I. Introduction

The Federal Trade Commission (“Commission” or “FTC”) has issued a complaint (“Complaint”) alleging that the proposed merger of Chevron Corporation (“Chevron,” formerly ChevronTexaco Corporation) and Unocal Corporation (“Unocal”) (collectively “Respondents”) would violate Section 7 of the Clayton Act, as amended, 15 U.S.C. § 18, and Section 5 of the Federal Trade Commission Act, as amended, 15 U.S.C. § 45, and has entered into an agreement containing consent order (“Agreement Containing Consent Order”) pursuant to which Respondents agree to be bound by a proposed consent order (“Proposed Consent Order”). The Proposed Consent Order remedies the likely anticompetitive effects arising from Respondents’ proposed merger, as alleged in the Complaint.

II. Description of the Parties and the Transaction

A. Chevron

Chevron is a major international energy firm with operations in North America and about 180 foreign countries in Europe, Africa, South America, Central America, Indonesia, and the Asia-Pacific region. Its petroleum operations consist of exploring for, developing and producing crude oil and natural gas; refining crude oil into finished petroleum products; marketing crude oil, natural gas, and various finished products derived from petroleum; and transporting crude oil, natural gas, and finished petroleum products by pipeline, marine vessels, and other means. The company operates light petroleum refineries for products such as gasoline, jet fuel, kerosene and fuel oil at Pascagoula, Mississippi; El Segundo, California; Richmond, California; Salt Lake City, Utah; and Kapolei, Hawaii. Chevron is a major refiner and marketer of gasoline that meets the requirements of the California Air Resources Board (“CARB”). Chevron also has operations for the manufacture and marketing of commodity petrochemicals for industrial uses and additives for fuels and lubricants. For 2004, the company had total revenues of approximately $155.3 billion and total assets of approximately $93.2 billion.

B. Unocal

Unocal is also a major international energy firm with operations in North America, Asia, and other locations around the world. Its primary activities are oil and gas exploration, development and production. It has oil and gas operations located in various countries, including Thailand, Myanmar, Indonesia, Azerbaijan, Bangladesh, and Vietnam. Unocal sold most of its downstream operations in the United States to another company in the mid-1990's. As a result, Unocal has no downstream operations in refining or gasoline retailing, and with a few exceptions almost all of Unocal’s operations are in the upstream segment of the industry, i.e., exploration and production. The company had total revenues for 2004 of approximately $8.2 billion and total assets of approximately $13.1 billion.
III. The Transaction

Pursuant to an Agreement and Plan of Merger dated April 4, 2005, Chevron plans to acquire 100% of the voting securities of Unocal. Unocal will merge into a direct wholly-owned subsidiary of Chevron, with the subsidiary continuing as the surviving entity and a wholly-owned subsidiary of Chevron. Under the terms of the agreement, Unocal shareholders may elect to receive 1.03 shares of Chevron stock, $65 in cash, or the combination of $16.25 in cash and 0.7725 of a share of Chevron common stock. The election is subject to the limitation that 75% of the outstanding shares of Unocal common stock will be exchanged for Chevron common stock and 25% will be exchanged for cash, with prorationing in the event the cash election is oversubscribed or undersubscribed. The total value of the transaction is estimated at approximately $18 billion, which includes approximately $1.6 billion in assumed debt.

The transaction is subject to various closing conditions, including the approval of Unocal shareholders and the expiration or early termination of the waiting period under the Hart-Scott-Rodino Act, 15 U.S.C. § 18A. The parties expect to close the transaction as soon as practicable after the last of the conditions to closing have been satisfied.

IV. The Complaint

The Complaint alleges that the merger of Chevron and Unocal would violate Section 7 of the Clayton Act, as amended, 15 U.S.C. § 18, and Section 5 of the Federal Trade Commission Act, as amended, 15 U.S.C. § 45, by substantially lessening competition in the refining and marketing of reformulated gasoline that has been approved by the California Air Resources Board (“CARB”) for sale in California. Through its wholly-owned subsidiary, Union Oil Company of California (“Union Oil”), Unocal owns a portfolio of five U.S. patents relating to reformulated gasoline (“RFG”). These patents (the “Relevant U.S. Patents”) cover the production and supply of CARB RFG, particularly in warmer weather months. To remedy the alleged anticompetitive effects of the merger, the Proposed Consent Order requires Respondents to take certain actions, including (1) to cease and desist from any efforts to assert or enforce any of the Relevant U.S. Patents against any person, to recover any damages or costs for alleged infringements of any of the Relevant U.S. Patents, or to collect any fees, royalties or other payments for the practice of the Relevant U.S. Patents; and (2) to take the necessary actions to dedicate to the public the remaining terms of the patents.

According to the Complaint, gasoline is a motor fuel used in automobiles and other vehicles. It is produced in various grades and formulations, including conventional unleaded gasoline, low emissions reformulated gasoline (“RFG”), California Air Resources Board (“CARB”) compliant reformulated gasoline, and others. CARB compliant reformulated gasoline (“CARB RFG”) is a type of gasoline that meets the specifications of the California Air Resources Board. CARB RFG is cleaner burning and causes less air pollution than conventional unleaded gasoline. The sale of any gasoline other than CARB RFG is prohibited in California, and there is no substitute for CARB RFG as a fuel for automobiles and other vehicles that use
gasoline purchased in California. As a result, CARB RFG is a relevant line of commerce in which to analyze the potential effects of the merger.

CARB RFG is produced primarily in California and at a few other locations on the West Coast. The Complaint alleges that the state of California, and smaller areas contained therein, are relevant sections of the country in which to analyze the potential effects of the merger.

Chevron is a leading refiner and marketer of CARB RFG. Unocal does not refine or market CARB RFG. However, through its wholly-owned subsidiary, Union Oil, Unocal owns Relevant U.S. Patents relating to CARB RFG. Refiners must use the technology covered by the Unocal Relevant U.S. Patents for producing CARB RFG during warmer weather months – i.e., CARB “summertime” gasoline. Thus, Unocal controls an important input used by CARB refiners to produce CARB gasoline.

Unocal licenses its RFG patents to others in exchange for payments ranging from 1.2 to 3.4 cents per gallon. In addition, Unocal has won a patent infringement suit against major refiners of CARB RFG and obtained a court judgment awarding Unocal royalties of 5.75 cents per infringing gallon produced in California.

There are relatively few producers of CARB RFG. As a result, the relevant markets for the refining and marketing of CARB RFG are either highly concentrated or moderately concentrated. The Complaint further alleges that entry into the relevant lines of commerce in the relevant sections of the country is difficult and would not be timely, likely or sufficient to prevent anticompetitive effects resulting from the proposed merger.

The Complaint states that, because of factors such as Unocal’s perception of possible actions by the California Air Resources Board or other governmental authorities, Unocal is likely to be constrained in charging the full monopoly level price to licensees of the Unocal patents. Moreover, Unocal has no operations at downstream levels of the industry through which it could attempt to recoup any additional profits.

Because of its significant operations at the refining and marketing levels, Chevron will have a greater ability than Unocal to obtain additional profits by coordinating with its competitors at the downstream refining and marketing levels. As part of Unocal’s license agreements, Unocal regularly collects detailed reports from licensees about their production of CARB RFG and other refinery operations. By obtaining the Unocal patents, Chevron would receive additional information about the production of competitors and other information not otherwise available to members of the industry. Chevron could facilitate coordination among refiners and marketers of CARB RFG by using this information to monitor a collusive agreement and thus detect cheating on a collusive agreement. The anticompetitive effects from such coordination would be likely to outweigh any efficiencies that would be obtained by the integrated firm.
As a result, the Complaint charges that the effect of the proposed merger, if consummated, may be substantially to lessen competition in the marketing and refining of CARB RFG in the relevant sections of the country, in violation of Section 7 of the Clayton Act, as amended, 15 U.S.C. § 18, and Section 5 of the Federal Trade Commission Act, as amended, 15 U.S.C. § 45.

V. Resolution of the Competitive Concerns

The Commission has provisionally entered into an Agreement Containing Consent Order with Chevron and Unocal in settlement of the Complaint. The Agreement Containing Consent Orders contemplates that the Commission would issue the Complaint and enter the Proposed Consent Order requiring the relief described below.

In order to remedy the anticompetitive effects that have been identified, Chevron and Unocal have agreed to take several actions. First, they will cease and desist from any and all efforts, and will not undertake any new efforts, to assert or enforce any of Unocal’s Relevant U.S. Patents against any person, to recover any damages or costs for alleged infringements of any of the Relevant U.S. Patents, or to collect any fees, royalties or other payments, in cash or in kind, for the practice of any of the Relevant U.S. Patents, including but not limited to fees, royalties, or other payments, in cash or in kind, to be collected pursuant to any License Agreement. These obligations become effective as of the “Merger Effective Date,” which is defined as the earlier of (1) the date that the certificate of merger for the Merger is filed with the Secretary of State of Delaware or such later time as specified in such certificate of merger, or (2) the date that Chevron acquires control of Unocal Corporation, as “control” is defined by 16 C.F.R. § 801.1(b).

Second, the Proposed Consent Order requires that, within thirty (30) days following the Merger Effective Date, Respondents shall file, or cause to be filed, with the United States Patent and Trademark Office, the necessary documents pursuant to 35 U.S.C. § 253, 37 C.F.R. § 1.321, and the Manual of Patent Examining Procedure to disclaim or dedicate to the public the remaining term of the Relevant U.S. Patents. The Proposed Consent Order further requires that Respondents shall correct as necessary, and shall not withdraw or seek to nullify, any disclaimers or dedications filed pursuant to the order.

Third, the order requires that, within thirty (30) days following the Merger Effective Date, Respondents shall move to dismiss, with prejudice, all pending legal actions relating to the alleged infringement of any Relevant U.S. Patents, including but not limited to the following actions pending in the United States District Court for the Central District of California: Union Oil Company of California v. Atlantic Richfield Company, et al., Case No. CV-95-2379-CAS and Union Oil Company of California v. Valero Energy Corporation, Case No. CV-02- 00593 SVW.

Paragraph V of the Proposed Consent Order requires Respondents to distribute a copy of the Order and the Complaint in this matter to certain interested parties, including (1) any person...
that either Respondent has contacted regarding possible infringement of any of the Relevant U.S. Patents, (2) any person against which either Respondent is, or was, involved in any legal action regarding possible infringement of any of the Relevant U.S. Patents, (3) any licensee or other person from which either Respondent has collected any fees, royalties or other payments, in cash or in kind, for the practice of the Relevant U.S. Patents, and (4) any person that either Respondent has contacted with regard to the possible collection of any fees, royalties or other payments, in cash or in kind, for the practice of the Relevant U.S. Patents.

Paragraph V also requires Respondents to distribute a copy of the Order and the Complaint to present and future officers and directors of Respondents having responsibility for any of Respondents’ obligations under the Order, and to employees and agents having managerial responsibility for any of Respondents’ obligations under the Order.

Paragraphs VI, VII and VIII of the Proposed Consent Order contain standard reporting, access, and notification provisions designed to allow the Commission to monitor compliance with the order. Paragraph IX provides that the Order shall terminate twenty (20) years after the date it becomes final.

VI. Opportunity for Public Comment

The Proposed Consent Order has been placed on the public record for thirty (30) days for receipt of comments by interested persons. Comments received during this thirty day comment period will become part of the public record. After thirty (30) days, the Commission will again review the Proposed Order and the comments received and will decide whether it should withdraw from the Proposed Order or make final the agreement’s Proposed Order.

By accepting the Proposed Order subject to final approval, the Commission anticipates that the competitive problems alleged in the Complaint will be resolved. The purpose of this analysis is to invite public comment on the Proposed Order, and to aid the Commission in its determination of whether it should make final the Proposed Order contained in the agreement. This analysis is not intended to constitute an official interpretation of the Proposed Order, nor is it intended to modify the terms of the Proposed Order in any way.