



## Public Competition Assessment

22 December 2015

### Elgas Limited – proposed acquisition of Wesfarmers Kleenheat Gas Pty Ltd's east coast LPG assets

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#### Purpose

1. This public competition assessment outlines reasons for the Australian Competition and Consumer Commission (**ACCC**) decision to not oppose the proposed acquisition of Wesfarmers Kleenheat Gas Pty Ltd's east coast liquefied petroleum gas assets (**Kleenheat**) by Elgas Limited (**Elgas**) (the **proposed acquisition**), subject to enforceable undertakings.
2. ACCC public competition assessments aim to improve transparency and ensure procedural fairness. We aim to provide the public with a better understanding of our analysis of various markets and competition issues. We generally issue a public competition assessment for transactions when:
  - an acquisition is opposed
  - an acquisition is subject to enforceable undertakings
  - the parties to the acquisition seek such disclosure, or
  - an acquisition is not opposed but raises important issues that the ACCC considers should be made public.
3. The ACCC considers each matter on a case-by-case basis. While some transactions may involve the same or related markets, the analysis and decision outlined in one assessment will not necessarily reflect the ACCC's view about other transactions.
4. The ACCC considers confidential information from parties and market participants when making a decision. Our public assessments may not identify and explain all issues that we considered because we must maintain confidentiality about certain information and sources.

#### The ACCC's decision

5. Section 50 of the *Competition and Consumer Act 2010* (the **Act**) is the relevant provision for the ACCC's assessment. Section 50 prohibits acquisitions that would have the effect, or be likely to have the effect, of substantially lessening competition in any market.

6. On 18 December 2014, the ACCC announced its decision not to oppose the proposed acquisition, after accepting section 87B undertakings from Elgas and Kleenheat (together, the **undertakings**).
7. On 29 August 2014, the ACCC suspended the timeline for its review in anticipation of receiving an undertaking from Elgas. Subsequent negotiations resulted in Elgas offering an undertaking to the ACCC on 5 December 2014.
8. On 10 April 2014, Elgas announced its proposal to acquire the east coast liquefied petroleum gas (**LPG**) assets of Kleenheat. The assets included Kleenheat's depots, trucks, storage tanks and cylinders. For the purposes of the proposed acquisition and this public competition assessment, 'east coast' refers to Queensland, New South Wales, the Australian Capital Territory, Victoria, Tasmania and South Australia. Kleenheat's LPG assets in Western Australia and the Northern Territory were not part of the proposed acquisition.
9. The ACCC decided that the proposed acquisition, after taking into account the undertakings given by the merger parties, would not be likely to have the effect of substantially lessening competition in contravention of section 50 of the Act. The ACCC considered the competitive effects of the proposed acquisition in the following markets:
  - state and regional markets for the distribution of non-automotive LPG in bulk and in cylinders
  - state-wide markets for the wholesale supply of LPG, and
  - markets for the supply of automotive LPG.
10. Further details regarding the ACCC's reasoning are provided below.

## **The parties**

### **The acquirer: Elgas Limited**

11. Elgas is a major wholesaler and distributor of automotive and non-automotive LPG in Australia. It uses a range of transport options and storage facilities to distribute LPG in both cylinders and bulk to a variety of customer segments.
12. Elgas owns and operates the 'Cavern', which is a major LPG import and storage facility in Port Botany, New South Wales. Elgas also owns and operates an extensive network of LPG depots throughout Australia.
13. Elgas is a member of the BOC Group of companies, which is owned by the Linde Group, an international gas and engineering company.

### **The target: Wesfarmers Kleenheat Gas Pty Ltd's east coast LPG assets**

14. Kleenheat is a major wholesaler and distributor of automotive and non-automotive LPG in Australia, supplying LPG in cylinders and in bulk to serve the needs of different customers.
15. Kleenheat owns an LPG extraction plant in Kwinana, Western Australia, and operates a large network of depots throughout Australia. It is a wholly-owned

subsidiary of Wesfarmers Limited, a public company listed on the Australian Securities Exchange.

## Other industry participants

### Origin

16. Origin Energy Limited (**Origin**) is a national energy retailer which wholesales and distributes automotive and non-automotive LPG (bulk and cylinder) to a variety of customer segments. Origin has LPG operations in all Australian states and territories. It owns and operates seven seaboard terminals on the east coast of Australia, and a network of depots throughout Australia. Origin operates its LPG businesses under four brands: Origin LPG, Speed-e-gas, Powergas and Quickswap. Origin is listed on the Australian Securities Exchange.

### Supagas

17. Supagas Pty Ltd (**Supagas**) is a non-automotive LPG distributor (bulk and cylinder) operating in Victoria, South Australia, Tasmania, the Northern Territory, and Western Australia. It operates a number of depot facilities within these states and territories. Supagas is a private company which began in Melbourne in 1968 under the name of Australian Forklifts.

### Renegade

18. Renegade Gas Pty Ltd (**Renegade**) is a non-automotive LPG distributor (bulk and cylinder) operating in New South Wales, Queensland, and the Australian Capital Territory. It operates a number of depot facilities within these states and territories. Renegade is a private company which was established in 1997. Renegade trades under the name "Supagas", but is a separate entity and business from Supagas Pty Ltd.

### United Gas

19. United Gas is a non-automotive LPG distributor (bulk and cylinder) operating in South Australia and Victoria. United Gas is owned by Arcadia Energy Trading Limited (**Arcadia**), which acquired the United Gas business from United Petroleum in 2013. Arcadia is a wholesale commodity trader specialising in the energy sector. It is part of the global Farahead Group of companies which owns major oil shipping and physical oil trading companies worldwide.

### Direct Gas

20. Direct Gas is a non-automotive LPG distributor (bulk and cylinder) operating out of Dandenong, Victoria. Direct Gas began supplying non-automotive LPG in 2012. Direct Gas also operates the United Gas business (as contractors) for Arcadia.

### Air Liquide Australia

21. Air Liquide Australia is a member of the Air Liquide Group, an international industrial gas company. In Australia, Air Liquide Australia's business is predominantly in industrial gases, with limited distribution of non-automotive LPG (in cylinders only).

## Review timeline

22. The following table outlines the timeline of key events in this matter.

Date	Event
10 April 2014	ACCC commenced review under the Merger Process Guidelines.
17 April 2014	ACCC requested further information from the merger parties.
9 May 2014	ACCC received information from the merger parties.
5 June 2014	ACCC published a Statement of Issues outlining preliminary competition concerns.
27 June 2014	ACCC requested further information from the merger parties.
18 July 2014	ACCC received information from the merger parties.
14 August 2014	ACCC requested further information from the merger parties. Former proposed date for announcement of ACCC's final decision (28 August) delayed to allow the merger parties time to provide additional information.
19 August 2014	ACCC received further information from the merger parties.
26 August 2014	Former proposed decision date of 4 September delayed to allow the vendor to provide more information in response to issues raised by the ACCC.
29 August 2014	ACCC received further information from the vendor. Former proposed decision date of 11 September delayed to allow more time for the acquirer to provide additional information.
5 December 2014	Elgas offered a section 87B undertaking to the ACCC.
8 December 2014	ACCC commenced market inquiries in relation to proposed section 87B undertaking offered by Elgas.
18 December 2014	ACCC announced it would not oppose the proposed acquisition, subject to section 87B undertakings accepted by ACCC.

## Market inquiries

23. The ACCC conducted market inquiries with a range of industry participants, including LPG wholesalers, retailers, distributors, dealers, agents and customers (residential, commercial and industrial). Submissions were sought in relation to the substantive competition issues and the proposed undertakings.

## Statement of Issues

24. The ACCC published a Statement of Issues on 5 June 2014. In the Statement of Issues the ACCC expressed the preliminary view that the proposed acquisition

would be likely to result in a substantial lessening of competition in the distribution of bulk and cylinder non-automotive LPG in regional markets and to national customers in Australia.

25. The ACCC was particularly concerned that the proposed acquisition would be likely to have the effect of substantially lessening competition by aggregating two of the three largest distributors of non-automotive cylinder and bulk LPG.
26. The ACCC also expressed the preliminary view that:
  - the proposed acquisition had the potential to harm competition for the wholesale supply of LPG in state-based markets, especially in New South Wales
  - the proposed acquisition would be unlikely to substantially lessen competition in any relevant automotive LPG market.

## **Future with and without the proposed acquisition**

27. Section 50 of the Act prohibits acquisitions that would have the effect or be likely to have the effect of substantially lessening competition in a market. In assessing a proposed acquisition pursuant to section 50 of the Act, the ACCC considers the likely effects of the acquisition by comparing the likely future competitive environment if the acquisition proceeds (the “with” position) to the likely future competitive environment if the acquisition does not proceed (the “without” position) to determine whether the proposed acquisition is likely to have the effect of substantially lessening competition in any relevant market.

### **Preliminary view in the Statement of Issues**

28. In the Statement of Issues the ACCC expressed the preliminary view that, without the proposed acquisition, Kleenheat would continue to operate its LPG assets on the east coast independently of Elgas. Therefore, in the Statement of Issues the ACCC assessed the competitive effects of the proposed acquisition against a future in which competition remained broadly as it stood before the proposed acquisition.

### **ACCC consideration since the Statement of Issues**

29. After the release of the Statement of Issues, Kleenheat submitted to the ACCC that, in the absence of the proposed acquisition, Kleenheat would cease to operate its LPG business on the east coast of Australia.
30. The ACCC conducted market inquiries and carefully considered information provided by interested parties on this issue. The ACCC also examined in detail extensive confidential information provided by the merger parties, including financial information and internal company documents that preceded contemplation of the proposed acquisition.
31. Taking account of this information and other materials before it, the ACCC formed the view that Kleenheat’s LPG business on the east coast would be likely to cease trading if the proposed acquisition did not proceed.

32. However, even if a business ceases trading it does not necessarily follow that its assets would also exit the relevant markets. In this case, the ACCC considered what would happen to the assets of Kleenheat in the absence of the acquisition. The ACCC concluded that, absent the proposed acquisition, most of Kleenheat's east coast LPG assets (such as depots, trucks, storage tanks and cylinders) would be likely to become available for alternative distributors to purchase and use these assets to compete in the relevant markets and would not exit the industry.
33. The ACCC also concluded that in the likely future without the proposed acquisition, Kleenheat's customers would become contestable, thereby providing opportunities for alternative distributors to acquire new customers and strengthen their competitive position.

## Industry background

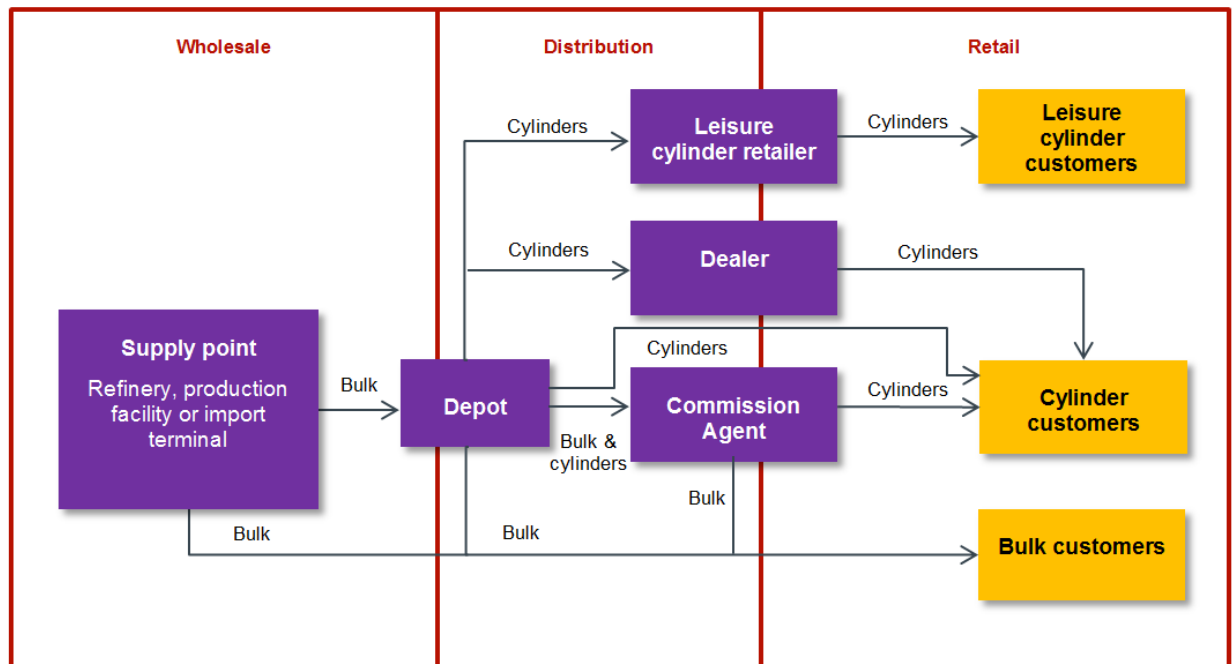
### LPG overview

34. LPG is the generic name for mixtures of light hydrocarbon gas, consisting mainly of propane and butane, or propane only. Broadly, the multiple uses of LPG may be characterised into two main streams:
  - automotive, often referred to in the industry as 'autogas'
  - non-automotive, often referred to in the industry as 'traditional' LPG.
35. LPG has a variety of different end uses, including automotive (e.g. motor vehicles), domestic (e.g. heating), leisure (e.g. barbeques), commercial (e.g. cooking) and industrial.
36. LPG businesses differ in how they organise their supply chains and the terminology they use. There are many different levels in the supply chains of LPG, and the business models vary in the way that customers are serviced. Although the definitions are not always precise, for the purposes of the ACCC's competition assessment:
  - **Wholesale** is the supply of LPG from a production or import facility. This may include LPG from oil refineries or gas production facilities where LPG is produced as a by-product.
  - **Distributors** of LPG purchase LPG from wholesalers or resellers and transport the product to a depot where it is:
    - stored and decanted to fill LPG cylinders and then supplied to customers in pre-filled cylinders
    - stored and supplied to customers in bulk.Distributors may also supply customers directly from a wholesale supply point rather than via an LPG depot, dealer or agent, especially large bulk customers.
  - **Dealers** (e.g. hardware stores, rural retail outlets) and **agents** act as intermediaries between distributors and end customers. Distributors such as Elgas, Kleenheat and Origin often engage dealers or agents to reach end customers in outer regional areas, located at a distance from the distributor's depot or supply point.

- **Leisure cylinder retailers** supply leisure cylinders to end customers. These cylinders are swap cylinders such as those used for barbeques. Examples of leisure retailers are Bunnings, Masters Home Improvement, Woolworths Petrol, Coles Express, BP and Caltex.

37. Figure 1 below illustrates a typical LPG supply chain for non-automotive LPG. There may be variations depending on factors such as a customer's proximity to a depot.

**Figure 1: Typical supply chain for non-automotive LPG**



## Production and importation of LPG

### Production

38. LPG is produced:
- directly by refining crude oil and natural gas during processing
  - as a by-product of refining crude oil.
39. Natural gas processing plants and crude oil refineries supply LPG on a wholesale basis to large customers such as Origin, Elgas and Kleenheat.
40. Crude oil refineries that produce LPG on the east coast as a by-product of their main activity include:
- BP at its refinery on Bulwer Island in Brisbane, Queensland (BP closed this refinery in 2015)
  - Vitol at its refinery in Geelong, Victoria
  - Mobil at its refinery in Altona, Victoria
  - Caltex at its refinery in Lytton, Queensland.

41. Producers of LPG as a by-product typically favour contracts with large downstream LPG distributors which are able to commit to regular offtake. This is to reduce the risk of interrupting their main activity due to LPG overflow.
42. There are also major companies involved in extracting LPG from gas fields on the east coast of Australia such as the Otway Gas Project – a joint venture between Origin, Benaris and CalEnergy. This gas processing plant is located in Port Campbell, Victoria.
43. Some LPG producers are vertically integrated: they use LPG in their own operations, and also sell it to their competitors in downstream markets. For instance, Kleenheat owns an LPG extraction plant in Kwinana, Western Australia. It uses the LPG in its downstream distribution business, but also sells wholesale LPG from the Kwinana plant to other distributors.

### Imports

44. LPG is also imported (mostly from the Middle East) in shipments and stored at an import terminal. Elgas owns and operates the 'Cavern', located at Port Botany in New South Wales. The Cavern is the largest LPG import storage terminal on the east coast and is capable of receiving large volumes of LPG from large gas ships.
45. Origin also operates a smaller import storage facility at Port Botany, and ships LPG from various sources to smaller seaboard terminals along the Queensland coast, the Northern Territory and Tasmania.

### Distribution of LPG

46. The three largest distributors of LPG on the east coast are Elgas, Kleenheat and Origin. Elgas and Origin are the only vertically integrated non-automotive LPG distributors on the east coast. They both have LPG import terminals and extensive downstream LPG distribution networks. Elgas and Origin act as wholesalers to other distributors and each other. Kleenheat itself does not have any import terminals or production facilities on the east coast.

### Bulk and cylinder distribution

47. Within non-automotive LPG, the two main methods of distribution are:
  - bulk supply – LPG supply via trucks which refill tanks installed permanently at the customer's premises
  - cylinder supply – LPG supply to customers in pre-filled cylinders.
48. Bulk LPG is distributed to small, medium and large commercial and industrial customers. Residential customers may also receive LPG in bulk form. Customers use a variety of bulk tank sizes to store LPG. Depending on the customer, bulk tanks vary in size, from 210 kg up to 100 tonnes.
49. Bulk LPG may be delivered directly from a wholesale supply source to end customers, without passing through depots, dealers or agents. This is especially the case for large bulk customers and some other customers located en route to a depot (or other delivery point) being supplied by truck from a wholesale source.



Bulk customers requiring smaller quantities are often served via depots, dealers or agents.

50. Cylinder LPG is typically supplied in pre-filled cylinders on an exchange basis. Cylinders are supplied in different sizes, including (approximate):
  - 9 kg cylinders (e.g. for residential customers and leisure retailers)
  - 15 kg cylinders (e.g. for forklift cylinder customers)
  - 45 kg cylinders (e.g. for residential customers and commercial/industrial customers).
51. LPG cylinders are re-filled at depots and then transported by flatbed truck or utility vehicle from a depot (or other distribution point such as a staging yard) to end customers, dealers or agents.

### Depots

52. LPG is transported within Australia by road and supported by a network of depot and distribution infrastructure. Depots often comprise LPG bulk storage tanks, LPG cylinder filling, testing and refurbishing equipment, delivery trucks and an office (sometimes with a retail presence).
53. Depots are generally located in industrial areas and are equipped to provide both bulk and cylinder services (although some smaller distributors only supply cylinder services).

### Dealers and agents

54. Dealers (e.g. hardware stores and rural retail outlets) and agents act as intermediaries between distributors and end customers. Distributors such as Kleenheat and Elgas typically engage dealers or agents to reach end customers in outer regional areas located a large distance from the distributor's depot. End customers in outer regional areas are therefore often served by a dealer (e.g. their local hardware store), rather than direct by a distributor.
55. The business models for dealers and agents are generally different:
  - Under an agent model, the distributor sets the retail price of LPG, and the agent receives a commission for their delivery and other services.
  - Under a dealer model, the distributor sells the dealer a quantity of LPG, and the dealer sets its own retail price for customers (the dealer is a customer of the distributor).

### Customers

56. The LPG network described above is developed around the multiple uses of LPG and to meet the needs of different customers. These customers include:
  - large bulk customers (e.g. industrial)
  - medium bulk customers (e.g. commercial)
  - small bulk customers (e.g. restaurants and some residential)
  - leisure retailers (e.g. retailers that sell pre-filled barbeque cylinders)

- national customers (e.g. customers such as leisure retailers that have a presence in more than one state and are served by a single LPG distributor)
- residential (e.g. residential customers that use LPG for heating).

## Market definition

57. The ACCC assessed the competitive effects of the proposed acquisition in the context of the following markets:
- State and regional markets for the distribution of non-automotive LPG in bulk.
  - State and regional markets for the distribution of non-automotive LPG in cylinders.
  - State markets for the wholesale supply of LPG.
  - Markets for the supply of automotive LPG.

### Markets for the distribution of non-automotive LPG

58. As noted earlier, the merger parties primarily overlap in the distribution of bulk and cylinder non-automotive LPG.

### Product dimension

59. The ACCC considered whether the distribution of bulk and cylinder non-automotive LPG formed a single or two separate markets, but as this issue was not determinative in this review, the ACCC did not form a concluded view and therefore assessed the proposed acquisition based on separate markets. The ACCC considered there were many overlapping competition issues between the two forms of distribution.
60. In the Statement of Issues the ACCC expressed the preliminary view that there was likely to be a separate market for the distribution of non-automotive LPG to large national customers. However, market inquiries since the Statement of Issues indicated that defining a separate market may not be appropriate. Some national customers expressed a view that they could disaggregate their contract into separate components for each state if faced with a price rise for national services. For the purposes of the competition assessment, the ACCC did not consider it critical to form a concluded view on whether a separate national market existed. The competition analysis below considers the effects of the proposed acquisition on national customers as part of the analysis of state and regional distribution markets.

### Geographic dimension

61. The ACCC assessed the effects of the proposed acquisition in, broadly, state-wide and regional markets. Some distributors organise their operations on a state-wide basis. However, the boundaries of state-wide markets do not necessarily coincide with official state borders (given the boundaries of competition are not determined by such borders).

62. The ACCC concluded that competition occurred not just on a state-wide basis, but also at a regional level through the presence of local distributors (such as a local depot or via a dealer and/or agent). For instance, some distributors operate in particular regions without having state-wide coverage. Elgas and Kleenheat have state-wide non-automotive LPG distribution in New South Wales and Victoria. Therefore, the ACCC found that competition for the distribution of non-automotive LPG occurred on both a state-wide and narrower regional basis.
63. The geographic distances over which it is economically viable to deliver non-automotive LPG differs between distributors due to a range of factors. These factors include their respective business model, distance between points in their distribution network, transport costs and the volume demand densities of different regions. The evidence showed that the majority of cylinder and bulk deliveries were made within 100 km of the relevant depot, dealer or agent, but there were also variations in distances for the reasons outlined above.
64. The ACCC concluded that competitive harm resulting from the proposed acquisition would likely manifest in some particular regions more strongly than in other regions within the same market. These particular regions are discussed further below in the context of the undertakings given by the merger parties.

## Other markets

### State markets for the wholesale supply of LPG

65. Consistent with its preliminary view in the Statement of Issues, the ACCC considered that there are markets for the wholesale supply of LPG, either state-wide or broader geographic markets. For the purposes of the ACCC's review, we did not consider it necessary to precisely define these markets.

### Automotive LPG markets

66. The ACCC formed the view that the supply of automotive LPG was likely to be a separate product market to non-automotive LPG, given the different distribution models. In addition, depending on the intended customer use, one type of LPG may not necessarily be used in place of the other. The ACCC did not consider it necessary to define the geographic scope of the market for the supply of automotive LPG as we ultimately found that the proposed acquisition was unlikely to raise significant competition concerns in any automotive LPG market.

## Conclusion on market definition

67. The defined markets are listed at paragraph 57. However, given the overlap between the merger parties, the ACCC concluded that the markets of particular relevance in assessing the competitive effects of the proposed acquisition were state and regional markets for the distribution of non-automotive LPG in bulk and cylinders.

## **Competition analysis – issues unlikely to substantially lessen competition**

68. This section considers issues that the ACCC ultimately concluded were not likely to result in a substantial lessening of competition in any relevant market.

## Horizontal aggregation in wholesale markets

69. In its Statement of Issues, the ACCC expressed the preliminary view that the proposed acquisition had the potential to harm competition for wholesale supply of LPG. In particular, some market participants were concerned that Kleenheat would be removed from the markets as an alternative wholesale supplier.
70. As noted above (paragraph 46), Kleenheat does not operate wholesale facilities (i.e. production or import facilities) on the east coast of Australia. However, information available to the ACCC indicated that Kleenheat did at times resell LPG to smaller downstream distributors. Kleenheat was therefore viewed by some parties as an alternative reseller of LPG.
71. However, the ACCC's market inquiries and information obtained from Kleenheat indicated that Kleenheat undertakes only limited reselling activity. Therefore the ACCC considered that the removal of Kleenheat would not materially alter the ability of distributors to access wholesale sources of LPG.
72. The ACCC acknowledged that Elgas would increase its utilisation of the Cavern post-acquisition given the increase in its downstream operations. However, the ACCC did not consider this would lead to a significant reduction in competition.

## Vertical foreclosure

73. In its Statement of Issues, the ACCC reflected the views of some market participants that Elgas may have the ability and incentive to foreclose downstream rivals' (i.e. other distributors') access to wholesale LPG. The Statement of Issues indicated that Elgas' incentive to foreclose may be increased post acquisition in line with its downstream market share, because of the likelihood that Elgas would capture a higher proportion of customers if it foreclosed its downstream rivals.
74. As noted earlier, Elgas owns and operates the 'Cavern' at Port Botany which is a wholesale source of imported LPG. Origin also has an import and storage facility at Port Botany, and operates a number of other seaboard terminals. Elgas and Origin are the only vertically integrated LPG participants with large downstream LPG distribution networks on the east coast of Australia.
75. The ACCC considered that the proposed acquisition would not significantly alter Elgas' ability and incentive to supply LPG to other distributors. The ACCC noted that some distributors source and transport LPG by road from alternative sources in Victoria and therefore could bypass Elgas if necessary. In addition, at the time of the ACCC's review, Kleenheat did not own or operate any wholesale LPG production or import facilities on the east coast. Therefore, no wholesale LPG assets would be acquired by Elgas as part of the proposed acquisition.
76. For these reasons, the ACCC concluded that Elgas' ability and incentive to supply wholesale LPG to downstream rivals would not be materially different after the acquisition.

## Automotive LPG

77. Consistent with the ACCC's preliminary view in the Statement of Issues, concerns were not raised by any interested party about the likely effect of the proposed acquisition on competition in any relevant automotive LPG market.

### **Competition analysis – issues of concern**

78. This section considers the impact of the proposed acquisition on competition for the distribution of non-automotive LPG in state and regional markets. It discusses the ACCC's competition concerns in these markets and the section 87B undertakings received from the merger parties.

#### Reduction in the number of distributors of non-automotive LPG in state and regional markets

79. The three major distributors of non-automotive LPG in bulk and cylinders on the east coast are Kleenheat, Elgas and Origin. These distributors have extensive geographic coverage in their networks, including through agent and/or dealer networks in metropolitan and regional areas.
80. The ACCC was particularly concerned that aggregating two of the three largest distributors of non-automotive LPG would enhance the ability and incentive of the merged entity to raise prices and/or reduce service levels in bulk and cylinder markets.
81. Following the acquisition, markets for the distribution of non-automotive LPG in Victoria, New South Wales and the Australian Capital Territory would be highly concentrated with the merged entity becoming the largest distributor by a significant margin. This is of particular concern as barriers to entry or expansion in these markets are considered high (discussed below at paragraphs 89 to 91).
82. The ACCC noted that non-automotive LPG prices charged to customers varied significantly not only between states, but also between regions within states. The ACCC's market inquiries revealed that these price differences were influenced by the intensity of competition, which depended on the number and effectiveness of competitors present. Therefore, the ACCC considered both state and regional aspects of the competitive process.
83. The ACCC recognised the complexity of distribution networks and the large number of variables that determine whether a particular customer could be served on competitive terms by an alternative distributor, dealer or agent. For instance, the ACCC's market inquiries since the Statement of Issues highlighted that having a locally based LPG depot can provide a competitive advantage for an incumbent distributor.
84. However, it is possible for distributors in some circumstances to compete effectively for customers in a town without having a depot in that town or surrounding region. In particular, the more extensive a competitor's network is, the better placed it is to compete for and attract new customers. Elgas and Kleenheat have extensive distribution networks with the ability to serve different customers in both metropolitan and regional areas.

85. The ACCC considered that the proposed acquisition would not be likely to have the effect of substantially lessening competition in the other relevant eastern states (Queensland, South Australia and Tasmania). Elgas and Kleenheat have a smaller presence in these states, while Origin has a stronger competitive presence. There are also a number of smaller distributors. Taken collectively, the ACCC found that these competitors would be sufficient to constrain the merged entity in the other states.

#### Level of constraint provided by other distributors

86. Smaller distributors such as Supagas and Renegade operate in metropolitan areas and major regional hubs. At the time of the ACCC's review, these distributors had limited network coverage in regional or rural areas, especially in areas where there is low demand.
87. Origin is a larger market participant but it has a limited network in some areas, especially in parts of regional Victoria. The ACCC was concerned that Origin would not constrain Elgas after the acquisition due to gaps in Origin's network in these areas, and the barriers to expanding into new areas (discussed below at paragraphs 89 to 91).
88. Accordingly, absent the undertakings, the ACCC was concerned that Origin and smaller distributors would pose a limited constraint on Elgas after the acquisition in certain geographic areas (mainly regional) in Victoria, New South Wales and the Australian Capital Territory.

#### Barriers to entry and expansion

89. The ACCC considered that there are high barriers to entry and expansion in the distribution of non-automotive LPG and there was unlikely to be any significant new entry or expansion in the foreseeable future.
90. Market inquiries identified a number of barriers, including:
- high capital costs required to establish a distribution network, including sunk costs, relative to the potential returns and long recoupment period
  - a critical mass of customers required to support investment in a distribution network and to achieve economies of scale, which is made more difficult in areas where there is low demand
  - access to a competitive source of wholesale LPG which would allow parties to compete effectively with incumbent distributors
  - strategic barriers, whether real or perceived, such as retaliatory action against potential rivals designed to deter them from seeking to compete to attract a critical mass of customers.
91. The ACCC considered that the barriers to entry identified above would deter potential new entrants, or existing distributors considering expanding, thus limiting the level of constraint on Elgas post-acquisition from existing or new rivals.

## Conclusion on competition concerns, absent the section 87B undertakings

92. In light of the above, the ACCC was concerned that absent the section 87B undertakings, the proposed acquisition would be likely to have the effect of substantially lessening competition in the distribution of non-automotive LPG in state and regional markets.

## Undertakings

93. On 17 December 2014, the ACCC accepted section 87B undertakings given by Kleenheat and Elgas. An undertaking accepted by the ACCC pursuant to section 87B of the Act is a court-enforceable commitment. The section 87B undertakings accepted by the ACCC in this review are available on the ACCC's mergers public register at:  
<http://registers.accc.gov.au/content/index.phtml/itemId/1183747/fromItemId/751043>.
94. Elgas gave a section 87B undertaking to the ACCC to address the competition issues likely to arise as a result of the proposed acquisition. In particular, the Elgas undertaking is intended to preserve competition in areas where Elgas would be otherwise likely to face substantially less competition from other non-automotive LPG distributors post-acquisition in the absence of the undertaking. Kleenheat also gave a section 87B undertaking to the ACCC to facilitate transitional issues associated with the Elgas undertaking.
95. The section 87B undertaking given by Elgas focuses on the geographic areas (mainly regional) in Victoria, New South Wales and the Australian Capital Territory where Elgas and Kleenheat competed before the proposed acquisition, but had few other competitors.
96. These regions were identified on the basis of feedback received by the ACCC during market inquiries, and were assessed by the ACCC as being the regions where competitive harm was likely. The undertakings address these concerns. Importantly, the undertakings strengthen the ability of Renegade and Origin to compete and facilitate their expansion into areas where Elgas would have faced limited competition absent the undertakings.
97. The Elgas undertaking requires Elgas to divest Kleenheat's physical assets associated with the distribution of LPG in certain regions, and contracted customers in those regions, to Origin and Renegade.
98. Specifically, Elgas must divest specified assets including freehold property, leases, contracts, plant and equipment, cylinders, vehicles and inventory associated with the following Kleenheat sites to Renegade in New South Wales and the Australian Capital Territory:
- Dubbo, NSW
  - Griffith, NSW
  - Kempsey, NSW
  - Moama, NSW
  - Nowra, NSW
  - Stroud, NSW
  - Tamworth, NSW

- Mitchell, ACT.
99. Similarly, Elgas must divest the following Kleenheat sites (and associated assets) to Origin in Victoria:
- Maryborough
  - Swan Hill
  - Warrnambool (only customers and certain assets in this region, there is no physical Kleenheat site in Warrnambool).
100. The objective of the Elgas and Kleenheat undertakings is to address the ACCC's competition concerns (as set out above) raised by the proposed acquisition. In particular, as set out in the Elgas undertaking, this objective would be met by:
- ensuring that certain Kleenheat LPG distribution assets based in regional Victoria are divested to Origin (or to another approved purchaser if the divestiture does not occur within a certain period)
  - ensuring that certain Kleenheat LPG distribution assets based in the Australian Capital Territory and regional New South Wales are divested to Renegade (or to another approved purchaser if the divestiture does not occur within a certain period)
  - creating or strengthening Origin's (or an alternative approved purchaser's) position as a viable, effective, stand-alone, independent and long term competitor in the distribution of cylinder and bulk non-automotive LPG by enhancing its presence in regional Victoria (including some areas across the border into New South Wales)
  - creating or strengthening Renegade's (or an alternative approved purchaser's) position as a viable, effective, stand-alone, independent and long term competitor in the distribution of cylinder and bulk non-automotive LPG by enhancing its presence in regional New South Wales (including some areas across the border into Victoria) and the Australian Capital Territory
  - ensuring that Origin and Renegade (or any other approved purchasers of the divestiture assets) have all the necessary related assets, personnel, transitional and other assistance and other rights to compete effectively with Elgas in the distribution of cylinder and bulk non-automotive LPG
  - maintaining the economic viability, marketability, competitiveness and goodwill of the divestiture assets, and
  - providing for the effective oversight of Elgas' compliance with the Elgas undertaking.
101. The ACCC considered that the divestitures provided for in the Elgas undertaking would address the competition concerns in both state and regional markets, for the following reasons:
- The ACCC-approved purchasers of the assets to be divested, Origin and Renegade, already have businesses distributing non-automotive LPG. They are capable of effectively using their experience and existing assets to compete with Elgas and any other competitors in the divestment regions.



- The divestures would maintain or increase competition in the regions where competitive harm would be most likely to materialise as a result of the proposed acquisition. By acquiring the assets to be divested by Elgas, Renegade and Origin would immediately extend the reach of their respective distribution networks in Victoria, New South Wales and the Australian Capital Territory. This would strengthen their ability to compete with Elgas, and other competitors, in particular regional areas and more broadly on a state-wide basis.
- The acquisition of depots and transfer of customers would provide Renegade and Origin with greater economies of scale in their respective distribution networks, strengthening their competitive position.

## **Conclusion**

102. Taking into account the undertakings given by Elgas and Kleenheat, the ACCC concluded that the proposed acquisition of Kleenheat's east coast LPG business by Elgas would not be likely to have the effect of substantially lessening competition in any relevant market.