ENTERPRISE AND LIFELONG LEARNING COMMITTEE

Monday 31 January 2000
(*Afternoon*)

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ENTERPRISE AND LIFELONG LEARNING COMMITTEE
3rd Meeting 2000 (Chamber)

CONVENER:

*Mr John Swinney (North Tayside) (SNP)

DEPUTY CONVENER:

*Miss Annabel Goldie (West of Scotland) (Con)

COMMITTEE MEMBERS:

*Fergus Ewing (Inverness East, Nairn and Lochaber) (SNP)
Mr Nick Johnston (Mid Scotland and Fife) (Con)
Marilyn Livingstone (Kirkcaldy) (Lab)
*George Lyon (Argyll and Bute) (LD)
Ms Margo MacDonald (Lothians) (SNP)
Mr Duncan McNeil (Greenock and Inverclyde) (Lab)
*Dr Elaine Murray (Dumfries) (Lab)
*Elaine Thomson (Aberdeen North) (Lab)
*Allan Wilson (Cunninghame North) (Lab)

*attended

THE FOLLOWING MEMBERS ALSO ATTENDED:

Linda Fabiani (Central Scotland) (SNP)
Rhoda Grant (Highlands and Islands) (Lab)
Irene McGugan (North-East Scotland) (SNP)
Mr John Munro (Ross, Skye and Inverness West) (LD)
Mr Murray Tosh (South of Scotland) (Con)

WITNESSES:

Simon Graham (Shell UK)
Ray Holloway (Petrol Retailers Association)
Sheila Johnstone (Arran Council for Voluntary Service)
Billy Laing (Gleaner Oils Ltd)
Jim Lees (Arran Council for Voluntary Service)
Mike Lunan (Arran Council for Voluntary Service)
Councillor Donald Maclean (Highlands and Islands Hydrocarbon Action Group)
Councillor Alison Magee (Highlands and Islands Hydrocarbon Action Group)
John Mumford (BP Oil UK Ltd)
Nancy Race (Office of Fair Trading)
Ian Wells (Esso Petroleum Co Ltd)
Alan Williams (Office of Fair Trading)

CLERK TEAM LEADER:

Simon Watkins

SENIOR ASSISTANT CLERK:

David McLaren

ASSISTANT CLERK:

Mark MacPherson

Scottish Parliament

Enterprise and Lifelong Learning Committee

Monday 31 January 2000

(*Afternoon*)

[THE CONVENER *opened the meeting at 13:33*]

Petrol Pricing

The Convener (Mr John Swinney): The first item on the agenda is our inquiry into petrol pricing. The committee agreed to hold a single-session inquiry into differential petrol pricing in remote and rural areas of Scotland. The committee agreed, as part of its remit, to inquire into the pricing of vehicle fuel in remoter rural areas as it affects local business. We agreed in particular to establish the basis for the higher prices charged by fuel stations in such areas and to determine whether that is reasonable.

We have a full list of witnesses today and I thank them all for attending the meeting; we will take each group of witnesses in succession. We have received apologies from a few committee members. Duncan McNeil has been detained on constituency business in Inverclyde, and Margo MacDonald and Marilyn Livingstone cannot be with us. Nick Johnston had intended to be here but, as he has declarable and registrable interests in the motor industry, he considered it appropriate not to attend; the committee notes his discretion.

We have been joined by John Farquhar Munro, Rhoda Grant and Irene McGugan from the Rural Affairs Committee. Murray Tosh from the Transport and the Environment Committee may join us in the course of the afternoon.

Our first group of witnesses is from the Highlands and Islands hydrocarbon action group and is led by Councillor Alison Magee. Councillor Magee, I shall ask you first to introduce yourself and your colleagues and then to make some opening remarks.

Councillor Alison Magee (Highlands and Islands Hydrocarbon Action Group): Thank you. I am Alison Magee, vice-convener of the Highland Council. On my left is Councillor Donald Maclean, chairman of the economic development committee of Western Isles Council. Next to him are Harry Miller, a trading standards officer with Western Isles Council, and Ken McCorquodale, a policy officer with the Highland Council.

The Convener: Thank you. Would you like to make some introductory remarks to the committee before we start to ask questions?

Councillor Magee: I welcome the opportunity to be here today. With your permission, convener, I would like to make a few comments, as petrol pricing is a complex issue.

We have just commissioned research into the economic impact of fuel pricing in the Highlands and Islands, which has been very revealing. There are a number of complex matters at play. Average incomes in the Highlands and Islands are less than 80 per cent of the average Scottish income. Car and transport users travel distances almost double the Scottish average. Sixty-five per cent of people live more than one hour’s drive from a major centre, compared with 10 per cent of people nationally. Average fuel costs are 10 to 20 per cent higher. Car dependency is far greater because of the difficulty of providing affordable and adequate public transport. The other factor is the fuel escalator. Those issues combine to create the situation that we are in today.

Our research suggests that motorists in the Highlands and Islands—an area where incomes are much lower—spend an additional £88 million a year on motoring compared with motorists in the rest of Scotland. Of that, £17.8 million is spent as a direct result of the higher cost of fuel, and VAT accounts for £2.7 million.

An on-going Office of Fair Trading inquiry was set up in March last year. Our group had the opportunity to spend a great deal of time with the OFT. The reason that it gave for setting up a local Highlands and Islands inquiry was that the differential had widened dramatically between 1988 and 1999.

In March last year, the differential of the net cost of fuel—that is the cost of the product once all the tax has been taken off—was 88 per cent. That means that people in the Highlands and Islands were paying, on average, 88 per cent more than people elsewhere. In the Highlands and Islands, I include Inverness and the inner Moray firth, which is a single economic zone. There is no reason why prices should be any higher there. The supply chain was taking 88 per cent more from the Highlands and Islands than from the rest of Scotland. We want to hear some justification for that.

The unleaded fuel price differential has increased by 438 per cent during the past nine years. Last year, there were differentials of 16p per litre within the inner Moray firth, which, as I said, is a single, compact economic zone where there have been major infrastructure improvements, mainly on trunk roads.

There are more remote areas. Lochinver, for example, is an important tourist destination and fishing port in west Sutherland. It is 45 miles from the nearest supermarket and 45 miles from the nearest high school. If children want to undertake after-school activities, parents have to drive 45 miles there, wait for their children and then drive them home again. Lochinver is 50 miles from the nearest coal merchant and 110 miles from the nearest hospital. It is a car-dependent location. Unleaded fuel in Lochinver costs 83.5p per litre. The next nearest filling station is 40 miles away.

Further north, in Durness, unleaded fuel costs 85.5p per litre. The point is that prices are really expensive not only on the islands, but in mainland Scotland—Lochaber, Wester Ross and west Sutherland.

The OFT's national survey in 1988 stated that the highest that the additional cost for delivery, even to the most remote location, should be was just under 2p per litre. However, there are still enormous differentials.

We want a regulator for the industry, possibly funded by the industry itself, because we feel that that would solve problems elsewhere in the country—not just in the Highlands and Islands, where the research has been done, but in rural Aberdeenshire, for example. We want some form of rebate for the remotest lifeline filling stations, whether against delivery costs or direct to retailers, who are surviving on incredibly narrow margins.

We also want a corporate Government task force or working group to tackle the problem with the involvement of the oil industry. That could involve many Government departments and policy areas, including the Treasury, economic development and transport.

We need solutions. The amount of money taken out of the Highlands and Islands by excessive transport costs runs completely counter to so many of the Government's policies, on social inclusion for example, and to its efforts to secure post-objective 1 funding.

The Convener: Thank you very much, Councillor Magee, for that full introduction. I will begin the committee's questioning by asking what dialogue on this subject has taken place between HIHAG, the councils that it represents and the fuel companies. Has there been any progress in your negotiations with the fuel companies?

Councillor Donald Maclean (Highlands and Islands Hydrocarbon Action Group): There is, of course, very close co-operation.

I was going to make a few remarks, with your permission, convener, on behalf of the western isles, if you could spare me one minute. I would first like to thank the committee for allowing us to make the first contribution, as we have a council meeting in Stornoway tonight and will now be able to catch the only plane of the day back there.

The Convener: The special pleading of your member of Parliament was successful.

Councillor Maclean: We have to face harsh reality from the word go. The Treasury has told us that it is in no way, shape or form going to consider different levels of duty. A member of the Western Isles Council met representatives of the Treasury last week, and told us that to have different levels of duty would be against European Union regulations.

It is no exaggeration to say that the cost of transportation to and from the islands, and between the islands, is the biggest single factor leading to depopulation and to an exceptionally high cost of living—possibly higher than anywhere else in the United Kingdom. We understand that the transportation of fuel to the islands—not just petrol, but marine diesel and, more important, heating oil—costs in the region of 2p per litre. Today, however, diesel in Glasgow costs 76p per litre; in Stornoway it costs 86p per litre; and in Lochmaddy on North Uist, it costs 91p per litre. That is a vast differential by any standards.

A petrol station closed at Horgabost, at the south end of Harris, with the result that anyone from the south of Harris has to travel 23 miles in each direction merely to fill their tanks. The local bus driver, who transports the children to school, has to use a gallon of petrol merely to get to the filling station and fill his tank. That is the distance and isolation involved.

Members have been given the latest price differentials. Our heartfelt plea to this committee—although it is not for us to tell you what to do, and we are not in the slightest bit interested in attributing blame to the Government, to the Opposition or to petrol companies—is that it does something to help us. It might be possible to have uniform prices throughout the United Kingdom. So little fuel is sold in the remote areas that an increase would hardly be noticeable in the bigger, populated areas, and it would certainly help us.

I recently went to Sweden on behalf of Western Isles Council. In that country, similar schemes are run—we would be happy to supply details to the committee. The Scottish Executive has confirmed that a number of schemes are operating throughout Europe—including in Italy, France, Greece and Portugal—to deal with the impact of high fuel prices.

I will make one final plea. I know that the Government is always telling people to use public transport, such as rail. I need hardly say that it is impossible to take a train across the Minch. A car is not a luxury in the western isles or in the

Highlands; it is an absolute necessity. All that we want is a level playing field; we call on this committee to do something positive.

We are grateful for this opportunity to talk to you and we will be happy to answer any questions.

13:45

The Convener: What response have you had following your dialogue with the petrol companies?

Councillor Magee: Courtesy of David Stewart, MP, and Calum MacDonald, MP, we met representatives of the petrol companies about 18 months ago. I was startled to discover that, when I asked in what position they expected to be in the Highlands and Islands in five years' time, all but one appeared to have no strategy.

British Petroleum has almost a monopoly of supply to the area. It has 51 per cent of the filling stations in the Highlands and Islands and is particularly prominent in the north and west and on the islands. There is no serious competition, even around Inverness and the inner Moray firth. The Highlands and Islands did not experience the supermarket price wars that took place in the rest of the country, although we have supermarket outlets. The area seems to be treated as if it were separate from the rest of the country.

I welcome further dialogue with the oil companies to help us to get over the problem. I can think of no other lifeline commodity whose price fluctuates so much and which gives retailers such a small profit margin. Many retailers sell petrol only because of their social conscience. The oil companies must be aware of that.

Shell has a company called Gleaner that supplies a basic kind of filling station in Easter Ross and east Sutherland. Its prices tend to be marginally lower than other filling stations'. Perhaps that means that there should be a more basic system in the Highlands and Islands.

We cannot go on as we are. In the past 10 years, about 171 filling stations have closed. I am aware that infrastructure grants are available, but good filling station infrastructure counts for nothing if it is impossible to make a profit selling petrol.

The Convener: We are pressed for time this afternoon, so I ask for brief questions and brief answers.

George Lyon (Argyll and Bute) (LD): Did your investigation come up with any evidence that the major oil companies intended to withdraw from the Highlands and Islands? I know of evidence from my area that the major oil companies are not renewing contracts with rural petrol stations but are trying to make them deal with one of their subsidiary companies, such as Gleaner, which you mentioned.

Councillor Magee: In the case of BP, almost the reverse has taken place—it took over its subsidiary. Our concern is that BP has such a huge market share that, if it withdrew, the area would be left high and dry. As I said, BP has the monopoly of supply in the western isles—although the petrol might be rebranded—and owns the majority of petrol stations on the mainland.

Fergus Ewing (Inverness East, Nairn and Lochaber) (SNP): I congratulate the members of the Highlands and Islands hydrocarbon action group. I am impressed by the work of EKOS, which, in a short time, produced a report that will help us to consider solutions in this debate. Page 27 of the report states that the average expenditure on motoring in the Highlands is £12 more than elsewhere in Scotland. That is an extremely damning statistic.

I would like to ask about your recommendations. Reference has been made to the lowering of fuel duties being illegal—that followed the comments of Mr Brian Wilson. You recommend that consideration be given to offering low-income households access to fuel at a discounted rate through the use of a form of SMART card. Many constituents have approached me—and, I am sure, other members who represent the Highlands and Islands—to point out the difficulties of travel, often when two members of the family are working. I would be interested to know in more detail how your recommendation would operate to help people in the Highlands and Islands who are on low incomes.

Councillor Magee: I am glad that you like our research: I think that it is an absolutely first-class piece of work, which was undertaken in a very short time. We are open to any suggestions for solutions. We have mentioned incomes and the possibility of postcode zones. There are all kinds of precedents: for example, cold-weather payments are made in the Highlands and Islands and there is a London weighting allowance for public sector jobs.

Incomes in the Highlands and Islands are around 76 per cent of the Scottish average. The research proves that low-income families in the Highlands and Islands own cars—in a more urban setting they would not need to—and that they make considerable sacrifices to do so. Any kind of subsidy to assist low-income families would be helpful. That would also help the wider economy of the Highlands and Islands, as more money would be circulating through the economy if families did not have to fork out for petrol. It costs about £3.50 more to fill up a car in the inner Moray firth than it does in Edinburgh and about £7.50 more in John o' Groats than here.

The problem could also be addressed by having some sort of rebate on delivery costs to remote retailers, to help them with their margins. A combination of measures could be considered. It seems absurd that we are applying for post-objective 1 funding. The £88 million of additional motoring costs in the Highlands and Islands is more than the entire annual budget of Highlands and Islands Enterprise.

Allan Wilson (Cunninghame North) (Lab): Like Fergus Ewing, I pay tribute to the quality of the research that has been done.

The differential between the Highlands and Islands and urban areas has been maintained in the context of real price increases. Fuel prices have been increasing not only in urban areas, but in the Highlands and Islands. Your report states that the reasons for that disparity are primarily attributable to the commercial policies and practices of the major oil companies. As you know, the oil companies will be here to give evidence to the committee shortly. You also mention the monopoly supply question. Given that price competition in the Highlands and Islands is determined largely by the wholesalers, how could independent retailers be liberated to set their own prices, in the context of the rebate scheme that you propose?

Councillor Magee: That is a question for the oil companies. If they are committed to remaining in the Highlands and Islands market, it is not beyond their intelligence—I am sure that they are all very intelligent people—to come up with suggestions. That would win them massive public acclaim from people in the Highlands and Islands.

One of the problems is that the discounting that goes on in more urban settings does not seem to apply to us. We seem to be subsidising price wars in the rest of Scotland—whether that is correct, I do not know. We find it extremely difficult to reconcile the 17p fluctuations with the Office of Fair Trading's statement that the maximum delivery price to the most remote location should be 2p a litre. Donald Maclean would probably like to comment on that.

Councillor Maclean: I will be brief because I am conscious of the fact that time is running out.

The example that members have been given is that there is, today, a 9.9p difference between the price of petrol in Stornoway and the price of petrol in the central belt. That difference equates to almost £6 when filling the tank of an average car. We are concerned not only about the cost of petrol in the islands, but about the cost of getting to the islands. It does not matter what one is buying—old age pensioners, for example, must pay all the differences in prices between the islands and the mainland. Given that the cost of transport of petrol to the islands is 2p per litre, it is totally unjustifiable that the oil companies impose a price differential of 9.9p—there must be an explanation for that. I am not asking you for one, convener, but somebody could give the explanation easily. That would be to our advantage.

Miss Annabel Goldie (West of Scotland) (Con): Councillor Maclean, you mentioned the Moray firth area in relation to price fluctuations. In a recent survey over a 20-mile stretch of the A9, fluctuations of between 8p and 16p were found. Have you had an opportunity to examine the reasons for the fluctuations in that small area? There has been speculation about the reasons and—to take Councillor Maclean's point—there is an extraordinary dimension to the fluctuations in the islands.

Councillor Magee: That survey was carried out in March 1999. Fuel was being sold in Inverness at 4p a litre above the average cost in the central belt. We can find no justification for that—fuel is landed at Inverness harbour. Asda has opened an outlet in Elgin, which is 40 miles to the east of Inverness on a trunk road—fuel was being sold there at 4p a litre less than in Inverness. In that case, there was a negative delivery cost—there was a price war going on in Elgin that did not extend to Inverness.

Evanton is 18 miles north of Inverness on a trunk road—petrol there was 4p a litre dearer than in Inverness. The further north one went, the dearer the petrol—in Dornoch, it was some 12p a litre dearer than in Inverness. Imagine Inverness as the middle of the area. Forty miles to the east—on a trunk road—petrol is 4p cheaper. Forty miles to the north—on a trunk road—petrol costs 12p more. That is the difference in the price of a litre of petrol and a litre is only the amount contained in a bottle of mineral water. It cannot rightly be claimed—as petrol companies and the OFT have done—that that differential is a result of remoteness, low turnover or distance. There must be another reason. It was clear to us that the price in Elgin was because of the competition involving Asda. It has never been clear to us, given that Safeway, the Co-op and Tesco—

Miss Goldie: Do you believe that a cartel is operating?

Councillor Magee: I am not going to make assertions that I cannot substantiate, but that might be inferred. At the very least it can be inferred that the Highlands and Islands is a soft market—the OFT has conceded that much. We are trying to find solutions without casting blame in all directions. It is for the oil companies to say why those differences exist. We can only say what Highlands and Islands residents and visitors to the area experience and what the impact is of the prices on families and businesses in the area.

Visitors view the Highlands and Islands as an extremely high-cost destination within which to travel. The situation in the inner Moray firth area last March was extraordinary.

George Lyon: I am aware that the witnesses do not want to cast blame. However, I have spoken to some local petrol station owners in my constituency of Argyll and Bute. They have said categorically that the price of delivery, the margin that they receive and the retail price are set as part of their contracts with suppliers. I have seen the contractual slips that have been signed and which substantiate that claim. The blame for the huge differences in price that we see lies firmly with the suppliers to those rural petrol stations.

I would like to turn to some of the possible solutions that you mentioned. Many of us who run businesses know about petrol cards, which allegedly give those who hold them access to fuel at the average UK price. Could that mechanism be extended to a wider range of people than just those from businesses? Could it be used in the Highlands and Islands as a way of operating a pricing policy that would result in those of us who live in the area enjoying the same prices as those who live in urban and central Scotland?

14:00

Councillor Magee: That would be a solution only if there were an absolute guarantee that retailers got a decent margin. One of the problems with agency cards is that retailers—at least in my part of the world—make a loss on them. That seems to me almost to amount to a discriminatory practice. Several filling stations in my area have pulled out of accepting agency cards because they cannot make any margin on them. The Highland Council does not give staff agency cards, because of the effect that they have on Highlands and Islands retailers. Our staff pay through the nose for petrol, in order to support local filling stations.

A great many retailers have said to me that they cannot understand how a consumer can buy petrol cheaper across the forecourt than they are able to buy wholesale from their supplier. It is a total mystery to them. They have to support, or subsidise, their petrol business by running other businesses alongside it. Agency cards could be an answer, but not as they are set up at present. One would have to guarantee that the retailer could make a liveable margin on petrol.

Fergus Ewing: I know that the EKOS report considered the effects on business and on hauliers in particular, and that fuel costs, particularly diesel, add, I believe, around 4 per cent to hauliers' costs. What do you predict will happen to business in the Highlands, and to the haulage industry that operates in the more remote parts of the Highlands in particular, if no action is taken to deal with the problems that you have identified?

Councillor Maclean: I shudder to think what the future for business will be. Recently, we made inquiries about costs to and from the islands—I speak specifically about the western isles. An example has been quoted many times: an articulated lorry on a five-hour return journey costs £900 from Stornoway to Ullapool, whereas in Greece, the poorest country in the European Union, a 20-hour return journey from Crete costs £400. There must be some explanation for that.

Mr Ewing rightly suggested, if not stated, that businesses will suffer. We do not mind anyone making a profit; businesses have to make a profit. However, we are deeply and genuinely concerned about the serious plight of people who cannot afford fuel—old age pensioners, who have no other income, and people with minimal income—and about their suffering.

There are remedies and I have already suggested that of a uniform price across the UK. I do not know if that would be possible, but I hope that the Treasury might at least listen to your committee, convener. It most certainly will not listen to us, but it might take more cognisance of this committee's proposals. Generally, in the Highlands and Islands, all we are looking for is a level playing field—no more, no less—the same as everyone else.

Councillor Magee: I wish to add that we find that hauliers are making deliveries once a month, not once a week or once a fortnight, as they used to do, and the people who buy goods have to pay for them up front. There is anecdotal evidence to suggest that the hauliers are dropping off freight by the roadside to be collected by the person that they are supplying.

Whichever way one looks at the situation, it is becoming steadily unsustainable. The problem also has a tourism side to it. The report quotes a case study from Lochinver. Whether one looks at it from the freight side, from the tourism side or from the side of the ordinary family, fuel prices leech an enormous amount of money out of the Highlands and Islands, which could be at the cutting edge of the economic prosperity of Scotland. I am in no doubt about that.

The Convener: Thank you. John Munro will ask the final question in this session.

Mr John Munro (Ross, Skye and Inverness West) (LD): I am pleased to welcome the delegation from Highland Council, which includes some of my old colleagues. I am well aware of the campaign that the council has orchestrated over many months. In my days on the Highland Council, I was involved in a similar campaign and, prior to the Scottish Parliament elections, I circulated within the area a petition that asked for a fair deal on fuel and collected 20,000 signatures. The petition was presented to the House of Commons and, subsequently, to the Treasury; however, it seems to have fallen on deaf ears.

Perhaps we are not directing our venom in the right direction. We hear so much about the petrol companies, and blame seems to be directed to them. That is not my impression. After speaking to people who are involved in the trade, I quickly realised that the margins that are available to the petrol companies, the distributors and the vendors are very limited, as 85 per cent of the price that we pay at the pump goes in tax and VAT. Today the average price of a litre of fuel is 80p. In cash terms, 85 per cent of that—the proportion that goes in tax—amounts to something like 68p. The remaining 15 per cent, which amounts to 12p, is left to the fuel supplier—

The Convener: Could you move into a question, John?

Mr Munro: I do not have a question. I want simply to support the delegation and to suggest that it direct its attentions to the Treasury and try to persuade the Treasury to reduce the tax on fuel, which would make a significant difference very quickly.

Councillor Maclean: I would like to make one point in response to Mr Munro's non-question: if we take away the duty altogether, the differential is even greater.

Councillor Magee: The fuel price differential is £17.8 million a year. The fuel tax escalator, of which we are still feeling the effects, has impacted more strongly on the Highlands and Islands because we have lower incomes and seasonal employment. I know that the level is the same, but it is correct to say that the impact has been greater.

I want to make a final point about the Office of Fair Trading inquiry. Our concern is that the office does not use average prices based on Pricewatch surveys. I know that representatives of the office visited the Highlands and Islands again in November, but they need to examine the actual prices that are paid, because using averages smoothes out the real effects. The average rural Scottish price does not reflect the extremes that Donald Maclean has described in the western isles and I have described in north and west Sutherland. It is extremely important that the Office of Fair Trading addresses the reality when it conducts its inquiry.

The Convener: I want to draw this part of our evidence-taking session to a close. Thank you for your attendance today and for the forthright way in which you have set out your case. We will raise many of the issues that you have highlighted with our other witnesses. You will, of course, receive a full copy of the *Official Report* of this meeting.

There is no need for members and witnesses to switch their microphones on and off. That is done for us by our very professional and competent sound engineers, who can anticipate which person I intend to call next.

Our next group of witnesses is from the Arran Council for Voluntary Service. This inquiry arose out of a public meeting in Arran hosted by the council. My colleagues Annabel Goldie and Allan Wilson made representations for us to conduct the inquiry and were supported by Fergus Ewing, George Lyon and Elaine Thomson.

I welcome Jim Lees, the chairman of the Arran Council for Voluntary Service, and invite him to introduce himself and his colleagues.

Jim Lees (Arran Council for Voluntary Service): On my left is Mike Lunan, who is convener of the local branch of the Federation of Small Businesses and ex-executive member of the Arran Council for Voluntary Service. On my extreme left is Sheila Johnstone, who is the chair of Arran community council.

The Convener: After you have made some brief opening remarks, Mr Lees, we will proceed to the questioning.

Jim Lees: What my colleagues and I wish to submit in evidence is contained mainly in the document that I handed to the assistant clerk of the committee before the meeting. I want to emphasise two points that are made there.

First, by engaging in a price war the oil companies are subsidising the highly populated areas of the country at the expense of peripheral Scotland. The more peripheral an area is, the greater the expense is, so the islands top the expense league. My colleagues and I back the Highlands and Islands hydrocarbon action group in saying that a regulator would be of great assistance in putting some sense into the price differentials in the Highlands and Islands.

Secondly, I agree with Mr Munro that an inquiry into price differentials cannot ignore the taxes that are levied on these products. By its nature, value added tax increases the differential. As our paper argues, the huge increases in road fuel duty that have been caused by the fuel tax escalator have affected lower turnover filling stations to a much greater degree than high output operators; fillings stations in the Highlands and Islands tend to have low turnovers.

Although we understand that there cannot be a change in duty, we know that the Greek Government levies a level of VAT in the islands that differs from what applies on the mainland. As

Greece is in the European Union, that tax differential must be within EU law, so perhaps a VAT differential would be a way of levelling the playing field.

I will hand over to Mike Lunan, who conducted the survey that first raised this issue. After Mike, Sheila Johnstone will speak. Sheila has been majoring in the subject of fuel cards, which Mr Lyon mentioned, and you may find what she says interesting.

The Convener: I ask the witnesses to speak briefly at this stage.

Mike Lunan (Arran Council for Voluntary Service): I will be very brief. When this issue was first mooted in Arran about 15 months ago, the popular belief was that it was the fault of the wicked retailers, who were out to rip us all off. It quickly became apparent that not only was that not true, but that the retailers hardly made a decent living at all, given the expenses that they incurred.

I want to make it clear, as my report does, that the one group that seems wholly blameless are the poor guys who stand in the rain putting petrol in our tank and taking our money. The margin that is made by a rural retailer might be many pence per litre, but in view of the expenses of running the business, that represents remarkably few pounds in the year. Therefore, it seemed correct to focus on the two places where some degree of pressure might bring about change: first, oil companies; and, secondly, Her Majesty's Government, of which I will say no more at this stage.

Sheila Johnstone (Arran Council for Voluntary Service): As Jim Lees said, I have been examining the issue of fuel cards. There is definitely a train of thought among consumers that, if oil companies can offer fuel at the average British price to businesses using fuel cards, that option could be offered to all consumers.

That would be a disaster for retailers. I was horrified to discover that the retailers on Arran, with some of whom I spent a considerable time, make between about 0.8p and 1.2p profit per litre on sales involving a fuel card system. When a fuel card system is not used, the retailers only make 10 per cent gross profit, even though Arran has some of the dearest fuel in the country. Questions have to be asked about where the rest of the money goes. We know that it does not go into the pockets of the retailers.

Social inclusion and exclusion are the current buzzwords. Every retailer in Arran—I am sure that the situation is the same in the rest of rural Britain—has another income to support the fuel station. Retailers believe that they provide a community service. If people lose that service and have to travel miles to get fuel, they will decide to get their shopping and everything else at the same time. It is affecting rural communities. We have already seen that in the west coast of Arran with one station closing.

14:15

The Convener: Thank you for your contributions. I shall now invite questions from members.

Miss Goldie: Going back to the meeting on Arran, I seem to recall that the mystery was the component parts of the price. You have indicated strongly that you think that the retailers are not to blame for that on Arran. Are you in a position to give us your opinion of what the components of the price are?

Mike Lunan: According to figures that were taken towards the end of last year—in November, I think, although I do not have the exact date—a litre of unleaded on Arran cost a total of 83.5p, which I think is higher than just about anywhere else. Of that, rounding to the nearest tenth of a penny, 23.9p was the cost from getting it out of the ground to getting it into the pump. In other words, that was the cost of the oil majors drilling, refining, bringing it in a boat to Arran, selling it to me and getting a living out of it. Another 47.2p per litre was excise duty on the fuel and, on Arran, 12.4p per litre was value added tax.

Those figures compare with figures taken on the same day for an Edinburgh pump, where the total cost of a litre of unleaded was 69.9p. Of that sum, 12.3p was the cost of getting it out of the ground and into the tank. Again, 47.2p was the duty, which is constant. Value added tax, being ad valorem, was rather less in Edinburgh at 10.4p. There is a small differential in VAT of something like 2p per litre, but the major difference of 11.5p is, if you like, the cost of making the product.

Miss Goldie: Have you been able to do any sub-analysis of the element that cost 23.9p on Arran?

Mike Lunan: The short answer is no. We know what some of the costs are. It is reasonable to assume that the cost of getting it out of the ground, into the refinery and out again will not be very different from the Edinburgh price of 12.3p. We know that the cost of physically getting it out of a boat and into the tank on Arran is, at a maximum, 0.4p per litre—in other words, a negligible cost. The difference between the two prices is therefore the cost of getting the petrol to Arran.

The Convener: Does the cost you quoted for getting the fuel out of the ground also include the retailer's margin?

Mike Lunan: It does for both Edinburgh and Arran.

The Convener: So the margin is included.

Allan Wilson: The question of carriage to Scottish islands is obviously important in the context of Arran and other islands that are serviced. How is the fuel delivered? I notice that we have evidence from one of the oil companies concerned that says that supply costs are higher because the cost of shipping the product into sea-fed depots is greater than into the pipeline-fed depots of much of the United Kingdom. Do you have any information on the exact percentage of the retail cost of a litre that is directly attributable to carriage in island locations?

Jim Lees: I am afraid that we do not. We have written to the oil companies to try to ascertain those facts and figures, but it remains a mystery that the ACVS has failed to penetrate. What we can say is that fuel is delivered to Arran and to all other Scottish islands by means of a small coastal tanker. It leaves Grangemouth, goes up north to various ports of call and then goes down the west coast of Scotland and ends up in Arran.

Anecdotal evidence—and it is only anecdotal evidence, unfortunately, because we do not have hard facts to back it up—suggests that that is an exceedingly cost-effective method of delivering fuel to Arran. To bring a tanker on to the boat would cost considerably more. The docking costs at Brodick, as Mike Lunan has explained, are 0.4p per litre. As for the cost of getting to the pier, that is a mystery that I hope the committee will shed light on this afternoon.

Mike Lunan: To amplify that slightly, a report by the HIHAG said that, according to Asda, which sells petrol among other things,

"even shipping and delivering to remote islands costs only 1-1.5p more a litre."

Asda is better able to assimilate that kind of information than we are, therefore I can only assume that it is correct.

Dr Elaine Murray (Dumfries) (Lab): I am interested in exploring solutions. You mentioned the problems that small retailers face. One is that they seem to be being charged more per litre. The other is that when somebody has a low turnover, they have to make a bit more per litre to survive, because they do not have the turnovers that large suppliers have. A regulator would help the former problem, but what is the solution to the latter problem? What sort of assistance would help? Do derogations, such as rate rebates, help? Are they sufficient, or does more need to be done?

Jim Lees: As you point out, the regulator would help in the first instance. In the second instance, I believe that the Government needs to do something to reduce the cost. It is done in other areas of the European Union, so I do not see why it cannot be done in the Scottish islands. That is all that I have to say.

Mike Lunan: To put a bit of flesh on that, when people are asked to give evidence to committees, quite reasonably committees want to know what we want and what our preferred answers are. There are two areas that may be addressed. The first is the oil companies, from whom you will hear evidence later and of whom you will ask questions. However, it is impossible in this debate to blind oneself to the fact that 85 per cent of the cost trickles away to another place.

There are two elements of taxation. One is duty. Research paper 99-52 from the Scottish Parliament information centre states:

"Under EU legislation regional derogations from national rates of duty are already permitted in the Azores and on certain Greek islands (article 9 of Council Directive 92/82)."

I have not had the pleasure of reading that directive, but someone who wrote this report for the Scottish Parliament presumably has. The report continues:

"The UK government could apply for a similar derogation 'for specific policy considerations'"—

the magic form of words—

"which would require unanimous Council agreement".

In other words, it would require horse trading. Derogations on fuel duty already exist, and could be introduced here if there was the political will to do it, although I accept that that could not be done in this city.

As far as VAT is concerned—which is a smaller, but nevertheless more irritating burden, because it bites more heavily, being ad valorem—the Greek Government reduces its VAT rate on fuel from 18 per cent on the mainland to 13 per cent for small islands or islands with smaller populations. It will not surprise you to learn that I have done a sum. If, magically, we were able to persuade everyone that the duty should be reduced to the minimum allowed, which is 5 per cent, it would bring the price of petrol on Arran down from 83.5p to 74.6p per litre. So even if the VAT magic wand was flashed to the maximum extent, it would solve only about half of the problem.

There are two areas that need to be addressed, and one of them is taxation. A regulator could come along and say, "Why don't we have uniform pricing?" A state body, the Post Office, will deliver a letter from here to the bottom of the Mound, and a letter from here to John o' Groats, or indeed to Land's End, for the same price. What about private bodies? Mars bars cost pretty much the same in Arran as in Aldershot. Why does a litre of fuel not cost the same in those places?

Allan Wilson: An obvious question arises from that.

The Convener: I was about to ask if there is a specific arrangement for Mars bar pricing.

Allan Wilson: What guarantee would there be that, following the introduction of differential tax and duty rates and given that the rates in Ardrossan currently are exactly the same as those in Brodick, reductions would be passed on to consumers? Could retailers not simply increase their profit margin, which they know will be squeezed in Arran, where there are seven fuel outlets among a population of 4,643? Would the temptation not be to increase the retail profit margin at the expense of the taxpayers' subsidy?

Jim Lees: That is where a regulator comes in. It is essential that a regulator ensures that that money is not creamed off and the reduction is passed on to the public.

Sheila Johnstone: If the retailers on Arran got the opportunity to sell petrol at a price comparable to that on the mainland, they would jump at the chance. They keep their prices as low as they can, and they are still not making a living.

Rhoda Grant (Highlands and Islands) (Lab): Going back to the report that you let the committee have before the meeting, in one part you state that a mainland retailer was selling petrol at 9 per cent less than the wholesale price of petrol available to an Arran retailer. Was that a one-off, or is that the norm?

Jim Lees: That was something that came up in Mike's report, so I will ask him to answer.

Mike Lunan: The document that you are holding in your hand is not our report, because I do not think that ours had a paper-clip in that corner, so I cannot answer in relation to that document.

My document mentions that one of the retailers grumbled that he could buy petrol at a lower price from a retailer on the A80, or M80, somewhere between Glasgow and Stirling, than he could get it from the wholesalers. I have no idea whether that was a one-off and he was lucky to find that retailer. My guess is that it was not a result of detailed research; he simply noticed it as he was driving along.

The document that Rhoda Grant is holding is not my document.

Rhoda Grant: I think that it is.

Jim Lees: Mike produced a document, on 5 January 1999, which contained that figure. Unfortunately, you were holding up a different document. That was the figure of 9 per cent. It was just something that appeared from a random survey, which Mike undertook on behalf of ACVS. That figure came out and we used it to show that this was happening.

One of the retailers who gave evidence to ACVS told us that he regularly filled his car up when on the mainland, because he could get petrol cheaper there, in Ardrossan. He did not seek the retailer out and he got it cheaper than he could buy it wholesale on the island.

George Lyon: Coming back to the solutions, there is a lot of support for your proposals on tax. On the other part of the problem that you have highlighted, you have done a lot of work with your suppliers and retailers in Arran. How many of them are free to set the retail price? How many of them are free to negotiate their margin when they negotiate with the oil company that supplies them? Which companies supply them? Is it the mainline companies or subsidiary companies such as we have heard are operating in other areas?

Sheila Johnstone: There are seven stations on the island. As far as we are aware, two of them are supplied by Gleaner Oils Ltd. They are all supplied by BP, but Gleaner is the agent for two of them. One is independent and can set its prices as it wishes. It has the lowest mark-up on fuel cards, which is why it does not deal with the fuel card system. They are all relatively free to set their prices within a certain bracket, but they can do so only as long as it is realistic. It is not realistic to put the price up even higher; as it is, people are taking their cars to the mainland and filling up. That is socially a disaster for the island—really bad news.

If people take their cars away to fill up, they will fill up with other stuff as well. There is a petrol station right at Brodick pier. Staff there see people going away in their cars every day. The car ferry fares are not cheap—it is a big thing to take your car to the mainland—but folk will do it; if they are going away, they may as well take their car and fill it up with stuff before they return.

Within limits, the retailers can set their own prices but they know that they could price themselves out of the market, so they try to keep prices as low as they can. Even then, they are not making a crumb out of it.

14:30

Elaine Thomson (Aberdeen North) (Lab): George Lyon covered much of what I wanted to ask.

If the wholesale price on Arran is higher than the retail price elsewhere, do you have any idea whether that problem is linked to one particular wholesaler or company? Within the price that is being paid, do you know how much goes towards paying the supposed extra transport costs caused by remoteness, or by Arran being an island?

Sheila Johnstone: No.

Jim Lees: We do not have that information, but we would dearly like to get it. We hope that the committee will get that information this afternoon.

Fergus Ewing: Your points on VAT and the lower rate of VAT in the Greek islands are worth pursuing, although several months ago I wrote to the Treasury on that matter and it said that nothing could be done. Perhaps we can revisit that, especially as the rate of duty in Greece is half that in Scotland and, so far as I know, Greece produces only olive oil.

Could you predict what the effect will be on particular businesses and petrol retailers in Arran if no effective action is taken by Government, whether in Holyrood or elsewhere?

Sheila Johnstone: In general, if no action is taken, I can see several petrol stations closing.

In addition, the big oil companies put no development money whatever into petrol stations. If the station needs a new pump, the retailer has to find the £3,500, or whatever it costs, to buy it. One of the independent stations put in three reconditioned pumps at a cost of £6,000; those pumps are not new and if something goes wrong with them, the retailer is up the creek again. It is not worth the hassle and I can see the stations closing if things do not improve. The public will vote with their feet—or their wheels—and we will end up with two stations on the east side of the island and none at all on the west. That would be very detrimental to the rest of the island economy.

Jim Lees: I concur with what Sheila said. Ultimately, there will be two petrol stations if we are lucky and possibly only one. Arran is a relatively small island, but it is still possible to travel quite a distance between petrol stations. For example, I know of a family who live in Lochranza, but are relocating to Brodick simply because of the cost of fuel. You cannot get fuel in Lochranza. The end result is centralisation; even in a peripheral area such as Arran, you are getting a periphery within a periphery. Such things will happen if nothing is done.

The Convener: I draw this session of evidence to a close. I thank the witnesses for their submissions and for travelling to Edinburgh to give us their views. The committee will reflect on those views during its discussion today.

Jim Lees: Thank you, convener.

The Convener: We move on to the next part of our evidence, which comes from the Office of Fair Trading. On behalf of the committee, I welcome Nancy Race and Alan Williams of the OFT's competition policy division.

Before we proceed, I should say that I am grateful to the OFT witnesses for agreeing to attend. Our committee would have had no power to compel the OFT to attend; the witnesses are here of their own free will.

There are some limitations on what the OFT can say to our inquiry. I will comment briefly on those limitations and if I do not get it fully correct, I would like to be corrected by the OFT representatives here, so that we are all clear about the ground rules within which we have to operate.

Section 1(3)(iii) of the Fair Trading Act 1973 prevents disclosure of information about businesses during an inquiry—any such disclosure could be subject to criminal prosecution. The OFT could be guilty of maladministration and subject to investigation by the ombudsman if information which was prejudicial to the activities of any business was disclosed during one of its inquiries. That is relevant because the Office of Fair Trading is undertaking an inquiry similar to that of the committee.

Perhaps the representatives of the OFT would clarify whether I am correct and say any more that needs to be said. I ask them to introduce themselves and to say a few words about the OFT's work. I advise committee members that, during the conduct of the inquiry, I will judiciously protect the OFT's statutory responsibilities.

Alan Williams (Office of Fair Trading): I am the director of the branch of the OFT that is responsible for basic industries, energy and vehicles. My colleague, Nancy Race, deals specifically with the oil and petrol industries.

What you said about the limitations on what we can say is true—because we are in the middle of an investigation and have not reached any conclusions. With the best will in the world therefore, we cannot say what our findings might be.

It is clear, from what the committee has heard from previous witnesses, that there are many reasons why people in the Highlands and Islands are concerned about the level of petrol prices. The director general of fair trading—and therefore we as his officials—are bound by strict statutory limitations on the issues that we can consider. The differential between petrol prices in the Highlands and Islands and elsewhere falls within our responsibility if it involves failure of competition, or anti-competitive practices. However, we can do nothing about other causes of high prices.

The Convener: Thank you for that introduction, Alan.

Will you outline the nature of the inquiry that you are undertaking? For example, when did it commence and what was the reasoning behind its instigation? What stage have you reached in that inquiry and when do you expect to report?

Alan Williams: The inquiry began in about March of last year. We launched another inquiry because of the increase in differential, which we had observed prior to that date, between Highlands and Islands prices and prices elsewhere in the UK. The increase was sufficiently great for it to be thought that it deserved a revised inquiry.

You might recall that we have considered this subject quite a lot in the past. In 1990, a Monopolies and Mergers Commission report on petrol prices in general had a section on the Highlands and Islands. In 1997, the OFT considered the issue. In 1998, it was covered in our report on petrol prices. We have considered the subject several times. We returned to it this year because of an increase in the differential between the Highlands and Islands and elsewhere.

We have done several things since then. We have sent an extensive questionnaire to the major oil suppliers, we have visited several retailers in the Highlands and Islands and have sent a questionnaire to other retailers. We have instituted a series of price surveys—there have been four so far—and are beginning to analyse that information. However, before we reach any conclusions we have a lot more analysis to do—we need to talk to the major oil companies and others. I hope that in two or three months' time we will be in a position to reach a final conclusion one way or another.

The Convener: Was the realisation that there was an increase in differential between the Highlands and Islands and other places in the United Kingdom pointed out to the OFT or was it the result of monitoring work carried out by the OFT to detect whether there was any recurrence of the issues that had been examined in the 1997 report?

Alan Williams: I understand that it was chiefly because several parties who were anxious about the matter wrote to us.

The Convener: What were the conclusions of the report that was produced in 1997? What action was taken?

Alan Williams: The conclusions were broadly similar to those of the 1990 MMC report, which found that the reasons for the price differential between the Highlands and Islands and the rest of the UK were the sparsity of population in the region and geographical factors leading to higher costs and less intense competition. No action was taken because the problem did not arise from anti-competitive practices.

I should emphasise that that was the conclusion that was reached at that time. We begin with fresh minds, so the conclusions we reach in the current inquiry will not necessarily be the same.

The Convener: I do not understand your comment about the problem not arising from anti-competitive practice, when the report concluded that one of problems was less intense competition. That does not seem to follow.

Alan Williams: If a low volume of petrol is being sold, there is not much room in the market for competition. In an urban area, a higher volume of petrol would be sold and therefore there would be room for more retailers and wholesalers to enter the market and make a profit. If there are low volumes there is inevitably less competition—that is not a result of anti-competitive practice on the part of the retailers or wholesalers, but because of the nature of the market.

The Convener: Is that not a very narrow definition of competition? If one lives 100 miles away from Inverness and there is only one petrol station in a 100-mile radius, the absence of competition can lead to a certain sort of anti-competitive behaviour.

Alan Williams: If we conclude that, as a result of there being one outlet in the area, a market is being abused by a dominant wholesaler or retailer, the OFT can take action. However, we must establish that there has been some abuse.

George Lyon: I am interested in the previous study that you mentioned. You said that you visited several sites in the Highlands and Islands—

Alan Williams: That is the current study.

George Lyon: Thank you. Have you established how the price is arrived at? Who is free to set the price? Are retailers free to set the retail price or are the margins already set when they negotiate with the major oil companies? How free is the market in terms of small rural retailers' ability to set their price and make their own margins?

Alan Williams: Strictly speaking, retailers are free to set their own prices. If we found any evidence that retailers are being constrained by their suppliers—being told what the retail price should be—that would be a cause for concern and for us to take action. However, retailers' ability to set their own prices is constrained not because of instruction from wholesalers, but because of the difference in the price of the petrol they buy and the price they can sell it for. They should not be told what level of prices to set.

George Lyon: Are you saying that they could have access to petrol or white diesel at the same price as retailers on the mainland?

Alan Williams: No. Arriving at the wholesale price that any retailer will pay is quite a complex procedure. It depends on a lot of factors—including the intensity of competition in the area. Where competition is intense, suppliers may give the retailer a special rebate to allow him to compete. Where competition is less intense, that allowance may be lower or non-existent. The wholesale price will not be the same for every retailer throughout the country or, indeed, throughout the Highlands and Islands.

14:45

George Lyon: Basically, you are saying that the major oil companies decide, depending on the level of competition, what the wholesale price will be. As a result, the price is much higher in rural Scotland.

I wonder whether you will recognise this example. I live on the island of Bute and I buy white diesel for the farms cheaper than a retailer would claim he can buy it from the major companies. Is that not an example of a problem with competition?

Alan Williams: Not necessarily—but I am unable to comment without knowing the suppliers' cost structures.

Fergus Ewing: You mentioned that the OFT has considered this issue before and that the MMC looked at it in 1990. I am indebted to *The Press and Journal* for an editorial of 3 February 1976, which raised the issue of poor motorists who were worried about a two-year delay before an MMC report came out. If an assumption is made that the finding will be against the oil companies—that must remain hypothetical because of the rules—what procedures will be followed?

Will you describe the procedure John Bridgeman—the director general of fair trading—described to me in his letter of 16 November 1999? Can you confirm that unless the oil companies give an undertaking in lieu—which seems extremely unlikely, as they are not going to put up their hands and say that they are guilty—it will take a minimum of a further two years, assuming they use the appellate procedure, for anything to happen and before the procedure is exhausted?

Alan Williams: Saying two years is a bit pessimistic. When we have completed our investigations, one possible outcome—I emphasise that it is only one of the possible outcomes—is that the director general will refer Highlands and Islands petrol prices to the Competition Commission. Under the monopoly provisions of the Fair Trading Act 1973, the normal time limit set for the Competition Commission for such an inquiry is nine months, although it has the power to request an extension. However, given that this is an investigation in a limited area of the UK, I would have thought that nine months would be reasonable; so it would take nine months after our decision for it to report. After that, it would take some further months—although perhaps only a couple—to decide on what further action to take. Although overall it would take more than a year, two years would be an outside estimate.

The Convener: What action could follow at that stage?

Alan Williams: The Competition Commission has a fairly wide remit. I emphasised at the beginning that we could consider only competition matters, but once a reference has been made to the Competition Commission—provided that it is satisfied that it falls within its remit—it can look more widely at public interest matters. Provided that the remedy could be implemented under the secretary of state's order-making powers under the Fair Trading Act 1973, it could include a variety of measures—for example, a cap on prices in the Highlands. However, that would be for the Competition Commission to recommend.

Fergus Ewing: In his letter, Mr Bridgeman stated:

"The Competition Commission would report within 12 months."

He also stated that:

"If Orders were to be required the DTI would take this forward, again this would be likely to take at least 6 months."

If we consider that the report was requested in January, it will be two years or more before anything happens. Does not that indicate to objective onlookers, particularly people who might already be paying more in the Highlands, that the regulatory procedure is completely ineffective in providing a real remedy for the people who are punished?

Alan Williams: The procedure is not ineffective, but it takes time, because these matters are complex; it would be much easier if we knew the answer straight away. First, we have to carry out a careful analysis of whether a reference is justified; and when there is a reference, the Competition Commission needs to be thorough about determining whether there is an effect on public interest and, if so, what remedies might be taken. Those are not easy matters.

Fergus Ewing: I appreciate that. However, the EKOS report took around three months to produce and it seems to be extremely detailed. Could you be a bit quicker with your reports?

Alan Williams: From my reading, the EKOS report did not even address whether there are competition problems.

Dr Murray: I am not sure whether you will be able to answer this question, but I want to probe your views on whether it would be helpful to have a regulator who determines a national petrol price.

Your previous report suggests that the retail market is just a series of local markets and that, in most areas, competition simply allows people to go elsewhere to buy petrol.

A year ago, a family from Dumfries could drive to Carlisle, do its shopping, fill its tank up with petrol and go back to Dumfries, and the journey would not have cost anything because there was such a difference between petrol prices in Carlisle and Dumfries. That is no longer the case, but it affected not only the petrol market but the whole local economy, as people were also shopping outside the area. Some regulation of petrol prices that guaranteed a constant wholesale price throughout the country might benefit rural communities in several ways. Are you able to comment on that point?

Alan Williams: Only generally. If markets are working, they should be allowed to do so, as any interference tends to cause distortions that push up costs throughout the economy. We would have to be quite clear that there was a market failure. However, even if there were a market failure that might justify intervention, we would need to be clear that a regulator would have beneficial effects rather than simply impose greater costs on everyone.

Allan Wilson: The Office of Fair Trading examined price competition in the Highlands and Islands and determined that prices are largely set by wholesalers and that many so-called independent retailers are not free to set their own prices. The OFT's 1996-97 inquiry also suggested that, after taking distribution costs into account, margins at the wholesale level in north-west Scotland were higher than the UK average. The OFT concluded that the difference in margin appears to be no more than a function of the intensity of competition in urban rather than remote rural areas. Is not the converse the case in islands such as Arran and in other remote rural locations: monopoly supply leads to price increases, and oil companies are discounting urban areas to the disadvantage of island and rural communities?

Alan Williams: I want to correct one statement. I did not say that retailers' prices were set by wholesalers, but that retailers were free to set their prices.

I cannot believe that there is much cross-subsidy between Highlands communities and other areas simply because only a small amount of money could be made in the Highlands compared with what would be needed to bring down prices in urban areas. Therefore, the issue of cross-subsidy is only a minor point.

The fact that there is less intense competition makes it possible for wholesalers and suppliers to have higher prices than they might otherwise have. However, we do not know whether they are earning unusual profits as a result—that is what our inquiry is about. Much lower volumes will affect the profitability of the operation in remote rural areas both at retail and wholesale level. If wholesalers are dealing in very small volumes, they are not necessarily making very large profits.

Allan Wilson: If the difference in margins is no more than a function of the intensity of competition in urban areas compared with that in remote rural areas, is not it conversely the case that the absence of such competition should be reflected in increased margins and profits for the companies?

Alan Williams: That is right—less intense competition should be reflected in higher margins, but without further work it cannot be concluded that the profits are particularly high.

Allan Wilson: Does it not depend on the disparity in the level of the respective margins?

Alan Williams: Yes, but margins on very small volumes do not necessarily bring in very much money.

Miss Goldie: Paragraph 11.11 of the extract of the 1998 OFT report states that higher prices in the north-west of Scotland

"are a function of the extra costs of supply and the fact that there is less intense competition there than in other areas."

We have heard today that estimates of supply costs range from 1.4p to an acknowledged cost of 2p. Is that a significant element of the final retail price?

Alan Williams: It is significant, although not huge.

Miss Goldie: I am curious. Is that figure worthy of comment as an element of the clear disparity that exists between prices in the north-west of Scotland and elsewhere?

Alan Williams: I am sorry. I did not follow your question. I beg your pardon.

Miss Goldie: Extra supply costs of 1.4p to 2p do not seem a particularly significant element of the whole pricing structure that we are examining. We are trying to discover what the components of the differential are. Are you saying that that 2p is a clear part of the explanation for higher costs in the north-west of Scotland?

Alan Williams: It is one part of the reason, but as you say, it is not the whole reason.

Miss Goldie: I was interested in the case study to which the Highlands and Islands hydrocarbon action group alluded and which is referred to in other papers that we have received. We have been told that in the Moray firth there have been price fluctuations of 8p to 16p within 20 miles on the A9. On further examination, Councillor Magee confirmed that if one went east from Inverness, the average price was 4p lower; in Inverness the average price was 4p higher; and further north the price increased dramatically. She said that there was an element of competition within Inverness, but that it did not appear to have led to a reduction in price. Do you have any comment on that scenario?

Alan Williams: I cannot explain precisely why that particular set of figures should emerge, although they suggest that where there is more intense competition, prices are lower. I imagine that there is much less competition in Dornoch than there is Nairn. That level of disparity is rather unusual anywhere, but some rather surprising disparities can be found even in urban areas, as I know myself from filling my tank in different parts of London. It is not easy to explain.

Miss Goldie: Can you comment on the wholesale element in relation to the study so far? It is very difficult to elicit any information on the structure of wholesale prices, which are covert at the moment.

Alan Williams: I am not sure what you want me to say.

15:00

Miss Goldie: I have been unable to find very much information on wholesale prices in your report. I only found broad-structured information on retail prices. It may be just me, in which case I apologise, but I do not quite understand how the wholesale price structure works throughout the north-west of Scotland.

Alan Williams: The wholesale price structure in the north of Scotland is quite a complicated matter, as it is elsewhere, with several factors involved. As I understand it, there is a standard wholesale price, which is adjusted by various factors, including volumes. In the case of some oil companies, zonal price differences, which reflect remoteness and other factors, may be involved. Rebates are also given to retailers who are subject to intense competition.

I also point out that our report on competition in petrol supply is two years old, and the situation may well have changed. Part of our current work—and we need to do more—is to understand the basis of wholesale costs. That is one of the things that we want to discuss with the oil companies.

The Convener: That strikes me as a fundamental issue. If we return to the evidence given to us by Mr Lunan of the Arran Council for Voluntary Service, he made a comparison of refinery and transportation costs and the profit margin of approximately 12.3p per litre for fuel bought in Edinburgh against 23.9p for fuel bought in Arran, where the margin is clearly under sustained pressure. That suggests to me that there is a great deal of explaining to be done about that 11p per litre difference.

Alan Williams: I agree that that certainly requires explaining, but I do not think that one should conclude without further work that there is necessarily anything very sinister about it. That does not mean, however, that it is not horrible for the people of Arran.

Elaine Thomson: I am suffering from other members having asked my questions already.

I want to pursue the question about the wholesale price. You have talked, Mr Williams, about the various factors that go towards how that price is made up. Would you say that the intensity of competition is one of the larger factors, or the major factor, in the wholesale price differentials between urban and island communities?

Alan Williams: It is a big factor. Not having completed our analysis, I would not like to say whether it is more important than cost differences. Cost differences and intensity of competition are both relevant factors, but I am not sure if the intensity of competition is the major one.

Elaine Thomson: How much work is being done now on comparing wholesale prices? Is it an area in which more work needs to be done?

Alan Williams: We do need to do more work on it, and we are doing more work on the structure of wholesale costs. That is the other side to the increase in the margin.

Mr Murray Tosh (South of Scotland) (Con): My apologies for my late arrival, convener: I was at another meeting. I am trying to pick up the discussion from the report provided by the OFT in advance, and from what I have heard.

I would like to establish that I am right in this understanding: the case that the OFT is putting is that the variation in the wholesale price of petrol relates entirely to the transport cost of supplying it and to the absence of a competition factor. If I understand the argument, that factor artificially deflates prices in urban areas. Am I right in also thinking that the retail price differential is entirely made up of the wholesale cost and the relatively low turnover of a business, the low volume of sales against which overheads are set?

If I have got that right, is it realistic to break down the differentials in that generalised way? Can we put meaningful figures on them? Is it subject to variation, even within the Highlands and Islands, to such an extent that we cannot identify a sum to be allocated to each factor? Will the report that you produce provide a stark, simple man's guide, which says that the differentials are an average of 11p, let us say, and that 3p is due to this, 4p to that, the balance to something else? Can we have a report that will make the matter simple, understandable and easily debatable for lay people, the press and us simple politicians to follow?

Alan Williams: We will do our best. However, as you said in your question, there is a fair amount of variation, so the position might be more complicated than we would like. We will try to explain the situation as best we can, but I cannot give you a detailed breakdown as the work has not been done yet.

Irene McGugan (North-East of Scotland) (SNP): Explanations that have been advanced about geographical areas and low volume of sales do not seem to adequately account for evidence that we have about the wide variations in prices between rural areas. Can you confirm that your investigation will examine the issue?

Alan Williams: I agree that there is a wide variation in prices between rural areas and that the matter must be explained.

Nancy Race (Office of Fair Trading): We cannot explain every difference in every local market. Obviously, however, we will examine areas that have great differences.

Rhoda Grant: I want to talk about rebates for petrol companies that are coming under competitive pressure. It was mentioned earlier that some companies are getting rebates on the wholesale price. I would have thought that a price differential means that one company is getting a higher wholesale price than another. I cannot see how that creates fair competition. It might be classed as a rebate, but it could also be described as a price increase for the smaller company.

Alan Williams: There is a variation in wholesale price for different retailers. That might be due to a number of things, such as the fact that a supplier might be willing to give a better price to someone who has invested a lot in their station.

George Lyon: I want to return to the issue of wholesale pricing, which lies at the nub of the problem. We hear about anomalies in the system. An owner of a rural petrol station might claim that the wholesale-delivered price is 2p or 3p above the retail price in the central belt of Scotland. We must hear a clear explanation of how the system works so that we can be reassured that there is no predatory pricing going on in the supply trade in the Highlands and Islands. Many members of the committee would like some assurance about that in the report.

Alan Williams: If the outcome of our inquiry is that the matter is referred to the Competition Commission, we will not say much in our report. If the outcome is that there will be no further investigation, we will do our best to explain the points that you have raised.

The Convener: I would like to clarify that point as it will help the committee decide what steps it will take on the subject.

You say that one of two things will happen at the end of the inquiry. Either it will be decided that an issue of competitiveness must be addressed and the matter will be referred to the Competition Commission or the matter will not be referred to the Competition Commission and you will issue a report that will—and I use this word advisedly—justify the current regime as being fair and defensible under competition law.

Alan Williams: Yes, that is probably right. If we do not refer, whatever we produce will try to explain why we did not think that a reference was justified.

The Convener: How much more likely is it that you will refer the case this time than last time?

Alan Williams: Pass.

The Convener: George Lyon—sorry, Fergus Ewing.

Fergus Ewing: I have never before been mistaken for George Lyon.

In the 1998 report, you indicated that you considered only leaded petrol. Is that correct?

Alan Williams: I am not sure. It does not say that, does it?

Fergus Ewing: In paragraph 11.8 of that report, you state that you did not consider unleaded petrol or diesel. However, you say that

> "there is no evidence to suggest that there are significant differences in the differential between the price of leaded and unleaded petrol",

despite having no evidence before you on which to base that conclusion.

In this report, will you take a sufficient range of evidence throughout the Highlands to allow us to draw conclusions on which any weight can be placed? Will every scrap and shred of evidence that you take be made available to the public and interested parties, as we have heard today?

Alan Williams: I do not know about every scrap and shred, as a lot of evidence will be commercially confidential. For the reasons to which the convener alluded at the beginning of the meeting, that information cannot be made public.

You commented on the types of petrol that were not considered. This time, we are concentrating on unleaded and diesel, as the leaded market is now very small.

Fergus Ewing: We appreciate that you are bound by confidentiality today, which is perfectly reasonable. However, are you telling us that once your report is published, some of the evidence on which it is based will be kept secret because it is commercially confidential?

Alan Williams: Yes, that is standard practice. Our 1998 report contains some tables from which figures have been taken out. Any report by the Competition Commission, the former Monopolies and Mergers Commission, will have had chunks—figures, usually—taken out because of commercial confidentiality. That is what the act requires.

Fergus Ewing: Surely that could be waived with the consent of the oil companies.

Alan Williams: Yes, if they did not mind. If they said that that information was not commercially confidential, we would include it.

The Convener: I shall pursue that line of argument, on the relationship between the OFT and the oil companies. What degree of co-operation are you receiving from the oil companies? How confident are you that you will be able to convince a wider audience, or even this audience, of the substance and the nature of the inquiry that is being carried out on the basis of evidence that we will not be able to see?

Alan Williams: I have no complaints about the co-operation that we receive from the oil companies.

George Lyon: Can the committee have your assurance that you will ensure that the full geographical spread of the Highlands and Islands is taken into consideration? There was a feeling in Argyll and Bute that there had been no visits to that part of the world, yet, according to the Arran CVS study, Argyllshire has some of the highest prices, especially in Mull and Islay. Mrs Michie and I wrote to you, asking you to visit Argyll and Bute and to ensure that you take the full spread of the Highlands and Islands into consideration.

Alan Williams: I hear what you are saying. However, if we were to extend the geographical spread wider than we have so far, it would push out the timetable, which people are anxious about.

George Lyon: I would point out that Argyll and Bute is within the Highlands and Islands.

The Convener: Can you tell us what geographical spread will be taken into account by the inquiry?

Alan Williams: Nancy can tell you what it is so far.

Nancy Race: We are considering the area north of the Great Glen at the moment.

The Convener: How many sampling points might there be north of the Great Glen?

Nancy Race: Our survey takes in roughly 100 stations.

The Convener: I thank you for your attendance today. I hope that we have not breached any parliamentary rules. I am sure that I will hear about it if we have.

I adjourn the committee until 3.30 pm.

15:14

Meeting adjourned.

15:30

On resuming—

The Convener: Members may have noticed a buzzing in the sound system. The technicians have advised me that the mobile phones of some members affected the system, even though they were switched to silent. I ask members to switch off mobile phones and pagers entirely.

We are joined by representatives of the oil companies and petrol suppliers. Please introduce yourselves before I open up the meeting for questions.

Ian Wells (Esso Petroleum Co Ltd): My name is Ian Wells. I am the divisional manager for Esso Petroleum Co Ltd with responsibility for the branded fuels operations throughout the UK.

John Mumford (BP Oil UK Ltd): I am John Mumford, head of BP Oil UK Ltd, which is the marketing company for the operation here.

Simon Graham (Shell UK): I am Simon Graham, the distributor business manager for Shell UK with responsibility for our distributor in the Highlands and Islands, Gleaner Oils, the managing director of which is Billy Laing.

Billy Laing (Gleaner Oils Ltd): I am Billy Laing, managing director of Gleaner Oils. We operate from Elgin, but we cover all the Highlands and Islands, including the west coast.

The Convener: Thank you for attending this meeting. You will have heard the evidence that we have taken so far. We are interested in learning the petrol companies' perspective as well.

Ian Wells: As the leading marketer of fuel in the UK, Esso is conscious of the need to supply fuel at competitive prices in both rural and urban areas—nowhere more so than in Scotland.

I wish to make three main points. First, Esso controls the pump price at only three of the outlets that it supplies in the Highlands and Islands, except where the retailer chooses to take margin support from Esso.

Secondly, as has been said, the costs, for both Esso and its retailers, of operating in the Highlands and Islands are significantly higher than elsewhere due to the remoteness of many locations and low throughputs.

The third point, which has not had much exposure so far today, is that the price of petrol, excluding taxes and duty, has fallen steadily over the past 20 years. In the past 10 years the UK price has fallen by 25 per cent. Excluding duty and VAT, the UK petrol price is the cheapest in the whole of Europe, but when duty and VAT are included, the UK fuel price is the most expensive in Europe. More important, excluding duty and VAT, the average recommended prices in the Highlands and Islands are the same as prices in France, and are cheaper than those in Italy and Benelux.

John Mumford: BP takes this issue extremely seriously, and we are glad to participate in this important debate. We will do whatever we can to help the committee or any other body find a solution.

BP has taken some initiatives to help the situation. We reduced prices throughout the Highlands and Islands a couple of years ago in an attempt to bring about greater harmony. We operate the same price schedule throughout the country. There is no difference between the way we price in the Highlands and Islands and the way we price in the urban areas.

To clarify another point, we own only one petrol station in the Highlands and Islands. We have been called a monopolist, but we have only one station in Fort William. The rest of our sites are all independent dealers who are free to make their own commercial decisions on pricing.

Simon Graham: I do not want to risk repeating too much of what has already been said by my colleagues, but I want to say that Shell UK is also extremely keen to work with the Government, councils and other interested parties to resolve this matter. Shell takes extremely seriously the plight of our rural communities—not just in Scotland, I may add. In this case, we have already done quite a lot to ensure that rural communities continue to be serviced by filling stations. I am sure that Billy Laing will go into more detail about what we have done.

We have increased the number of filling stations in the Highlands and Islands over the past three years and we feel that we are now at a level at which there is some stability in terms of network closures. All things being equal, we do not expect drastically to restructure our network any more. We are fairly comfortable with the strategic locations that we have and believe that we can sustain them, subject to any other factors outside our control.

Allow me to address a few issues that were raised by other witnesses and to reinforce the points that have already been made. We have a national pricing policy, as one would expect, and it is applied equally throughout the Scotland region. The prices charged to the retailer will, as has already been discovered, vary according to the nature of the deal that has been struck with that independent retailer at the time when he signed his contract. There are many components to pricing; it is quite a complex issue.

The key point on pricing is that we have a floor and ceiling spread that, at the moment, on ULG gasoline 95, is just 4p per litre. The sort of figures that we were hearing about—10p, 12p, 14p or 16p—have not existed for a very long time. Where they do persist in some remote locations, it is purely because the retailer has decided, for whatever reason, to add on an extra margin of his own. It is a simple case of economics: if he decides that he has to earn a unit margin of 8p or 10p, as opposed to 2p or 3p, to sustain his business, that is what he will do and he is totally free to do that.

The Convener: Mr Laing, do you want to add anything?

Billy Laing: I may take the opportunity later to develop more thoughts and to talk about our concerns.

The Convener: Let me be quite clear about this. Each of you has said that you have a national pricing policy. So, if I am a retailer and I am negotiating with any of the three companies represented here, I will be offered a certain quantity of fuel at a certain price, regardless of where my petrol station is located. Is that correct?

Ian Wells: Most Esso service stations in the UK—97 per cent of them—participate in our Pricewatch scheme, under which there are defined competitors within a certain radius of the service station. Those stations' prices vary from day to day as competitors move their own prices. Our policy is that our prices should be among the lowest against all the competitors in that area. If you were a retailer talking to Esso, your price each day might vary, but during the period of the contract you may negotiate with us for the sole supply of fuel. We would discuss with you rebates, investment and other parts of a package that would contribute to your overall margin, which would the difference between the supply price and the pump price, which, if you were a member of Pricewatch, would be recommended by Esso.

The Convener: So, if I were to give up my parliamentary work tomorrow and take over the Lochinver petrol station, I would be able to negotiate with Esso a deal that would allow me to purchase fuel for the same price as if I decided to set up a petrol station in Corstorphine in Edinburgh?

Ian Wells: It would not be the same, because we would be looking at the logistics of supplying your service station.

The Convener: Now we are getting somewhere.

Ian Wells: There would be added supply costs.

The Convener: So there is a difference between taking fuel to Corstorphine and taking it to Lochinver. What are the components of the price difference in delivering fuel to those places?

Ian Wells: As you will appreciate, that sort of information is commercially sensitive, but we would be happy to supply it on a confidential basis, and to answer any other questions of that nature. We have already given that sort of information to the Office of Fair Trading for its inquiry.

The Convener: Is that the case for the other two companies? I do not want to single out Esso.

John Mumford: I can give you slightly more guidance. We have already given this information in written evidence. We have a schedule price, which is the same wherever you are. If you are in a remote location, there is a zonal premium. That zonal premium is a fraction of a penny. It is a small amount. In addition, if you take a small load of fuel—in other words, the delivery truck is only partly full—there is a differential. Those are the elements of the pricing schedule that differ.

Simon Graham: Perhaps I can ask Billy Laing to talk about this issue. There are two elements to the difference in wholesale price. One has to be the logistics in supplying remote locations with smaller loads and in more difficult driving conditions. The other is the competitive scene, which we have talked about a lot, and can do so in more detail.

Billy Laing: I have no problems with giving prices for how much it costs our company to deliver a litre of fuel. In fact, I submitted the information to the OFT. The information can be confidential, but we need clarity in relation to prices, and I want to demonstrate that by trying to answer some of your questions. For the first nine months of last year it cost Gleaner £1.79 per mile run, which equated to 1.02p per litre.

As the BP representative said, you have to take other factors into account. If you are going up to Lochinver, it is not economically sensible to go unless you take 30,000 litres, rather than a few thousand litres. There is a big difference. Economics comes in to play. I feel for the small filling stations, because there are problems.

The Convener: Let me sum up. From what has been said, if you are a petrol station that is turning over low volume, and you are located far away from the source of supply, you will carry more of a financial burden than if you were a high-volume station located along the road from the refinery.

Billy Laing: We have many island environments, and Gleaner has 20 tankers—

The Convener: But my point is that it is a misnomer to say that you have a national uniform price. You may have a national pricing mechanism, but it has enormous variables in it, such as how far away your petrol station is from the refinery and how much petrol you can sell.

15:45

Allan Wilson: We are concentrating on the price differential, as opposed to tax and duty, which are standard across the board. You say that Esso's average recommended pump price in the Highlands and Islands is higher than the UK average, so you admit that there is a premium on the pump price in that area. However, your wholesale income from the Highlands and Islands is broadly the same as the UK average. What does that mean in terms of profit margins?

Although BP may have a single price schedule, there are numerous add-ons, as you describe them. One of those is the small load surcharge premium, which is variable and depends on the load size taken by a customer. In the case of Esso and BP, is that dependent on remoteness or volume, or are the two the same?

If you are going to have a discount and a premium, why do you not have the discount on the low-volume operator, which is often in a remote location, so that there would be less of a price follow-on for the consumer in the remote area? Oil companies, rather than being the villain of the piece, could help to reduce petrol prices in rural areas and contribute towards the social inclusion policies that the Executive is promoting.

It would be remiss of me—as the constituency member—not to ask specifically about the contribution that the cost of transportation makes to the overall retail price of fuel on Arran. We heard evidence on that from the ACVS, which had tried to establish the add-on to the retail or wholesale cost in Arran as a consequence of the method of transportation. The only evidence that I can see on that is in Esso's submission, which states that supply costs are higher because shipping the product into sea-fed depots is more expensive than taking it into pipeline-fed depots in much of the UK. What is the cost and how does it compare to the 2p average per litre?

Ian Wells: I can confirm that—as we stated in our submission—our earnings from the Highlands and Islands are broadly the same proportionately as they are from the rest of the UK. You are correct in assuming that the high cost of delivering in the Highlands and Islands is a combination of two factors—first, the remoteness of the locations and the cost of shipping and trucking over the distances involved and, secondly, the low-volume throughputs of each of the retailers. The differential between the average recommended pump prices in the Highlands and Islands and those in the rest of Scotland is currently less than 3p. That recognises the fact that we must recover the higher costs in the remoter locations.

John Mumford: I can confirm that the cost differential that we are talking about is of the order of 2p to 3p. Two years ago, we made a pledge that there would never be a differential in the delivered cost of more than 4p between the most remote area and an urban area. We have lived up to that pledge, so we are comfortable that the price differential and the cost differential are around 2p to 3p.

The discounting and prices in some parts of the Highlands and Islands—not all—are in line with those in Edinburgh. If one strips away duty and VAT, the pump price in Oban, Fort William and Inverness today is 16.9p per litre. That gives a measure of the amount of money coming from those markets to the oil companies and the dealers.

The Convener: What is the price in Edinburgh?

John Mumford: The price in Edinburgh is the same.

The Convener: What is the price in, for example, Thurso?

John Mumford: I do not know. I assume that it would be substantially more than 20p per litre. I can tell you the price at which we are delivering fuel into that station and the limits that we are putting on that price; what the dealer does afterwards reflects his costs and the way in which he views his commercial circumstances.

The Convener: You said that you felt that you had to recover the high costs of delivery and dispatch from the remote areas. Why is it necessary to take that view? Could not you say, “Why don’t we try to recover the high costs of distribution to the isolated areas from the much larger, more profitable market that dominates the rest of Scotland?”

John Mumford: Competition in the petrol market is extremely fierce. There are no profits to cross-subsidise—

The Convener: You all look like reasonable men. Why cannot you come to some mutually acceptable agreement and adopt a petrol pricing arrangement that protects rural communities and recovers that high cost from more profitable areas?

John Mumford: Unfortunately, that would be against the law.

Simon Graham: The convener’s point about why the profit-making sector of our retail business does not subsidise the Highlands and Islands, and other remote areas for that matter, is interesting. There is a misconception that we earn a tremendous amount of money from our retail business and, although I do not expect to hear violins playing, I must make it absolutely clear that we do not. The margins are very small. In fact, since the hypermarket situation in 1996—when our colleagues at Esso decided that they had had enough and would meet the hypermarkets head on—we estimate that we have given around £1 billion back to the motorist. That sum has come out of the wholesale and retail margins and gone back to the motorist; the motorist has gained. There are not huge profits to be redistributed.

It was also suggested that the higher prices that are charged in the Highlands and Islands might be subsidising the lower prices elsewhere. To put that in perspective, Shell’s branded business in the Highlands and Islands is between 0.5 and 1 per cent of its total UK volume, so clearly that is not the case.

Allan Wilson: So if you were to discount in that area, you could do so at the absolute margins of your entire operation?

Ian Wells: As I mentioned earlier, the income that Esso derives from rural and urban locations is broadly the same; that is key. The fact is that the urban locations contain the highest competition. Our realisations tend to be lower there because of that competition, while the costs in the Highlands and Islands are that much greater.

Miss Goldie: Mr Wells, the conclusion of your submission deals with three types of retailer. Is there a retail price distinction between those types?

Ian Wells: Yes. As I said, we control the price at only three service stations in the Highlands and Islands. Those are company-owned stations, operated by agents, at which Esso owns the fuel underground. Other service stations are operated either by licensees of company-owned stations or by independent dealers. Those retailers are free to set their own pump prices, unless they participate in Pricewatch, whereby prices are recommended by Esso and we expect them to be passed on to the consumer.

Miss Goldie: That is helpful. Paragraph 1.6 of your submission, Mr Wells, says:

> "Esso's net wholesale income from the Highlands & Islands is broadly the same as the UK average."

Do I infer from that that Esso is absorbing some of the extra cost?

Ian Wells: On a site-by-site basis, we may be, but in general we try to balance the books between the costs that each retail site incurs and the volume of sales that it has. That is why those incomes are broadly the same across the UK.

Miss Goldie: I also have a couple of questions for Mr Laing. I am interested in the relationship between Gleaner Oils and Shell—is Gleaner a wholly owned subsidiary?

Billy Laing: Gleaner is a private company. We have been operating since 1954, since which time we have been a distributor for Shell. Our head office is in Elgin, but we have depots in Inverness, Connel, Mull, Islay, Dunoon and Ardrishaig. Further east, we have depots at Mintlaw and Aberdeen.

Miss Goldie: Would I be correct in assuming that Shell is one of your major clients, Mr Laing?

Billy Laing: We are a distributor for Shell. We purchase the product at a wholesale price and sell it onward. However, we stick closely to the retail pricing. We are a Highland company and, in our commitment to the area, we hope that we will find a way out of this through some innovative idea.

Miss Goldie: I got the impression from earlier evidence that retailers on Arran were being pared to the bone, implying that there is little margin between what they have to pay for the petrol they sell and what they can hope to get from Arran residents. Who is the principal wholesaler on Arran?

Billy Laing: It is BP. We get BP to deliver to a few of our filling stations; the price that we charge—would you believe it—is the same as on the mainland. The only variable might be the load size.

Miss Goldie: Are you agents for BP in the distribution of petrol to Arran?

Billy Laing: No. BP delivers on our behalf, in an exchange deal. However, the price that we charge the retailer is Gleaner's price. The price that retailers are charged is the same as on the mainland. I could not understand some of the Arran prices mentioned earlier. Privately, if you wish, I could show you our prices.

Miss Goldie: That might be helpful—we certainly need facts.

Fergus Ewing: Any rational person would recognise that the overwhelming and central problem is that the UK as a whole has the highest excise duty and VAT in Europe. During the evidence from the OFT, I was concerned to learn that some of the information that is submitted to this inquiry will be kept secret. I invite you to ponder the consequences of that—there may not be a great deal of public faith in the outcome of the inquiry if any information is kept secret. First, will you indicate whether you would be willing, in your evidence, to allow such information to be made public? Secondly, would you be willing to meet representatives of Highland Council and Highlands and Islands Enterprise, to establish whether—as I believe was suggested in two of your submissions—innovative solutions can be found?

Ian Wells: As we do with the OFT, we are happy to supply this committee—and anybody else—with data on costs, on a commercially confidential basis. We will provide you with anything that you ask for. We are also happy to co-operate with anybody who has shown an interest, including Highland Council, which we have met previously.

John Mumford: The issue of commercial confidentiality relates to the specific arrangements between individual oil companies and individual dealers. In such cases, where there are two parties, it would be difficult to reveal information. However, information on average costs is already substantially in the public domain—we would be happy to see that data debated and to take part in the sort of process that you are suggesting. A solution to the cost problem would be a win-win for everybody.

Fergus Ewing: The impact of the vapour recovery regulations on rural petrol stations could be extremely damaging. Can you give us any specific information on that?

16:00

Ian Wells: The Government required vapour recovery stage 1 to be installed at all service stations by the end of last year, although a derogation was given to service stations that sold less than a million litres. The next step will probably be to lower the volume criteria. We will work with our retailers—as we have done already—to invest in meeting those legislative requirements. We will consider the next tier if the Government decides to lower the derogation.

John Mumford: I agree with that completely.

Billy Laing: I would like to tell you what vapour recovery will do to the Highlands, to companies such as ours and to retailers. In Islay, just over 1 million litres is distributed through six operators, which, as yet, are not required to carry out vapour recovery. The law says that any new tanker must have vapour recovery. With effect from 1 January 2000, in addition to vapour recovery, we must have sealed dipsticks. I have ordered a new tanker for Islay; if I were to introduce it without vapour recovery and a sealed dipstick, I would be breaking the law.

Stations that sell about half a million litres do not have the margin to allow them to meet the regulations and nor do we. When such stations want to redevelop any aspect of their filling station, the enforcing authorities demand a new intercepter, double-skinned tanks, tank gauges and tanker stances. Alison Magee spoke about this in relation to the western Highlands; we have had real problems in helping those retailers to make a profit on their investment. If this continues, we will lose many more filling stations.

A well-respected company, Datamonitor, estimated that 20,000 rural filling stations in western Europe would close by 2004. I hope that very few of those are in our area. We want to look after our rural areas, but the legislation does not help us. I hope that the committee will help us on that.

Gleaner has met the Scottish Office and the Scottish Executive, seeking a derogation. A filling station in Fort William must have vapour recovery, even though the tanker does not need it and the depot does not have it. The guidance says that we must have vapour recovery and that a licence fee should be paid to Scottish Environment Protection Agency, the enforcing authority. Something must be done. I would like to work with the Scottish Parliament on that.

The Convener: I represent a large rural constituency in Perthshire and Angus and I am aware of the implementation issue. You have made a good point, Mr Laing.

Fergus Ewing: Are you aware whether it is within UK competence to grant a derogation?

Billy Laing: When I attended the Scottish Office meeting, I was told that the derogation would be difficult, unless we could define the difference between a terminal and a depot. We said that we were sure that we could manage that. However, the legislation relates to EU regulations and we must be careful.

The Convener: We will take that point on board.

George Lyon: Some capital grants money is available, but you seem to be saying that the derogation is what we need to push, rather than an increase in the capital grants scheme. Is that right?

Billy Laing: Derogation is the key. All the sites in Rothesay will close down if we do not get derogation.

George Lyon: Are you saying that derogation is the key, rather than an increase in the capital grants scheme, as happened last year?

Billy Laing: Yes.

George Lyon: I have a general point that goes back to the issue that we have been pursuing from the start about the wholesale price that the retailers must pay, which is our greatest concern. Friends of mine in the trade have said that the strategic objectives are UK-wide in order to rationalise the small petrol retail stations and to maximise volumes through the large ones, which happen to be owned by the major oil companies.

The major oil companies control the wholesale price for small retailers and so control their destiny. Because the retailers cannot increase their prices very easily, they are either going to survive or die by the deal—the rebate—that you give them. Is that part of the strategic objective that is being pursued by the major companies in rural Scotland?

Ian Wells: Answering on behalf of Esso, I can say absolutely not. As I said earlier, we are a national marketer and one of our strengths is that we can offer petrol from Land's End to John o' Groats. That is important to us in terms of promotion, brand and any other feature of a big company that you could mention. We have no strategic policy to withdraw from any rural area.

John Mumford: On behalf of BP, I totally agree with that. I can think of no reason why our strategic objective would be anything other than continuing to supply the market.

Simon Graham: To put it in simple terms, we will invest in sites wherever we get our required return on investment. I think that I mentioned earlier that we are currently fairly satisfied with the locations that we have for Shell-branded stations. We do not expect a dramatic fall-away in Shell-branded sites in the area.

George Lyon: You have highlighted the issue that I was getting at. How do you decide which sites should have a Shell, an Esso or a BP brand and which should not? Which sites are the ones that we should therefore deduce will survive in the longer term? Is the decision based on volume?

Ian Wells: Our prime concern, obviously, is to make money. When we negotiate with a retailer, we will examine the potential to make money from the deal that we are striking. We have invested heavily in the Highlands and Islands. We have even purchased and opened a brand-new site in the past three years. As I said, with our dealers, we invest in such things as new pumps, canopies, tanks and vapour recovery for appropriate sites. The dealer chooses who he wants to supply his fuel for the following five years. Competition is obviously fierce, as it would be in any other area.

The Convener: Mr Wells, you made a point about making money, and we understand that.

With its pricing mechanism, does your company try to get the same margin from isolated, rural, low-volume petrol stations as it tries to get from high-volume, urban petrol stations?

Ian Wells: Costs vary from site to site but, provided that we can cover those costs, all we want to do is to supply the site and to make a return on the capital that we have usually invested in that business.

The Convener: Is the return the same? Let me go back to my comparison of a Corstorphine filling station and a Lochinver filling station: if you want to get a certain margin in Corstorphine, do you want to get the same margin in Lochinver?

Ian Wells: Yes—the same net margin.

George Lyon: You said that dealers had a choice over which company they went with, yet the evidence from my part of the world is that dealers do not have a choice. Esso and Shell have been unwilling to renew contracts with small rural petrol stations, and are trying to push them on to the likes of Billy Laing's company or the other big distributor for Esso. What is the reason for that? Why are you withdrawing contracts and refusing to renew them—because that leads on to the issue of agency cards and who can use them? Why do you want a subdealer to supply those small rural petrol stations? Is it not worth your while to bother about such stations? Do you not think that they will last very long?

Ian Wells: We offer every dealer terms for a renewal of their contract; we do not intentionally say that we do not want to supply that dealer any more. However, often the dealer will find our terms uncompetitive and commercially unattractive. Like Shell, we have a branded reseller in the Highlands and Islands—Highland Fuels Ltd—whose operation costs are that much lower. It operates smaller trucks and can cover remote areas and will often take over the supply of the fuel to smaller dealers. As I said, however, we do not tell dealers that we are not going to supply them; instead, they may find the terms that we offer commercially unattractive.

On the question of cards, all the companies who are represented here operate a commercial card, which is for business fleet use and is part of the proprietary sector of our brand. Shell, BP and Esso have their own cards. We have a reciprocity arrangement with Shell which means that its card can be used on our forecourts and vice versa.

George Lyon: However, dealers that you do not directly supply are not allowed to access that system. Furthermore, you said that you passed on business to firms such as Gleaner because they operate smaller tankers and units, which means that their distribution costs are cheaper. Is that true?

Ian Wells: Obviously such companies have more flexibility and are able to cope with retailers who do not take full truckloads of petrol. We have one fleet of trucks that carry only petrol. I suspect that Mr Laing knows more about running the smaller truck business.

Simon Graham: On the issue of cards, Shell is the only company that sells its product wholesale as another brand to Gleaner. There are more than 40 Gleaner sites—every Shell site where contracts were not renewed, along with some Esso sites, converted to Gleaner—all of which have the full range of card offering from Shell.

George Lyon: Are your agency cards available to companies that are supplied by subdealers, or have you withdrawn them?

John Mumford: We have not withdrawn cards from any of our sites.

Ian Wells: At the moment, Highland Fuels does not operate the Esso card. We have a pan-European reciprocity arrangement with Shell, and we are considering offering the Esso cards at certain sites supplied by Highland Fuels.

Dr Murray: Ian Wells said that competition was very fierce, particularly in urban areas, and profit margins have become very small since the hypermarkets became involved some years ago. The gentleman from BP gave us a figure of 16.9p on today's prices in Fort William, Edinburgh and some other locations. How much profit is made on a litre of petrol in Edinburgh and in Fort William?

Simon Graham: We mentioned the recommended retail price for unleaded gasoline 95, which is our most commonly purchased product. I do not mind sharing these figures with my colleagues from BP and Esso, because they are in the public domain. The recommended retail pump price for ULG 95 is 77.9p per litre, 11.6p of which is VAT and 47.21p of which is duty; on the 27 or 28 January, the cost of product was 11.58p per litre. That leaves a total gross margin of 7.5p for Shell and the retailer, which is less than 10 per cent of the pump price.

Dr Murray: How much of that gross margin does Shell receive?

Simon Graham: I am not prepared to split down that margin.

Dr Murray: Are those figures from an urban or a rural location?

Simon Graham: The figures are based on the pump price wherever that may be. That 7.5p profit includes our primary and secondary distribution costs.

Dr Murray: But was the initial 77.9p per litre on ULG 95 taken from an urban location?

Simon Graham: The range of recommended retail prices we set was between 3p and 4p. Although that changes from time to time, the differentials have been fairly narrow since the last budget. Unless a retailer added an extra margin for himself, we would not expect prices to be lower than 74.9p per litre or higher than 77.9p per litre.

16:15

Rhoda Grant: I have a few questions, which I would like to ask separately, as they jump around and I want to clarify some of the points that others have made.

You said that the 7p is split between the retailer and the dealer, although you would not say how. Is the split the same in urban and rural areas?

John Mumford: The split varies considerably, basically because it is not a split. There is a wholesale price and then the dealer adds whatever he needs to operate. People have talked about dealers in some places adding sums in excess of 10p per litre—perhaps 12p per litre. I have no idea whether that is true. The cost differential for the oil companies is about 2p or 3p per litre. You will see from the numbers that we have talked about that the margin that comes back to the oil company is typically about 1p or 2p per litre—that figure is pretty constant.

The question of split is difficult because there is not one margin that is split. There is the commercial world in which the oil company operates, which is about what happens before the product goes to the site and drops into the tank; then there is the commercial world once the product is delivered from the tank to the customer. There is no thought process of which I am aware according to which someone says, "Here is the total margin. How will we carve it up?"

Rhoda Grant: There are three types of retailer—companies' retailers, licensees and independents. Do they all get petrol at the same wholesale cost?

Ian Wells: Agents who run company-owned service stations sell fuel on our behalf—we own the fuel. Licensees get petrol at the same price, depending on the pump price that is decreed by Pricewatch at the time. As I mentioned, our system is slightly different from that of the other oil companies in that if they participate in Pricewatch, each of our service stations has a specific supply price, which varies from day to day. Independent dealers have differing prices because, when they negotiate their contract, they enjoy benefits that a company-owned operator does not, such as rebates and investment in their premises, in exchange for a five-year solo-supplier agreement.

Rhoda Grant: So, to clarify, do the independents usually pay more for their petrol than company-owned agents?

Ian Wells: I did not hear. Did you ask whether dealers pay more?

Rhoda Grant: Do independent dealers pay more than those on company-owned premises?

Ian Wells: There is no straight answer to that. The price varies from site to site for the reasons that I have outlined.

Rhoda Grant: We have been told that a smaller load size incurs added cost. Can you give an indication of what that cost would be?

Ian Wells: It is difficult to be specific. The smaller the outlet and the more remote it is, the more expensive it is for us to supply it. Similarly, dealers have to work with very low margins on the fuel. We encourage them to take on as many other profit centres as they can. As you know, many retailers have shops, post offices, workshops or car sales outlets to generate income to support their petrol activity.

John Mumford: I can give a specific answer to Rhoda Grant's question about the small load charge that we include in the price. If the load is more than 26,000 litres, there is no incremental charge. Other than that, the charge gradually increases and, typically, at 2,250 litres, which is less than 10 per cent of the 26,000 litre threshold, the increase in charge is 0.4p per litre. If the load is very small, say 1,000 litres, the increase is 0.8p per litre. That is what we charge. We believe that the actual cost is somewhat more than that.

Miss Goldie: I have a brief technical question for you, Mr Laing. You referred to the EU petrol vapour recovery directive in relation to tankers. As far as I am aware, the Government secured a derogation in respect of small petrol filling stations. You mentioned having approached the Executive about the matter. Is that because tankers are included under the directive and you are trying to get them excluded?

Billy Laing: No. The derogation is only for a certain period of time, which corresponds to up to 1 million litres. There is no derogation after 1 million litres; they should have registered and put vapour recovery in. Many filling stations have not put it in. Even if they had, it would have been delivered by tankers from depots that did not need to have it in. This is silly—fuel is being delivered and the system is being enforced and you have to pay £300 a year for a licence for something we cannot do and do not need to do.

Another factor is the new directive that applies from the first day of this year. I will give it to you, Miss Goldie. I have it here with me, or I will give it to you afterwards.

Miss Goldie: It would be helpful to include it as part of the record, convener.

Billy Laing: Just a moment: if you give me a second, I will find it.

Miss Goldie: Is it the one that refers to the sealed dipstick?

Billy Laing: Yes, it is the one that does the dipstick. If you want to take up this issue, Miss Goldie, I will love you for ever.

Miss Goldie: Irresistible, Mr Laing, irresistible.

The Convener: If we could perhaps bring some order to the proceedings.

Your point will have been noted by the official reporters, but we will return to you in a moment so that you can put it on the record in more detail.

George Lyon: I would like to ask one more question about the wholesale price. I purchase diesel commercially. I find, from speaking to some local retailers and to others further afield, that I appear to be able to buy at a lower price than the wholesale price at which the local retailer has to purchase, and to which they have to add a margin. How can that possibly be, given that the retailer purchases far greater quantities than I do? It does not seem to make any sense.

Ian Wells: I am sorry, I cannot comment on that. I do not deal with that side of the business, although I know that there are differential duty rates on agricultural diesel—

George Lyon: This is nothing to do with that.

The Convener: We could open up a series of other questions, I am sure.

George Lyon: My point is about the same product—

Simon Graham: To be fair to Esso, we operate in all markets in the area: commercial, aviation, marine, retail and domestic. We are a fully integrated oil company in the area, whereas Esso is not.

It may not be clear to members, but it is perfectly clear to me why we are cheaper in our commercial business: we do not have any of the associated retail costs. It costs many thousands of pounds to image a Shell-branded filling station. We offer all the credit cards that we have mentioned, our SMART promotion and other promotions from time to time. None of those costs apply to the commercial market. In addition, fuel additives are added to fuel. We call it Shell Pura—that may not mean anything to members, but it means a lot to us.

All the factors that I have mentioned have a cost attached, and the retail market has to bear that cost. We have corporate overheads: we sponsor the Ferrari racing team, for example. Such costs have to be shared among the parts of the business that benefit.

The Convener: I am sure that it will come as a great reassurance to the public of Lochinver that they are sponsoring Ferrari when they are buying their petrol.

Simon Graham: I am sure that there are many Ferrari fans up there, as there are all around the world.

Fergus Ewing: We heard from the Office of Fair Trading that if it is minded to refer the matter to the Competition Commission, it would accept an undertaking in lieu from you gentlemen. Will you confirm that it is unlikely that you will grant such an undertaking and that, if you did, it would relate only to the areas on which evidence was taken? Will you also confirm that you would attack the Office of Fair Trading's findings because it seems that the extent of the geographical areas from which it has taken evidence is ridiculously limited?

John Mumford: The oil industry has been subject to inquiries by the Office of Fair Trading and the Monopolies and Mergers Commission almost continuously for as long as I have been in the industry. Nothing adverse has ever been found, so the question is hypothetical.

Simon Graham: I have nothing to add to that, except to point out that although the way we do business has not changed in the more than 20 years I have been involved in the company, investigations seem to come up with alarming regularity.

The Convener: I must draw this part of the proceedings to a close. Mr Laing, do you have that reference?

Billy Laing: The regulation relates to article 5 of European directive 94/63/EC, which is implemented into UK law by the approved tank requirements under regulation 6(c) of the Carriage of Dangerous Goods by Road Regulations 1996 (SI 1996/2095). The regulations state that the measurement of the content of the tank or compartment was effective with effect from 31 December 1999.

Fergus Ewing: It would be useful for committee members to have written submissions from the gentlemen here about the effect of the regulations. That will give us a better understanding of the impact that they might have.

Billy Laing: I will supply the committee with a copy of the information that I have sent to the Scottish Executive.

The Convener: Thank you for your attendance today.

We now move to the last part of the evidence-taking session of our meeting. I am pleased to welcome Ray Holloway, the director of the Petrol Retailers Association.

Would you say some words of introduction before I open the meeting up to members of the committee?

Ray Holloway (Petrol Retailers Association): The Petrol Retailers Association works with the Scottish Motor Trade Association. We represent retailers in Scotland and the rest of the UK.

I hope that the evidence that I have submitted to the committee will enable us to take something positive away from this committee that can be worked on. As we know, the subject of pricing differential has raised its head many times in the past. I, like many other retailers, hope that this meeting can produce firm recommendations.

The Convener: You have listened to some of the evidence that we have heard today. Putting aside the issues of taxation that your submission details graphically, there seems to be an implicit feeling on the part of the fuel companies that little account is taken of the difference in business opportunity between a filling station in an urban location and one in an isolated location and that volume and cost of delivery is carried by the individual business entity rather than by the market as a whole. Is that a fair representation? Are there any initiatives that the Petrol Retailers Association could suggest to address this matter?

16:30

Ray Holloway: On the relationship between the oil company and the retailer, you have heard about the practice that has developed down the years. I have not heard anything that I would disagree with about the way in which the oil companies view costs. In my submission, I point out that the oil companies are in this market as a commercial venture and must remunerate their shareholders. I also point out that the retailer is in this market voluntarily; he has a responsibility to himself to make his business profitable. Unless this inquiry deals with those issues positively, it will not find a solution.

It might have been interesting to ask the oil companies how they deal with their costs in other parts of the UK when they are addressing an issue. I heard one question on the averaging of costs when they view a market. If you were to ask them that same question today, you may get a different answer. The question is one of desirability. In the remote parts of Scotland, they are not able to transfer volume to assets that they own or to develop assets that they want to own. Their attitude to the small dealers is commercially different.

Allan Wilson: We heard from BP on that issue. BP operates two pricing mechanisms that are available to retailers: schedule and Platts. The schedule price, as I understand it, is variable and depends on the load size. What is not variable is the margin of return that is demanded of the retailer by the wholesaler. In low-volume, remote locations, the two may be the same, which means that a retailer has to increase the price per litre substantially higher than his counterpart in a high-volume, urban location. Is that a fair reflection of the situation?

Ray Holloway: Yes, it is. We have talked about the schedule price. It would have been interesting if you had asked the oil companies where in the UK they achieve the full schedule price. In practice, the schedule price is a myth.

The Convener: Would you like to say a little bit more about that?

Ray Holloway: The schedule price varies a lot, depending on the competition within trading areas. Is the schedule price the price at which an oil company sells its product to the majority of its customers, or is it the highest price that it can obtain in an area? That question needs to be answered.

Allan Wilson: It is the latter, I presume, if there is no flexibility in the margin to account for location.

Ray Holloway: Yes. It would be unsurprising if, when it entered a supply relationship with any filling station, an oil company said that it expected the same rate of return as elsewhere. That is good business practice; it is a way of ranking one opportunity against another. I have no difficulty accepting that. However, I return to the fact that you are not considering the extent of desirability— how much an oil company wants to be in a particular area— that is reflected in the economics

George Lyon: That is a central point that we have been trying to get at since we started this afternoon. If the oil companies believe that it is desirable to stay in the market in certain areas, bigger discounts are given to ensure that those stations can compete, especially if they are owned by the major oil companies.

I would like to return to the independent retailers. Would it be true to say that their number has fallen rapidly in the past few years and that that trend is continuing and, perhaps, being exacerbated in rural areas?

Ray Holloway: That is very true. Since 1996, approximately 1,200 filling stations have closed each year. If one goes back as far as 1980, the figure was 850 per annum. Approximately 65 to 70 per cent of those sites were rural. The rest were urban.

George Lyon: What proportion of the retail market have the oil companies taken over? Do BP and Esso, for example, own a much greater percentage of that market?

Ray Holloway: Yes. The market is not expanding—it is contracting. For a business to grow in the retail market, it must take someone else's business.

Approximately 70 per cent of the retail market in the UK is controlled by the major oil companies through a network that they own and operate.

Rhoda Grant: Have you tried to ascertain—through, for example, a survey of your members—the variation in the wholesale prices that they are charged?

Ray Holloway: I am aware of our members' feelings about wholesale price, but the wholesale price has not been the cause of any specific complaints. Retailers have, however, directed at oil companies many complaints to do with the relationship between them.

I will give an example of that by referring to a question that was asked of the OFT about who sets the retail price of petrol. I will quote from an OFT document entitled "Competition and supply of petrol in the UK." It is a fairly worthless document that was produced in May 1998. The gentleman responsible for the report was not aware of the work that had been done by his own department. In relation to retail price the report says:

"There is virtually no pricing autonomy for the independent retailer, who can only lower prices if in receipt of SPS".

SPS stands for selective pricing policy. The report goes on to say that the independent retailer

"must lower the price of petrol at the pumps if support is forthcoming."

So—what is the OFT likely to find when it examines the position of the independent retailer in relation to the oil companies and supermarkets? The document also says that such retailers are not threatened and are not likely to be missed while inter-supermarket competition and competition between supermarkets and oil companies persists.

The OFT is blinded totally by the hypermarkets and major oil companies, because it only ever examines issues in relation to competition law. It does not look at the unfair practice that exists behind the agreements between the oil companies and retailers. The wholesale price is a small part of the problem.

The Convener: What are the other strands of that relationship that require being unravelled?

Ray Holloway: There are many, which this inquiry is probably not set to address. In terms of pricing and margins there is a practice in the industry of delivering warm product. That product shrinks. Retailers have a contract to buy a set amount of product and that amount is not delivered. The industry has failed to address that problem in its relationship with its retailers. Somebody commented earlier on inter-trading between oil companies—the problem I have just described is addressed when they trade among themselves. Retailers operate on an impossible margin and the gross margin is a myth. I have heard the net margin being quoted as 4 per cent today—we are lucky if the gross margin in our industry reaches 2 per cent.

Rhoda Grant: Obviously the Office of Fair Trading is not going to examine such issues. Do you have a solution that would allow the committee to examine those issues?

Ray Holloway: As I sought to establish in my submission, that will require some thinking outside the box.

I have been very much involved in the issue of fuel smuggling from the Republic of Ireland into the north of Ireland. Many small retailers located in the border areas of the north of Ireland are losing their businesses because of the differential in pricing—the prices in the north are approximately double the prices in the south. The pricing differential between retailers in the western isles and those in the central belt has been almost at that point in the past, although it is not so much today. However, it is almost impossible for the Government to act to save those small businesses under EC restrictions. We must find another way of identifying who can provide the money to address the problem—if, indeed, one wants to address it correctly.

As the major oil companies are independent entities, I do not see that an agreement can be reached that would embrace all three of the majors that are here. A quite different approach is required. Also, with the decline in the number of independent retailers in Scotland, we are reaching a critical numbers point, where a strategic network of filling stations will not exist to the north and west of Scotland or in the islands. If Government does not recognise that and do something to sustain the network's survival, it will disappear.

As I said earlier, the independent retailers can choose not to be in this business. Therefore, I suggest that, as is the case in some Scandinavian countries, the small filling stations are seen as an essential service and are sustained through payment of a salary, similar to that calculated by the Post Office. This is probably not a good time to make that suggestion as, from comments made at Westminster, I know that the Post Office is under some threat. Nevertheless, that is a way forward. If one were to work out the practicalities of that approach, the cost could be met.

From my knowledge of the ability to subsidise individuals or businesses, it would be practically impossible to obtain funding from central Government for the agency card idea.

Rhoda Grant: Would your members be agreeable to an almost public ownership of rural petrol stations, whereby they were paid a salary?

Ray Holloway: As with everything else, one consults a number of members, some of whom may have different opinions. However, 70 per cent of those whom I have consulted so far are totally in favour of that approach. About 15 per cent have also said that they want more information about the level at which the sustaining salary would be set. The others have said that if they cannot survive on their own, they do not need help to do so—and so on.

There is a fair feeling in favour of some kind of support system—it is a question of help that one can design and obtain approval for. I am very pessimistic about this committee's ability to bring together the three major oil brands to work towards one solution.

Fergus Ewing: To your knowledge, are any of your members subject, in their contractual arrangements with the oil companies, to a commercial confidentiality clause that gags them from describing the difficulties that they may experience to anyone other than the oil company?

Ray Holloway: To answer honestly, yes. Such a clause would have been introduced not at the signing of the agreement but at the time of a particular dispute.

Fergus Ewing: At page three of your submission, you suggest six positive proposals—we all want to be positive. Will you briefly describe how you imagine those proposals would operate?

Ray Holloway: I do not think that, even under these proposals, it would be easy to achieve a complete agreement. However, the starting point should be to bring together individuals in the industry who can examine the options that I have set out. Those options are quite straightforward. As at 31 December last year, the remaining rural filling stations ought to be determined to be strategic and available for Government licence.

Following a process of negotiation with the industry, a salary level should be set for those filling stations. That would need to be assessed subject to the business already being enacted and there being the underpinning for an annual salary.

16:45

There is a system for paying short-term subsidies in Holland, where there is a cross-border differential with Germany. In Finland, there is a scheme where the annual rate is declared and adjusted monthly on the basis of actual sales. There is also a retail price that is set as part of the negotiation and declared monthly. It is not controlled by law, so there is the ability to vary the price. If the Office of Fair Trading undertook a monitoring role, we could expose those who were seeking to sell at above the agreed price.

The wholesale or schedule price is the biggest single problem in terms of how we deal with the differential between pricing in rural areas and the central belt. I choose the central belt rather than the UK average—in fact, the price in the central belt is below the UK average and has been for some time. Dealing with the differential is a vexing problem, because it can be done only within the oil companies' required cost cover for delivering product into rural areas.

Today I have heard the figure of 2p mentioned, which the oil companies did not dispute when the Office of Fair Trading report was produced. It has been quoted at higher than that, but let us accept the figure of 2p to 3p, in some cases. The salary would also have to take into account what the retailers want. If we can create a mechanism that does all those things, we will have a positive way forward. If the oil companies will consider it only on the basis of competition between them, let us make the oil companies compete with one another. Let us make the licence that the Government issues a collective bargaining tool and make the oil companies compete to supply the oil office. That would make them address whether they want to be in Sutherland or the western isles.

Fergus Ewing: Is the example that you describe—which I find extremely interesting—followed in any of the countries to which you have referred, such as Holland, Germany or Finland?

Ray Holloway: They do not have the same island problem. I agree totally that putting coasters into small ports adds to costs. There is an on-cost. However, I believe that the real on-cost of supplying some of the remote parts of Scotland has never been examined by anyone apart from the oil companies. Some of those costs ought to be challenged. There is a refinery here in Scotland. One interesting question that you might have asked when you were considering how the pricing mechanism worked was why petrol at a filling station in Grangemouth costs more than petrol in Falkirk or Edinburgh. It is an interesting thought—transportation obviously costs a great deal. If we want to have an inquiry into the real costs of moving product around in Scotland, there is a way forward—a way of making the oil companies compete with one another, if they are not prepared to go along with the process. It works elsewhere. I have not submitted the information for this meeting, but I will be happy to do so afterwards.

Allan Wilson: Would the only differential between the advised retail price and the invoice price be the cost of transportation? Would that vary between island and other rural locations?

Ray Holloway: Today I have heard a lot about being locked into the price and how it breaks down. It does not break down in quite the way that I have heard described. In reality, retailers earn between 0.75p per litre if they are working with Esso, and just over 3p if they own the site. The margins are not huge, and the rest of whatever margin exists goes to the oil company.

Today you have heard margins of 16.9p mentioned. Of the 16.9p, between three quarters of 1p and 3p goes to the retailer; the rest goes to the oil company. Do not be bamboozled when the oil companies say that they get only the little bit above the 3p. In fact, they get the rest of whatever margin exists. The oil companies and supermarkets have done an excellent job of bamboozling people about margins in this industry. The retailers earn a fixed margin, which is agreed at the time of signing their contract.

Miss Goldie: What percentage of petrol retail outlets in Scotland does your association represent?

Ray Holloway: Around 60 per cent—in terms of the Scottish Motor Trade Association—but that figure will vary in different parts of Scotland.

Miss Goldie: I was interested to read your recommendations. Unlike some other organisations, you make no reference to possible fiscal rebate or to reduction in duty or VAT. Is there a reason for that omission?

Ray Holloway: It is my humble submission that the person who can afford to fund licences similar to those held by post offices is the Chancellor of the Exchequer. Under EC regulations there is a de minimis guideline in the directive that allows a small amount of support to be given. In the main, the businesses in Scotland that we are discussing would qualify for that support. That has to be paid for by someone, and in this case the Treasury is the purse. I stress in my letter that the Government takes £32 billion from the motorist in the UK every year, and invests less than £6 billion. Therefore, there is a purse out of which such support could be funded.

Mr Tosh: A moment ago, Mr Holloway said that the retailer got a fixed amount from the 16.9p per litre, which depended on the contract that he had signed, and that the wholesaler received the rest of that amount. I noticed that while he said that, the remaining representatives of the wholesalers shook their heads vigorously. I wonder whether we can call those representatives back to pursue that point, or whether there is some other way to get at the truth, because there is clearly a sharp difference in the evidence of the two parties. We must put each party's evidence to the other and get to the truth of the matter.

The Convener: Mr Holloway is giving evidence at the moment. I can hold him to account. We will pursue Murray Tosh's point when we discuss how to proceed.

Ray Holloway: I will clear up Mr Tosh's point. We were talking about the margins that were available to the wholesaler. The retail price at the pump determines the retailer's total margin. The company may be committed to paying a rebate, which is an allowance for the quantity purchased. It is normal practice to pay that rebate three months in arrears, but sometimes it is paid off invoice and sometimes it is paid monthly; practice varies. Other than that, it is indeed up to the retailer to set the retail margin. I have sympathy for the companies in some small cases in which they do not direct the pump price, but in many cases the oil companies do direct the pump price.

George Lyon: You have given us figures for the shrinking of the total market and have told us that 77 per cent of retail outlets are controlled by the major multiples. I put it to the oil companies that their longer-term strategy was to buy up the best available locations to maximise throughput. Do you agree that their long-term strategic aim is to maximise those sites at the expense of the small independent retailers?

Ray Holloway: Yes, but not in the areas under discussion. I do not think that any of the oil companies that have given evidence today would buy properties in those areas. You heard the Esso witness say that his company owned only three sites in the area under discussion, and I think that the BP witness said that BP owned only one site there. I did not hear a figure for Shell.

The interest is very low for the simple reason that the oil companies are working on scale to affect costs. That is the whole problem; they are dealing with very small businesses. When the oil companies cannot make one big business out of closing down a large number of small ones, the interest is clearly not there. The strategy, as you have adequately described it, is employed elsewhere in the UK and has been for some time, but it is not employed in the subject area.

George Lyon: It must have knock-on effects for the area that we are discussing, in that there is not a lot of interest in what happens in that area. That leaves the Highlands and Islands and rural Scotland out of the interest of the major insurers to ensure that a competitive price is offered so that we get the same benefits as those in urban

Scotland and the rest of the UK, where there is real competition.

Ray Holloway: The three brands represented here are all very jealous of their national presence. I therefore see risk of any of them withdrawing from any of the subject areas. There are many ways to operate in our industry; the one that we have here is perfectly acceptable. The differential in pump price is the emotional part of all of this. It has come about because of the damaging price war that the major oil companies have engaged in with the hypermarkets in the populated areas, and because of high taxation. High taxation does not get in the way of either the hypermarket or the major company reducing prices to the point at which they are at cost or below if it suits them. That does not have to apply to less competitive areas, and therefore it does not.

Fergus Ewing: On 16 November last year, the director general of fair trading, John Bridgeman, informed me in a letter that the purpose of the Office of Fair Trading inquiry is

"to see whether competition problems rather than just the higher costs of distribution are the cause of high fuel prices in the Highlands and Islands."

If that is the remit of the OFT inquiry, does it not allow the OFT to include all the aspects that you have mentioned that you feel impinge upon competition? Are you saying that the remit of the OFT inquiry is somehow too narrow and limited?

Ray Holloway: I find it difficult to predict what Mr Bridgeman will accept. If the narrow view that he takes of competition law and how it applies to the UK fuels market is as consistent as his past record, he will find nothing wrong.

Fergus Ewing: Have you submitted evidence to the OFT? If not, will you do so in the course of this inquiry?

Ray Holloway: The Office of Fair Trading has received a great deal of evidence from the Petrol Retailers Association going back over a long period of time, but Mr Bridgeman has failed totally to study or respond to it. In the Office of Fair Trading report that was published in 1998, he did not include diesel in the survey at all, and did not correct that omission until we pointed it out. He also completely omitted to consider the motorway service area network, which is consistently priced above most other parts of the UK.

I have pointed out to Mr Bridgeman what he should examine in his inquiry. His response has been negative.

Fergus Ewing: How effective do you think the OFT is as a means of giving redress to Highlanders and Highland businesses?

Ray Holloway: If you will forgive a flippant response, you would not spot if he had measles.

The Convener: On that medical judgment, I close this evidence session. Thank you, Mr Holloway, for your attendance today and for the information that you have given us. As we take our inquiry further, we may want to speak to you and to other witnesses in due course.

The committee will now discuss the issues arising from the evidence that has been taken and will consider whether any other action is required. We have heard interesting information from a wide variety of perspectives, and many complex issues are involved. In the limited survey that we have conducted, we have heard the views of consumers, the fuel companies, observers and the OFT. There are many perspectives that we have to draw together.

With those comments, I open up for discussion the issues of how we will proceed and whether we wish to take additional steps.

17:00

George Lyon: At this time it is hard to draw together the conclusions from what we have just heard. We have heard a range of evidence that we need some time to think about. Issues have been raised about the competence of the OFT investigation and what it will deliver, and we have to take that into account. In addition, the timing of the OFT report is important. I suggest that we have a session at the beginning of our next meeting, after we have had a little time to reflect on what was said today.

Miss Goldie: I support that view. In particular, the last submission was only received by us today, and I must confess that I was reading it as Mr Holloway was making his submission. That is not a structured way in which to consider evidence. Also, I feel that we have been presented with a great deal of complex information—I have been taking my own notes—and I welcome an opportunity for the clerk to formulate a note of evidence and for us to read the *Official Report*. George is right. It would be premature to try to arrive at any sensible conclusions until we have an opportunity to look at the evidence that was presented today.

Fergus Ewing: I felt that the evidence that emerged today undermined the OFT inquiry in relation to the limited nature of the evidence and the approach taken in its previous report. I am concerned that the report is not going to achieve anything. However, Mr Holloway's evidence is such that those whom he criticised—the oil companies—should be given an opportunity to respond. Natural justice requires that, and the question is whether that is done now, while they are here, or, if they have had enough at the end of a long day, whether we invite them to make written submissions to us in a short time period. I, for one, would like to hear their responses to the serious charges that Mr Holloway made.

Allan Wilson: That is a fair point. I am not sure whether our deliberations supplement or complement the activities of the OFT in this area. As ever, there is a common approach in this committee. Given that we invited a number of witnesses to supplement their submissions, and that others volunteered to do so, and that there were contradictory statements, particularly latterly, from a number of witnesses, it would be sensible to receive written submissions to hear what the contradictory evidence is, if any, and to consider it in detail at our next meeting, with the clerks having gone over it in the interim.

The Convener: That was a helpful exchange of views. Clearly, there are different perspectives on issues that are of enormous significance to all the parties in the discussion that we had. It would be most appropriate for us to ask our clerk to produce a paper that we can consider at our next meeting, and to issue a copy of the *Official Report* to all the organisations that gave evidence, and ask them to make submissions to the clerk on the issues on which they wish to set the record straight.

In addition, our papers are available on the Parliament's website, and by other means. I am sure that there will be some press interest in what we have been discussing today. I hope that we will be able to draw together some more feedback on the issues that we have covered, and the clerks can draw it to our attention for our next meeting in about 10 days' time.

I will conclude by saying that the issues that have come out today—and certainly the formal way in which the OFT goes about its business by statute—suggest that the committee will have to do further work in this area if we wish to pursue some of the lines of evidence that we have heard. Some of the issues that we are concerned about may not naturally fit in with the issues that statute allows the OFT to examine. In that sense, we have a much deeper role to perform in searching for some of the answers on those issues.

To sum that up for the record, the committee is asking its clerk to come back with a report on the issues arising from this meeting. We are inviting all the contributors to reflect on the *Official Report* when it is published, which I assume will be tomorrow. The issues and evidence that have come out, and any other issues that are drawn to the attention of the clerks by any external parties, will be drawn to the attention of the committee in 10 days' time.

Fergus Ewing: If anybody who has given evidence today wishes to see the background papers that we received, I presume that they will have access to all those papers as well as the *Official Report*. Those papers contained a lot of information that we were not able to cover in the oral session today.

The Convener: None of the papers that we received today are in any way restricted, so they are available to members of the public on request.

Meeting closed at 17:06.

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