14. Conclusion and recommendations

14.1. The recommendations resulting from the market inquiry seek to introduce or encourage changes in the domestic LPG sector that will promote efficiency, improve security of supply, encourage investment and provide customers with competitive prices and product choices.

14.2. The recommendations have been summarised from the various sections of the report. The relevant sections should be referred to directly for more detail.

Recommendations on the regulatory issues identified

14.3. The Commission's analysis identified a need for measures aimed at improving the regulatory environment the LPG sector.

14.4. Regarding price regulation, the Commission found that the DoE has not been able to finalise its review of the MRGP since issuing a draft framework for comment in 2012, despite commitments that it would review the MRGP periodically. Similarly, the Commission found evidence that the MRP framework has not been updated since the regulation commenced in 2010. The Commission recommends the following:

14.4.1. NERSA must undertake pricing and the monitoring of MRGP and MRP.

14.4.2. Price deregulation after supply constraints have been resolved. The reason for this is that the immediate deregulation of pricing may cause price increases above the current MRGP and consequently MRP, given the significant regulatory bottlenecks identified as well as the supply constraints faced by the sector. To circumvent this concern, the Commission is of the view that import efficiency and optimisation should be prioritised. This would result in an increase in import storage capacity and make it possible to accommodate larger LPG parcels, allowing for an increase in LPG supply domestically.

14.4.3. To give effect to the recommendation in 14.4.2. above, the DoE must undertake a study on how price deregulation in the LPG industry can be achieved.

14.5. The Commission is of the view that the deregulation of prices in the sector must be regarded as a long-term solution and should only be considered after the existing supply bottlenecks have been resolved. The priority in the short-term must be to improve import efficiency, increase import storage capacity and accommodate larger LPG parcels in order to allow for an increase in LPG supply domestically.

14.6. In terms of non-price regulation, the Commission found that the LPG sector has a number of regulators, regulations and licensing requirements at different levels of the value chain. These regulators were found to have overlapping jurisdictions, leading to projects being stalled. Overlapping jurisdictions between NERSA and the TNPA have resulted in delays and cost escalation in relation to approvals for the construction of import and storage facilities at the ports. The Commission recommends the following:

14.6.1. NERSA must be the regulator responsible for issuing wholesale licences and the monitoring thereof. NERSA is also involved in licensing import, loading and storage facilities for market participants including wholesalers.

14.6.2. NERSA and the TNPA's adjudication processes should be aligned to avoid delays in the construction of import and storage facilities and resolve the issues identified. As an MOU has been signed between the two entities, the Commission recommends that it be used as a mechanism to give effect to this recommendation. In addition, there should also be a sequencing of legal processes.

Recommendations on the limited domestic supply

14.7. The Commission's analysis found that the limited domestic production of LPG necessitates that imports must be used to fill in gaps in the supply of same. The Commission also found that the current inadequate import infrastructure has stifled the uptake of LPG. In particular, the Commission found that significant obstacles are caused by the overlapping jurisdictions of NERSA and the TNPA in relation to approvals for the construction of import and storage facilities at the ports. The Commission recommends the following:

14.7.1. A review of the regulatory frameworks applicable to the construction of LPG import and storage facilities at ports, as outlined in the applicable legislation including the National Ports Act and the Petroleum Pipelines Act.

Recommendations on the long-term LPG supply agreements

14.7. The Commission's analysis found that long-term supply agreements offered by the refineries to large wholesalers have conferred some degree of competitive advantage to these wholesalers. The Commission also found that these long-term supply agreements are offered on a preferential basis, which has allowed the major/large wholesalers to maintain their positions in the market regardless of new entry.

14.8. The competitive position of a wholesaler (large or small) is dependent on its ability to obtain a sufficient and consistent supply of LPG. Accordingly, the Commission is of the view that the market is likely to be more competitive if smaller wholesalers are able to secure sufficient volumes of LPG on a consistent basis. This has been clearly demonstrated by the price competitiveness of the smaller wholesalers who have been able to secure LPG volumes.

14.9. The Commission recommends the following:

14.9.1. Existing evergreen agreements or agreements with more than a ten-year duration must be capped to a maximum of ten years.

14.9.2. All automatic renewal clauses must be removed from all supply agreements.

14.9.3. Refineries must allocate a minimum of ten percent of LPG production (excluding internal consumption) to small wholesalers[270] on at least two-year supply agreements.

14.10. These recommendations are a short-term solution to the supply constraints in the LPG sector, as it is envisaged that within five years South Africa's LPG import infrastructure and the storage facilities at its ports will support increased LPG imports, averting the domestic supply shortage.

Recommendations on the sale of LPG through cylinders

14.11. The Commission's analysis found that contrary to the terms of the MRP Working Rules (2010), cylinder deposit fees have not been reviewed since 2010. In addition, the Commission has reason to believe that collusion in fixing cylinder deposits has taken place in this sector and that this conduct is likely to be continuing. The Commission recommends the following:

270 The definition of a small wholesaler proposed by the Commission is any wholesaler that requires between 2 500 and 10 000 tonnes of LPG per annum. This definition was determined using the average volumes supplied to [redacted] and [redacted] over the 2010 – 2014 period.

14.11.1. NERSA must be responsible for the determination of the cylinder deposit fees and must review same on an annual basis, so that they are aligned with changes in market conditions.

14.11.2. The deposit fee for each cylinder size must be linked to the cost of the cylinder.

14.12. The Commission will continue with its ongoing cartel investigations separate from the market inquiry process.

14.13. In relation to the cylinder exchange practice, the Commission recommends the following:

14.13.1. The cyclinder exchange practice must be more inclusive. No wholesaler should unreasonably deny another party the opportunity to enter a bilateral agreement to facilitate the exchange of cylinders. Any wholesaler who has invested in cylinders and complies with all relevant regulations, including those relating to safety, should not be barred from participating in cylinder exchange.

14.13.2. The current hybrid cylinder ownership model must continue to enhance customer choice. More specifically:

14.13.2.1. For 9 kg cylinders and below,[271] customers must have the choice to either lease a cylinder from a wholesaler or purchase a cylinder directly from a wholesaler or retailer.

14.13.2.2. If a customer chooses to lease the cylinder, they may only fill their cylinder at the respective wholesaler or its designated distributor or they may exchange the cylinder at any accredited cylinder exchange site.

14.13.2.3. If a customer chooses to purchase a cylinder, they may fill their cylinder at any accredited filling site.

271 The Commission notes that the logistics of handling and distributing a larger-sized cylinder (those larger than 9 kg) makes the cylinder exchange practice limited. The Commission notes that currently most wholesalers supply and fill these cylinders and as such, these cylinders are excluded from the Commission's recommendation outlined above as they do not ordinarily form part of the cylinder exchange practice.

14.14. Regarding cross-filling, the Commission recommends the following:

14.14.1. Cross-filling of LPG cylinders should occur within the confines of the law, which under section 10(4) of the OHSA requires written consent prior to a wholesaler filling the LPG cylinders of another wholesaler. The Commission is of the view that this practice must continue and the responsible enforcement authorities must impose the necessary sanctions to curtail any violation.

Recommendations on the high switching costs

14.14. The Commission recommends that the following measures be implemented to facilitate switching:

14.15. The Commission recommends the following:

14.15.1. Separating the LPG supply agreement from the LPG equipment agreement. The parties to any supply agreement must separate the agreement in relation to the supply of LPG from that pertaining to the use of LPG equipment. The LPG equipment agreement must reflect the cost and usage of the installed LPG equipment, while the LPG supply agreement should reflect the cost of the supply of LPG. The agreement pertaining to the cost and usage of LPG equipment must provide for the end-user to own the installed equipment after the costs have been fully amortised; or, alternatively, it must be clear that the equipment is subject to a rental agreement. The contracts contemplated in this recommendation should, at a minimum, include the following terms:

14.15.1.1. By default, contracts between customers and wholesalers must contain provisions for transferring tanks, with a clear methodology for valuing the equipment.

14.15.1.2. Incoming suppliers must have a right, subject to a commercially agreeable arrangement, to buy the existing tank and piping equipment from the outgoing supplier. The incoming supplier must have two options: first, to negotiate with the incumbent for the transfer of the equipment; or, take over the equipment based on the existing terms between the customer and incumbent supplier. The outgoing supplier will have an obligation to sell the equipment at a price determined by applying the appropriate methodology.

14.15.1.3. Customers must be provided with information on how to switch in their contracts. This information must be clearly explained before they sign the contract, and both parties must sign a legal declaration to prove that this discussion took place. All future supply agreements must contain this legal declaration and that it must be added as an addendum to supply agreements already in existence.

14.15.2. Guidelines for the valuation methodology of LPG equipment. In order to facilitate the transfer of LPG equipment and reduce any potential impediments in commercial negotiations relating to same, NERSA must develop and publish guidelines setting out the appropriate valuation methodology that market participants can use for the sale and transfer of bulk installation LPG equipment (e.g. bulk tanks, cylinder manifold and reticulation system). This is specifically in relation to those instances wherein a new LPG supplier seeks to purchase existing and previously used LPG equipment from the incumbent supplier for the purposes of supplying a bulk customer.

14.15.3. The mandate of NERSA must be expanded to include the resolution of disputes relating to the interpretation and application of the valuation methodology of LPG equipment. In the event of a dispute in the interpretation and application of the valuation methodology for the transfer of LPG equipment, such disputes should be referred to NERSA.

14.16. Table 25 provides a comprehensive summary of all the Commission's findings and applicable recommendations. This table outlines the relevant regulatory bodies and market participants deemed responsible for implementing the recommendations.

Table 25: Implementation plan for LPG market inquiry recommendations

Sections	Commission's findings	Commission's recommendations	Who will implement	Timeline
Section 7: **Non-Pricing Regulation**	The overlap in mandates and misaligned regulatory between NERSA and TNPA creates uncertainty amongst market participants regarding approvals for constructing import and storage facilities at the ports.	NERSA and the TNPA's adjudication processes should be aligned. The MOU signed between the two regulators should be used as a mechanism to give effect to the recommendation. In addition, there should also be a sequencing of legal processes.	DoE in consultation with NERSA and TNPA	20 June 2018
	Lack of monitoring of wholesale licensees.	NERSA to undertake wholesale licensing activities.	DoE	20 March 2019
Section 8: **Pricing regulation**	MRGP and MRP methodology had not been periodically reviewed. Lack of monitoring of adherence to the MRGP and MRP by the DoE.	NERSA to undertake pricing and the monitoring of MRGP and MRP.	DoE	20 March 2019
	Import efficiency and optimisation should be prioritised.	DoE to undertake a market study on how price deregulation can be achieved in the LPG industry.	DoE	20 March 2019
	MRGP in its current form is not creating an incentive for refineries to expand their production and storage capacity of LPG.	Price deregulation once sufficient supplies of LPG in the domestic market are established.	DoE	To be implemented following the recommendations of the Market Study
Section 9: **Addressing the limited domestic supply of LPG**	The significant bottlenecks are caused by the overlapping jurisdictions of NERSA and the TNPA in relation to approvals for constructing import and storage facilities at ports.	The Commission recommends a review of the applicable regulatory frameworks, relating to LPG construction and storage facilities at ports, as outlined in applicable legislation, including the Petroleum Pipelines Act and the National Ports Act.	DoE in consultation with the Department of Transport	20 June 2018

Sections	Commission's findings	Commission's recommendations	Who will implement	Timeline
Section 10: **LPG supply agreements with refineries**	Wholesalers with long-term contractual agreements have a competitive advantage over those that rely on short-term contracts or the spot market.	Existing evergreen agreements or agreements with over ten year duration should be capped to a maximum of ten years.	Refineries and wholesalers	30 September 2017
	There is evidence of contracts with some large wholesalers that included unlimited renewal clauses. These clauses have the effect of making them "evergreen contracts".	The automatic renewal clauses should be removed from all supply agreements.	Refineries and wholesalers	30 September 2017
	Smaller wholesalers are unable to attain economies of scale due to the existence of the long-term contractual agreements in place.	10% allocation should be made available through a supply agreement with at least two year duration.	Refineries and wholesalers	30 September 2017
Section 11: **Possible co-ordinated behaviour**	DoE had not reviewed the deposit fees since 2010 in terms of the MRP Working Rules (2010.	DoE to amend the MRP Working Rules to enable NERSA to undertake the determination of deposit fees. NERSA to undertake the determination of deposit fees and the subsequent annual reviews.	DoE and NERSA	20 March 2019
Section 12: **The sale of LPG through cylinders**	The cylinder exchange practice acts as a potential barrier to entry into the cylinder market as it is governed through bilateral agreements and participation by new entrants has been difficult.	The cylinder exchange practice should be more inclusive, any unjustifiable restrictions in place should be removed. No wholesaler should unreasonably be denied the opportunity by another party to enter a bilateral agreement to facilitate the exchange of cylinders.	Wholesalers and distributors	30 September 2017

Sections	Commission's findings	Commission's recommendations	Who will implement	Timeline
Section 13: **The high cost of switching**	Bulk LPG supply agreements are structured in a vague manner regarding equipment ownership during and after the expiration of the initial supply agreement. There is limited disclosure of when the costs of the installed LPG equipment will be fully amortised and whether the end-user will ever own the installed equipment. The majority of cases, equipment ownership lies with the wholesale supplier and that equipment ownership is not transferred to the bulk end-user at the end of the term.	Recommends separating the LPG supply agreement from the LPG equipment agreement. The agreement pertaining to the cost and usage of LPG equipment should provide for the end-user to own the installed equipment after the costs have been fully amortised; or, alternatively, it should be clear that the equipment is subject to a rental agreement.	Wholesalers and end-users	30 September 2017
	Limited disclosure of the salient features of supply agreements creates an environment wherein end-users are unable to switch seamlessly at the end of a contractual period.	The mandate of NERSA must be expanded to include the resolution of disputes relating to the interpretation and application of the *valuation methodology of LPG equipment.* NERSA to develop and publish a bulk LPG equipment installation valuation methodology. NERSA to adjudicate on disputes in the valuation of bulk equipment and installations leading to switching impediments.	NERSA	30 June 2018