that's done in a transparent way through trading and posting of rack prices.

As for the third element of your question, the cost of refining is relatively stable, but it does change over time. Probably the most significant change to refining costs is the costs imposed on refiners due to increasing environmental regulations. We've talked about the costs that industry incurred in terms of a $5 billion dollar investment to respond to the desulphurization of gasoline and diesel, and we have looked beyond that, potentially, to other costs imposed on refining through the imposition of more strict regimes in terms of air pollutants. So yes, refining costs are an element of that, but this goes all the way from the price of crude to the retail margins, and ultimately it's the decisions of retailers who set the price of what consumers pay at the pump.

The Chair: Okay.

Trente seconds, monsieur Vincent.

[*Translation*]

Mr. Robert Vincent: Could you tell me why oil cost $73 a barrel two years ago and a litre of gas was $1.06? A year later, the same litre of gas sold for $1.10, but a barrel of oil was $61. The difference was $12, but the price of gas at the pump stayed the same. Why did your profit margin go from 9 cents to 28 cents per litre in the same year?

[*English*]

The Chair: Be very brief, Mr. Boag.

Mr. Peter Boag: I'm not able to give you a definitive answer. You've thrown out some numbers that I can't respond to here. And certainly I would again caution you that margins don't necessarily mean profit margins: the margins are the difference between an input cost and a selling price.

The Chair: Thank you. *Merci*.

We'll go to Mr. Alghabra, please, for three minutes.

Mr. Omar Alghabra: Thank you, Mr. Chair.

I know, and I think Canadians know, that there's a lot we can't do about crude oil prices. We are price takers when it comes to crude oil.

Also, today, I'm not going to ask you a whole lot of questions about the speculators, because we have a panel on that later on. I think what we're trying to do is to figure out, given the restrictive nature of competition in the refinery and wholesale market, is how we can ensure that there's some fairness in that market. So yes, we can't control crude oil prices, and yes, there are issues with the financial market, but we're talking about inventory levels and price monitoring.

Regarding the point that was made earlier about the 5¢ up and down fluctuations that frequently are seen at the gas pumps, I'm curious to see if they are a direct reflection of...which, by the way, is not usually associated with the movements of crude oil prices up and down. Usually crude oil is stable or could go down, but still, on a weekly basis we'll see gas prices go and down about 5¢ or so. That's not relevant to the crude price, but is it relevant to the supply or the wholesalers—or is it the retailers? And if it is, and if we have such a competitive market at the retail level, why wouldn't the gas station next door be willing to accept a little lower margin and not follow the 5¢ increase, but instead accept a higher volume at the lower margin?

This is what I think a lot of Canadians have questions about, as they are not understanding these frequent 5¢ increases and decreases.

Mrs. Jane Savage: The most important thing for Canadians to understand is that the price at the pump is underpinned by the wholesale price of gasoline. Crude affects the wholesale price of gasoline, but gasoline impacts the wholesale price of gasoline. In other words, the world trades in gasoline as well as crude oil. So the difference between crude oil and gasoline changes, and that difference is how much margin is available to refiners. It is the wholesale price of gasoline, not the cost of gasoline, that moves every single day in Canada. So when a rack price increase or decrease goes through, the independent retailers, who make up 70% of the market, have to buy at that price every day. So the daily fluctuations in price at the pump are fundamentally underpinned by the daily fluctuations in wholesale gasoline prices.

● (1205)

The Chair: Mr. MacLean.

Mr. Warren MacLean: As Peter said, there's a world market for crude oil, there's a regional market for refining, and then there's a local market for retail. Each has its own dynamics. I think you're talking about the regional market for refining, which is either North American or, I would suggest, Atlantic basin. If the wholesale price in the gulf coast goes up, guess what? The wholesale price in Toronto is going to go up.

The Chair: Mr. Boag.

Mr. Peter Boag: At the wholesale level, we operate in essentially a continental market, and Canada represents a relatively small portion of that continental market. So for the most part we're price takers on wholesale gasoline. Today, the most recent numbers out of Natural Resources Canada show that on a national basis Canadian wholesale prices are within 1¢ of wholesale prices of the United States.

The Chair: Mr. Carrie.

Mr. Colin Carrie: I'd like to give the last thoughts to our panellists.

We've heard today about speculators; we've heard about the price of crude, the price of gasoline; we've heard about refining margins and retail margins; and we've heard about the carbon tax. Basically, what is the one thing Canadian consumers need to know? What message do you want to get to them?

Mrs. Jane Savage: For Canadians buying gasoline day in and day out, it is not the person who owns the gas station who's making the money. It is, recently anyway, the crude oil producer.

The Chair: Mr. MacLean.

Mr. Warren MacLean: It is an international market for oil and gasoline, a competitive market, and the Canadian consumer is well served by the marketplace.

Mr. Peter Boag: We understand Canadians' frustration with fuel price volatility, but that's the best evidence of a well-functioning, competitive market. In our view, notwithstanding the volatility, Canadians are well served by a competitive marketplace, and today they still pay the second lowest price for fuel in the western world.

The Chair: Ms. Nash.

Ms. Peggy Nash: Thank you.

I don't think it's the volatility of the price, but it's the high prices that are really bothering Canadians. I talk to a lot of seniors, for example, who are worried about keeping their homes over the winter because of heating costs. Each of you is saying it's someone else who is responsible for it, but one thing we know is that when crude prices go up—often for no reason pertaining to production—the industry makes windfall profits. It's nice to point fingers at others, and the industry may say it has no control over this, but coincidentally the oil industry makes huge profits when consumers are dinged at the pumps.

So my question to you is, why are the oil companies making such huge profits, if it's out of their hands that these prices are so high? Quite frankly, consumers don't buy it. They believe they're being gouged. Speculation is clearly part of this. We're going to deal with a panel on that this afternoon. People believe the oil companies are gouging them, and it's more than just a PR problem; it's a real concern for Canadians. We own huge supplies of oil in this country and, at the same time, we have the largest polluting project in the country, the tar sands, which are going to supply more oil. That's a huge concern for Canadians. Frankly, we have a problem with the way the oil industry is pricing the supply here and with the environmental impacts it is causing for all Canadians.

This is mainly a statement, but if you have any comments on it, I'd appreciate them.

● (1210)

Mrs. Jane Savage: I can start.

There's no question that there is a very strong correlation between price at the pump and oil industry profits—no question. The oil industry profits we're talking about relate fundamentally to the oil industry that's what we call the upstream. Call it pointing fingers if you like, but it is not the folks who are delivering fuel to Canadians all over rural parts of Canada who are making money—not that making money is necessarily evil. In fact, it's not evil at all; it's probably quite a good thing that people are making money. But having said that, it is without question the crude oil piece of this business, the upstream piece, that is making money. If your question really is who is making the money, it is the upstream, the crude oil production part of this business.

Why? I hope we've explained the various sectors, the crude oil piece of it, etc. That is fundamentally, yes, profits and gasoline prices, for example, and heating oil prices. We too are very concerned about the heating season coming up, when prices are going to be much higher than they were last year. For our customers it's going to be a very tough winter. We're as concerned as consumers, being just grown-up, great big consumers as independents. We are extremely concerned about it.

The Chair: Thank you, Ms. Savage.

Thank you, Ms. Nash.

Thank you all. Thank you to the witnesses for being here. I know you've been on the hot seat for two hours. We appreciate your coming forward and addressing this very complicated and very serious topic.

Members, we will resume here at one o'clock. I ask you to be back in the room at about five minutes to one. We'll resume our afternoon session at one o'clock.

I declare this meeting adjourned.

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