Statement of The Federal Trade Commission

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Mr. Chairman, our thanks to you and the Committee for the opportunity to discuss the Federal Trade Commission's role in enforcing the antitrust laws to protect consumers in the petroleum industry. The Commission shares the view that a viable and competitive energy sector is vitally important to the economic health of the United States and the world. The Commission has an extensive history of carefully examining mergers in the petroleum industry, and has used its authority to enforce the antitrust laws to assure that mergers in this industry do not lead to lessened competition or its consequence - higher prices for gasoline and other fuels, and the consequent harm to the economy of the nation or of any region.

As has been publicly observed, the combination of Exxon and Mobil is the largest industrial merger ever, and will create the largest private oil company worldwide and the largest US-based company of any type (by revenues). Today, Exxon and Mobil face each other at just about every level of the industry - exploration for and production of crude oil, refining of crude oil into petroleum products, manufacture of petrochemicals and lubricants, and the marketing of gasoline and other fuels in many parts of the United States (in particular the northeast, the Gulf Coast, and California). Exxon/Mobil is likely to be the largest or one of the largest players in each of these market sectors.

Obviously, a transaction of this size alone merits our close attention. As antitrust enforcers, we need to consider whether Exxon/Mobil's size - or other attributes - will change the competitive dynamics of this industry. This merger will be scrutinized carefully, not only by us and by our colleagues, 21 State Attorneys General, but also by antitrust enforcers in Europe and possibly elsewhere.

As you know, the Commission cannot comment in any detail on the specifics of any pending nonpublic law enforcement investigation. However, the Commission can provide a general discussion of how it approaches its merger investigation responsibilities, the special issues that arise with respect to petroleum industry mergers, and our prior enforcement experiences in this sector. We will begin by reviewing recent merger activity in the petroleum industry, and then describe how antitrust analyzes mergers generally, as well as in this sector specifically, and the relief we are authorized to seek.

As many have noted, this merger does not occur in a vacuum, but appears to be part of an ongoing trend of consolidation and concentration in this industry. In recent months, we have seen the merger of BP and Amoco - which was the largest industrial merger in history until Exxon/Mobil was announced -- and the combination of the refining and marketing businesses of Shell, Texaco and Star Enterprises to create the largest refining and marketing company in the United States. In addition, Tosco acquired Unocal's California refineries and marketing business; Ultramar Diamond Shamrock acquired Total's North American refining and marketing operations; and Marathon and Ashland combined their refining and marketing businesses. We also have seen the worldwide combination of the additives businesses of Shell and Exxon. Other combinations, such as the pending combination of the refining and marketing businesses of Ultramar Diamond Shamrock and Phillips (which we are currently examining), likely will follow. These consolidations and joint ventures are not limited to the United States: BP and Mobil have combined their refining and marketing operations in Europe, and Total and Petrofina have recently announced their own merger plans.

This is the second wave of consolidation in this industry in the last 20 years. The first wave, in the 1980s, saw Mobil's attempted takeover of Marathon, which was blocked by the courts,[(2)] and the mergers of Standard of California and Gulf (into Chevron) and Texaco's acquisition of Getty, as well as many smaller deals.

During that earlier merger wave and today, the Federal Trade Commission has carefully reviewed each proposed merger, and intervened where appropriate to prevent those mergers from significantly reducing competition in any sector of this industry that affects the United States or its citizens. The Commission's inquiry is and has been to determine whether a merger would make it substantially likely that the remaining firms in the industry could reduce output and raise prices by even a small amount, to the detriment of consumers and, in this industry in particular, of the competitiveness of the American economy or the economy of any particular region. This is the goal of antitrust enforcement across all industries; its vital role is particularly clear in the petroleum industry, where even small price increases can have a direct and lasting impact on the entire economy.

As a general matter, the Commission approaches its antitrust mission by examining the areas in which merging companies compete, looking at the existing state of competition in that marketplace and the likely changes in that marketplace in the future - both from new competition entering and from existing competition exiting. We also look at the effect of recent mergers on competition in the particular marketplaces at issue. And we look at the trends in the industry, including trends toward further concentration. The Commission has recognized the existence of such a trend toward consolidation in this industry.[(3)]

We also want to know whether a merger will yield efficiencies that might counteract the anticompetitive effects the merger would otherwise threaten. Merely claiming cost savings is not enough to allow an anticompetitive merger. The cost savings must be real; they must be substantial; they cannot themselves result from reductions in output; they cannot be practicably achievable by the companies independently of the merger; and they must counteract the merger's anticompetitive effect - not merely flow to the shareholders' bottom line.

In examining mergers, particularly in this industry, the Commission recognized - and continues to recognize - that it must look both at broad effects on broad markets, such as the worldwide crude oil market, and narrow effects on specific local and regional markets. A merger that did not substantially reduce competition nationally might nonetheless substantially reduce competition in specific parts of the country - as the Commission found in both *BP/Amoco* and *Shell/Texaco.* When the anticompetitive problems could be isolated, and when businesses and operating assets could be divested to new competitors and thereby restore the competition lost by the merger, the Commission has frequently entered into consent orders allowing the merger to proceed while preventing the anticompetitive harm through divestiture. When, however, anticompetitive problems infect the entire merger, so that there is no practical way to allow the companies to merge without threatening consumers with a substantial loss of competition, the Commission can go to federal district court to seek an injunction blocking the merger. The Commission has not hesitated to seek to block mergers, in this industry and elsewhere, where other remedies were insufficient.[(4)]

In the petroleum industry, we apply these general points of antitrust analysis by looking at each level of production separately. Some firms, such as Exxon and Mobil, are vertically integrated through all levels of the industry; there are "upstream only" companies, such as Unocal and Occidental, that are only engaged in exploration and production; "downstream only" companies, such as Tosco and Ultramar Diamond Shamrock, that are only engaged in refining and marketing; and other firms that are even more specialized. Most firms do not operate at every level in every geographic market. Therefore, the Commission begins its analysis by asking at what specific level do these companies compete, and who else competes with them at that level.[(5)]

Exploration and Production. In looking at the "upstream" or exploration and production sector, we observe that the crude oil market is for most purposes a worldwide market.[(6)] We recognize that major oil producing nations (such as Saudi Arabia, Iran, Iraq and Venezuela) are significant factors in this worldwide market. Consolidation in this industry in the 1980s does not appear to have given the merging companies, such as Standard of California and Gulf into Chevron, or Texaco and Getty, the ability to increase the price of crude oil by withholding production or exploration and development of reserves. That does not necessarily mean that *further* consolidation in exploration and production will be equally harmless. It may well be that the Exxon/Mobil merger will not reduce competition in the worldwide crude oil market. However, because of the significance of this merger to the industry, creating the world's largest privately owned oil producer, it is important for the Commission to examine carefully its likely effects on the exploration and production sector.

Refining. Mergers involving oil refineries have long been a matter of intense interest to the Commission. The nation's principal refining market, the Gulf Coast, not only supplies that immediate area, but also sends substantial amounts of gasoline by pipeline to the southeast, the northeast and the midwest. It is vitally important for nearly all of this country east of the Mississippi to maintain a competitive Gulf Coast refining market. Similarly, we must ensure that the pipelines that deliver Gulf Coast product to these markets remain competitive. In the

1980s, the Commission acted to preserve competition in Gulf Coast refining in connection with Standard of California's merger with Gulf by requiring the divestiture of a Louisiana refinery and an interest in the Colonial Pipeline, one of the two pipelines that carries gasoline and other fuels from the Gulf Coast to southeastern and northeastern markets. When Shell and Texaco combined their refining and marketing arrangements, the Commission required a similar pipeline divestiture.[(7)]

Not all parts of the country have access to Gulf Coast gasoline supply, and some areas - in particular the Rocky Mountains and the West Coast - have substantially less refinery competition. Not surprisingly, these areas also tend to have higher prices for gasoline and other fuels. In *Shell/Texaco*, we therefore prevented the parties from combining two of the four major refineries in the Pacific Northwest. One refinery that the Commission required to be divested also supplied California markets, and its operation by a new competitor in West Coast markets should ameliorate some of the effects of concentration in California.

Even so, California refining markets remain an area of concern to the Commission. Our colleagues at the Energy Information Administration have studied the tight supply situations in California, where the unexpected shutdown of even one refinery can significantly disrupt supply and lead to sharp price increases.[(8)] According to press reports, the tragic fire at Tosco's Avon refinery last month already has caused a 30% wholesale price increase in California, even though that refinery produces only six percent of California's gasoline needs.[(9)] While the supply disruption caused by that fire obviously does not raise antitrust issues itself, it does show how a small reduction of supply by firms in a concentrated market can provoke huge price increases.

Refineries -- and oil companies -- make more than just fuels. The Commission has examined refinery mergers and other oil company combinations to ensure that competition will not be reduced in petrochemical and lubricant markets. After examining the proposed joint venture combining Shell's and Exxon's additive business, the Commission ordered divestiture of Exxon's viscosity index improver business to Chevron, rather than allow them to create a joint venture that would have controlled more than half of the U.S. market for that motor oil additive.

Gasoline Marketing. The Commission is also concerned about the risk to competition in the marketing of gasoline and other fuels once they leave the refinery and reach their local markets. On several occasions, the Commission has blocked mergers or demanded divestitures to prevent the elimination of competition at the terminal or tank farm level - thus ensuring that there are competitive sources of supply to local marketers.[(10)]

Competition between branded marketers in local markets can be reduced by merger. As a result, a relatively small number of branded marketers in a local gasoline market may have the ability to raise price oligopolistically, without fear that the price increase will be eroded by a small fringe of independent marketers or by new entry. That appeared to be the case in San Diego, California, where branded marketers were able to maintain higher prices even in a market defined as "moderately concentrated" by the *Merger Guidelines*. The Commission therefore ordered divestitures of gasoline stations in San Diego as a condition precedent to the *Shell/Texaco* merger, and is continuing to examine the marketing of gasoline in California. Based on this experience, the Commission in *BP/Amoco* required divestitures and other relief intended to prevent substantial increases in concentration in branded gasoline marketing.

Prior Commission Enforcement Actions. The Commission has examined every significant petroleum industry merger over the last 20 years, and has used its enforcement authority to protect consumers from petroleum mergers that would lessen competition on at least 10 occasions during that period, several of which I have already mentioned:

- In *BP/Amoco*, the Commission acted to preserve marketing competition in 30 local gasoline markets.

- In *Shell/Texaco*, the Commission acted to preserve competition in local gasoline markets in San Diego and Hawaii, and to preserve competition in broader refining and pipeline markets in the Pacific Northwest, California and the Southeast.

- In *Shell/Exxon (additives)*, the Commission required the joint venturers to sell Exxon's viscosity index improver business to Chevron, rather than allow them to create a joint venture that would have more than half the U.S. market for that motor oil additive.

- In *Shell/Exxon (Guam)*, the Commission prepared to challenge Shell's acquisition of Exxon's gasoline marketing on Guam, which would have left Guam with only two gasoline marketers - Shell and Mobil. The parties abandoned the deal.

- In *PRI/Shell*, the Commission prevented a merger that would have reduced gasoline marketing competition in Hawaii.

- In *Chevron/Gulf*, the Commission required the divestiture of a refinery and marketing assets in the southeast, as well as pipelines and other assets, to prevent a reduction in regional competition from that merger.

- In *Texaco/Getty*, the Commission required the divestiture of a refinery and marketing operations in the northeast, and pipelines and other assets, to prevent a reduction in regional competition from that merger.

These are all cases where the Commission believed that *local* or *regional* competition was sufficiently threatened to require enforcement action. We carefully tailored our relief to address the problems and to restore any competition that would have been lost from the merger or other combination. If competition could not be preserved through divestiture, the Commission has gone to court to block anticompetitive mergers in the petroleum industry in their entirety.

What we have learned from these and other investigations is that competition is critical to this industry and that concentration, as well as increases in concentration - even to levels that the antitrust agencies call "moderately concentrated" - can have substantial adverse effects on competition.

Our investigation of the Exxon/Mobil merger is still at an early stage, and neither the Commission nor its staff has reached any conclusions about the effects of the merger on competition, or whether the merger violates the antitrust laws in any respect. We are working closely with the Attorneys General of many of the states in which Exxon and Mobil compete, as well as with our European allies, to understand this merger and its likely effects on competition locally, nationally and internationally.

I can assure you that the Commission will examine these issues thoroughly and expeditiously. We appreciate the parties' pledge of full cooperation with our investigation, and we intend to rely on that cooperation to do our job quickly and completely.

Thank you.

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1. The written statement reflects the views of the Federal Trade Commission. My oral remarks and responses to questions reflect my views and are not necessarily the views of the Commission or of any Commissioner.

2. *Marathon Oil Co. v. Mobil Corp.*, 669 F.2d 378 (6th Cir. 1981).

3. Analysis to Aid Public Comment, *British Petroleum Company p.l.c.*, FTC File No. 981-0345 (Dec. 30, 1998). The Supreme Court has found the existence of a trend toward concentration to be highly relevant in examining the competitive consequences of a merger. *United States v. Pabst Brewing Co.*, 384 U.S. 546, 552-53 (1966); *United States v. Von's Grocery Co.*, 384 U.S. 270, 277-78 (1966); *United States v. Philadelphia Nat'l Bank*, 374 U.S. 321, 362-63 (1963).

4. In 1987, the Commission successfully challenged the proposed acquisition by Pacific Resources, Inc. of Shell Oil Company's assets in Hawaii, which the Commission believed (and proved) would reduce competition in the terminaling and wholesale marketing of gasoline and other fuels. In 1997, the Commission prepared to challenge Shell's proposed acquisition of Exxon's operations on Guam, which would have had a similar effect; the parties abandoned the transaction. Last year, the Commission successfully challenged proposed mergers among the nation's four largest drug wholesalers, which wanted to become two; the Commission recognized - and the Court agreed - that nothing short of a full stop injunction would preserve competition and prevent the elimination of two significant competitors. *FTC v. Cardinal Health, Inc.*, 12 F. Supp. 2d 34 (D.D.C. 1998).

5. For example, although BP and Amoco were each substantial companies, and their merger created the second largest privately owned oil company in the world (after the Royal Dutch/Shell Group), the Commission found that BP and Amoco did not overlap significantly in most of their operations, but did overlap in terminaling and wholesale marketing in particular geographic areas. In those areas where BP and Amoco would have substantial market shares, and there would be few significant competitors, the Commission required divestiture and other relief.

6. There can be specific local crude oil and natural gas production markets, and the Commission has acted to preserve competition in local crude markets. In both *Texaco/Getty* and *Shell/Texaco* the Commission required pipeline relief to prevent a lessening of competition in California heavy crude oil from harming refineries in the San Francisco Bay area that relied on that crude oil.

7. *Chevron Corp.*, 104 F.T.C. 597, 608 (1984); *Shell Oil Co.*, Docket No. C-3803 (April 21, 1998).

8. Energy Information Administration, "Motor Gasoline Assessment: Spring 1997," pp. 25-30 (1997).

9. "Refinery Closure Hasn't Hit Retail Gas Prices - Yet," *San Francisco Chronicle* (March 4, 1999).

10. *BP/Amoco*, FTC File No. 981-0345 (Dec. 30, 1998) (terminals in nine markets); *Shell/Texaco*, Docket No. C-3803 (April 21, 1998) (terminal in Oahu, Hawaii); *Shell/Exxon*, FTC File No. 971-0003 (terminal on Guam; transaction abandoned); *Sun/Atlantic* (1988) (terminals in Pennsylvania and New York); *FTC v. Pacific Resources, Inc.*, (1987) (terminal in Oahu, Hawaii); *Texaco, Inc.*, 104 F.T.C. 241 (1984); *Chevron Corp.*, 104 F.T.C. 597 (1984).