

# FEDERAL TRADE COMMISSION DECISIONS

Findings, Opinions and Orders

IN THE MATTER OF

SEARS, ROEBUCK AND COMPANY

MODIFYING ORDER IN REGARD TO ALLEGED VIOLATION OF  
SEC. 5 OF THE FEDERAL TRADE COMMISSION ACT

*Docket C-2885. Consent Order, April 20, 1977—Modifying Order, July 5, 1989*

This order reopens the proceeding and modifies the Commission's 1977 consent order [89 F.T.C. 240] by deleting the prohibition on respondent's use of radius clauses, modifying the prohibition on use clauses, and modifying the order so that when it applies to Sears in its capacity as a shopping center tenant it does so only when Sears is a major tenant.

ORDER REOPENING AND MODIFYING FINAL ORDER  
TO CEASE AND DESIST

On February 24, 1989, respondent Sears, Roebuck and Co. filed a "Petition to Set Aside Consent Order" ("Petition") asking the Commission to reopen and set aside the consent order issued in this matter on April 20, 1977, 89 FTC 240 (1977). In the event the order is not reopened and set aside in its entirety, Sears spells out in an "Alternative Proposed Modification of Order with Explanation" ("Alternative Proposal") specific modifications to the order that Sears requests for "all of the difficulties which have been caused to Sears by this order." Sears filed its request pursuant to subsection 5(b) of the FTC Act, 15 U.S.C. 45(b), and section 2.51 of the Federal Trade Commission Procedures and Rules of Practice, 16 CFR 2.51. One public comment was received.

The order prohibits Sears from, among other things, entering or enforcing certain restrictive lease or easement agreements in connection with its participation in regional and super regional shopping centers.<sup>1</sup> Sears operates department and specialty stores in shopping centers through its Sears Merchandise Group and engages in shopping center development and management through its Homart Development Co. See Petition at 25, 45.

<sup>1</sup> The order is limited to Sears' participation in shopping centers containing (1) 200,000 square feet or more of total floor area designed for retail occupancy, (2) at least two tenants other than respondent, (3) at least one major tenant other than respondent, and (4) on-site parking. See Paragraph I.(b).

Sears maintains in the Petition that changed conditions of fact and law require the Commission to reopen and set aside the order. Sears also requests that the Commission reopen and set aside the order in the public interest. In the event the Commission decides not to reopen the order in its entirety, Sears' Alternative Proposal asks the Commission to reopen and set aside or modify specific portions of the order that Sears finds particularly onerous and harmful to competition.

The Commission has carefully considered Sears' requests and has concluded that Sears has not made a satisfactory showing that reopening of the entire order is warranted based upon changed conditions of fact or law or in the public interest. Nor has Sears established that changed conditions require reopening of any prohibition in the order. However, the Commission has concluded that Sears has made a satisfactory showing that it would be in the public interest to reopen and set aside or modify several prohibitions in the order.

#### I. THE ORDER TO CEASE AND DESIST

The Commission issued its complaint and order on April 20, 1977, with the consent of Sears. *See Sears, Roebuck and Co.*, 89 FTC 240 (1977). The order prohibits five generic types of restrictions in shopping center leases or operating agreements, namely, (1) radius clauses, that is, restrictions on a tenant's ability to operate a like store within a specified distance of the shopping center; (2) use clauses specifying the types of products or services that tenants shall sell; (3) rights held by major tenants to approve or disapprove admission of other tenants into the shopping center; (4) clauses that require developers to exclude specified types of retail merchants or specifically named retail merchants; and (5) tying clauses that require a retail merchant in one shopping center to operate one or more stores in other shopping centers developed or managed by Sears.

#### II. STANDARD FOR REOPENING A FINAL ORDER OF THE COMMISSION

Section 5(b) of the Federal Trade Commission Act, 15 U.S.C. 45(b), provides that the Commission shall reopen an order to consider whether it should be modified if the respondent "makes a satisfactory showing that changed conditions of law or fact" so require. A satisfactory showing sufficient to require reopening is made when a request to reopen identifies significant changes in circumstances and

shows that the changes eliminate the need for the order or make continued application of the order inequitable or harmful to competition. S. Rep. No. 96-500, 96th Cong., 2d Sess. 9 (1979) (significant changes or changes causing unfair disadvantage); *Louisiana-Pacific Corp.*, Docket No. C-2956, Letter to John C. Hart (June 5, 1986), at 4.

Section 5(b) also provides that the Commission may modify an order when, although changed circumstances would not require reopening, the Commission determines that the public interest so requires. Respondents are therefore invited to show how the public interest warrants the requested modification. 16 CFR 2.51. In such a case, the respondent must demonstrate as a threshold matter some affirmative need to modify the order. *Damon Corp.*, Docket No. C-2916, Letter to Joel E. Hoffman, Esq. (March 24, 1983), at 2. For example, it may be in the public interest to modify an order to "relieve any impediment to effective competition that may result from the order." *Damon Corp.*, Docket No. C-2916, 101 FTC 689, 692 (1983). Once showing of need is made, the Commission will balance the reasons favoring the modification requested against any reasons not to make the modification. *Damon* Letter at 2. The Commission will consider whether the particular modification sought is appropriate to remedy the identified harm.

The language of section 5(b) plainly indicates that the burden is on the petitioner to make "a satisfactory showing" of changed conditions to obtain reopening of the order. The legislative history also makes clear that the petitioner has the burden of showing, by means other than conclusory statements, why an order should be modified. The Commission "may properly decline to reopen an order if a request is merely conclusory or otherwise fails to set forth specific facts demonstrating in detail the nature of the changed conditions and the reasons why these changed conditions require the requested modification of the order." S. Rep. No. 96-500, 96th Cong., 2d Sess. 9-10 (1979). If the Commission determines that the petitioner has made the necessary showing, the Commission must reopen the order to determine whether modification is required and, if so, the nature and extent of the modification. The petitioner's burden is not a light one in view of the public interest in repose and the finality of Commission orders. See *Federated Department Stores, Inc. v. Moitie*, 425 U.S. 394 (1981).

### III. SEARS' REQUEST TO REOPEN AND SET ASIDE THE ORDER IN ITS ENTIRETY

Sears requests that the order be reopened in its entirety either to set aside the order at this time or set a future date on which the order will expire. Sears, however, fails to show either changed conditions of law or fact that require reopening, now or in the future, or that such action is warranted in the public interest.

Sears first claims that recent changes of law now require that all restrictive shopping center covenants be judged under a rule of reason rather than the *per se* prohibitions contained in the Commission's order. Sears maintains that these restrictive covenants would be found to be reasonable under a reasonableness test. Sears relies upon *Continental T.V. Inc. v. GTE Sylvania, Inc.*, 433 U.S. 36 (1977), and the "accelerated trend away from widespread application of *per se* rules." See Petition at 4.

Although the *Sylvania* decision was a turning point in the law of vertical restraints, the Commission has consistently declined to reopen proceedings absent a specific showing that the order prohibits activity that subsequently has been found lawful.<sup>2</sup> Under a rule of reason analysis, the restraints in question here likely would not be found to restrain trade unreasonably absent a degree of market power. See *Northwest Wholesale Stationers, Inc. v. Pacific Stationery and Printing Co.*, 472 U.S. 284, 296 (1985). Sears, however, makes no showing either that the shopping centers it was associated with in 1977 did not possess market power or that the shopping centers it is associated with today do not possess market power. Without both showings, the Commission is unable to conclude that changes in law require reopening the entire order.

Additionally, Sears fails to make a sufficient showing that any factual changes in the shopping center industry occurring since the order was issued require reopening. Sears highlights an increase in the numbers of developers, major tenants, and mall tenants at a time when construction of new regional shopping centers "has virtually stopped;" an increase in the number of shopping centers built since the Commission's order was issued; and an increase in specialization of shopping centers. See Petition at 3. Sears also points to a trend toward the greater use of firms to manage shopping centers who do not have an ownership interest in the center. However, Sears has

<sup>2</sup> See *Encyclopaedia Britannica Inc.*, Docket No. 8908, Order Reopening the Proceeding and Modifying

failed to show how any of these changes alone or together eliminate the need for the order or make continued application of the order inequitable or harmful to competition.

Nor has Sears established sufficient public interest reasons to reopen the entire order. Sears claims that it is unfairly constrained by the order's prohibitions when most if not all competing tenants and developers in the shopping center industry are not so encumbered. According to Sears, it consented to the order because it believed that the Commission in the late 1970's was likely to issue a trade regulation rule for shopping centers that would proscribe the same activities prohibited by the order. However, that threatened trade regulation rule was never issued.

Although the reopening of several portions of the order may be in the public interest, Sears has not demonstrated that all of the order's provisions cause significant harm that outweigh the reasons not to make the modifications. Thus, Sears has not made a sufficient showing to warrant reopening the entire order in the public interest.<sup>3</sup>

#### IV. SEARS' REQUEST TO REOPEN PORTIONS OF THE ORDER

The Commission has carefully considered Sears' request that certain specific prohibitions need reopening and modification in the event the Commission does not reopen and set aside the entire order. These prohibitions include the prohibition of radius clauses, use restrictive clauses, clauses giving rights of prior approval to Sears in its capacity as a tenant, tying clauses used by Sears in its capacity as a developer, and the joint use of employees by Sears' Merchandise Group and Sears' shopping center development group. Sears seeks also modification to exclude from the order Sears in its capacity as a specialty tenant and Sears in its capacity as a minority investor or non-owner shopping center manager. *See Alternative Proposal.*

#### Radius Clauses

Sears challenges the continuing need for the prohibition against the use of radius clauses by Sears in its capacity as a developer. *See Paragraphs III.A.3.* Sears' petition describes the efficiencies gained from radius clauses. According to Sears, radius restrictions increase

<sup>3</sup> Sears requests also that the Commission sunset the order in three years. The age of an order, standing alone, is not sufficient to satisfy the standard for reopening in the public interest. Moreover, the Commission generally does not sunset orders that prohibit unlawful conduct. *See William H. Rorer, Inc.*, Docket No. 8599, Order Modifying Cease and Desist Order, 104 FTC 544, 545-46 (1984); *Corn Products Refining Co.*, Docket No. 5502, Letter to Morton M. Maneker, Esq. (August 22, 1985), at 7-8.

traffic in the shopping center by requiring the tenant to concentrate on its store in the shopping center. A nearby store could siphon away customers from the center.

Sears has made the necessary showing of affirmative need to reopen and modify the prohibition against radius clauses in the public interest. Sears presents examples where tenants in Sears-owned centers have opened retail locations in nearby centers to the detriment of Sears' shopping center. Sears' petition also documents industry-wide usage of radius restrictions. Radius clauses that are limited in scope may stimulate competition and are unlikely to be anticompetitive. In the absence of competitive concerns about these restrictions, the harm to Sears outweighs any reasons for retaining the prohibition, and reopening is warranted in the public interest. Under the circumstances, the Commission will reopen and set aside this prohibition as the appropriate remedy to address Sears' showing of affirmative need.

#### Use Clauses

Sears challenges the continuing need for the prohibition against the employment of use clauses by Sears in its capacity as a developer. Use clauses specify the types of products or services that tenants shall sell. *See* Paragraph III.A.1, III.B.1. Sears' petition describes the efficiencies gained from use clauses. According to Sears, use clauses promote an optimum tenant mix and preserve the desired character of a shopping center.

Sears' petition demonstrates an affirmative need for modification of this prohibition. Sears shows that descriptions of range of price and fashion and quality in use clauses serve a competitive purpose, are unlikely to threaten tenants' pricing discretion, and are commonly used in the industry. The prohibitions particularly interfere with Sears' ability to draft use clauses narrowly enough to achieve an optimum tenant mix and to preserve the desired character of a shopping center. The Commission has long recognized that use clauses can play an important role in maintaining an optimal tenant mix in a shopping center. *See* Federal Trade Commission Statement Regarding Shopping Centers (March 1981); *Tyson's Corner Regional Shopping Center*, 85 FTC 970, 1008, 1012, 1012 n.12, 1014, 1017-18 (1975).

Thus, Sears makes a satisfactory showing to warrant reopening of the prohibition of use clauses in the public interest. The Commission

has concluded that this harm can be appropriately remedied by deleting the language prohibiting use clauses that refer to ranges of price or fashion or quality.<sup>4</sup> However, the core prohibition against price fixing remains intact.<sup>5</sup>

#### Prior Approval

Paragraph II.A.2. prohibits Sears, in its capacity as a tenant, from entering or enforcing agreements granting it the right to approve or disapprove the entry into a shopping center of any other tenants. There are related paragraphs that prohibit more limited prior approval clauses, *e.g.*, preventing other tenants' expansion of floor space in the mall without the major tenant's approval. *See* Paragraphs II.A.3., II.A.4., II.A.7, II.A.8, II.A.11.

Sears challenges the order's approach to rights of prior approval exercised by tenants because the prohibition fails to recognize, according to Sears, the purported efficiency justifications for tenant-held rights of prior approval. Sears claims that it needs a voice in the selection of major tenants because the success of the shopping center and Sears' store in the center depend upon the other major tenants being an asset to the center. *See* Petition at 46. Accordingly, Sears seeks to reopen and modify these prohibitions to enable it to exercise a right of approval over entry by other major tenants into the center.

Sears fails to make the necessary showing of affirmative need to reopen the prohibitions against rights of prior approval in the public interest. Sears provides examples where a promised anchor tenant backed out and less desirable anchor tenants got locations in shopping centers where Sears was also an anchor. The examples do not indicate whether the harm to Sears resulted after the promised anchor backed out, did the developer have many anchors to choose from, some of whom Sears preferred? Or, was the developer having a hard time finding any anchor, so that Sears might have settled for the less desirable anchor? Sears has not made a satisfactory showing that

<sup>4</sup> As set forth below, the modification to Paragraph III.B.1. adds the language "of other tenants" consistent with Sears' proposed modification. *See* Alternative Proposal, Order, Paragraph III.B.1. This clarifies that the prohibition only applies to a tenant or to Sears specifying or controlling the prices of any other tenant. *See* Paragraph III.B.2.

<sup>5</sup> Paragraph III.G. imposes certain reporting requirements upon Sears in its capacity as a developer. Sears asks that the Commission modify the subparagraph to accord with any changes in the substantive prohibitions made by the Commission. In view of the modifications made herein to permit use clauses, Paragraph III.G.3. should be reopened and modified to strike references to price ranges, fashion ranges, and quality ranges.

Sears requests that the Commission add a new Paragraph III.F.3. to make clear that Sears could employ use clauses in off-price shopping centers requiring the tenant to sell high quality merchandise. The foregoing modification by the Commission to Paragraphs III.A.1. and III.B.1. makes such a modification unnecessary.

tenant-held rights of prior approval, in fact, enhance competition, or that Sears has been unable to protect its "legally cognizable interests" by requiring developers to select tenants only according to defined standards contained in shopping center agreements. Accordingly, Sears has not carried its burden to demonstrate an affirmative need to reopen and modify the prohibition against rights of prior approval.<sup>6</sup>

#### Tying Clauses

Paragraph III.A.4. prohibits Sears, in its capacity as a developer, from conditioning entry of a tenant into one shopping center upon that tenant's entry into another Sears shopping center. Sears claims that the prohibition may prevent it from offering a tenant a package rental rate covering locations in several shopping centers whereby it charges a lower relative rent than the rate for space in one center. Thus, Sears requests that the Commission reopen the prohibition by adding a new Paragraph III.F.2. Such a package rental rate would not necessarily violate Paragraph III.A.4. Thus, Sears has not shown an affirmative need to reopen and modify Paragraph III.A.4.

#### Joint Use of Common Officers and Employees by Sears' Merchandising and Development Groups

Paragraph III.C. prohibits Sears from using the same officers or employees in Sears' separate capacities as a tenant in or as a developer of shopping centers. Sears represents that the possible joint

<sup>6</sup> Sears' failure to carry its burden regarding rights of prior approval disposes also of Sears' request that the Commission adopt Sears' proposed order paragraphs in its Alternative Proposal, namely, Paragraphs II.A.2., II.A.3., II.A.4., II.A.7., II.A.8., II.A.11., III.E.9.

Sears asks that Paragraph III.E. be modified to expand the stated criterion that Sears can permissibly require a developer to following in selecting new or replacement tenants. See Alternative Proposal, Explanation of Amendments at 4, Proposed Paragraphs III.E.1., III.E.7, III.E.8., and III.E.10. The Commission has concluded that such reopening and modification of the order is unnecessary. Paragraph III.E. was not intended to be a definitive list of standards and Sears has flexibility in drafting criteria necessary to protect its "legally cognizable interests" without modification so long as the standards are not a cover for price fixing. In *Tyson's Corner*, the Commission noted that the criteria set forth in Paragraph III.E. were

not intended to constitute an exhaustive listing of the factors which [respondent major tenant] may insist be considered by a shopping center landlord in the management of the center, as a condition of [the respondent major tenant]'s signing a shopping center lease.

*Tyson's Corner*, 85 FTC at 1017 n.19.

The Commission, however, will reopen and modify Paragraph III.E.3., which permits Sears to exercise limited approval rights for tenants within 150 feet of a Sears store. Sears has made a sufficient showing of an affirmative need for modification. Currently, Sears may prepare a list of acceptable tenant categories from which the developer can select tenants to be located next to Sears with certain limitations as to, for example, price ranges. Sears requests that the paragraph be modified to permit it to designate categories of retailers who are unacceptable rather than acceptable subject to the same limitations. Sears represents that it becomes nearly impossible under the current procedure to list all possible permissible uses. Thus, modification will facilitate operation of this paragraph without changing the substance of the prohibition.

use of officers by Sears' Merchandise Group and Homart, Sears' shopping center development arm, is not now a problem because Homart long ago became an autonomous unit. Sears argues, however, that both Sears units would benefit from using common corporate headquarters staff personnel for such matters as tax counseling, procurement assistance, computer expertise, personnel administration, insurance advice, legal advice, and accounting and general office management.

Sears fails to make the necessary showing of affirmative need to reopen Paragraph III.C. in the public interest. Sears does not refer to any instances where it has forgone benefits from using common corporate headquarters staff or suffered competitive harm. In any event, the Commission recognizes the potential benefits that may arise through use of common corporate headquarters staff and does not interpret Paragraph III.C. to prohibit Sears in its capacity as tenant and developer from drawing upon common staff expertise.

#### Sears as a Specialty Tenant

The order prohibitions against Sears in its capacity as a tenant apply broadly to Sears whether it is acting as a major tenant or as a satellite tenant in a shopping center. See Paragraph I.(c), I.(d), II.A., II.B. At the time the order was issued, Sears, as a tenant, was generally involved in shopping centers only in the capacity of a major tenant, according to Sears. Sears has now begun to branch into specialty stores, and eye care centers, and requests that the order be modified to exclude Sears as a specialty tenant.

Sears has made a satisfactory showing to warrant reopening of this aspect of the order in the public interest. In its capacity as a satellite tenant, Sears is unlikely to have the necessary leverage to obtain any unlawful restrictive covenants from developers. The Commission in *Tysons Corner* only focused upon restrictive covenants held by major tenants and not covenants held by satellite tenants. The value of Sears as a satellite tenant being able to compete without the order outweighs the likelihood that Sears in that capacity could secure any anticompetitive restrictive covenants in negotiations with developers. Under the circumstances, the Commission will modify the order to exclude Sears as a satellite tenant.<sup>7</sup> Previously, the Commission made

<sup>7</sup> Paragraph I.(d) defines "major tenant" as

a tenant providing primary drawing power in a shopping center. A tenant which occupies at least 50,000 square feet of floor area will be deemed to provide primary drawing power.

this same distinction between a specialty store operation and a major tenant operation in *Tyson's Corner* where the Commission modified the order in the public interest so as not to limit the ability of that respondent's specialty furniture store to secure exclusivity clauses in shopping center leases. *See Tyson's Corner*, 86 FTC 921 (1975).<sup>8</sup>

#### Definition of "Developer"

Sears claims that the order prevents Sears from investing in some shopping center joint ventures. According to Sears, the order's strict requirements against radius and use clauses cause other investors to view Sears as a less attractive investment partner. Sears cites experiences where the order has impeded Sears' ability to participate in investment opportunities. *See* Petition at 42-43.

Similarly, Sears finds that the order frustrates its ability to compete for shopping center management services jobs in centers where it will have no ownership interest. According to Sears, shopping center owners prefer management firms who are not under prohibitions against radius and use clauses. Sears cites cases in which the order has placed Sears at a disadvantage in competing for such shopping center manager services positions. *See* Petition at 43-45.

Sears requests that the order's definition of developer be reopened and modified to exclude Sears when it holds a 30 percent or less ownership interest in a shopping center or is not the shopping center manager. *See* Alternative Proposal, Explanation at 1. Sears, however, has not made a satisfactory showing that this definition needs reopening. Central to Sears' claim is the order's prohibition against Sears' employment of radius and use clauses. However, the Commission has decided already to reopen and modify these prohibitions generally in the manner sought by Sears. Thus, Sears is no longer disadvantaged in relationship to competing investors or management services firms. Accordingly, the Commission denies Sears' request to reopen the order's definition of developer.<sup>9</sup>

<sup>8</sup> Paragraph IV.B. imposes upon Sears as a tenant an obligation to send a copy of the order within 30 days after service of the order to each major tenant, shopping center joint venturer, and developer in every shopping center in which Sears is a major tenant. Sears asks that the requirement be set aside as obsolete. This paragraph is, indeed, obsolete because compliance was required and completed in 1977 and for that reason there is no affirmative need to set aside the paragraph.

<sup>9</sup> Sears also asks the Commission to reopen the order for the purpose of exempting shopping center agreements that Sears inherits when Sears acquires a shopping center in its capacity as a developer. *See* Alternative Proposal, Proposed Paragraphs III.E.11., III.F.6., Explanation of Amendments at 6. Sears, however, shows no affirmative need for such a modification. Restrictive shopping center agreements pose the same problem whether or not Sears negotiates or inherits them. Moreover, in the future, Sears will likely

## V. REOPENING AND MODIFICATION

Accordingly, *it is ordered*, that the order issued in this matter on April 20, 1977, be, and it hereby is, reopened and modified, as of the date of service of this order, as follows.

1. Paragraph III.A.3. shall be set aside.
2. Paragraph III.A.1. shall be modified by striking "price, or within any range of prices, or within any range of fashions, or within any range of quality, when such descriptions identify tenants as members of a class of merchants which sell their merchandise within a generally identifiable range of prices" and adding "specific prices or specific ranges of prices."
3. Paragraph III.B.1. shall be modified by striking "prices, price ranges, fashion ranges, quality ranges, which identify tenants as members of a class of merchants which sell their merchandise within a generally identifiable range of prices" and adding "specific prices or specific ranges of prices of other tenants".
4. Paragraph II.A. and Paragraph II.B. shall be modified by substituting "major tenant" for "tenant" as that term is used to define the capacity in which Sears is acting.
5. Paragraph III.G.3. shall be modified by striking "price ranges, fashion ranges, quality ranges."
6. Paragraph III.E.3. shall be modified by inserting "not" following "landlord may."

## STATEMENT OF CHAIRMAN DANIEL OLIVER

I concur in the decision to grant in part Sears' Petition to reopen and set aside the order in Docket No. C-2885; however, I would have set aside the order in its entirety. I concur wholly in the cogent antitrust analysis set forth in Commissioner Machol's separate statement. In my view, the procompetitive justifications for the restrictions prohibited by the order, as detailed by Commissioner Machol, warrant reopening and setting aside the order on public interest grounds.

In addition, I agree with the statement in today's order that a showing to require reopening is made when there are "significant changes in circumstances," that "eliminate the need for the order or make continued application of the order inequitable or harmful to

inherit fewer shopping center leases that do not conform to the order in view of this order's modification of the prohibitions against radius and use clauses.

competition." I cannot agree, however, with the further suggestion that for the Commission to reopen and set aside an order today, on the basis of a claim of change in law, Sears would have to show that it did not possess market power in 1977.

To answer whether there has been a change in law, we should look at the law.<sup>1</sup> In this case, the addition of the element of market power to the legal analysis is a significant change in law since the decision in *Tyson's Corner*, 85 FTC 970 (1975). That being the case, a petitioner in Sears' position need only demonstrate that it has no market power today, and thus that there is no longer a need for the order. Otherwise, it is likely that there would be an absence of record evidence to address what was not an issue at the time an order was entered, and that such historical evidence would be nearly impossible to develop anew. When the law has changed as significantly as it has in this case, the petitioner's required factual showing should be limited to whether consumers today would be injured by the conduct that the order sought to prevent.

STATEMENT OF COMMISSIONER MARGOT E. MACHOL

While I concur in the decision to grant in part and deny in part Sears' Petition to reopen and set aside, or in the alternative, modify the order in Docket No. C-2885, I would prefer to reopen additional portions of the order and grant further modifications on public interest grounds.

Sears, in its capacity as both a shopping center developer and tenant, requests that the order's prohibitions on certain restrictions in shopping center leases and operating agreements, such as prior approval clauses, be set aside. A shopping center is essentially a joint venture between a shopping center developer (acting as landlord) and the retail tenant to operate a group of commercial establishments as a unit. See Clarkson & Muris, eds., *The Federal Trade Commission Since 1970: Economic Regulation and Bureaucratic Behavior* (1981) at 141. Shopping centers can provide significant efficiencies that are not available when retail establishments operate as stand-alone businesses or in downtown commercial areas. These efficiencies include lower search costs for consumers, and maximized traffic flow and lower operating costs for retailers.

<sup>1</sup> Such a construction will not open the floodgates to petitions to reopen every time a court or the Commission issues a new decision, because there is still the requirement that the change in law be significant.

Restrictions agreed upon by the joint venture participants that constrain tenant characteristics but do not fix the prices charged by any tenant may reasonably be related to the efficient operation and success of the shopping center. As such, these restrictions would generally be analyzed under the rule of reason. Such restraints are methods of controlling tenant mix and the character or marketing concept of a shopping center, which are important factors in the center's success. Shopping centers seek to provide a wide variety of stores that would appeal to particular groups of consumers. For example, some shopping centers cater to consumers who want high quality/high priced goods and services (*e.g.*, Water Tower Place in Chicago; Trump Tower in New York City), some to consumers who want discount goods (*e.g.*, Biggs Hypermarket in Cincinnati), and still others to consumers whose tastes fall between these extremes. While lease restrictions may reduce aspects of competition among stores within a particular shopping center, they may serve to stimulate competition among different shopping centers.

Sears explains that a major ("anchor") tenant makes a significant investment in a shopping center that is at risk for a considerable period of time. The ability to have a voice in the selection of other tenants is a way of protecting the investment of anchor tenants and encouraging their participation in shopping centers. In my view, Sears has shown that its inability to take a more active role in the selection of other tenants has caused it competitive injury, and may also have affected the ability of the shopping centers in which Sears participates to compete effectively with other shopping centers. Sears has also shown that it has been unable to protect its interests adequately by the means left available to it under the order. As a result, I conclude that Sears has made a showing sufficient to warrant reopening additional portions of the order.

Under a rule of reason analysis of the kinds of restraints at issue in the Sears order, the shopping centers in which Sears participates would at least need to possess market power before these restraints would be found to restrain trade unreasonably. See *Northwest Wholesale Stationers, Inc. v. Pacific Stationery and Printing Co.*, 472 U.S. 284 (1985); *Jefferson Parish Hospital District No. 2 v. Hyde*, 466 U.S. 2 (1984); *Broadcast Music, Inc. v. Columbia Broadcasting System, Inc.*, 441 U.S. 1 (1979); *Continental T.V., Inc. v. GTE Sylvania Inc.*, 433 U.S. 36 (1977). While Sears did not specifically address in its Petition whether the shopping centers with

which it is associated may in fact possess market power, I believe that Sears provided sufficient evidence from which one could conclude that few, if any, of these shopping centers are likely to have market power. As a result, I believe we can properly conclude that the injury to Sears' ability to compete, and the potential for enhancing the competitive posture of those shopping centers in which Sears participates, outweigh any continuing need for certain of the order's remaining prohibitions. Accordingly, further modification of the order would be justified on public interest grounds.

I have a general observation about petitions to reopen and modify that assert public interest grounds as justification. Given the public interest in repose and finality of Commission orders, the burden is on the petitioner when public interest grounds are invoked to make a satisfactory showing in support of each specific aspect of an order for which the petitioner is requesting relief. Particularly in cases involving lengthy or complex orders, the Commission's review can be greatly facilitated if the petitioner identifies precisely the portion of the order to which a showing is meant to relate.

Finally, because the Commission decided to grant certain modifications requested by Sears on public interest grounds, we did not reach the issue of what showing would be required of Sears to mandate reopening on the ground of changed conditions of law. I disagree with the statement in the Modifying Order suggesting that Sears should be required to show that the shopping centers with which it was associated in 1977 did not then possess market power. In my view, the petitioner should not be required to demonstrate that the Commission's earlier decision was wrong in terms of modern-day law. Instead, the critical issue is whether the petitioner identifies significant changes in circumstances, and shows that those changes eliminate the need for the order or make continued application of the order inequitable or harmful to competition. *See* S. Rep. No. 96-500, 96th Cong., 2d Sess. 9 (1979); *Louisiana-Pacific Corp.*, Docket No. C-2956, Letter to John C. Hart (June 5, 1986), at 4. Moreover, to require a showing about market power that existed in the past would impose a nearly impossible burden on many petitioners, particularly those with orders that are more than ten years old. Accordingly, I believe reopening would be mandatory if Sears showed that the shopping centers with which it is associated today do not possess market power. If that is true, the existence of market power in 1977 is irrelevant.

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IN THE MATTER OF  
CARL'S DRUG CO., INC.

CONSENT ORDER, ETC., IN REGARD TO ALLEGED VIOLATION OF  
SEC. 5 OF THE FEDERAL TRADE COMMISSION ACT

*Docket C-3257. Complaint, July 12, 1989—Decision, July 12, 1989*

This consent order prohibits, among other things, the Rome, N.Y. based corporation from entering into any agreement with other pharmacy firms to withdraw from or refuse to enter into any participation agreement. It further prohibits respondent, for a period of ten years, from communicating to another pharmacy firm their decision or intention to enter or refuse to enter into such a participation agreement. In addition, for eight years, it prohibits respondent from advising another pharmacy firm on whether to enter into any participation agreement.

*Appearances*

For the Commission: *Karen Bokat and Michael D. McNeely.*

For the respondent: *Tod Bogan and Fred Feola, in-house counsel,* Rome, N.Y. and *Garret G. Rasmussen, Patton, Boggs, & Row,* Washington, D.C.

COMPLAINT

Pursuant to the provisions of the Federal Trade Commission Act, and by virtue of the authority vested in it by said Act, the Federal Trade Commission, having reason to believe that Brooks Drug, Inc., Carl's Drug Co., Inc. and Genovese Drug Stores, Inc. have violated the provisions of said Act, and it appearing to the Commission that a proceeding by it in respect thereof would be in the public interest, hereby issues its complaint stating its charges as follows:

PARAGRAPH 1. Respondent Brooks Drug, Inc. ("Brooks") is a corporation organized, existing and doing business under and by virtue of the laws of the State of Delaware, with its principal offices located at 75 Sabin Street, Pawtucket, Rhode Island. In 1986, the retail sale of prescription drugs accounted for a significant portion of the sales of the approximately 60 pharmacies that respondent Brooks operated in New York State. In 1986, respondent Brooks was a member of the Chain Pharmacy Association of New York State, Inc. ("Chain Association").

PAR. 2. Respondent Carl's Drug Co., Inc. ("Carl's") is a corporation organized, existing and doing business under and by virtue of the laws of the State of New York, with its principal office address at Box 203 Success Drive, Rome, New York. In 1986, the retail sale of prescription drugs accounted for a significant portion of the sales of the approximately 42 pharmacies that Carl's operated in New York State. In 1986, respondent Carl's was a member of the Chain Association.

PAR. 3. Respondent Genovese Drug Stores, Inc. ("Genovese") is a corporation organized, existing and doing business under and by virtue of the laws of the State of Delaware, with its principal offices located at 80 Marcus Drive, Melville, New York. The retail sale of prescription drugs accounts for a significant portion of the sales of the approximately 72 pharmacies that respondent Genovese operates in New York State. In 1986, respondent Genovese was a member of the Chain Association.

PAR. 4. Except to the extent that competition has been restrained as alleged herein, respondents have been and now are in competition with other pharmacy firms and other health care providers in the state of New York.

PAR. 5. Respondents' general business activities, and the acts and practices described below, are in or affect commerce, as "commerce" is defined in the Federal Trade Commission Act, 15 U.S.C. 45.

PAR. 6. Customers often receive prescriptions through health benefit programs under which a third-party payer compensates the pharmacy for the prescription according to a predetermined formula. The New York State Employees Prescription Program is a prescription drug benefit plan made available by the State of New York to its employees, its retirees, certain other persons, and their dependents. There were approximately 500,000 beneficiaries covered by the Employees Prescription Program in 1986. Since July 1, 1986, The Equitable Life Assurance Society of the United States has insured the Employees Prescription Program, and PAID Prescriptions, Inc., a wholly-owned subsidiary of Medco Containment Services, Inc., has administered it.

PAR. 7. Pharmacies are solicited to participate in the Employees Prescription Program. Pharmacies that participate in the Employees Prescription Program accept as payment in full a reimbursement of the ingredient cost of the drug and a professional fee for dispensing the drug. The Employees Prescription Program provides a formula for

determining the reimbursement of the ingredient cost of drugs dispensed.

PAR. 8. Absent collusion between or among pharmacy firms, each pharmacy firm would decide independently whether to participate in the Employees Prescription Program, and the State of New York would enjoy the benefits of competition among pharmacy firms.

PAR. 9. In May 1986, PAID Prescriptions, Inc. formally solicited pharmacy participation in the Employees Prescription Program under terms to become effective on July 1, 1986. Among the proposed terms were changes in the reimbursement level for ingredient costs, an increase in the professional fee, and the offer of additional reimbursement for the use of generic drugs. The proposed terms were intended to reduce the price the State paid for the Employees Prescription Program, and thus minimize costs, and yet to offer reimbursement high enough to attract a sufficient number of participating pharmacies to ensure that Employees Prescription Program beneficiaries would have adequate access to medication.

PAR. 10. In 1986, respondents participated in many prescription drug benefit plans offered by third-party payers, including the Employees Prescription Program as it existed prior to July 1. Respondents purchased prescription drugs at a cost which on average was below the Employees Prescription Program's proposed level of reimbursement for ingredient costs. Each respondent would have suffered a significant loss of customers had its competitors participated in the Employees Prescription Program at a time when it was not participating.

PAR. 11. Even before PAID formally solicited pharmacy participation in the Employees Prescription Program, New York State began to inform pharmacists' associations of the proposed terms. In or before March 1986, the Chain Association became aware of the proposed terms of the Employees Prescription Program, and, in response, communicated to members that the extent to which pharmacies participated in the Employees Prescription Program could affect state officials' consideration of the reimbursement level. The Chain Association held meetings at which some pharmacy firms informed other pharmacy firms that they would not participate in the proposed Employees Prescription Program. Respondents were involved with other pharmacy firms in exchanges of information regarding firms' intentions concerning participation in the Employees Prescription Program. The Chain Association communicated to Chain Association

members and other pharmacy firms information regarding the intentions of Chain Association members and other pharmacy firms concerning participation in the Employees Prescription Program. Through these exchanges of information and other acts, respondents and other pharmacy firms agreed to refuse to participate in the Employees Prescription Program at the proposed reimbursement level, for the purpose of increasing the level of reimbursement offered by the State of New York under the Employees Prescription Program.

PAR. 12. Respondents have restrained competition among pharmacy firms by conspiring with other pharmacy firms, or by acting with other pharmacy firms as a combination, to increase the price paid to participating pharmacies under the Employees Prescription Program and to deny to the State the benefits of competition.

PAR. 13. The combination of conspiracy and the acts and practices described above have unreasonably restrained and continue unreasonably to restrain competition among pharmacists and pharmacies in New York, and have injured consumers in the following ways, among others:

A. Price competition among pharmacy firms with respect to third-party prescription benefit plans has been and continues to be reduced;

B. The State of New York was coerced into raising the prices paid to pharmacies under the Employees Prescription Program; and,

C. The State of New York has been and continues to be forced to pay substantial additional sums for prescription drugs provided to Employees Prescription Program beneficiaries.

PAR. 14. The combination or conspiracy and the acts described above constitute unfair methods of competition in or affecting commerce in violation of Section 5 of the Federal Trade Commission Act. The combination or conspiracy, or the effects thereof, are continuing, will continue, or will recur in the absence of the relief herein requested.

Commissions Azcuenaga and Machol dissenting.

#### DECISION AND ORDER

The Federal Trade Commission having initiated an investigation of certain acts and practices of the respondent named in the caption hereof, and the respondent having been furnished thereafter with a copy of a draft of the complaint which the Bureau of Competition proposed to present to the Commission for its consideration and

which, if issued by the Commission, would charge respondent with violation of the Federal Trade Commission Act; and

The respondent, its attorney, and counsel for the Commission having thereafter executed an agreement containing a consent order, an admission by the respondent of all jurisdictional facts set forth in the aforesaid draft complaint, a statement that the signing of said agreement is for settlement purposes only and does not constitute an admission by respondent that the law has been violated as alleged in such complaint, and waivers and other provisions as required by the Commission's Rules; and

The Commission having thereafter considered the matter and having determined that it had reason to believe that the respondent has violated the said Act, and that complaint should issue stating its charges in that respect, and having thereupon accepted the executed consent agreement and placed such agreement on the public record for a period of sixty (60) days, now in further conformity with the procedure prescribed in Section 2.34 of its Rules, the Commission hereby issues its complaint, makes the following jurisdictional findings and enters the following order:

1. Respondent Carl's is a corporation organized, existing, and doing business under and by virtue of the laws of the State of New York, with its office and principal place of business at Box 203 Success Drive, Rome, New York.

2. The Federal Trade Commission has jurisdiction of the subject matter of this proceeding and of the respondent, and the proceeding is in the public interest.

#### ORDER

##### I.

For purposes of the order, the following definitions shall apply:

A. "*Carl's*" means Carl's Drug Co., Inc., its directors, officers, agents, employees, divisions, subsidiaries, successors and assigns;

B. "*Third-party payer*" means any person or entity that provides a program or plan pursuant to which such a person or entity agrees to pay for prescriptions dispensed by pharmacies to individuals described in such plan or program as eligible for such coverage ("Covered Persons"), and includes, but is not limited to, health insurance

companies; prepaid hospital, medical, or other health service plans, such as Blue Cross and Blue Shield plans; health maintenance organizations; preferred provider organizations; prescription service administrative organizations; and health benefit programs for government employees, retirees or dependents;

C. "*Participation agreement*" means any existing or proposed agreement, oral or written, in which a third-party payer agrees to reimburse a pharmacy for the dispensing of prescription drugs to Covered Persons, and the pharmacy agrees to accept such payment from the third-party payer for such prescriptions dispensed during the term of the agreement;

D. "*Pharmacy Firm*" means any partnership, sole proprietorship or corporation, including all of its subsidiaries, affiliates, divisions and joint ventures, that owns, controls or operates one or more pharmacies, including the directors, officers, employees, and agents of such partnership, sole proprietorship or corporation as well as the directors, officers, employees, and agents of such partnership's, sole proprietorship's or corporation's subsidiaries, affiliates, divisions and joint ventures, but excludes any partnership, sole proprietorship or corporation, including all of its subsidiaries, affiliates, divisions and joint ventures, which own, are owned by, control or are under common control with Carl's. The words "subsidiary", "affiliate", and "joint venture" refer to any firm in which there is partial (10% or more) or total ownership or control between corporations.

## II.

*It is ordered*, That Carl's, directly, indirectly, or through any corporate or other device, in or in connection with its activities in or affecting commerce, as "commerce" is defined in Section 4 of the Federal Trade Commission Act, shall forthwith cease and desist from:

A. Agreeing or combining, attempting to agree or combine, or taking any action in furtherance of any agreement or combination, advocating an agreement, or organizing or cooperating with any Pharmacy Firm(s) to (1) boycott, refuse to enter into, withdraw from, or not participate in, any Participation Agreement or (2) threaten to boycott, threaten to refuse to enter into, threaten to withdraw from, or threaten not to participate in, any participation agreement;

B. For a period of ten (10) years after the date this order becomes final, stating or communicating in any way to any pharmacy firm the

intention or decision of Carl's with respect to entering into, refusing to enter into, threatening to refuse to enter into, participating in, threatening to withdraw from, or withdrawing from any existing or proposed participation agreement into which Carl's and the other pharmacy firm have entered, could enter or are considering entering;

C. For a period of eight (8) years after the date this order becomes final, advising any pharmacy firm with respect to entering into, refusing to enter into, participating in, or withdrawing from any existing or proposed participation agreement into which Carl's and the other pharmacy firm have entered, could enter or are considering entering.

*Provided*, that nothing in this order shall prevent Carl's from:

(1) Exercising rights permitted under the First Amendment to the United States Constitution to petition any federal or state government executive agency or legislative body concerning legislation, rules or procedures, or to participate in any federal or state administrative or judicial proceeding;

(2) Subcontracting, preparing joint bids, or otherwise jointly undertaking with pharmacy firms to provide prescription drug services under a participation agreement if requested to do so in writing by the third-party payer;

(3) Communicating to the public truthful, nondeceptive statements concerning any existing or proposed participation agreement.

### III.

*It is further ordered*, That Carl's:

A. Provide a copy of this order within thirty (30) days after the date this order becomes final to each officer, director, employee pharmacist who is employed in New York state, and each employee whose responsibilities include recommending or deciding whether to enter into any participation agreement, and each employee who regularly attends meetings on Carl's behalf that include representatives of other pharmacies; and

B. For a period of five (5) years after the date this order becomes final, provide each new director and each employee who enters a position described in Paragraph A a copy of the order within ten (10) days of the date the employee or director assumes the new position.

## IV.

*It is further ordered, That Carl's:*

A. File a verified, written report with the Commission within ninety (90) days after the date this order becomes final, and annually thereafter for five (5) years on the anniversary of the date this order becomes final, and at such other times as the Commission may, by written notice to Carl's, require, setting forth in detail the manner and form in which it has complied and is complying with this order;

B. For a period of five (5) years after the date this order becomes final, maintain and make available to Commission staff for inspection and copying upon reasonable notice all documents generated by Carl's or that come into Carl's possession, custody, or control regardless of source, that embody, discuss or refer to the decision or upon which Carl's relies in deciding whether to enter into any participation agreement in which Carl's participates, has participated, or has considered participating; and

C. Notify the Commission at least thirty (30) days prior to any proposed change in Carl's such as, assignment or sale resulting in the emergence of a successor corporation or association, change of name, change of address, dissolution, the creation, sale or dissolution of a subsidiary, or any other change that may affect compliance with this order.

Commissioners Azcuenaga and Machol dissenting.

GENOVESE DRUG STORES, INC.

IN THE MATTER OF

GENOVESE DRUG STORES, INC.

CONSENT ORDER, ETC., IN REGARD TO ALLEGED VIOLATION OF  
SEC. 5 OF THE FEDERAL TRADE COMMISSION ACT

*Docket C-3258. Complaint,\* July 12, 1989—Decision, July 12, 1989*

This consent order prohibits, among other things, the Melville, N.Y. based corporation from entering into any agreement with other pharmacy firms to withdraw from or refuse to enter into any participation agreement. It further prohibits respondent, for a period of ten years, from communicating to another pharmacy firm their decision or intention to enter or refuse to enter into such a participation agreement. In addition, for eight years, it prohibits respondent from advising another pharmacy firm on whether to enter into any participation agreement.

*Appearances*

For the Commission: *Karen Bokat and Michael D. McNeely.*

For the respondent: *Edward J. Brady, Brady & Tarpey, New York City.*

DECISION AND ORDER

The Federal Trade Commission having initiated an investigation of certain acts and practices of the respondent named in the caption hereof, and the respondent having been furnished thereafter with a copy of a draft of the complaint which the Bureau of Competition proposed to present to the Commission for its consideration and which, if issued by the Commission, would charge respondent with violation of the Federal Trade Commission Act; and

The respondent, its attorney, and counsel for the Commission having thereafter executed an agreement containing a consent order, an admission by the respondent of all jurisdictional facts set forth in the aforesaid draft complaint, a statement that the signing of said agreement is for settlement purposes only and does not constitute an admission by respondents that the law has been violated as alleged in such complaint, and waivers and other provisions as required by the Commission's Rules; and

The Commission having thereafter considered the matter and

\*Complaint previously published at 112 FTC 15 (1989).

having determined that it had reason to believe that the respondent has violated the said Act, and that complaint should issue stating its charges in that respect, and having thereupon accepted the executed consent agreement and placed such agreement on the public record for a period of sixty (60) days, now in further conformity with the procedure prescribed in Section 2.34 of its Rules, the Commission hereby issues its complaint, makes the following jurisdictional findings and enters the following order:

1. Respondent Genovese is a corporation organized, existing and doing business under and by virtue of the laws of the State of Delaware, with its office and principal place of business at 80 Marcus Drive, Melville, N.Y.

2. The Federal Trade Commission has jurisdiction of the subject matter of this proceeding and of the respondent, and the proceeding is in the public interest.

#### ORDER

##### I.

For purposes of the order, the following definitions shall apply:

A. "*Genovese*" means Genovese Drug Stores, Inc., its directors, officers, agents, employees, divisions, subsidiaries, successors and assigns;

B. "*Third-party payer*" means any person or entity that provides a program or plan pursuant to which such a person or entity agrees to pay for prescriptions dispensed by pharmacies to individuals described in such plan or program as eligible for such coverage ("Covered Persons"), and includes, but is not limited to, health insurance companies; prepaid hospital, medical, or other health service plans, such as Blue Cross and Blue Shield plans; health maintenance organizations; preferred provider organizations; prescription service administrative organizations; and health benefit programs for government employees, retirees or dependents;

C. "*Participation agreement*" means any existing or proposed agreement, oral or written, in which a third-party payer agrees to reimburse a pharmacy for the dispensing of prescription drugs to Covered Persons, and the pharmacy agrees to accept such payment from the third-party payer for such prescriptions dispensed during the term of the agreement;

D. "*Pharmacy firm*" means any partnership, sole proprietorship or corporation, including all of its subsidiaries, affiliates, divisions and joint ventures, that owns, controls or operates one or more pharmacies, including the directors, officers, employees, and agents of such partnership, sole proprietorship or corporation as well as the directors, officers, employees, and agents of such partnership's, sole proprietorship's or corporation's subsidiaries, affiliates, divisions and joint ventures, but excludes any partnership, sole proprietorship or corporation, including all of its subsidiaries, affiliates, divisions and joint ventures, which own, are owned by, control or are under common control with Genovese. The words "subsidiary", "affiliate", and "joint venture" refer to any firm in which there is partial (10% or more) or total ownership or control between corporations.

## II.

*It is ordered*, That Genovese, directly, indirectly, or through any corporate or other device, in or in connection with its activities in or affecting commerce, as "commerce" is defined in Section 4 of the Federal Trade Commission Act, shall forthwith cease and desist from:

A. Agreeing or combining, attempting to agree or combine, or taking any action in furtherance of any agreement or combination, advocating an agreement, or organizing or cooperating with any Pharmacy Firm(s) to (1) boycott, refuse to enter into, withdraw from, or not participate in, any Participation Agreement or (2) threaten to boycott, threaten to refuse to enter into, threaten to withdraw from, or threaten not to participate in, any participation agreement;

B. For a period of ten (10) years after the date this order becomes final, stating or communicating in any way to any pharmacy firm the intention or decision of Genovese with respect to entering into, refusing to enter into, threatening to refuse to enter into, participating in, threatening to withdraw from, or withdrawing from any existing or proposed participation agreement into which Genovese and the other pharmacy firm have entered, could enter or are considering entering;

C. For a period of eight (8) years after the date this order becomes final, advising any pharmacy firm with respect to entering into, refusing to enter into, participating in, or withdrawing from any existing or proposed participation agreement into which Genovese and

the other pharmacy firm have entered, could enter or are considering entering.

*Provided*, that nothing in this order shall prevent Genovese from:

(1) Exercising rights permitted under the First Amendment to the United States Constitution to petition any federal or state government executive agency or legislative body concerning legislation, rules or procedures, or to participate in any federal or state administrative or judicial proceeding;

(2) Subcontracting, preparing joint bids, or otherwise jointly undertaking with pharmacy firms to provide prescription drug services under a participation agreement if requested to do so in writing by the third-party payer;

(3) Communicating to the public truthful, nondeceptive statements concerning any existing or proposed participation agreement.

### III.

*It is further ordered*, That Genovese:

A. Provide a copy of this order within thirty (30) days after the date this order becomes final to each officer, director, employee pharmacist who is employed in New York state, and each employee whose responsibilities include recommending or deciding whether to enter into any participation agreement, and each employee who regularly attends meetings on Genovese's behalf that include representatives of other pharmacies; and

B. For a period of five (5) years after the date this order becomes final, provide each new director and each employee who enters a position described in Paragraph A a copy of the order within ten (10) days of the date the employee or director assumes the new position.

### IV.

*It is further ordered*, That Genovese:

A. File a verified, written report with the Commission within ninety (90) days after the date this order becomes final, and annually thereafter for five (5) years on the anniversary of the date this order becomes final, and at such other times as the Commission may, by written notice to Genovese, require, setting forth in detail the manner and form in which it has complied and is complying with this order:

B. For a period of five (5) years after the date this order becomes final, maintain and make available to Commission staff for inspection and copying upon reasonable notice all documents generated by Genovese or that come into Genovese's possession, custody, or control regardless of source, that embody, discuss or refer to the decision or upon which Genovese relies in deciding whether to enter into any participation agreement in which Genovese participates, has participated, or has considered participating; and

C. Notify the Commission at least thirty (30) days prior to any proposed change in Genovese such as, assignment or sale resulting in the emergence of a successor corporation or association, change of name, change of address, dissolution, the creation, sale or dissolution of a subsidiary, or any other change that may affect compliance with this order.

Commissioners Azcuenaga and Machol dissenting.

## IN THE MATTER OF

## BROOKS DRUG, INC.

CONSENT ORDER, ETC., IN REGARD TO ALLEGED VIOLATION OF  
SEC. 5 OF THE FEDERAL TRADE COMMISSION ACT

*Docket C-3256. Complaint,\* July 12, 1989—Decision, July 13, 1989*

This consent order prohibits, among other things, the Pawtucket, R.I. based corporation from entering into any agreement with other pharmacy firms to withdraw from or refuse to enter into any participation agreement. It further prohibits respondent, for a period of ten years, from communicating to another pharmacy firm their decision or intention to enter or refuse to enter into such a participation agreement. In addition, for eight years, it prohibits respondent from advising another pharmacy firm on whether to enter into any participation agreement.

*Appearances*

For the Commission: *Karen Bokat and Michael D. McNeely.*

For the respondent: *Gayl W. Doster, in-house counsel, Pawtucket, R.I. and Neal R. Stoll, Skadden, Arps, Slater, Meagher & Flom, New York City.*

## DECISION AND ORDER

The Federal Trade Commission having initiated an investigation of certain acts and practices of the respondent named in the caption hereof, and the respondent having been furnished thereafter with a copy of a draft of the complaint which the Bureau of Competition proposed to present to the Commission for its consideration and which, if issued by the Commission, would charge respondent with violation of the Federal Trade Commission Act; and

The respondent, its attorney, and counsel for the Commission having thereafter executed an agreement containing a consent order, an admission by the respondent of all jurisdictional facts set forth in the aforesaid draft complaint, a statement that the signing of said agreement is for settlement purposes only and does not constitute an admission by respondent that the law has been violated as alleged in

\*Complaint previously published at 112 FTC 15 (1989).

such complaint, and waivers and other provisions as required by the Commission's Rules; and

The Commission having thereafter considered the matter and having determined that it had reason to believe that the respondent has violated the said Act, and that complaint should issue stating its charges in that respect, and having thereupon accepted the executed consent agreement and placed such agreement on the public record for a period of sixty (60) days, now in further conformity with the procedure prescribed in Section 2.34 of its Rules, the Commission hereby issues its complaint, makes the following jurisdictional findings and enters the following order:

1. Respondent Brooks is a corporation organized, existing, and doing business under and by virtue of the laws of the State of Delaware, with its office and principal place of business at 75 Sabin Street, Pawtucket, Rhode Island.

2. The Federal Trade Commission has jurisdiction of the subject matter of this proceeding and of the respondent, and the proceeding is in the public interest.

#### ORDER

##### I.

For purposes of the order, the following definitions shall apply:

A. "*Brooks*" means Brooks Drug, Inc., a Delaware corporation, its directors, officers, agents, employees, divisions, subsidiaries, successors and assigns;

B. "*Third-party payer*" means any person or entity that provides a program or plan pursuant to which such a person or entity agrees to pay for prescriptions dispensed by pharmacies to individuals described in such plan or program as eligible for such coverage ("Covered Persons"), and includes, but is not limited to, health insurance companies; prepaid hospital, medical, or other health service plans, such as Blue Cross and Blue Shield plans; health maintenance organizations; preferred provider organizations; prescription service administrative organizations; and health benefit programs for government employees, retirees or dependents;

C. "*Participation agreement*" means any existing or proposed agreement, oral or written, in which a third-party payer agrees to

reimburse a pharmacy for the dispensing of prescription drugs to Covered Persons, and the pharmacy agrees to accept such payment from the third-party payer for such prescriptions dispensed during the term of the agreement;

D. "*Pharmacy firm*" means any partnership, sole proprietorship or corporation, including all of its subsidiaries, affiliates, divisions and joint ventures, that owns, controls or operates one or more pharmacies, including the directors, officers, employees, and agents of such partnership, sole proprietorship or corporation as well as the directors, officers, employees, and agents of such partnership's, sole proprietorship's or corporation's subsidiaries, affiliates, divisions and joint ventures, but excludes any partnership, sole proprietorship or corporation, including all of its subsidiaries, affiliates, divisions and joint ventures, which own, are owned by, control or are under common control with Brooks. The words "subsidiary", "affiliate", and "joint venture" refer to any firm in which there is partial (10% or more) or total ownership or control between corporations.

## II.

*It is ordered.* That Brooks, directly, indirectly, or through any corporate or other device, in or in connection with its activities in or affecting commerce, as "commerce" is defined in Section 4 of the Federal Trade Commission Act, shall forthwith cease and desist from:

A. Agreeing or combining, attempting to agree or combine, or taking any action in furtherance of any agreement or combination, advocating an agreement, or organizing or cooperating with any Pharmacy Firm(s) to (1) boycott, refuse to enter into, withdraw from, or not participate in, any Participation Agreement or (2) threaten to boycott, threaten to refuse to enter into, threaten to withdraw from, or threaten not to participate in, any participation agreement;

B. For a period of ten (10) years after the date this order becomes final, stating or communicating in any way to any pharmacy firm the intention or decision of Brooks with respect to entering into, refusing to enter into, threatening to refuse to enter into, participating in, threatening to withdraw from, or withdrawing from any existing or proposed participation agreement into which Brooks and the other pharmacy firm have entered, could enter or are considering entering;

C. For a period of eight (8) years after the date this order becomes final, advising any pharmacy firm with respect to entering into.

refusing to enter into, participating in, or withdrawing from any existing or proposed participation agreement into which Brooks and the other pharmacy firm have entered, could enter or are considering entering.

*Provided*, that nothing in this order shall prevent Brooks from:

(1) Exercising rights permitted under the First Amendment to the United States Constitution to petition any federal or state government executive agency or legislative body concerning legislation, rules or procedures, or to participate in any federal or state administrative or judicial proceeding;

(2) Subcontracting, preparing joint bids, or jointly undertaking with pharmacy firms to provide prescription drug services under a participation agreement if requested to do so in writing by the third-party payer;

(3) Communicating to the public truthful, nondeceptive statements concerning any existing or proposed participation agreement.

In the event that Brooks is merged into or consolidated with its parent corporation, Hook-SupeRx, Inc., the provisions of Paragraph II.B. and C. shall only apply to activities related to or affecting participation agreements in New York, Massachusetts, Vermont, New Hampshire, Rhode Island, Pennsylvania, Connecticut, Maine, New Jersey, and Maryland.

### III.

*It is further ordered*, That Brooks:

A. Provide a copy of this order within thirty (30) days after the date this order becomes final to each officer, director, employee pharmacist who is employed in New York state, and each employee whose responsibilities include recommending or deciding whether to enter into any participation agreement, and each employee who regularly attends meetings on Brooks' behalf that include representatives of other pharmacies; and

B. For a period of five (5) years after the date this order becomes final, provide each new director and each employee who enters a position described in Paragraph A a copy of the order within ten (10) days of the date the employee or director assumes the new position.

## IV.

*It is further ordered,* That Brooks:

A. File a verified, written report with the Commission within ninety (90) days after the date this order becomes final, and annually thereafter for five (5) years on the anniversary of the date this order becomes final, and at such other times as the Commission may, by written notice to Brooks, require, setting forth in detail the manner and form in which it has complied and is complying with this order;

B. For a period of five (5) years after the date this order becomes final, maintain and make available to Commission staff for inspection and copying upon reasonable notice all documents generated by Brooks or that come into Brooks' possession, custody, or control regardless of source, that embody, discuss or refer to the decision or upon which Brooks relies in deciding whether to enter into any participation agreement in which Brooks participates, has participated, or has considered participating; and

C. Notify the Commission at least thirty (30) days prior to any proposed change in Brooks such as, assignment or sale resulting in the emergence of a successor corporation or association, change of name, change of address, dissolution, the creation, sale or dissolution of a subsidiary, or any other change that may affect compliance with this order. Provided however that with respect to the sale of a single subsidiary consisting of three or fewer retail locations, Brooks shall provide such advance notice as is practicable.

Commissioners Azcuenaga and Machol dissenting.

IN THE MATTER OF  
MEDICAL STAFF OF DICKINSON COUNTY  
MEMORIAL HOSPITAL, ET AL.

CONSENT ORDER, ETC., IN REGARD TO ALLEGED VIOLATION OF  
SEC. 5 OF THE FEDERAL TRADE COMMISSION ACT

*Docket C-3259. Complaint, July 17, 1989—Decision, July 17, 1989*

This consent order prohibits, among other things, 12 doctors, the medical staff and two medical societies of Michigan from combining or conspiring to coerce, intimidate, threaten to boycott or boycott other physicians, hospitals and health care providers. In addition, the order requires the respondent Medical Staff to mail a copy of the complaint and order to certain medical officials.

*Appearances*

For the Commission: *David Pender and Paul Nolan.*

For the respondents: *Larry J. Saylor, Miller, Canfield, Paddock & Stone, Detroit, Mi.*

COMPLAINT

Pursuant to the provisions of the Federal Trade Commission Act, and by virtue of the authority vested in it by said Act, the Federal Trade Commission, having reason to believe that the Medical Staff of Dickinson County Memorial Hospital ("Medical Staff"), the individuals named ("individual respondents"), the Dickinson-Iron County Medical Society, and the Delta County Medical Society have violated the provisions of said Act, and it appearing to the Commission that a proceeding by it in respect thereof would be in the public interest, hereby issues its complaint, stating in that respect its charges as follows:

PARAGRAPH 1. Respondent Medical Staff is an unincorporated association, organized and existing under and by virtue of the laws of the State of Michigan, and is located at Dickinson County Memorial Hospital, 400 Woodward Avenue, Iron Mountain, Michigan. The Medical Staff is composed of physicians and other health care practitioners who have privileges to attend patients at Dickinson

County Memorial Hospital. The Medical Staff's physician members constitute almost all of the practicing physicians in Dickinson County.

PAR. 2. Respondent Medical Staff's purposes as expressed in Article II of its by-laws include providing the organizational structure through which the "benefits of membership on the Staff may be obtained by individual practitioners," and providing "a means through which the Medical Staff may participate in the hospital's policy making and planning processes." The Medical Staff's functions include substantial activities that further its members' pecuniary interests. By virtue of its purposes and activities, the Medical Staff is a corporation within the meaning of Section 4 of the Federal Trade Commission Act, as amended, 15 U.S.C. 44.

PAR. 3. The individual respondents are licensed by the State of Michigan and practice in the Upper Peninsula of Michigan in Dickinson County. Their office addresses are: William A. Belding, M.D., Dickinson County Memorial Hospital (DCMH), 400 Woodward Ave., Iron Mountain, MI.; Robert G. Calderwood, D.M.D., Medical Park Clinic, 1005 South Hemlock Street, Iron Mountain, MI.; John M. Cook, M.D., 1001 Hemlock Street, Iron Mountain, MI.; J. Michael Garrett, M.D., 1301 S. Carpenter Avenue, Iron Mountain, MI.; William R. Gladstone, M.D., 804 Main Street, Norway, MI.; Stephen R. Leonard, M.D., Medical Park Clinic, Hemlock Street, Iron Mountain, MI.; John L. Loewen, M.D., 615 Washington Street, Niagara, WI.; Carl H. Reinighaus, D.O., 441 Florence Ave., Florence, WI.; Gary J. Roberts, M.D., Medical Park Clinic, Hemlock Street, Iron Mountain, MI.; John F. Selden, M.D., 401 N. Boulevard, Kingsford, MI.; Mervin J. Specht, M.D., DCMH, 400 Woodward Ave., Iron Mountain, MI.; and Kirk L. Susott, M.D., Medical Park Clinic, Hemlock Street, Iron Mountain, MI. Except to the extent that competition has been restrained as alleged herein, each of the individual respondents has been and now is in competition with at least some of the other individual respondents, or with other physicians or health care practitioners, in the provision of health care services in or near Dickinson County. The individual respondents are engaged in the business of providing health care services to patients for a fee.

PAR. 4. Respondent Dickinson-Iron County Medical Society is an unincorporated association, organized and existing under and by virtue of the laws of the State of Michigan, and is located at 400 Woodward Avenue, Iron Mountain, Michigan. The Dickinson-Iron County Medical Society is composed of physicians in the private

practice of medicine in Dickinson County and in Iron County, in the Upper Peninsula of Michigan. The Dickinson-Iron County Medical Society's physician members constitute almost all of the practicing physicians in Dickinson County, in Iron County, and on the respondent Medical Staff. The Dickinson-Iron County Medical Society's functions include substantial activities that further its members' pecuniary interests. By virtue of its purposes and activities, the Dickinson-Iron County Medical Society is a corporation within the meaning of Section 4 of the Federal Trade Commission Act, 15 U.S.C. 44.

PAR. 5. Respondent Delta County Medical Society is an unincorporated association, organized and existing under and by virtue of the laws of the State of Michigan, and is located at Doctors Park, Escanaba, Michigan. The Delta County Medical Society is composed of physicians in the private practice of medicine in Delta County in the Upper Peninsula of Michigan. The Delta County Medical Society's physician members constitute almost all of the practicing physicians in Delta County. The Delta County Medical Society's functions include substantial activities that further its members' pecuniary interests. By virtue of its purposes and activities, the Delta County Medical Society is a corporation within the meaning of Section 4 of the Federal Trade Commission Act, 15 U.S.C. 44.

PAR. 6. The acts and practices of the respondents, including those herein alleged, are in or affect commerce within the meaning of Section 5 of the Federal Trade Commission Act, as amended, 15 U.S.C. 45.

PAR. 7. Dickinson County Hospitals, a non-profit organization, operates two hospitals in Dickinson County—Dickinson County Memorial Hospital, a 110-bed hospital in the city of Iron Mountain, and Anderson Hospital, a 19-bed hospital in the city of Norway. The Veterans' Administration operates the only other hospital in Dickinson County. Residents of the county receive most of their health care services from physicians and other health care practitioners on the respondent Medical Staff, including the individual respondents, and from Dickinson County Memorial Hospital. For diagnosis and treatment using some complex medical procedures, or by physicians who practice specialties not available in Dickinson County, residents of Dickinson County usually travel to physicians and/or hospitals in Green Bay, Wisconsin (approximately 85 miles south of Dickinson County), Marquette, Michigan (approximately 85 miles north of Dickinson County), or Marshfield, Wisconsin (approximately 140 miles southwest of Dickinson County).

PAR. 8. The individual respondents have been on the active medical staff of Dickinson County Memorial Hospital or Anderson Hospital since at least September, 1986. The individual respondents are either general practitioners, specialize in internal medicine or family practice, or practice in other medical, surgical or dental specialties.

PAR. 9. Marquette General Hospital, which is located in the city and county of Marquette, in the Upper Peninsula of Michigan, is a tertiary care hospital that provides specialized diagnostic and treatment services not available at smaller hospitals in the Upper Peninsula of Michigan, such as Dickinson County Memorial Hospital and Anderson Hospital. Marquette General Hospital provides tertiary care services in such areas as cardiac care, oncology, neurological services, neonatal services, and nephrology. Many specialty and subspecialty physicians on Marquette General Hospital's Medical Staff receive a significant number of referrals from physicians in other parts of the Upper Peninsula, because they offer diagnostic and treatment techniques not available locally. Marquette General Hospital, in turn, derives a substantial portion of its revenues as a result of tests and hospital admissions of patients who were referred to physicians on its medical staff by physicians in other parts of the Upper Peninsula.

PAR. 10. On September 3, 1986, Marquette General Hospital announced plans to build a multispecialty medical office in Kingsford, Michigan, the second largest city in Dickinson County. Kingsford borders Iron Mountain, the largest city in the county, and is within several miles of the Wisconsin border. Marquette General Hospital planned to staff the new office with three salaried primary care physicians, to have some specialty and subspecialty physicians visit Dickinson County more frequently, and to offer some specialized physician services and diagnostic tests that were not previously available in Dickinson County. Marquette General Hospital officials believed that their new medical office in Kingsford would provide valuable primary care and specialty services to consumers of health care services in the Dickinson County area and consequently would attract a substantial number of patients to, and enhance the revenues of, Marquette General Hospital. Marquette General Hospital officials believed the new medical office would permit it to compete more effectively with hospitals in Green Bay, Wisconsin, and Marshfield, Wisconsin, for patients in the Dickinson County area.

PAR. 11. The individual respondents and respondent Medical Staff saw as a competitive threat the prospect of increased competition

from both specialty and primary care physicians who would work in Marquette General Hospital's planned office in Dickinson County, including the salaried primary care physicians who would work there. As a result, beginning in September 1986, the individual respondents entered into a combination or conspiracy to coerce, intimidate, threaten to boycott, or boycott Marquette General Hospital and its physicians in order to prevent the proposed new medical office from offering services to consumers in competition with them. In September 1986, respondent Medical Staff and respondent Dickinson-Iron County Medical Society, acting as combinations of their members or in conspiracy with at least some of their members, joined in the conspiracy to suppress competition from Marquette General Hospital's proposed new medical office in Kingsford, Michigan. In November 1986, respondent Delta County Medical Society, acting as a combination of its members or in conspiracy with at least some of its members, joined in the conspiracy. Throughout the course of the conspiracy, respondent Dickinson-Iron County Medical Society provided support to, and advised its physician members of, the actions undertaken in furtherance of the combination or conspiracy to suppress competition from the proposed new medical office.

PAR. 12. In furtherance of the aforesaid combination or conspiracy, and as described in paragraphs thirteen through twenty-one below:

A. The individual respondents, respondent Medical Staff, and respondent Dickinson-Iron County Medical Society, in response to the Marquette General Hospital's plan to establish a medical office in Dickinson County:

1. Threatened to refuse to refer, or refused to refer, patients to specialist physicians practicing at a Marquette General Hospital medical office in Dickinson County;

2. Agreed to refuse to enter into any contractual relationship with, including possible salaried employment in, Marquette General Hospital's medical office in Dickinson County; and

3. Solicited physicians throughout the Upper Peninsula of Michigan to join in a combination or conspiracy to threaten to cease referring, or to cease referring, patients to physicians practicing at Marquette General Hospital.

B. The individual respondents, respondent Medical Staff, respondent Dickinson-Iron County Medical Society, and respondent Delta County Medical Society threatened to cease referring, or ceased to

refer, patients to specialist physicians practicing at Marquette General Hospital.

PAR. 13. On September 4, 1986, respondent Medical Staff and some individual respondents, at an emergency meeting held to discuss the proposed Marquette General Hospital medical office, authorized an Ad-hoc Executive Committee of the Medical Staff to "actively pursue effective counter measures to this move by Marquette," *i.e.*, its plan to open the clinic. Respondent Loewen was named to this committee because he was then president of respondent Dickinson-Iron County Medical Society. This committee, consisting of individual respondents Belding, Calderwood, Cook, Garrett, Gladstone, Leonard, Loewen, Reinighaus, Roberts, and Specht, met on September 8, 1986, and approved the issuance of a press release which stated in part that: (1) the Medical Staff objected to the establishment of the new medical office in Dickinson County, which was not under "local control," and (2) the new medical office "not only brings in specialists unavailable locally, but also competes directly with services and specialties already present in our hospital." Substantial portions of this press release subsequently appeared in the local newspapers.

PAR. 14. On September 13, 1986, respondent Medical Staff met and the physicians and other health care practitioners present, including Dr. Robert Koski and individual respondents Belding, Calderwood, Cook, Garrett, Leonard, Loewen, Reinighaus, Roberts, and Susott, voted unanimously to approve the following commitment and to seek a written commitment to that effect from each Medical Staff member:

We the Medical Staff of DCH, support the right of the individual practitioner to be non-aligned to any specific institution and, therefore, pledge that we will not cooperate or be hired by the Marquette Hospital Clinic or any subsidiary thereof.

One or more members of respondent Medical Staff distributed a typed version of this statement to the members of the Medical Staff, and it was signed by many of them. On September 22, 1986, the Medical Staff approved a second statement expressing opposition to the medical office. This second statement, which was understood by some or all of the individual respondents to have the same meaning and to serve the same purpose as the first statement, read as follows: "I am opposed to Marquette General Hospital placing a clinic in Dickinson County." Shortly thereafter, the second statement was distributed to, and signed by, almost every member of respondent Medical Staff.

PAR. 15. On September 29, 1986, individual respondents Cook, Leonard, and Specht met on behalf of respondent Medical Staff and all individual respondents with physician representatives of the Medical Staff of Marquette General Hospital. At this meeting, these three individual respondents presented the Marquette physicians with a statement, dated September 29, 1986, which (1) expressed the united opposition of respondent Medical Staff and the individual respondents to Marquette General Hospital's plan to open the new medical office in Dickinson County, and (2) stated they would use "whatever means necessary" to prevent the new office from offering services to patients in competition with them. Respondent Specht, relying on the statements of opposition referred to in paragraph fourteen above, signed this letter as "Chief of Staff and Representative of the Forty-two (42) Physicians on the Medical Staff."

PAR. 16. The Tri-County Medical Society and the Delta County Medical Society have physician members who frequently refer patients to physicians on the staff of Marquette General Hospital. A significant number of these patients undergo tests at, or are admitted to, Marquette General Hospital. On or about January, 1986, officers of the Dickinson-Iron County and Delta County Medical Societies discussed "turf protection and it was unanimously voted by all parties concerned that our relationship with Marquette is favorable and we wish to continue this, however all communities absolutely insist on having the freedom to choose a consultant and recent moves by Marquette administration which signify a move towards mandatory consultation will be aggressively opposed by our societies jointly." This action took place because members of the respondent Dickinson-Iron County and Delta County Medical Societies were concerned that physicians who signed such contracts would increase their referrals to specialists at Marquette General Hospital and decrease their referrals to specialists who belonged to the respondent medical societies. On October 7, 1986, Dr. Robert Koski and individual respondent Selden, as representatives of the other individual respondents and respondent Medical Staff, solicited the Tri-County Medical Society in Calumet, Michigan, to join the combination or conspiracy described in paragraphs eleven through fifteen. On October 21, 1986 individual respondents Leonard, Susott, Belding, and Specht, as representatives of the other individual respondents and respondent Medical Staff, and respondent Loewen, as representative of respondent Dickinson-Iron County Medical Society, solicited the Delta County Medical Society in

Escanaba, Michigan, to join the conspiracy described in paragraphs eleven through fifteen.

PAR. 17. After the individual respondents and Dr. Robert Koski solicited the participation of the Tri-County and Delta County Medical Societies as discussed in paragraph sixteen, the Tri-County Medical Society advised its membership to write individual letters personally expressing their opinion to the physicians in Marquette, but took no other action. On November 18, 1986, however, the Delta County Medical Society unanimously approved a letter that stated the society's official position. The Delta County Medical Society sent this letter to the Presidents of both the Dickinson-Iron County and Marquette-Alger Medical Societies. This letter stated that "if the clinic is constructed as proposed, there will be a definite change in the referral patterns of many Delta County physicians and perhaps physicians in other U.P. counties. We feel that this would be unfortunate for all involved." Officials of Marquette General Hospital saw this as a threat to cut referrals to physicians on its medical staff. One purpose of the letter was to put pressure on Marquette General not to open a similar clinic in the Delta County area. The president of the Delta County Medical Society, accompanied by two society members, thereafter spoke at a meeting of the Marquette-Alger Medical Society and told them "they would have to be aware [a number of Delta] physicians would no longer utilize the services of Marquette unless their patient specifically requested it."

PAR. 18. On October 10, 1986, the Medical Staff Ad-hoc Executive Committee, which was empowered to represent and act on behalf of respondent Medical Staff and the individual respondents, sent a letter to many members of the respondent Medical Staff and to most, if not all, of the physicians in the Upper Peninsula, including physicians on the Medical Staff of Marquette General Hospital. The letter included the following statements: (1) that the Medical Staff intended to do "everything in our power" to prevent the Kingsford, Michigan, medical office from opening as planned; (2) that Upper Peninsula physicians should "reevaluate our relationship with Marquette"; and (3) that Marquette physicians were not welcome in Dickinson County "as salaried employees whose purpose in our community will be to direct traffic to" Marquette. Individual respondents Belding, Calderwood, Cook, Garrett, Gladstone, Leonard, Loewen, Reinighaus, Roberts, and Specht signed this letter as the "Ad hoc Executive Committee on behalf of the forty-two physicians of Dickinson County

Hospitals." Officials of Marquette General Hospital perceived these statements as a threat to cut referrals to physicians on its Medical Staff.

PAR. 19. On December 10, 1986, respondent Medical Staff held a special meeting and voted unanimously that they "remain firmly opposed to the Marquette Clinic." The Medical Staff confirmed its opposition in a March 2, 1987, letter from individual respondents Specht, as chief of respondent Medical Staff, and Leonard, as spokesman for respondent Medical Staff, to the chief of the Marquette General Hospital Medical Staff.

PAR. 20. As a result of the actions described in paragraphs eleven through nineteen, Marquette General Hospital opened a medical office in Kingsford that was smaller than its originally proposed medical office building. This medical office did not offer primary care services to consumers as had originally been planned by Marquette General Hospital. On May 11, 1987, as a result of the actions of respondent Medical Staff, the individual respondents, Dr. Robert Koski, respondent Dickinson-Iron County Medical Society, and respondent Delta County Medical Society, as set forth above, Marquette General Hospital suspended action on its plan to offer primary care services at its Kingsford medical office.

PAR. 21. None of the individual respondents contacted by Marquette General Hospital has agreed to work in the Marquette General Hospital medical office, and a number of the individual respondents, unless requested to do so by their patients, continue to refuse to refer patients to physicians who provide specialized services at the Kingsford medical office.

PAR. 22. The purposes or effects or the tendency and capacity of the combination or conspiracy and conduct described in paragraphs eleven through twenty-one are and have been to restrain trade unreasonably in the provision of health care services in or near Dickinson County, Michigan, and deprive consumers of the benefits of competition, in the following ways, among others:

A. Hindering competition among physicians and hospitals in the provision of health care services;

B. Depriving consumers of their ability to choose among a variety of alternative types of health care facilities and primary care and specialty physicians competing on the basis of price, service, and quality;

C. Impairing Marquette General Hospital's efforts to increase

consumer access to primary care and specialty medical services, including services offered by salaried primary care physicians; and

D. Deterring other hospitals or medical clinics from operating medical facilities in competition with the private practice of physicians.

PAR. 23. The combination or conspiracy and the acts and practices described above constitute unfair methods of competition in violation of Section 5 of the Federal Trade Commission Act, 15 U.S.C. 45. The violation, or the effects thereof, as herein alleged, is continuing and will continue in the absence of the relief herein requested.

#### DECISION AND ORDER

The Federal Trade Commission having initiated an investigation of certain acts and practices of the proposed respondents, and the proposed respondents having been furnished thereafter with a copy of a draft of complaint which the Bureau of Competition proposed to present to the Commission for its consideration and which, if issued by the Commission, would charge respondents with violation of the Federal Trade Commission Act; and

The proposed respondents, and counsel for the Federal Trade Commission having thereafter executed an agreement containing a consent order, an admission by the respondents of all of the jurisdictional facts set forth in the aforesaid complaint, a statement that the signing of said agreement is for settlement purposes only and does not constitute an admission by respondents that the law has been violated as alleged in such complaint, and waivers and other provisions as required by the Commission's Rules; and

The Commission having thereafter considered the matter and having determined that it had reason to believe that the respondents have violated the said Act, and that the complaint should issue stating its charges in that respect, and having thereupon accepted the executed consent agreement and placed such agreement on the public record for a period of sixty (60) days, and having duly considered the comments filed thereafter by interested persons pursuant to Section 2.34 of its Rules, now in further conformity with the procedures prescribed in Section 2.34 of its Rules, the Commission hereby issues its complaint, makes the following jurisdictional findings and enters the following order:

1. Proposed respondent Medical Staff of Dickinson County Memori-

al Hospital ("Medical Staff"), an unincorporated association organized and existing under and by virtue of the laws of the State of Michigan, has its principal place of business at Dickinson County Memorial Hospital, 400 Woodward Avenue, Iron Mountain, Michigan. Proposed respondent Dickinson-Iron County Medical Society is an unincorporated association, organized and existing under and by virtue of the laws of the State of Michigan, and is located at 400 Woodward Avenue, Iron Mountain, Michigan. Proposed respondent Delta County Medical Society is an unincorporated association, organized and existing under and by virtue of the laws of the State of Michigan, and is located at Doctors Park, Escanaba, Michigan. Proposed individual respondents are licensed and do business under and by virtue of the laws of the State of Michigan. Their office addresses are: William A. Belding, M.D., Dickinson County Memorial Hospital (DCMH), 400 Woodward Ave., Iron Mountain, MI.; Robert G. Calderwood, D.M.D., Medical Park Clinic, 1005 South Hemlock Street, Iron Mountain, MI.; John M. Cook, M.D., 1001 Hemlock Street, Iron Mountain, MI.; J. Michael Garrett, M.D., 1301 S. Carpenter Avenue, Iron Mountain, MI.; William R. Gladstone, M.D., 804 Main Street, Norway, MI.; Stephen R. Leonard, M.D., Medical Park Clinic, Hemlock Street, Iron Mountain, MI.; John L. Loewen, M.D., 615 Washington Street, Niagara, WI.; Carl H. Reinighaus, D.O., 441 Florence Ave., Florence, WI.; Gary J. Roberts, M.D., Medical Park Clinic, Hemlock Street, Iron Mountain, MI.; John F. Selden, M.D., 401 N. Boulevard, Kingsford, MI.; Mervin J. Specht, M.D., DCMH, 400 Woodward Ave., Iron Mountain, MI.; and Kirk L. Susott, M.D., Medical Park Clinic, Hemlock Street, Iron Mountain, MI.

2. Proposed individual respondents and proposed respondents Medical Staff, Dickinson-Iron County Medical Society, and Delta County Medical Society admit all of the jurisdictional facts set forth in the draft of complaint here attached.

3. The Federal Trade Commission has jurisdiction of the subject matter of this proceeding and of the respondents, and the proceeding is in the public interest.

#### ORDER

##### I.

For the purposes of this order, the following definitions shall apply:

1. "*Medical Staff*" shall mean the Medical Staff of Dickinson County Memorial Hospital, and its successors, assigns, officers, directors, committees, agents, employees, or representatives.

2. "*Upper Peninsula*" shall mean the Michigan counties of Alger, Baraga, Chippewa, Delta, Dickinson, Gogebic, Houghton, Iron, Keweenaw, Luce, Mackinac, Marquette, Menominee, Ontonagon, and Schoolcraft.

3. "*Individual respondents*" shall mean William A. Belding, M.D.; Robert G. Calderwood, D.M.D.; John M. Cook, M.D.; J. Michael Garrett, M.D.; William R. Gladstone, M.D.; Stephen R. Leonard, M.D.; John L. Loewen, M.D.; Carl H. Reinighaus, D.O.; Gary J. Roberts, M.D.; John F. Selden, M.D.; Mervin J. Specht, M.D.; Kirk L. Susott, M.D.; and their agents, employees, or representatives.

4. "*Dickinson-Iron County Medical Society*" shall mean the Dickinson-Iron County Medical Society, and its successors, assigns, officers, directors, committees, agents, employees, or representatives.

5. "*Delta County Medical Society*" shall mean the Delta County Medical Society, and its successors, assigns, officers, directors, committees, agents, employees, or representatives.

6. "*Integrated joint venture*" means a joint arrangement to provide pre-paid health care services in which physicians who would otherwise be competitors pool their capital to finance the venture, by themselves or together with others, and share substantial risk of adverse financial results caused by unexpectedly high utilization or costs of health care services.

## II.

*It is ordered,* That each individual respondent, respondent Medical Staff, respondent Dickinson-Iron County Medical Society, and respondent Delta County Medical Society, directly or indirectly or through any device, shall henceforth cease and desist from entering into, maintaining, or continuing, or attempting to enter into, maintain, or continue, any agreement or understanding, either express or implied, between or among themselves or with other physicians, health care practitioners, medical societies, hospitals, or medical staffs to:

A. Refuse to deal, threaten to refuse to deal, or attempt to induce others to refuse to deal or threaten to refuse to deal, with any physician, group of physicians, hospital, medical clinic, or other health care provider; and

B. Withhold patient referrals, threaten to withhold patient referrals, or attempt to induce others to withhold patient referrals or threaten to withhold patient referrals, from any physician, group of physicians, hospital, medical clinic, or other health care provider.

### III.

A. *It is provided*, That this order shall not be construed to prohibit the respondent Medical Staff or its members from engaging, pursuant to the Medical Staff's by-laws, in credentialing, corrective action, utilization review, quality assurance, peer review, or hospital policy-making at Dickinson County Memorial Hospital, where such conduct by the Medical Staff neither constitutes nor is part of any agreement, combination, or conspiracy, the purpose or effect of which is to impede competition unreasonably.

B. *It is further provided* That this order shall not be construed to prohibit any individual respondent from entering into an agreement or combination with any physician or other health care practitioner with whom the individual respondent practices in partnership or in a professional corporation, or who is employed by the same person as the respondent.

C. *It is further provided*, That this order shall not be construed to prohibit any respondent physician, respondent Medical Staff, respondent Dickinson-Iron County Medical Society, or respondent Delta County Medical Society from forming, facilitating the formation of, or participating in an integrated joint venture that refuses to deal with any person or entity, as long as the physicians participating in the joint venture remain free to deal with any third-party payor other than through the joint venture.

### IV.

A. *It is further ordered*, That within thirty (30) days after this order becomes final, the respondent Medical Staff shall mail a copy of this order and the accompanying complaint to: (1) the President and each member of the Board of Trustees of Dickinson County Hospitals, Iron Mountain, Michigan; (2) the President of the Board of Trustees of Marquette General Hospital, Marquette, Michigan; and (3) each physician practicing in the Upper Peninsula of Michigan as of the date of service of this order.

B. *It is further ordered,* That each individual respondent shall, within sixty (60) days after this order becomes final, and at any time the Commission, by written notice, may require, file with the Commission a report, in writing, setting forth in detail the manner and form in which the respondent complied with this order and intends to comply with this order.

C. *It is further ordered,* That respondent Medical Staff, respondent Dickinson-Iron County Medical Society, and respondent Delta County Medical Society shall, within sixty (60) days after this order becomes final, and annually on the anniversary date of the initial report for each of the five years thereafter, and at such other times as the Commission by written notice may require, file with the Commission a report, in writing, setting forth in detail the manner and form in which the respondent complied with this order and intends to comply with this order.

D. *It is further ordered,* That for a period of seven (7) years after this order becomes final each individual respondent: (1) shall promptly notify the Commission of any change in respondent's business address; and (2) shall promptly notify the Commission whenever he or she enters into any new business, employment, or hospital affiliation that involves the provision of medical care. Each such notice shall include the individual respondent's new business address and a statement of the business, employment or hospital affiliation in which the individual respondent is newly engaged as well as a description of the individual respondent's duties and responsibilities in connection with the business or employment. The expiration of the notice provision of this paragraph shall not affect any other obligation arising under this order.

E. *It is further ordered,* That respondent Medical Staff, respondent Dickinson-Iron County Medical Society, and respondent Delta County Medical Society shall promptly notify the Commission of any change in their business addresses or of any proposed change in their organizations that may affect compliance obligations arising out of this order.

## IN THE MATTER OF

## PANHANDLE EASTERN CORPORATION

CONSENT ORDER, ETC., IN REGARD TO ALLEGED VIOLATION OF SEC. 7 OF  
THE CLAYTON ACT AND SEC. 5 OF THE FEDERAL TRADE COMMISSION ACT

*Docket C-3260. Complaint, July 17, 1989—Decision, July 17, 1989*

This consent order allows, among other things, the respondent to acquire Texas Eastern Transmission Corp. The order requires respondent to divest its ownership of Truckline Offshore Co. and, for ten years, to obtain FTC approval before acquiring any natural gas pipelines in the affected offshore area.

*Appearances*

For the Commission: *Anthony Low Joseph* and *Ronald B. Rowe*.

For the respondent: *Ky P. Ewing, Jr., Vinson & Elkins*, Washington, D.C. and *Stuart Meiklejohn, Sullivan & Cromwell*, New York City.

## COMPLAINT

The Federal Trade Commission, having reason to believe that respondent Panhandle Eastern Corporation, a corporation subject to the jurisdiction of the Federal Trade Commission, intends to acquire, or has acquired the stock or assets of Texas Eastern Corporation, 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), and that a proceeding in respect thereof would be in the public interest, hereby issues its complaint, pursuant to Section 11 of the Clayton Act (15 U.S.C. 21) and Section 5(b) of the Federal Trade Commission Act (15 U.S.C. 45(b)), stating its charges as follows:

## I. DEFINITIONS

1. For purposes of this complaint, the following definitions shall apply:

a. "*Panhandle*" means Panhandle Eastern Corporation, its subsidiaries, divisions, groups, affiliate entities, and each of their directors, officers, employees, agents and representatives; and each partnership, joint venture, joint stock company or concession in which Panhandle is a participant.

b. "*Texas Eastern*" means Texas Eastern Corporation, its subsidiaries, divisions, groups, affiliate entities, and each of their directors, officers, employees, agents and representatives; and each partnership, joint venture, joint stock company or concession in which Texas Eastern is a participant.

c. "*The acquisition*" means the transaction described, in whole or in part, in paragraph 14 of this Complaint.

d. "*Transportation*" means transportation of natural gas for one's own account as well as for others.

## II. RESPONDENT AND ACQUIRED COMPANY

### A. *Panhandle*

2. Respondent Panhandle is a corporation organized and doing business under the laws of the state of Delaware with its executive offices at 5400 Westheimer Court, Houston, Texas.

3. Respondent Panhandle owns businesses that operate at several levels in the natural gas transportation industry.

4. Respondent had 1987 net income of \$108.2 million on operating revenues of \$1,563.4 million.

5. As of April 25, 1989, respondent Panhandle owns and operates two interstate natural gas pipeline systems consisting of over 17,000 miles of pipeline and 32 mainline compressor stations in the United States.

6. Respondent Panhandle wholly or partially owns (or owns interests in companies that wholly or partially own) the following natural gas pipelines in the United States: Panhandle Eastern Pipe Line Company; Trunkline Gas Company; Stingray Pipeline Company; Northern Border Pipeline Company.

7. At all times relevant herein, respondent Panhandle has been and is now engaged in commerce as "commerce" is defined in Section 1 of the Clayton Act, as amended, 15 U.S.C. 12, and is a corporation whose business is in or affecting commerce as "commerce" is defined in Section 4 of the Federal Trade Commission Act, as amended, 15 U.S.C. 44.

### B. *Texas Eastern*

8. Texas Eastern is a corporation organized and doing business under the laws of the state of Delaware with its executive offices at 1221 McKinney Street, Houston, Texas.

9. Texas Eastern is engaged in the transmission and sale of natural gas, and in the exploration for and production of oil and gas.

10. Texas Eastern had 1987 net income of \$96.1 million on operation revenues of \$3,572.5 million.

11. As of April 25, 1989, Texas Eastern owns and operates a natural gas pipeline system in the United States consisting of approximately 10,495 miles of pipeline.

12. Texas Eastern wholly or partially owns (or owns interests in companies that wholly or partially own) the following pipelines: Texas Eastern Transmission Company; Algonquin Gas Transmission Company.

13. At all times relevant herein, Texas Eastern, has been and is now engaged in commerce as "commerce" is defined in Section 1 of the Clayton Act, as amended, 15 U.S.C. 12, and is a corporation whose business is in or affecting commerce as "commerce" is defined in Section 4 of the Federal Trade Commission Act, as amended, 15 U.S.C. 44.

### III. THE ACQUISITION

14. On or about February 21, 1989, Panhandle commenced a cash tender offer for up to 80 percent of the outstanding shares of the Texas Eastern common stock at \$53 per share with the intent of effecting a merger of Pan Acquisition Company, a Delaware corporation wholly-owned by Panhandle, into Texas Eastern, pursuant to which Texas Eastern would become a wholly-owned subsidiary of Panhandle, all as contemplated in that certain Agreement and Plan of Reorganization entered into among Panhandle, its subsidiary, and Texas Eastern on February 20, 1989. Texas Eastern's Board of Directors has approved the tender offer and recommended its acceptance by Texas Eastern shareholders. If the acquisition is consummated as presently contemplated, the total value of the transaction will be about \$3.22 billion.

### IV. EFFECTS

15. One relevant line of commerce is the transportation of natural gas from producing fields and basins.

16. One relevant section of the country is the area of the Gulf of Mexico off the coast of the states of Louisiana and Texas that contains portions of the areas known as the High Island East Addition Area, High Island East Addition South Extension Area, West

Cameron Area, West Cameron South Addition Area, East Cameron Area, East Cameron South Addition Area and the Garden Banks Area, and any submarkets thereof.

17. Consumption of natural gas in the relevant section of the country is substantially below production, with the result that most production in each of these sections of the country is transported by pipelines to consuming areas along the Gulf Coast and elsewhere in the United States.

18. The business of transporting natural gas by pipeline out of the relevant section of the country is concentrated.

19. It is difficult to enter into the business of transporting natural gas by pipeline in the relevant section of the country.

20. Respondent Panhandle is a 50 percent owner and operator of Stingray Pipeline Company, which operates a large natural gas gathering system extending more than 100 miles into the Gulf of Mexico off the coast of Louisiana. It is primarily in the West Cameron and East Cameron areas.

21. Texas Eastern owns and operates Texas Eastern Gas Pipeline Cameron System, which starts from shore a few miles to the east of Stingray. The Cameron System gathers gas from the West Cameron, East Cameron and Vermilion areas and delivers it onshore.

22. Respondent Panhandle and Texas Eastern, through their ownership interests in the Stingray Pipeline Company and the Texas Eastern Gas Pipeline Cameron System, and in other ways, are direct and substantial competitors in the business of transporting natural gas out of producing fields and basins in the relevant section of the country set out in complaint paragraph 16.

23. The effect of the acquisition may be substantially to lessen competition or tend to create a monopoly in the transportation of natural gas out of producing fields and basins in the relevant section of the country set out in complaint paragraph 16, 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, in the following ways among others:

- a. The acquisition will eliminate actual and potential competition between Panhandle and Texas Eastern;
- b. The acquisition will eliminate actual and potential competition among competitors generally; and
- c. The acquisition will increase concentration in the transportation of natural gas out of producing fields and basins in the relevant

section of the country set out in complaint paragraph 16, therefore increasing the likelihood of collusion.

#### V. VIOLATION CHARGED

24. The proposed acquisition of the stock or assets of Texas Eastern by Panhandle, as set forth in paragraph 14 herein, if consummated, 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.

#### DECISION AND ORDER

The Federal Trade Commission ("the Commission"), having initiated an investigation of the proposed acquisition of the common stock of Texas Eastern Corporation ("Texas Eastern") by Panhandle Eastern Corporation ("Panhandle Eastern") and Panhandle Eastern having been furnished with a copy of a draft complaint that the Bureau of Competition presented to the Commission for its consideration and which, if issued by the Commission, would charge Panhandle Eastern with violations of Section 5 of the Federal Trade Commission Act, as amended, 15 U.S.C. 45, and Section 7 of the Clayton Act, as amended, 15 U.S.C. 18; and

Respondent, its attorneys, and counsel for the Commission having thereafter executed an agreement containing a consent order, an admission by respondent of all the jurisdictional facts set forth in the aforesaid draft of complaint, a statement that the signing of said agreement is for settlement purposes only and does not constitute an admission by respondent that the law has been violated as alleged in such complaint, and waivers and other provisions as required by the Commission's Rules; and

The Commission having thereafter considered the matter and having determined that it had reason to believe that respondent has violated Section 5 and Section 7, and that the complaint should issue stating its charges in that respect, and having thereupon accepted the executed consent agreement and placed such agreement on the public record for a period of sixty (60) days, now in further conformity with the procedure prescribed in Section 2.34 of its Rules, the Commission hereby issues its complaint, makes the following jurisdictional findings and enters the following order:

1. Respondent Panhandle Eastern is a corporation organized under

the laws of Delaware, with its executive offices at 5400 Westheimer Court, Houston, Texas.

2. Texas Eastern is a corporation organized under the laws of Delaware, with its executive offices at 1221 McKinney Street, P.O. Box 2521, Houston, Texas.

3. The Federal Trade Commission has jurisdiction of the subject matter of this proceeding and of respondent, and the proceeding is in the public interest.

#### ORDER

##### I.

As used in this order, the following definitions shall apply:

a. "*Acquisition*" means Panhandle Eastern's acquisition of shares of the common stock of Texas Eastern.

b. "*Panhandle Eastern*" means Panhandle Eastern Corporation, its predecessors, subsidiaries, divisions, groups and affiliates controlled by Panhandle Eastern and their respective directors, officers, employees, agents, and representatives, and their respective successors and assigns.

c. "*Texas Eastern*" means Texas Eastern Corporation as it was constituted prior to the acquisition, its predecessors, subsidiaries, divisions, groups and affiliates controlled by Texas Eastern and their respective directors, officers, employees, agents, and representatives, and their respective successors and assigns.

d. "*Schedule A Properties*" means the assets and businesses listed in Schedule A of this order.

e. "*Trustee*" means a trustee designated as such pursuant to the Voting and Selling Trust Agreement that is Amendment A to the Agreement to Establish a Voting and Selling Trust attached hereto and made part hereof as Appendix I to this order.

f. "*Voting and Selling Trust Agreement*" means the Voting and Selling Trust Agreement that is Attachment A to the Agreement to Establish a Voting and Selling Trust.

##### II

*It is ordered, That:*

(A) Panhandle Eastern shall divest, absolutely and in good faith, the

Schedule A Properties, as well as any additional assets and businesses relating to the transportation of natural gas that Panhandle Eastern may at its discretion include as a part of the assets to be divested and are acceptable to the acquiring entity or entities and the Federal Trade Commission. Provided, however, this obligation to divest shall be satisfied by the divestiture of the Schedule A Properties pursuant to the Agreement to Establish a Voting and Selling Trust. Provided, further, Panhandle Eastern may divest absolutely and in good faith and subject to this order, Texas Eastern Transmission Company if the Federal Trade Commission, in its sole discretion, approves the substitute divestiture of Texas Eastern Transmission Company.

(B) At the earliest opportunity, but no later than 15 days after the appointment of the Trustee, Panhandle Eastern shall resign as the operator of Stingray Pipeline Company.

(C) Panhandle Eastern shall provide the acquiring entity or entities of the Schedule A Properties gas transportation and exchange arrangements to the extent necessary to ensure divestiture of the properties as ongoing viable businesses engaged in the same business in which the Schedule A Properties are presently employed.

(D) The Agreement to Establish a Voting and Selling Trust shall continue in effect until such time as the Federal Trade Commission has approved Panhandle Eastern's divestitures of the Schedule A Properties or until such other time as that agreement provides, and Panhandle Eastern shall comply with all terms of that agreement.

(E) Divestiture of the Schedule A Properties shall be made only to an acquiring entity or entities that receive the prior approval of the Federal Trade Commission and only in a manner that receives the prior approval of the Federal Trade Commission. The purpose of the divestiture of the Schedule A Properties is to ensure the continuation of the assets as ongoing, viable businesses engaged in the same businesses in which the Properties are presently employed and to remedy the lessening of competition resulting from the Acquisition as alleged in the Federal Trade Commission's complaint.

(F) Panhandle Eastern shall take such action as is necessary to maintain the viability and marketability of the Schedule A Properties, including the payment of operating expenses if necessary, and shall not cause or permit the destruction, removal or impairment of any assets or businesses to be divested except in the ordinary course of business and except for ordinary wear and tear.

## III.

*It is further ordered, That:*

(A) Within ten (10) days of the appointment of the Trustee Panhandle Eastern shall transfer the Schedule A Properties to the Trustee whose powers and duties and terms of service are defined in the Voting and Selling Trust Agreement. Panhandle Eastern shall be bound by the terms and conditions of the Agreement to Establish a Voting and Selling Trust and by the Voting and Selling Trust Agreement. The appointment of the Trustee shall not preclude the Federal Trade Commission from seeking civil penalties or any other relief available to it for any failure by Panhandle Eastern to comply with this order.

(B) The Trustee shall have eighteen (18) months from the date the duty to sell arises under paragraph 6.c of Voting and Selling Trust Agreement to accomplish the divestiture, which shall be subject to the prior approval of the Federal Trade Commission. If, however, at the end of the eighteen-month period the Trustee has submitted a plan of divestiture or believes that divestiture can be achieved within a reasonable time, the Trustee's divestiture period may be extended by the Federal Trade Commission. Provided, however, that the Federal Trade Commission may extend the Trustee's divestiture period only two (2) times.

(C) No later than thirty (30) days after receiving the prior approval of the Federal Trade Commission of a divestiture of the Schedule A properties, Panhandle Eastern shall in good faith apply for (and cause the acquiring entity or entities as part of the agreement to apply for) approvals by any state or federal agency from which approval must be obtained before Panhandle Eastern may divest and the acquiring entity or entities may acquire, own and operate the Schedule A Properties. Panhandle Eastern shall cooperate with and shall support in good faith with all due diligence and expedition the acquiring entity or entities in obtaining necessary regulatory approvals, including filing a statement that demonstrates Panhandle Eastern's support for each such application. Panhandle Eastern shall take no action to impede or interfere with the necessary regulatory approvals.

(D) The Trustee shall have full and complete access to the personnel, books, records and facilities of any businesses that the Trustee has the duty to divest. Panhandle Eastern shall develop such financial or other information as such Trustee may reasonably request

and shall cooperate with the Trustee. Panhandle Eastern shall take no action to interfere with or impede the Trustee's accomplishment of the divestiture.

(E) Subject to Panhandle Eastern's absolute and unconditional obligation to divest at no minimum price and the purpose of the divestiture as stated in Section II(E) of this order, the Trustee shall use his or her best efforts to negotiate the most favorable price and terms available for the divestiture of the Schedule A Properties. The divestiture shall be made in the manner set out in Section II; provided, however, if the Trustee receives bona fide offers from more than one acquiring entity or entities, the Federal Trade Commission shall determine whether to approve each such purchaser, and the Trustee shall divest to the acquiring entity or entities selected by Panhandle Eastern from among those approved by the Federal Trade Commission.

(F) The Trustee shall be compensated as provided in the Voting and Selling Trust Agreement. He or she shall serve, on such reasonable and customary terms and conditions as the Federal Trade Commission may set, including the employment of accountants, attorneys or other persons reasonably necessary to carry out the Trustee's duties and responsibilities. To the extent the trust properties do not have sufficient working capital or distributions to cover expenses and assure that the Trustee can serve on reasonable terms and conditions, Panhandle shall provide the necessary working capital. The Trustee shall account for all monies derived from the sale and all expenses incurred. After approval by the Federal Trade Commission of the account of the Trustee, including fees for his or her services, all remaining monies shall be paid at the direction of Panhandle Eastern and the Trustee's power shall be terminated.

(G) If the Trustee ceases to act or fails to act diligently, a substitute Trustee shall be appointed in the same manner as provided in Section III(A) of this order.

(H) The Trustee shall report in writing to Panhandle Eastern and the Federal Trade Commission every sixty (60) days concerning the Trustee's efforts to accomplish divestiture.

(I) Panhandle Eastern may terminate the trust if the divestiture of Texas Eastern Transmission Company has been completed in accordance with the terms of the consent order.

## IV.

Within 12 months of the termination of the Voting and Selling Trust Agreement, pursuant to paragraph 6.a.iv thereof, Panhandle Eastern shall divest, absolutely and in good faith, the Schedule A Properties, as well as any additional assets and businesses relating to the transportation of natural gas that Panhandle Eastern may at its discretion include as a part of the assets to be divested and are acceptable to the acquiring entity or entities and the Federal Trade Commission.

## V.

*It is further ordered,* That within sixty (60) days after the date this order becomes final and every sixty (60) days thereafter until Panhandle Eastern has fully complied with the provisions of Sections II and III of this order, Panhandle Eastern shall submit to the Federal Trade Commission a verified written report setting forth in detail the manner and form in which it intends to comply, is complying or has complied with those provisions. Panhandle Eastern shall include in its compliance reports, among other things that are required from time to time, a full description of all contacts or negotiations with prospective acquirers for the divestiture of assets or businesses specified in Section II or Section IV of this order, including the identity of all parties contacted. Panhandle Eastern also shall include in its compliance reports, copies of all written communications to and from such parties, all internal memoranda, reports and recommendations concerning divestiture, and a description of the status of all regulatory proceedings filed in accordance with this order.

## VI.

*It is further ordered,* That for a period commencing on the date this order becomes final and continuing for ten (10) years, Panhandle Eastern shall cease and desist from acquiring, without the prior approval of the Federal Trade Commission, directly or indirectly, through subsidiaries or otherwise, assets used or previously used by (and still suitable for use by), any interest in, or the stock or share capital of any natural gas pipeline any part of which is located in a quadrilateral shaped area of the Central and Western Gulf of Mexico (as those areas are designated by the Mineral Management Service of

the United States Department of Interior) cornered by and including the following blocks: High Island East Addition Block A-221, Garden Banks Block 971, Garden Banks Block 999, and Vermilion Block 206. One year from the date this order becomes final and annually for nine years thereafter Panhandle Eastern shall file with the Federal Trade Commission a verified written report of its compliance with this paragraph. Provided nothing in this order shall require prior Federal Trade Commission approval (1) of the construction of new facilities or (2) if, and only if, Panhandle Eastern has provided the Federal Trade Commission with thirty (30) days prior notice, of the acquisition of stocks or assets if the total consideration, including assumption of liabilities of the present owner of such stock or assets, does not exceed one million dollars (\$1,000,000).

#### VII.

*It is further ordered,* That for the purposes of determining or securing compliance with this order, and subject to any legally recognized privilege, upon written request and on reasonable notice to Panhandle Eastern made to its principal office, Panhandle Eastern shall permit any duly authorized representatives of the Federal Trade Commission:

(A) Access, during office hours and in the presence of counsel, to inspect and copy all books, ledgers, accounts, correspondence, memoranda and other records and documents in the possession or under the control of Panhandle Eastern relating to any matters contained in this order; and

(B) Upon five days notice to Panhandle Eastern and without restraint or interference from Panhandle Eastern, to interview officers or employees of Panhandle Eastern who may have counsel present, regarding such matters.

#### VIII.

*It is further ordered,* That Panhandle Eastern shall notify the Federal Trade Commission at least thirty (30) days prior to any proposed change in the corporation that may affect compliance with this order. Panhandle Eastern shall also notify the Federal Trade Commission at least thirty (30) days prior to any proposed change in Trunkline Gas Company such as dissolution, assignment or sale

resulting in the emergence of a successor corporation, the creation or dissolution of subsidiaries or any other change that may affect compliance obligations arising out of the order.

### SCHEDULE A

#### Assets, Interests and Businesses

- (1) Panhandle Eastern's interest in the Stingray Pipeline Company.
- (2) Trunkline Offshore Company. Provided, however, if the divestiture of Trunkline Offshore Company results in the divestiture of Panhandle Eastern's interest in the Stingray Pipeline Company, Panhandle Eastern shall divest only Trunkline Offshore Company.

### APPENDIX I

#### AGREEMENT TO ESTABLISH A VOTING AND SELLING TRUST

This Agreement to Establish a Voting and Selling Trust (this "Agreement") is by and between Panhandle Eastern Corporation ("PEC"), a Delaware corporation, and the Federal Trade Commission (the "Commission"), an independent agency of the United States Government, established under the Federal Trade Commission Act of 1914, 15 U.S.C. 41, *et seq.* (collectively, the "Parties").

#### PREMISES

*Whereas*, Pan Acquisition Co., a wholly-owned subsidiary of PEC, commenced a tender offer on February 21, 1989, as amended, for up to 48,650,000 of the outstanding shares of Texas Eastern Corporation ("TEC") with the intent of effecting a merger of Pan Acquisition Co. into TEC pursuant to which TEC would survive and become a subsidiary of PEC (the "Acquisition"), all as contemplated by and provided for in that certain Merger Agreement entered into among PEC, Pan Acquisition Co. and TEC dated as of February 20, 1989;

*Whereas*, the Commission is now investigating the transaction to determine if the Acquisition would violate any of the statutes enforced by the Commission; and

*Whereas*, if the Commission accepts the attached Agreement Containing Consent Order ("Consent Order"), the Commission must place it on the public record for a period of at least sixty (60) days and

may subsequently withdraw such acceptance pursuant to the provisions of Section 2.34 of the Commission's Rules; and

*Whereas*, the Commission is concerned that if an understanding is not reached, preserving the *status quo ante* of certain pipeline assets and businesses of PEC's wholly-owned subsidiary, Trunkline Offshore Company ("TOC") and the associated interest as a fifty percent (50%) partner of Stingray Pipeline Company ("Stingray"), during the period prior to the final acceptance of the Consent Order by the Commission (after the 60-day public notice period), divestiture resulting from any proceeding challenging the legality of the Acquisition might not be possible, or might be less than an effective remedy; and

*Whereas*, the Commission is concerned that if the Acquisition is consummated, it will be necessary to preserve the Commission's ability to require the divestiture of properties described in Schedule A to the Consent Order (the "Schedule A Properties") as a viable competitor; and

*Whereas*, the purpose of this Agreement and the Consent Order is to put TOC and its associated interest in Stingray in the hands of a trustee who will be charged:

(a) If the Commission accepts the Consent Order, with selling TOC in order to remedy any anticompetitive effects of the Acquisition, and

(b) In the interim, with managing TOC and its interest in Stingray, to preserve the independence, viability and marketability of TOC and its interest in Stingray; and

*Whereas*, PEC entering into this Agreement shall in no way be construed as an admission by PEC that the Acquisition is illegal; and

*Whereas*, PEC understands that no act or transaction contemplated by this Agreement shall be deemed immune or exempt from the provisions of the antitrust laws or the Federal Trade Commission Act by reason of anything contained in this Agreement.

*Now, Therefore*, the Parties agree, upon understanding that the Commission has not yet determined whether the Acquisition will be challenged, and in consideration of the Commission's agreement that, unless the Commission determines to reject the Consent Order, it will not seek further relief from PEC with respect to the Acquisition, except that the Commission may exercise any and all rights to enforce this Agreement, the Voting and Selling Trust Agreement that is Attachment A to this Agreement ("Voting and Selling Trust Agreement"), and the Consent Order to which this Agreement is annexed and made a part thereof:

1. PEC agrees to execute and be bound by the attached Consent Order.

2. Within thirty (30) days of the date on which the Commission accepts this Agreement, the Commission shall appoint a trustee pursuant to an agreement with PEC on the appointment of a trustee. Such trustee shall act in accordance with the Voting and Selling Trust Agreement.

3. If PEC and the Commission are unable to agree on the appointment of a trustee within thirty (30) days, the Commission shall select the trustee, subject to the consent of PEC, which consent shall not be unreasonably withheld. The trustee shall be a person with experience and expertise in acquisitions and divestitures.

4. Within ten (10) days of appointment of the Trustee, PEC shall transfer to the Trustee, all the shares of TOC and the associated interest in Stingray. PEC shall observe all the terms and conditions of the Voting and Selling Trust Agreement once executed.

5. In the event the Commission has not finally approved and issued the Consent Order within one hundred twenty (120) days of its publication in the Federal Register, PEC, may, at its option, terminate this Agreement by delivering written notice of termination to the Commission, which termination shall be effective ten (10) days after the Commission's receipt of such notice, and the shares in TOC and the associated interest in Stingray shall then revert to PEC. If this Agreement is so terminated, the Commission may take such action as it deems appropriate, including but not limited to an action pursuant to Section 13 (b) of the Federal Trade Commission Act, 15 U.S.C. 53 (b). Termination of this Agreement shall in no way operate to terminate the Consent Order.

6. For the purpose of determining or securing compliance with this Agreement, subject to any legally recognized privilege, and upon written request with reasonable notice to PEC made to its principal office, PEC shall permit any duly authorized representative or representatives of the Commission:

a. Access during the office hours of PEC and in the presence of counsel to inspect and copy all books, ledgers, accounts, correspondence, memoranda, and other records and documents in the possession or under the control of PEC relating to compliance with this Agreement;

b. Upon five (5) days notice to PEC, and without restraint or

interference from it, to interview officers or employees of PEC, who may have counsel present, regarding any such matters.

No information or documents obtained by the Commission shall be divulged by any representative of the Commission to anyone outside the Commission, except in legal proceedings, a request from Congress, a request from a Congressional Committee, to secure compliance with this Consent Order, or as otherwise permitted by law.

If at any time information or documents are furnished by PEC and PEC identifies such documents as "Confidential," then the Commission shall provide to PEC ten (10) days notice or, if ten (10) days is not possible, as many days notice as possible prior to divulging such material.

7. This agreement shall not be binding until approved by the Commission.

## ATTACHMENT A

### VOTING AND SELLING TRUST AGREEMENT

This Voting and Selling Trust Agreement (this "Agreement") is entered into on \_\_\_\_\_ 1989, by and between Panhandle Eastern Corporation ("PEC"), and \_\_\_\_\_ ("Trustee"). For the purposes of this Agreement, PEC means Panhandle Eastern Corporation, its subsidiaries, divisions, groups, and affiliates controlled by PEC and their respective directors, officers, employees, agents and representatives, and their respective successors and assigns.

### WITNESSETH

*Whereas*, PEC has agreed, subject only to final approval and issuance by the Federal Trade Commission (the "Commission") of a proposed Agreement Containing Consent Order ("Consent Order"), to divest all of the outstanding stock and assets of Trunkline Offshore Company ("TOC") and its associated interest as a fifty percent (50%) partner in Stingray Pipeline Company ("Stingray");

*Whereas*, the Commission and PEC have agreed that pending Commission deliberations about whether finally to accept the Consent Order, the voting stock of TOC and its associated interest in Stingray be placed in a voting trust to be administered by an independent Trustee to effectuate the Consent Order and in accordance with the terms and conditions of this Agreement;

*Whereas*, the Trustee intends to act in furtherance of assuring that TOC and the associated interest in Stingray will remain viable and competitively independent of PEC, to allow the Commission the opportunity to complete its deliberations while preserving the Commission's ability to obtain effective divestiture or other appropriate relief if it decides any is needed;

*Whereas*, if the Commission finally accepts the Consent Order the Trustee will undertake to sell the shares of TOC, and its associated interest in Stingray, as promptly as practicable and at the highest available price that is consistent with the Consent Order, but at no minimum price, all in accordance with this Agreement, the Consent Order, and the Agreement to Establish a Voting and Selling Trust.

*Now, Therefore*, in consideration of the foregoing and of the mutual promises, covenants and agreements hereinafter set forth, the parties hereto agree as follows:

1. Creation, Purpose and Term of Voting and Selling Trust.

a. Subject to the terms and conditions hereof, a voting and selling trust (the "Voting and Selling Trust") in respect of the shares of common stock of TOC owned by PEC (the "Stock") is hereby created.

b. Trustee accepts the trust created by this Agreement, and agrees to his or her appointment as trustee hereunder.

c. The Voting and Selling Trust created hereunder shall remain in effect (i) until the earlier of (A) termination of the Agreement to Establish a Voting and Selling Trust, under Section 5 of that agreement or (b) the date the Commission withdraws the acceptance of the Consent Order, if it decides to do so, or, (ii) if the Commission finally accepts the Consent Order, until the termination date defined in Section 6.a, 6.b, or 6.c, of this Agreement.

2. Solicitation, Collection, Acquisition and Ownership of Stock;  
Voting Trust Certificates.

a. PEC agrees to transfer and deliver, within ten (10) days after appointment of the Trustee, certificates representing all shares of Stock endorsed or accompanied by proper instruments duly executed for transfer to the Trustee pursuant to this Agreement.

b. Such certificates shall at all times be and remain in the possession and under the control of the Trustee.

c. Each certificate representing shares of Stock shall bear a legend to the effect that it is subject to this Voting Trust Agreement. The

Trustee shall promptly file with the Secretary of TOC a duplicate of this Agreement. The Trustee shall also maintain such other records and books as are necessary or appropriate to enable him or her to carry out the terms and provisions of this Agreement.

### 3. Retention of Deposited Stock by Trustee.

The Trustee shall retain and hold, personally or through an agent, the certificates representing Stock only in accordance with, and subject to the terms and conditions set forth in, this Agreement. The Trustee shall not have authority to sell, transfer, assign, pledge or otherwise dispose of or encumber the Stock, except in the ordinary course of business, as necessary or appropriate to effectuate the Consent Order, or to the extent otherwise specifically provided in this Agreement.

### 4. Rights and Duties of the Trustee.

a. During the term of this Agreement and for so long as the Trustee shall hold the Stock pursuant to this Agreement, the Trustee shall possess, and, in his or her sole discretion, subject to the provisions of this Section, shall be entitled to and have the duty to exercise all voting rights of the Stock, including the right to vote the Stock on all matters upon which the holders of the Stock are entitled to vote, specifically including the right to appoint or elect members to the Management Committee of Stingray. PEC shall not attempt to exercise any voting power, influence, or control, directly or indirectly, over the conduct of business by TOC or Stingray. The Trustee shall use his or her best business judgment in exercising such voting trust power in a manner consistent with the purpose and requirements of this Agreement, the Consent Order and the Agreement to Establish a Voting and Selling Trust. The Trustee shall be independent of and unrelated to any current or prospective participant in the gathering or transmission of natural gas in the Outer Continental Shelf of the United States but may, consistent with this Agreement and in exercise of his or her discretion, seek to obtain from any such participant, including PEC, information deemed by the Trustee to be helpful to the conduct of the business of TOC.

b. The Trustee shall exercise his or her right to vote the Stock in the election of directors of TOC. The Trustee shall have sole discretion in choosing the identity of any directors he or she is authorized to nominate and to seek to elect. The Trustee may, but is not required to,

nominate and vote for the election of himself or herself to the Board of Directors of TOC. The Trustee shall not vote to elect to the Board of Directors of TOC or the Management Committee of Stingray any person who is an officer, employee, director, agent, representative, shareholder, or affiliate of PEC, nor, after due inquiry, any person who has a business or familial relationship with PEC or any officer, employee, director, agent, representative, shareholder or affiliate of PEC.

c. No other person shall have any voting right in respect to the Stock so long as this Agreement is in effect. The Trustee shall have no beneficial interest in the Stock in his or her capacity as trustee.

d. The Trustee shall have any and all such further powers, and shall take such further actions (including but not limited to legal action) as may be necessary to preserve the corporate assets and confidential, competitively sensitive information of TOC and to fulfill the Trustee's obligations under this Agreement.

e. The Trustee shall take or shall cause to be taken such action as is necessary or appropriate to effectuate the terms of the Consent Order.

f. The Trustee shall take all steps to ensure that TOC competes as vigorously with PEC as if there were no relationship between PEC and TOC. In furtherance of this obligation, the Trustee shall ensure there is no communication between TOC and PEC employees, except with respect to commercial arrangements made at arm's length in the ordinary course of business, in connection with the continued performance by Trunkline Gas Company of duties as Operator of Stingray (only as long as that is necessary to install a successor), and in connection with the provision of information required by PEC for financial and tax reporting purposes as set forth in the Order. The Trustee shall ensure there is no transfer or disclosure of confidential, competitively sensitive information between PEC and TOC; if any such communications or transfers or disclosures of information are made, the Trustee shall immediately notify the Commission.

#### 5. Restrictions on PEC.

a. PEC shall not be involved, directly or indirectly, in the operation or management of TOC or Stingray, nor seek to influence directly or indirectly the operation or management of TOC. TOC shall be maintained as a separate corporate entity with an independent Board of Directors. In no event shall any director, officer, employee, agent or representative of PEC become or remain a member of TOC's Board of

Directors or become or remain an officer of TOC or serve on the Stingray Management Committee. Nor may any director, officer, employee, agent or representative of TOC become or remain a member of PEC's Board of Directors or become or remain an officer of PEC. The independent TOC Board of Directors shall maintain separate corporate books and records for TOC. Except as authorized by this Agreement, PEC and TOC shall not transfer assets between them, except for commercial arrangements made at arm's length in the ordinary course of business, nor engage in any joint activity, during the term of this Order except following reasonable notice to the Commission. PEC and TOC (or Stingray) shall not extend any existing contracts or agreements between them, or change the terms of such agreements in any way, during the term of this Agreement except following reasonable notice to the Commission. The Trustee shall provide the Commission with a full description of the proposed transaction and copies of all documents related thereto. The Commission's Bureau of Competition shall also be promptly provided with copies of TOC's and Stingray's separate quarterly and annual financial statements and capital spending reports, and other financial information upon request, during the term of this Agreement.

b. PEC shall not seek or obtain, directly, or indirectly, any of TOC's or Stingray's trade secrets, nonpublic financial and accounting books and records, or other confidential, competitively sensitive information; *provided, however*, that PEC may seek and obtain upon application to the Trustee and 30 days notice to the Commission with a copy of the application, such financial information from TOC as is necessary for PEC to prepare and file financial and tax reports to the extent required by law, provided that (i) PEC's application shall specify in detail the need for the information requested; (ii) for purposes of tax reports PEC shall not seek or obtain information at a level of detail greater than necessary to prepare and file tax reports required by law, and shall certify to the Trustee that its request for information is so limited; (iii) the Trustee shall provide only the information that it determines is necessary for the preparation of the financial and tax reports; (iv) information required for tax reports shall be provided or disclosed only to designated individuals within PEC's tax department who are responsible for the analysis of the information and preparation of the required tax reports, and information required for financial reports shall be provided or disclosed only to designated individuals within PEC's accounting department; (v) each designated individual in

the tax department and accounting department shall submit to the Trustee an affidavit in the form appended hereto as Attachment 1 or Attachment 2, whichever is applicable; and (vi) PEC shall use such information only for the preparation and filing of such required financial and tax reports and not for any other purposes whatsoever.

c. PEC shall not make available to TOC or Stingray, directly or indirectly, any of PEC's trade secrets, nonpublic financial or accounting books or records, or other confidential or competitively sensitive information.

d. Except as otherwise permitted by the Order or by any other term of this Agreement, no communications shall be made to the Trustee by PEC regarding the operation or management of TOC or Stingray. PEC may communicate to the Trustee for ministerial purposes as to the transfer of the Stock pursuant to Sections 6.a, 6.b, and 6.c of this Agreement, *provided, however*, that any such permitted communication shall be in writing.

e. Nothing in this Agreement shall prevent PEC from finding and tendering to the Trustee potential purchasers for the Stock. Any such sale would be subject to the Consent Order.

#### 6. Termination of the Voting Trust Agreement

a. This Agreement and the voting trust created hereby shall terminate, on the first to occur of the following:

i. The distribution of the Stock to PEC pursuant to Section 6.b of this Agreement; or

ii. The sale or other disposition of all of the Stock to a party other than PEC pursuant to Section 6.c of this Agreement; or

iii. PEC's exercise of its right to terminate as provided in Section III(I) of the Consent Order; or

iv. The expiration of the divestiture period defined by Section III(B) of the Consent Order.

b. The Trustee shall cause the certificates representing all of the Stock to be delivered to PEC, properly endorsed for transfer to PEC, and shall take all other actions appropriate to effectuate the transfer to PEC of title of the Stock and all other property held by the Trustee pursuant to this Agreement, within five (5) business days, if the Commission issues a final order rejecting the proposed Consent Order or if the Agreement to Establish a Voting and Selling Trust is terminated under Section 5 of the Agreement to Establish a Voting and Selling Trust.

c. The Trustee shall cause the certificates representing all of the Stock to be sold if the Commission finally accepts the Consent Order.

d. In disposing of the Stock pursuant to Section 6.c hereof, the Trustee shall faithfully implement the Consent Order. The Trustee's charge shall be to sell the Stock pursuant to the Consent Order as promptly as possible at the highest available price but at no minimum price. PEC shall immediately be provided access to the information (other than competitively sensitive information) submitted to the Commission for its determination of whether this charge has been fulfilled. The implementation and interpretation of this Agreement and the Consent Order shall be in the sole discretion of the Commission.

e. Upon disposing of the Stock pursuant to Section 6.c hereof, the Voting and Selling Trust shall terminate in accordance with Section III(F) of the Consent Order.

#### 7. Concerning the Trustee.

a. Subject to the provisions of this Agreement, the voting trust created hereby shall be managed by the Trustee.

b. The Trustee shall be compensated by PEC in return for his or her services as trustee hereunder. As further provided in Section III(F) of the Consent Order, the Commission shall determine compensation when the Trustee is appointed. PEC may provide the Commission, solely as an aid to its determination in this respect, any information PEC deems appropriate, including compensation paid and other similar arrangements. The Trustee shall be compensated in the following manner. The Trustee shall receive his or her normal hourly billing rate, which shall constitute a draw against a future commission, plus reasonable expenses, if any. If the Stock is sold to a third party, the Trustee shall receive a commission, plus reasonable expenses, if any. If the Stock is returned to PEC in accordance with Section 6.b or 6.a.iii, the Trustee shall receive his or her normal hourly billing rate plus reasonable expenses.

c. The Trustee warrants that he or she is not and covenants that he or she shall not become an officer, employee, director, or shareholder of PEC, or of any of its affiliates.

d. The Trustee is expressly authorized to incur and pay from the Stingray cash contribution to TOC his or her draw, all reasonable charges and other expenses as provided in Section III(F) of the Consent Order. PEC agrees to indemnify and hold harmless the

Trustee against all claims, costs of defense of claims (including reasonable attorney's fees and disbursements), reasonable expenses and liability incurred by the Trustee in connection with the performance of his or her duties under this Agreement, except those incurred as a result of the Trustee's own intentional wrongful actions, willful misconduct, or gross negligence.

e. The Trustee shall be free from liability in acting upon any paper, document or signature believed by the Trustee to be genuine and to have been signed by the proper party. The Trustee shall not be liable for any error of judgment in any act done or omitted, nor for any mistake of fact or law, nor for anything the Trustee may do or refrain from doing in good faith. The Trustee may consult with legal counsel of his or her choice and any action under this Agreement taken or suffered in good faith by the Trustee in accordance with the opinion of the Trustee's counsel shall be conclusive on PEC and the Trustee shall be fully protected and be subject to no liability in respect thereto.

f. The rights and duties of the Trustee hereunder shall terminate upon the Trustee's incapacity to act, death, insolvency or dissolution, and no interest in any of the Stock held by the Trustee nor any of the rights and duties of the incapacitated, deceased, insolvent or dissolved Trustee may be transferred by will, devise, succession or in any manner except as provided in this Agreement. The heirs, administrators, executors or other representatives of such incapacitated, deceased, insolvent or dissolved Trustee shall, however, have the right and duty to convey the Stock held by the Trustee to one or more successor trustees.

g. The Trustee may resign by giving thirty (30) days advance written notice of his or her resignation to the Commission and PEC, provided that a successor Trustee has been appointed.

h. In the event of such resignation, incapacity to act or the death, insolvency or dissolution of the Trustee, the Trustee shall be succeeded by a successor Trustee chosen by the Commission, subject to the consent of PEC which shall not be unreasonably withheld, which successor Trustee shall be altogether independent of, and unrelated to, any current or prospective participant in the business of gathering or transmission of natural gas in the Outer Continental Shelf of the United States. Any successor Trustee appointed as herein provided shall indicate his or her acceptance of such appointment by executing a counterpart of this Agreement and thereupon such successor shall be vested with all the rights, powers, duties and

immunities herein conferred upon the Trustee as though such successor had been originally a party to this Agreement as Trustee. The term "Trustee" as used in this Agreement shall apply to and mean the original Trustee (so long as he or she is a Trustee) hereunder and his or her successors.

#### 8. Periodic Distributions, Conservation of Assets and Proceeds of Sale of Deposited Stock.

a. PEC shall be entitled to receive from time to time payments from Stingray cash distributions to TOC to whatever extent the Trustee, in his or her sole discretion, believes prudent in light of the purpose of the Voting and Selling Trust. Such payments shall be made by the Trustee as soon as practicable after the receipt of the distribution. In lieu of receiving cash distributions and paying them to PEC, the Trustee may instruct TOC in writing to pay the cash directly to PEC. In the event any such instruction is given to TOC, all liability of the Trustee with regard to payment shall cease, unless and until such instruction is revoked. The Trustee may at any time revoke such instruction by written notice to TOC and direct it to make subsequent payments to the Trustee.

b. In the event of the sale of all the Stock, the Trustee shall receive, for the benefit of PEC, the money, securities, rights or property that is or are distributed or distributable in respect of the Stock, or that is or are received in exchange for the Stock. During the term of this Agreement, the Trustee and the Board of Directors of TOC shall use their best efforts to maintain the value of TOC's assets and shall not sell, transfer, encumber or otherwise impair their marketability, other than in the normal course of business, upon reasonable notice to the Commission and PEC.

c. If at any time during the term of this Agreement the Trustee shall receive or collect any money or other property (other than voting securities of TOC) on behalf of TOC, other than as set forth in Sections 8.a or 8.b, the Trustee shall distribute such money or other property to PEC to the extent the Trustee, in his or her sole discretion, believes prudent in light of this Agreement.

#### 9. Miscellaneous.

a. This Agreement constitutes the entire agreement between the parties hereto with respect to the subject matter hereof and supersedes all prior oral and written agreements, commitments or understandings with respect to the matters provided for herein.

b. This Agreement shall be binding upon and shall inure to the benefit of the parties hereto and their respective permitted successors and permitted assigns. This Agreement shall not be assignable by any party, except in the event of the resignation, incapacity, insolvency, dissolution or death of any Trustee and the appointment of a successor Trustee in accordance with Section 7.h hereof.

c. All notices and other communications given under this Agreement shall be in writing and shall be deemed to have been duly given when delivered in person or mailed by first class, registered or certified mail, postage prepaid or transmitted by telex or telegram and addressed to:

i. If to PEC: John A. Sieger, Esquire, Panhandle Eastern Corporation, 5400 Westheimer Court, Houston, Texas

ii. If to the Trustee:

iii. If to the Commission: Anthony Low Joseph, Esquire, Federal Trade Commission, 601 Pennsylvania Avenue N.W., Washington, D.C. 20580

or to such other address as any of them designate, with copies also sent to such attorney as the Commission, PEC, or the Trustee may from time to time designate. Each notice or other communication which shall be personally delivered, mailed or transmitted in the manner described above shall be deemed sufficiently received for all purposes at such time as it is delivered to the addressee (with any return receipt or delivery receipt being deemed conclusive evidence of such delivery) or at such time as delivery is refused by the addressee upon presentation.

d. If any part of any provision of this Agreement or any other agreement, document or writing given pursuant to or in connection with this Agreement shall be invalid or unenforceable under applicable law, said part shall be ineffective to the extent of such invalidity only, without in any way affecting the remaining part of said provision or the remaining provisions of this Agreement.

e. The headings of the Sections of this Agreement are inserted for convenience of reference only and do not form a part or affect the meaning hereof.

f. This Agreement, the rights and obligations of the parties hereto, and any claims and disputes relating thereto, shall be governed by and construed in accordance with the laws of the State of Delaware (not including choice of law rules thereof).

g. This Agreement may be executed in any number of counterparts.

each of which shall be deemed to be an original and all of which shall be deemed to be one and the same instrument.

h. In the event of any conflict or inconsistency between the terms of this Agreement and of the Order, the terms of the Order shall govern.

*In witness whereof*, the parties hereto have executed this Agreement or caused this Agreement to be duly executed on their behalf as of the date and year first hereinabove set forth.

## IN THE MATTER OF

## AN-MAR INTERNATIONAL, LTD., INC., ET AL.

CONSENT ORDER, ETC., IN REGARD TO ALLEGED VIOLATION OF SECS.  
5 & 12 OF THE FEDERAL TRADE COMMISSION ACT

*Docket C-3261. Complaint, July 17, 1989—Decision, July 17, 1989*

This consent order prohibits, among other things, a Wood Dale, Ill. maker of suntanning devices, from misrepresenting that its devices provide health benefits and that they do not pose a risk of any harmful side effects. In addition, the order requires respondents' promotional materials to contain a warning statement regarding potential eye injury, skin cancer, skin aging and photosensitive reactions.

*Appearances*

For the Commission: *Mark Kindt* and *William Brinley*.

For the respondents: *Craig M. White, Wildman, Harrold, Allen & Dixon*, Chicago, Ill.

## COMPLAINT

The Federal Trade Commission, having reason to believe that An-Mar International, Ltd., Inc., a corporation, and Andrew Bobel, individually and as an officer of said corporation, and Marzenna Bobel, individually and as an officer of said corporation, hereinafter referred to as respondents, have violated Sections 5 and 12 of the Federal Trade Commission Act, and that an action by it is in the public interest, issues this complaint and alleges that:

PARAGRAPH 1. Respondent An-Mar International, Ltd., Inc., "respondent An-Mar") is an Illinois corporation, with its office and principal place of business located at 345 Beinoris Drive, Wood Dale, Illinois.

Respondents Andrew Bobel and Marzenna Bobel are officers of respondent An-Mar and are responsible for formulating, directing and controlling the policies of respondent An-Mar. Their address is the same as that for respondent An-Mar.

PAR. 2. Respondents have manufactured, advertised, offered for sale, sold and distributed tanning devices and related products for the

artificial tanning of humans, including tanning beds, facial units, overhead lamp systems, and other products to the public. These tanning devices are sometimes marketed under the trade name Solar Gold.

PAR. 3. The acts or practices of respondents alleged in this complaint have been and are in or affecting commerce.

PAR. 4. Respondents have disseminated and caused the dissemination of product brochures and other sales literature directly to consumers and to distributors and mail order companies across state lines. Typical of the representations made by respondents, but not necessarily all-inclusive thereof, are the attached Exhibits A and B. The aforesaid representations make the following statements or depictions:

1. "Some [people are] not allowed to tan outdoor because of large amount of UV-B (ultraviolet Beta) in the sun's spectrum." (Exhibit A.)

2. "In addition to a beautiful appearance, tanning contributes to good health by providing a positive and stabilizing effect on metabolism, respiration and blood formation. It has a beneficial effect on our power of resistance, makes us feel better and gives us stamina." (Exhibit A.)

3. Models are typically depicted using respondents' tanning devices without wearing protective eyewear. (Exhibit B.)

PAR. 5. Through the use of the statements and depictions referred to in paragraph four and others in advertisements not specifically set forth herein, respondents have represented, directly or by implication, that:

1. Use of respondents' tanning devices results in health benefits, including positive effects on metabolism, respiration, blood formation, power of resistance, and stamina;

2. Use of respondents' tanning devices does not pose a risk of the harmful side effects associated with exposure to the sun's radiation; and

3. Respondents' tanning devices can be used safely without protective eyewear.

PAR. 6. In truth and in fact:

1. Use of respondents' tanning devices results in no health benefit;

2. Use of respondents' tanning devices does pose a risk of the harmful side effects associated with exposure to the sun's radiation; and

3. Respondents' tanning devices cannot be used safely without protective eyewear.

Therefore, the representations set forth in paragraph four were, and are, false and misleading.

PAR. 7. Through the use of the representations referred to in paragraph five and others not specifically set forth herein, respondents have represented, directly or by implication, that at the time they made the representations, they possessed and relied upon a reasonable basis consisting of competent and reliable scientific evidence for each of the representations.

PAR. 8. In truth and in fact, respondents did not possess and rely upon a reasonable basis for making such representations. Therefore, respondents' representations as set forth herein were and are false and misleading.

PAR. 9. In the advertising and sale of their tanning devices, respondents have, as alleged in paragraph four, made health claims and safety claims without disclosing that the use of such tanning devices poses the risks of eye injury, skin cancer, skin aging, and impairment of the immune function. These facts would be material to consumers. The failure to disclose these facts, in light of the representations made as alleged in paragraph four, is a deceptive practice.

PAR. 10. The acts and practices of respondents as alleged in this complaint, and the placement in the hands of others of the means and instrumentalities by and through which others may have used said acts and practices, constitute unfair or deceptive acts or practices in or affecting commerce and the dissemination of false advertisements in violation of Sections 5(a) and 12 of the Federal Trade Commission Act.

## EXHIBIT A



**ARTFULLY TAN.** Each year at least 80% of U.S. population do not have a chance and time to tan outdoor—on the beach. Some of them not allowed to tan outdoor because of large amount of UV-B (ultraviolet Beta) in the sun's spectrum. Unlike the conventional beach or lawn suntan Solarium Tanning can be accomplished in any season, at any time, and on any day—whether cloudy, rainy or cold. Best of all, it can be done at your convenience, at your own home.

Most importantly, a deep, rich and even tan be obtained after a week's course of tanning sessions. In addition to a beautiful appearance, tanning contributes to good health by providing a positive and stabilizing effect on metabolism, respiration and blood formation. It has a beneficial effect on our power of resistance, makes us feel better and gives us stamina. And when we feel better, we look better!

000005 A

SOLAR GOLD UV-B

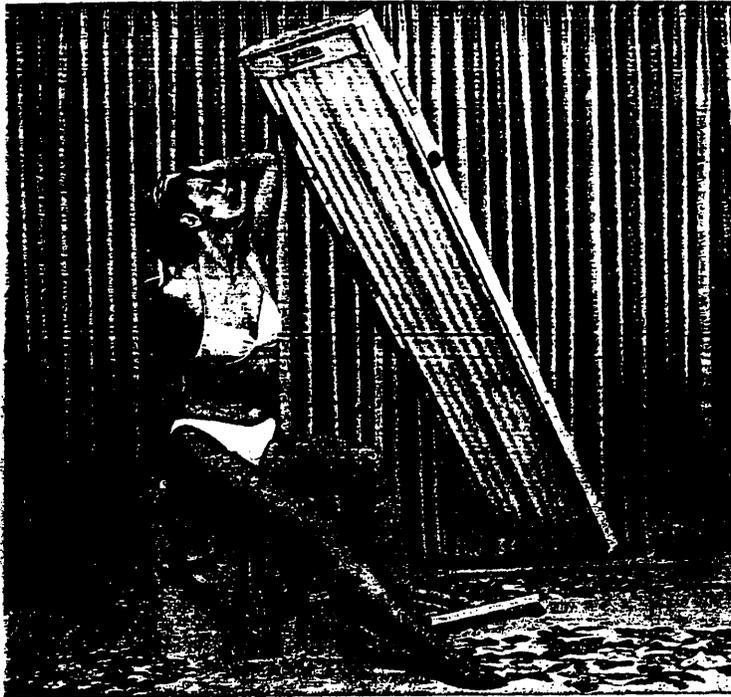
115 E. Bebons Drive • Wood Lake, Ill. 60190

EXHIBIT A

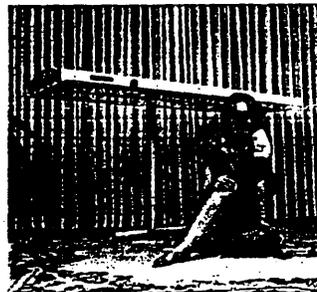
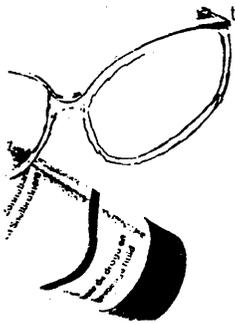
Complaint

112 F.T.C.

## EXHIBIT B



**800 FIFTH AVE.** The beautiful and practical design of this tanning canopy brings the real beach home. It has adjustable height. can be used *over a bed or with any chair or chaise.* A 30 minute timer turns it off automatically. Four to six 30 minute sessions will develop a full, golden, rich tan. It operates on 110 Volt household current, has 8 Philips UV-A bulbs, protective plexiglas and internal cooling fan. Wheels permit ease of movement and storage. Supply: 900 Watts:110 Volt 1.1 Amps



CLEOC 3

## DECISION AND ORDER

The Federal Trade Commission having initiated an investigation of certain acts and practices of the respondents named in the caption hereof, and the respondents having been furnished thereafter with a copy of a draft of complaint which the Cleveland Regional Office proposed to present to the Commission for its consideration and which, if issued by the Commission, would charge respondents with violation of the Federal Trade Commission Act; and

Respondents, their attorney, and counsel for the Commission having thereafter executed an agreement containing a consent order, an admission by respondents of all the jurisdictional facts set forth in the aforesaid draft of complaint, a statement that the signing of said agreement is for settlement purposes only and does not constitute an admission by respondents that the law has been violated as alleged in such complaint, and waivers and other provisions as required by the Commission's Rules; and

The Commission having thereafter considered the matter and having thereupon accepted the executed consent agreement and placed such agreement on the public record for a period of sixty (60) days, now in further conformity with the procedure prescribed in Section 2.34 of its Rules, the Commission hereby makes the following jurisdictional findings and enters the following order:

1. Respondent An-Mar International, Ltd., Inc. ("An-Mar") is a corporation organized, existing, and doing business under and by virtue of the laws of the State of Illinois, with its office and principal place of business located at 345 Beinoris Drive, Wood Dale, Illinois.

Respondents Andrew Bobel and Marzenna Bobel are officers of respondent An-Mar and are responsible for formulating, directing and controlling the policies, acts and practices of An-Mar.

2. The Federal Trade Commission has jurisdiction of the subject matter of this proceeding and of the respondents, and the proceeding is in the public interest.

## ORDER

For the purpose of this order, the following definition shall apply:

*"Tanning device"* means any product designed to incorporate one or more ultraviolet lamps and intended for irradiation of any part of the living human body by ultraviolet radiation to induce skin tanning.

## I.

*It is ordered,* That respondents An-Mar International, Ltd., Inc., a corporation, its successors and assigns, and its officers Andrew Bobel and Marzenna Bobel, individually and as officers of An-Mar International, Ltd., Inc., a corporation, and respondents' other officers and its agents, representatives, and employees, directly or through any corporation, subsidiary, division or other corporate device, in connection with the advertising, offering for sale, sale or distribution of any tanning device, in or affecting commerce, as "commerce" is defined in the Federal Trade Commission Act, do forthwith cease and desist from misrepresenting, directly or by implication, that:

A. Use of such tanning device may result in any health benefit, including a positive effect on metabolism, respiration, blood formation, power of resistance, or stamina;

B. Use of respondents' tanning devices does not pose a risk of the harmful side effects associated with exposure to the sun's radiation; and

C. Protective eye wear is not needed when using any such device.

## II.

*It is further ordered,* That, for the purposes of this order, any promotional material depicting models using tanning devices without appropriate protective eye wear will be deemed to represent that protective eye wear is not needed when using the tanning devices; *unless,* the promotional material clearly and conspicuously, and in close proximity to such depiction, discloses that protective eye wear is needed to prevent eye injury, *and further,* if such promotional material depicts models wearing what might appear to be ordinary sunglasses, the disclosure required by this Part must also disclose that ordinary sunglasses do not offer adequate protection.

## III.

*It is further ordered,* That for one (1) year after the date of service of this order, respondents, their successors and assigns, and their officers, agents, representatives, and employees, directly or through any corporation, subsidiary, division or other corporate device, in connection with the advertising, offering for sale, sale or distribution

of any tanning device, in or affecting commerce, as "commerce" is defined in the Federal Trade Commission Act, do forthwith cease and desist from failing to prominently disclose in any print advertisement, film, video tape or any other promotional material the following statement:

**Notice.** Read the mandatory FDA warning label found on every tanning machine for important information on potential eye injury, skin cancer, skin aging and photosensitive reactions.

The above-required language shall be included in printed material printed in a typeface and color that are clear and conspicuous, and, in multi-page documents, shall appear on the cover or first page; and in any film, video tape, or slide promotional material shall be included either orally or visually in a manner designed to ensure clarity and prominence; *provided, further*, that nothing contrary to, inconsistent with, or in mitigation of the above-required statement shall be used in any advertising or promotional materials.

#### IV.

*It is further ordered*, That, commencing one (1) year after the date of service of this order, respondents, their successors and assigns, and their officers, agents, representatives, and employees, directly or through any corporation, subsidiary, division or other corporate device, in connection with the advertising, offering for sale, sale or distribution of any tanning device, in or affecting commerce, as "commerce" is defined in the Federal Trade Commission Act, do forthwith cease and desist from making in any print advertisement, film, video tape or any promotional material any representation, directly or by implication, that the tanning device is safe or safer than other methods of tanning or that using the tanning device results in any health benefit unless the following statement is prominently disclosed:

**Notice.** Read the mandatory FDA warning label found on every tanning machine for important information on potential eye injury, skin cancer, skin aging and photosensitive reactions.

The above-required language shall be included in printed material printed in a typeface and color that are clear and conspicuous, and, in multi-page documents, shall appear on the cover or first page; and in

any film, video tape, or slide promotional material shall be included either orally or visually in a manner designed to ensure clarity and prominence; *provided, further*, that nothing contrary to, inconsistent with, or in mitigation of the above-required statement shall be used in any advertising or promotional materials.

V.

*It is further ordered*, That respondents, their successors and assigns, and their officers, agents, representatives, and employees, directly or through any corporation, subsidiary, division or other corporate device, in connection with the advertising, offering for sale, sale or distribution of any product for personal or household use, in or affecting commerce, as "commerce" is defined in the Federal Trade Commission Act, do forthwith cease and desist from making, directly or by implication, any health or safety representation unless, at the time of such representation, respondents possess and rely upon a reasonable basis for each such representation, consisting of reliable and competent scientific evidence that substantiates such representation; *provided, however*, that to the extent such evidence of a reasonable basis consists of scientific or professional tests, analyses, research, studies or any other evidence based on expertise of professionals in the relevant area, such evidence shall be "reliable and competent" only if those tests, analyses, research, studies, or other evidence are conducted and evaluated in an objective manner by persons qualified to do so, and using procedures generally accepted in the profession to yield accurate and reliable results.

VI.

*It is further ordered*, That for three (3) years from the date that the representations to which they pertain are last disseminated, respondents shall maintain and upon request make available to the Federal Trade Commission for inspection and copying:

A. All materials relied upon to substantiate any claim or representation covered by this order;

B. All test reports, studies, surveys, or other materials in its possession or control or of which it has knowledge that contradict, qualify, or call into question such representation or the basis upon which respondent relied for such representation, including complaints from consumers.

## VII.

*It is further ordered,* That respondents shall distribute a copy of this order to each current officer, employee, agent and/or representative having sales or promotional responsibilities with respect to the subject matter of this order, and to each current dealer, distributor, mail order retailer and purchaser or lessee for commercial use, of its tanning devices (such as health clubs, tanning salons, beauty catalogue houses, and tanning device retailers), and to each retail customer known through existing company records to have purchased its tanning devices.

## VIII.

*It is further ordered,* That for ten (10) years after the date of service of this order respondents shall maintain for three (3) years from the last date of dissemination of the material a copy of each nonidentical form of promotional and training material disseminated by respondent and upon request make such material available to the Federal Trade Commission or its staff for inspection and copying.

## IX.

*It is further ordered,* That for ten (10) years after the date of service of this order respondents shall maintain for three (3) years and upon request make available to the Federal Trade Commission for inspection and copying records of the name and last known address of each dealer, distributor, mail order retailer and purchaser or lessee for commercial use, of respondents' tanning devices.

## X.

*It is further ordered,* That respondents shall notify the Commission at least thirty (30) days prior to any proposed change in respondent An-Mar International, Inc., such as dissolution, assignment, or sale resulting in the emergence of a successor corporation, the creation or dissolution of subsidiaries, or any other change in the corporation which may affect compliance obligations arising out of this order.

## XI.

*It is further ordered,* That respondent Andrew Bobel and respondent Marzenna Bobel shall notify the Commission of the discontinuance of their present employment and of their affiliation with any new business or employment involving the manufacture, advertising, sale, offering for sale or distribution in commerce of any tanning device, or of their affiliation with any new business or employment in which their duties or responsibilities would involve the manufacture, advertising, sale, offering for sale or distribution of tanning devices, with each such notice to include respondent's new business address and a statement as to the nature of the new business or employment, as well as a description of their duties and responsibilities.

## XII.

*It is further ordered,* That respondents shall, within sixty (60) days after service of this order upon them and at such other times as the Commission may require, file with the Commission a report, in writing, setting forth in detail the manner and form in which they have complied or intend to comply with this order.

## IN THE MATTER OF

## THE B.F. GOODRICH COMPANY, ET AL.

MODIFIED FINAL ORDER, ETC., IN REGARD TO ALLEGED VIOLATION  
OF SEC. 7 OF THE CLAYTON ACT AND SEC. 5 OF THE  
FEDERAL TRADE COMMISSION ACT

*Docket 9159. Final Order\*, Mar. 15, 1988—Modified Final Order, July 18, 1989*

This modified final order, issued pursuant to a stipulation between the Commission and B.F. Goodrich and a joint motion granted in the court of appeals, requires Goodrich to divest its Calvert City, Ky. facility, for the production of vinyl chloride monomer (VCM) and ethylene dichloride, instead of the LaPorte VCM plant.

*Appearances*

For the Commission: *Rhett R. Krulla.*

For the respondents: *Tom D. Smith, Jones, Day, Reavis & Pogue,*  
Washington, D.C. *Richard W. Pogue, Jones, Day, Reavis & Pogue,*  
Cleveland, OH.

## MODIFIED FINAL ORDER

The Commission issued a Final Order in this proceeding on March 15, 1988, and respondent, The B.F. Goodrich Company ("Goodrich"), subsequently filed a petition for review of that Order in the United States Court of Appeals for the Second Circuit. On April 5, 1989, the Commission and Goodrich filed a joint motion asking that court to modify the Commission's Final Order pursuant to a Stipulation between the Commission and Goodrich. The parties expressly agreed that entering into the Stipulation did not "constitute an admission of any liability or of any issue of law or fact." Commissioner Azcuenaga issued the attached dissent to the Commission's entry into the Stipulation, later joined by Commissioner Strenio. On April 25, 1989, the court of appeals granted the parties' joint motion and entered its order modifying the Commission's Final Order of March 15, 1988.

Now therefore, *it is hereby ordered*, that the aforesaid "Final Order" be, and hereby is, modified in accordance with the order of the Court of Appeals to read as follows:

\*Complaint, Final Order, etc. previously published at 110 FTC 207 (1988).

## FINAL ORDER

## I.

## DEFINITIONS

*It is ordered,* That for purposes of this order the following definitions shall apply:

A. "*Goodrich*" means The B.F. Goodrich Company, a corporation organized under the laws of New York with its principal place of business in Akron, Ohio, and its directors, officers, agents, and employees, and its subsidiaries, divisions, affiliates, successors, and assigns.

B. "*Calvert City VCM Plant*" means the manufacturing facility for the production of VCM and ethylene dichloride ("EDC") owned by Goodrich and located at Calvert City, Kentucky, and all of the VCM and EDC assets, titles, properties, interests, rights and privileges, tangible and intangible, located at this facility.

C. "*VCM*" means vinyl chloride monomer, a gaseous, reactive, acyclic intermediate chemical, with chemical identity  $\text{CH}_2=\text{CHCl}$ , also called chloroethylene or monochloroethylene.

## II.

*It is ordered,* That within twelve (12) months from the date this order becomes final, Goodrich shall divest, absolutely and in good faith, at no minimum price, the Calvert City VCM Plant. At the option of the acquirer Goodrich shall also divest to the acquirer, at an appraised fair market value, up to 58 acres of land adjacent to the Calvert City VCM Plant, as well as all necessary or appropriate easements and rights-of-way. The purpose of the divestiture is to establish the Calvert City VCM Plant as a viable competitor in VCM, by insuring its continuation as an ongoing, viable enterprise in the VCM industry; and to remedy the lessening of competition resulting from the acquisition of certain VCM assets by Goodrich. The divestiture shall be made only to an acquirer or acquirers, and only in a manner, that receives the prior approval of the Federal Trade Commission.

Pending divestiture, Goodrich shall take all measures necessary to maintain the Calvert City VCM Plant in its present condition and to

prevent any deterioration, except for normal wear and tear, of any part of the Calvert City VCM Plant, so as not to impair the Calvert City VCM Plant's present operating viability or market value.

### III.

*It is further ordered,* That at the time of the divestiture required by this order, Goodrich shall provide to the acquirer of the Calvert City VCM Plant, on a nonexclusive basis, all VCM technology (including patent licenses and know-how) used by Goodrich or developed by Goodrich for use, in the Calvert City VCM Plant; and

For a period of one (1) year following the divestiture required by this order, Goodrich shall provide the acquirer of the Calvert City VCM Plant, if the acquirer so requests, such additional know-how as may reasonably be required to enable such acquirer to manufacture and sell VCM. Goodrich shall charge the acquirer no more than its own costs for providing such additional know-how.

### IV.

*It is further ordered,* That at the time of the divestiture required by this order, Goodrich shall assign to the acquirer of the Calvert City VCM Plant all VCM supply, sales, toll, or exchange agreements pertaining to the Calvert City VCM Plant, except for those agreements describing Goodrich's VCM supply arrangements with Occidental Chemical Corporation; and Goodrich shall make available to the acquirer all customer records and files (other than those describing its VCM supply arrangements with Occidental Chemical Corporation) relating to merchant sales of VCM (at any time since January 1, 1985) from the Calvert City VCM Plant, and Goodrich shall deliver to the acquirer such of those records and files as the acquirer may request.

### V.

*It is further ordered,* That if Goodrich has not divested the Calvert City VCM Plant within the twelve-month period provided in paragraph II of this order, the Federal Trade Commission may appoint a trustee to effect the divestiture. The trustee shall be a person with experience and expertise in acquisitions and divestitures. Neither the appointment of a trustee nor a Commission decision not to appoint a trustee under this paragraph V of the order shall preclude the

Commission from seeking civil penalties and other relief available to it including a court-appointed trustee, for any failure by Goodrich to comply with this order.

Any trustee appointed by the Commission pursuant to this paragraph V shall have the following powers, authority, duties, and responsibilities:

A. The trustee shall have the exclusive power and authority, subject to the prior approval of the Commission, to divest the Calvert City VCM Plant. The trustee shall have twelve (12) months from the date of appointment to accomplish the divestiture. If, however, at the end of the twelve-month period, the trustee has submitted a plan of divestiture or believes that divestiture can be accomplished within a reasonable time, the divestiture period may be extended by the Commission.

B. The trustee shall have full and complete access to the personnel, books, records and facilities of the Calvert City VCM Plant, and Goodrich shall develop such financial or other information relevant to the Calvert City VCM Plant as the trustee may reasonably request. Goodrich shall cooperate with the trustee, and shall take no action to interfere with or impede the trustee's accomplishment of the divestiture. Any delays in divestiture caused by Goodrich shall extend the time for divestiture under this paragraph V in an amount equal to the delay, as determined by the Commission.

C. The power and authority of the trustee to divest shall be at the most favorable price and terms available consistent with this order's absolute and unconditional obligation to divest at no minimum price, and with the purposes of the divestiture as stated in paragraph II of this order, subject to the prior approval of the Commission.

D. The trustee shall serve, without bond or other security, at the cost and expense of Goodrich on such reasonable and customary terms and conditions as the Commission may set. The trustee shall have authority to retain, at the cost and expense of Goodrich, such consultants, attorneys, investment bankers, business brokers, accountants, appraisers, and other representatives and assistants as are reasonably necessary to assist in the divestiture. The trustee shall account for all monies derived from the divestiture and for all expenses incurred. After approval by the Commission of the account of the trustee, including fees for his or her services, all remaining monies shall be paid to Goodrich, and the trustee's power shall be terminated. The trustee's compensation shall be based at least in

significant part on a commission arrangement contingent on the trustee divesting the Calvert City VCM Plant.

E. Goodrich shall indemnify the trustee and hold the trustee harmless against any losses, claims, damages, or liabilities arising in any manner out of, or in connection with, the trustee's duties under this order, unless the Commission determines that such losses, claims, damages, or liabilities arose out of the misfeasance, gross negligence, or the willful or wanton acts or bad faith of the trustee.

F. Promptly upon appointment of the trustee and subject to the approval of the Federal Trade Commission, Goodrich shall, subject to the Federal Trade Commission's prior approval and consistent with provisions of this order, transfer to the trustee all rights and powers necessary to permit the trustee to effect the divestiture required by this order.

G. If the trustee ceases to act or fails to act diligently, the Commission may appoint a substitute trustee.

H. The Commission may on its own initiative or at the request of the trustee issue such additional orders or directions as may be necessary or appropriate to accomplish the divestiture required by this order.

I. The trustee shall have no obligation or authority to operate or maintain the Calvert City VCM Plant.

J. The trustee shall report in writing to Goodrich and to the Commission every sixty (60) days concerning the trustee's efforts to accomplish divestiture.

## VI.

*It is further ordered,* That for a period of ten (10) years from the date the Calvert City VCM Plant is divested, Goodrich shall, at the acquirer's request, contract with the acquirer to provide to the Calvert City VCM Plant such utilities and services as are necessary for the operation of the Calvert City VCM Plant and such commercially reasonable quantities of ethylene and chlorine as the acquirer desires, up to the average 1986-1988 practical production capacity of Goodrich's ethylene and chlorine production facilities located at, or near, Calvert City. The price, terms, and conditions Goodrich shall offer the acquirer of the Calvert City VCM Plant for ethylene and chlorine shall be not greater than the prevailing market price, terms, and conditions for comparable domestic sales of chlorine and ethylene to Gulf Coast EDC/VCM producers, adjusted for a freight differential

to Calvert City (such freight differential for chlorine shall be no greater than the lowest available price for transportation of chlorine by barge from a mid-point location on the Gulf Coast; such per pound freight differential for ethylene shall be no greater than the then current average actual per pound cost which Goodrich incurs for the transportation of propane to Calvert City). The prices, terms, and conditions Goodrich shall offer the acquirer of the Calvert City VCM Plant for utilities and services shall not be greater than an amount that would be sufficient to allow Goodrich to recover its fully allocated costs, including a fair return on its investment. In the event of any dispute between Goodrich and the acquirer over the price, terms, and conditions at which Goodrich shall offer such utilities and services to the Calvert City VCM Plant, Goodrich shall submit to binding arbitration to resolve the dispute. Goodrich shall also supply to the acquirer, f.o.b. Gulf Coast manufacturing location, until November 30, 1991, at Goodrich's acquisition cost, such quantities of EDC as requested by the acquirer for use in the Calvert City VCM Plant.

#### VII.

*It is further ordered,* That, at the acquirer's request, and on fourteen (14) months' notice prior to the expiration of Goodrich's then current supply contract(s) for ethylene and/or chlorine for use in VCM manufacture at its La Porte, Texas plant, Goodrich shall exchange with the acquirer on a pound-for-pound basis with no differential payment by either party, such quantities as the acquirer may designate (not to exceed the amount under the contract then expiring and in total not to exceed the average 1986-1988 practical production capacity of Goodrich's ethylene and/or chlorine (as applicable) production facilities located at, or near, Calvert City) of ethylene, chlorine or both, by delivery by Goodrich to the Calvert City VCM Plant in exchange for delivery by the acquirer, or by such person(s) as the acquirer may designate, to Goodrich's La Porte VCM Plant. The length of such exchange shall be commercially reasonable, but in any event no less than the length of the common practice in the industry and shall not extend more than ten (10) years from the date of divestiture without Goodrich's consent. Goodrich shall notify the acquirer of the termination date(s) and quantities of each of its ethylene and chlorine supply contracts, subject to, in all instances, appropriate confidentiality agreements negotiated between Goodrich

and the acquirer. In the case of an ethylene or chlorine supply contract that by its term requires Goodrich to give notice in order for the contract to terminate, the acquirer may give the notice required by this paragraph six (6) months prior to any date such notice by Goodrich may be given. Goodrich's obligation to effect an exchange pursuant to such notice by the acquirer shall commence on the date the underlying contract would expire if Goodrich gave timely notice of cancellation to its supplier.

#### VIII.

*It is further ordered,* That Goodrich shall take all reasonable measures necessary to maintain in good operating condition the ethylene, chlorine, utilities, and service facilities that it owns and that are located at, or near, the Calvert City VCM Plant so long as Goodrich has any supply obligations pursuant to paragraphs VI or VII of this order; *provided, however,* Goodrich shall have no obligation to maintain in good operating condition the particular facilities used to provide ethylene, chlorine, utilities, and services if the acquirer permits the utilities contract(s), service contract(s), supply contract(s) or exchange agreement(s) pertaining to that particular utility, service, or feedstock to lapse without requesting renewal or if the acquirer does not, at the time of the divestiture, enter into utilities contract(s), service contract(s), supply contract(s), or exchange agreement(s) pertaining to that particular utility, service, or feedstock. Goodrich shall give the acquirer a right of first refusal on the purchase of the aforesaid ethylene facilities, chlorine facilities, utilities and service facilities located at or near the Calvert City VCM Plant; and Goodrich shall take no action that may unreasonably interfere with any plan, or attempt, by the acquirer to build or acquire ethylene, chlorine, utilities, service, or any other facility related to the production, sale, or distribution of VCM at or near the Calvert City VCM Plant.

#### IX.

*It is further ordered,* That, for a period of ten (10) years from the date this order becomes final, Goodrich shall not directly or indirectly acquire—other than the acquisition of manufactured product in the ordinary course of business—all or any part of the stock or assets of, or any interest in, any producer of VCM located in the United States without the prior approval of the Federal Trade Commission.

## X.

*It is further ordered,* That Goodrich shall, within sixty (60) days after the date this order becomes final and every sixty (60) days thereafter until it has fully complied with the provisions of paragraph II of this order, submit in writing to the Commission a report setting forth in detail the manner and form in which it intends to comply, is complying, or has complied with that provision. Such compliance reports shall include, among other things that may be required from time to time, a full description of all contacts and negotiations relating to the divestiture of the Calvert City VCM Plant, including the name and address of all parties contacted, copies of all written communications to and from such parties, and all internal memoranda, reports and recommendations concerning divestiture; and

Goodrich shall submit such further written reports of its compliance as the staff of the Commission may from time to time request in writing.

## XI.

*It is further ordered,* That Goodrich, upon written request and on reasonable notice, for the purpose of securing compliance with this order, and subject to any legally recognized privilege, shall permit duly authorized representatives of the Commission or of the Director of the Bureau of Competition:

A. Reasonable access during the office hours of Goodrich, which may have counsel present, to inspect and copy books, ledgers, accounts, correspondence, memoranda, reports, and other records and documents in the possession or control of Goodrich that relate to any matter contained in this order; and

B. Subject to the reasonable convenience of Goodrich, an opportunity to interview officers or employees of Goodrich, who may have counsel present, regarding such matters.

## XII.

*It is further ordered,* That Goodrich shall notify the Federal Trade Commission at least thirty (30) days prior to any proposed corporate change, such as dissolution, assignment or sale resulting in the emergence of a successor corporation, the creation or dissolution of

subsidiaries or any other change in the corporation, which may affect compliance with the obligations arising out of this order.

DISSENTING STATEMENT OF COMMISSIONER MARY L. AZCUENAGA

The Commission now joins, by a vote of 3 to 2, in a settlement to resolve the appeal of the B.F. Goodrich Co. from the Commission's order in this matter, which required a divestiture to restore competition in the vinyl chloride monomer ("VCM") market. Under the settlement, B.F. Goodrich will divest its Calvert City, Kentucky, VCM plant instead of divesting the LaPorte, Texas, VCM plant, as required by the Commission's order. I dissent.

With this settlement, the Commission relinquishes a procompetitive divestiture for a substantially less efficacious remedy. Indeed, the Calvert City plant is unlikely to be an independent competitive force in the industry for the long term, primarily because Goodrich will control essential raw materials. In agreeing to this settlement, the Commission also casts aside a substantial investment of time and resources, both public and private, in litigating and adjudicating this case, for no compelling reason and in haste.

This settlement perversely secures the worst of two worlds. On one hand, the settlement is insufficient to eliminate the competitive concerns at the heart of this case. On the other hand, the settlement, which requires detailed Commission review of complex pricing decisions for an extended time, is highly regulatory and usually would be rejected on that ground alone. The settlement establishes the Commission as a kind of "Office of Price Administration," intrusively monitoring and policing pricing decisions for years.

What is the rationale for this extraordinary "compromise"? Nothing has changed since the Commission issued its opinion and final order except that the case has been briefed and argued before the court. Does the Commission have second thoughts about its opinion and order? (One of the three commissioners who now supports the relief imposed by the settlement found no violation of law on which to predicate any relief whatsoever when the Commission issued its opinion and order.<sup>1</sup> Presumably, this commissioner now believes that Goodrich has indeed violated the law.) If we made a mistake in fact or in law, vacating the order would be the appropriate remedy. If we continue to believe that we have applied the law correctly, then

<sup>1</sup> See Separate Statement of Chairman Daniel Oliver in *The B.F. Goodrich Co.*, FTC Docket No. 9159.

prosecution of the appeal, rather than evisceration of the order, would seem to be consistent with the public interest.

I believe that the Commission's original opinion and order with respect to the VCM market are correct. Acceptance of this settlement with its inadequate remedy and regulatory format most assuredly is not in the public interest.<sup>2</sup>

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<sup>2</sup> I also dissent from the decision to file the settlement under seal.

IN THE MATTER OF  
MIDCON CORP., ET AL.

FINAL ORDER, ETC., IN REGARD TO ALLEGED VIOLATION OF  
SEC. 7 OF THE CLAYTON ACT AND  
SEC. 5 OF THE FEDERAL TRADE COMMISSION ACT

*Docket 9198. Complaint\*, Sept. 19, 1985—Final Order, July 18, 1989*

This final order adopts the initial decision in full, dismissing the complaint because of a failure to prove the likelihood of a substantial lessening of competition in a section of the country.

*Appearances*

For the Commission: *Marc G. Schildkraut* and *Robert Cheek*.

For the respondents: *Paul E. Goldstein, Philip R. Telleen, Priscilla A. Mims & Jane DiRenzo Segraves, Lombard, II. and James H. Sneed, Nathalie F. P. Gilfoyle, Carolyn Kay Weeder & Amy E. Hancock, McDermott, Will & Emery, Washington, D.C.*

INITIAL DECISION BY

LEWIS F. PARKER, ADMINISTRATIVE LAW JUDGE

FEBRUARY 2, 1987

I. HISTORY OF THE PROCEEDING

On September 19, 1985, the Federal Trade Commission issued a complaint charging that the acquisition of United Energy Resources, Inc. ("United")<sup>1</sup> by MidCon Corp. ("MidCon") violates Section 7 of

\*Complaint previously published at 107 FTC 48 (1986).

<sup>1</sup> Abbreviations of the company names referred to in this decision are:

<u>Company</u>	<u>Abbreviation</u>
Midcon Corp.	MidCon
United Energy Resources, Inc.	United (or UER)
Natural Gas Pipeline Company of America	NGPL
United Gas Pipe Line Company	UGPL
High Island Offshore System	HIOS
U-T Offshore System	UTOS

(footnote cont'd)

the Clayton Act, 15 U.S.C. 18 and Section 5 of the Federal Trade Commission Act, 15 U.S.C. 45.

Count One of the complaint alleges that MidCon and United, through their ownership of pipeline companies, and in other ways, are direct and substantial competitors in the business of transporting natural gas out of producing fields and basins in certain areas of the Gulf of Mexico Outer Continental Shelf ("OCS") off the coasts of Texas and Louisiana, and that the effect of the acquisition may be substantially to lessen competition or tend to create a monopoly in the transportation of natural gas out of producing fields and basins in relevant sections of the OCS.

Count Two, which alleges anticompetitive effects in the transportation and sale of natural gas from the Baton Rouge-New Orleans corridor was withdrawn from adjudication, and the Commission accepted a consent order requiring divestiture of certain subsidiaries holding partnership interests in natural gas pipelines in Louisiana. [3]

Respondents filed their joint answer to the complaint on October 25, 1985, admitting in part and denying in part the complaint's allegations. After extensive discovery, hearings began on November 4, 1986 and concluded on February 26, 1987.

On June 30, 1987, MidCon sold the stock and assets of United and UER marketing company to LaSalle Energy Corporation, thus divesting itself of the company whose acquisition is challenged by complaint counsel. Shortly thereafter, respondents moved to dismiss the case, claiming that no controversy remained to be decided. I certified respondents' motion to dismiss to the Commission which, in a November 16, 1987 Order, denied the motion and returned the matter to me for further proceedings. Pursuant to the Commission's directions, I ordered the parties to file answers to the proposed findings which had been filed before respondents moved to dismiss this case. The record was closed on November 27, 1987.

This decision is based on the transcript of testimony, the exhibits

Stingray Pipeline Co.	Stingray
Sea Robin Pipeline Co.	Sea Robin
The Bluewater Project	Bluewater
Tennessee Gas Pipeline Co.	Tennessee
Columbia Gulf Transmission Co.	Columbia Gulf
America Natural Resources Co.	ANR
Transcontinental Gas Pipeline Co.	Transco
Texas Gas Transmission Co.	Texas Gas
Trunkline Gas Co.	Trunkline
Panhandle Eastern Corp.	Panhandle Eastern
Texas Eastern Corp.	Texas Eastern

which I received in evidence, and the proposed findings of fact and conclusions of law, and answers thereto filed by the parties. I have adopted several of the proposed findings verbatim. Others have been adopted in substance. All other findings are rejected either because they are not supported by the record or because they are irrelevant. This decision is written as though the sale of United to LaSalle had not taken place.

## II. FINDINGS OF FACT

### A. *The Nature of Respondents' Businesses*

#### 1. MidCon

1. MidCon, the acquiring company, is a Delaware corporation with principal executive offices in Lombard, Illinois (Cplt.<sup>2</sup> ¶ 2; Ans. ¶ 2). MidCon is the parent of energy-related companies [4] operating throughout the Mid-Continental United States (CX 139B). Most of MidCon's subsidiaries are engaged in the transportation, distribution or sale of natural gas (CX 139E; Cplt. ¶ 3; Ans. ¶ 3). In the fiscal year ending September 30, 1984, MidCon had sales of \$4.2 billion and assets of \$3.5 billion (Cplt. ¶ 4; Ans. ¶ 4). In 1986, MidCon was acquired by Occidental Petroleum Corp. (51 Fed. Reg. ¶ 9,060 (March 17, 1986)).

2. MidCon's major natural gas pipeline subsidiary is Natural Gas Pipeline Company of American ("NGPL") (Cplt. ¶ 6; Ans. ¶ 6; CX 139E). This system essentially flows from south to north and has two legs. The western leg (known as the Amarillo line) begins in the Permian Basin of West Texas and Southeastern New Mexico, and has two extensions reaching into South Central Oklahoma and North Central Texas. It crosses the Texas and Oklahoma Panhandles, runs through Kansas, Nebraska, and Iowa, and terminates near Chicago, Illinois. The eastern leg (known as the Gulf Coast line) begins in the Texas and Louisiana Gulf Coast areas. It runs through East Texas, Arkansas, Missouri, and Illinois, and also terminates near Chicago (Tr. 1660-61; RX 2003; CX 176C).

<sup>2</sup> The following abbreviations are used in this decision:

CX: Commission Exhibit  
 RX: Respondents' Exhibit  
 F.: Finding number in this decision  
 Cplt.: Complaint  
 Ans.: Joint Answer  
 RPF: Respondents' Proposed Findings  
 CPF: Complaint Counsel's Proposed Findings

3. Prior to acquiring United, MidCon, through its ownership of NGPL, owned a 20 percent interest in the High Island Offshore System ("HIOS"), a 33 $\frac{1}{3}$  percent interest in U-T Offshore System ("UTOS") and a 50 percent interest in the Stingray Pipeline Company ("Stingray") (Cplt. ¶¶24-26; Ans. ¶¶24-26).

## 2. United

4. United, the acquired company, is a Delaware corporation with principal executive offices in Houston, Texas (Cplt. ¶ 8; Ans. ¶ 8). United's principal business is the transportation and sale of natural gas (CX's 139C, 318B; Cplt. ¶ 9; Ans. ¶ 9). In 1984, it had revenues of \$4.0 billion and assets of \$2.5 billion (Cplt. ¶ 10; Ans. ¶ 10).

5. United's two major pipeline systems are United Gas Pipe Line Company ("UGPL") and United Texas Transmission Company (Cplt. ¶ 12; Ans. ¶ 12; CX 318B). UGPL is an interstate pipeline system located primarily in the State of Louisiana. United Texas is a Texas intrastate pipeline (Tr. 1662-63; RX 2003; CX 318D-E).

6. United, through its ownership of UGPL, holds a 20 percent interest in HIOS, a 33 $\frac{1}{3}$  percent interest in UTOS, and a 50 percent interest in the Sea Robin Pipeline Company ("Sea Robin") (Cplt. ¶¶24, 25, 27; Ans. ¶¶24, 25, 27).

7. HIOS is an equally owned joint venture of five pipeline companies: NGPL, UGPL, Transcontinental Gas Pipeline Corp. ("Transco"), Texas Gas Transmission Co. ("Texas Gas"), and [5] American Natural Resources, Inc. ("ANR") (Tr. 145; CX's 128, 336A), and is located in the High Island and West Cameron areas of the Gulf of Mexico.

8. U-T Offshore System ("UTOS") is a joint venture owned in equal share by NGPL, UGPL and Transco (CX's 11, 330B, 337A).

9. Stingray is a partnership between a MidCon subsidiary, NGPL, and Trunkline Gas Company ("Trunkline"), a subsidiary of Panhandle Eastern Corporation (Tr. 1718). Each partner owns a 50 percent share (Tr. 1718; CX 54A).

10. Sea Robin is an unincorporated joint venture between UGPL and Southern Natural Resources, Inc. ("Sonat") (Tr. 1841; CX 335A). Each owner owns a 50 percent share (Tr. 1837; CX 335A).

## B. *The Acquisition*

11. On August 13, 1985, MidCon filed a premerger notification for its acquisition of United Energy Resources, Inc., as required by

Section 7A of the Clayton Act, as amended, 15 U.S.C. 18a. MidCon proposed to acquire, through a subsidiary established for this sole purpose, up to 18,100,000 shares of United for \$41 per share. The approximate total value of this cash tender offer was \$1.1 billion (Cplt. ¶ 14; Ans. ¶ 14). Midcon acquired United in 1985 (Tr. 1649). Since the acquisition, United has been assimilated as a MidCon subsidiary (Tr. 184, 1703-09; RX 2762).

12. As a result of the acquisition, MidCon's ownership share in HIOS rose from 20 percent to 40 percent and MidCon's ownership share in UTOS rose from 33 $\frac{1}{3}$  percent to 66 $\frac{2}{3}$  percent. MidCon retained its 50 percent share in Stingray and gained a 50 percent interest in Sea Robin (Cplt. ¶¶24-27; Ans. ¶¶24-27).

### C. *Jurisdiction And Commerce*

13. Respondents do not contest jurisdiction (Prehearing Conference Transcript, 16-18).

14. HIOS, UTOS, Stingray and Sea Robin are located in Federal waters (Tr. 1691; CX 904). Sea Robin, Stingray and UTOS cross state boundaries (*see* CX 904).

15. Some aspects of the operations of HIOS, UTOS, Stingray and Sea Robin are regulated by the Federal Energy Regulatory Commission ("FERC") as interstate pipelines (RX's 1987L, 1992X; CX's 1030Q, 1995D). [6]

16. Natural gas transported by HIOS, UTOS, Stingray and Sea Robin continues to destinations throughout the United States (Tr. 207-14, 1676-82; 1873; RX 2005).

17. The amount of natural gas flowing through each of these pipelines is substantial. For example, in 1984, HIOS delivered 500,065,579 Mcf (thousand cubic feet) of natural gas, Stingray delivered 284,175,462 Mcf, and Sea Robin delivered 289,745,636 Mcf (CX 1103A). In the same year, total natural gas consumption in the District of Columbia was 29,449,000 Mcf, and total United States consumption was 17,950,528,000 Mcf (CX 1015B). Thus, total deliveries on HIOS, Stingray and Sea Robin amounted to approximately six percent of total United States consumption in 1984.

### D. *The Natural Gas Industry*

#### 1. The Uses Of Natural Gas

18. Natural gas is a mixture of hydrocarbon compounds and small quantities of various nonhydrocarbons existing in the gaseous phase

or in a solution with crude oil in underground reservoirs (CX 1046E). A reservoir is a porous permeable underground formation containing an individual and separate natural accumulation of producible hydrocarbons (oil and/or gas) which is confined by impermeable rock or water barriers and is characterized by a single natural pressure system (CX 1047Z-27).

19. Natural gas is a major source of energy in the United States (CX's 1015A-B, 1046D) and is used in private dwellings for heating, air conditioning, cooking, waterheating, and other household uses, by manufacturing and mining establishments for heat, power, and as a chemical feedstock, and as a fuel in electric utility plants (CX 1046E-F).

## 2. Natural Gas Production In The OCS

### a. *OCS Leasing*

20. This case involves natural gas produced on the Outer Continental Shelf of the Gulf of Mexico ("OCS"). The OCS consists of those submerged lands on the continental margin of the United States lying beyond the jurisdiction of the coastal states (CX 1040Z-87). In 1984, gas production from the OCS accounted for approximately 25 percent of all marketed gas production in the United States (RX 1513). In 1984, gas [7] discoveries in the OCS represented about one-third of all gas discoveries in the United States (CX 1047N).

21. Congress has authorized the Secretary of Interior to lease the submerged lands of the OCS for the exploration and production of minerals, including gas and oil (CX 1038W; 43 U.S.C. 1334). To carry out its leasing responsibilities, the Minerals Management Service of the Department of the Interior ("MMS") has divided the OCS into "blocks." A block is an area measuring three miles square (or 5,760 acres) (CX 1040Z-85). Each block has a unique identifying designation consisting of an area name and a number, *e.g.*, East Cameron block 264.<sup>3</sup> Individual blocks can be located by area and block number on three maps in the record CX 902 (Offshore Texas); CX 903 (Western & Central Gulf of Mexico); CX 904 (Offshore Louisiana)).

22. Periodically, the MMS offers to lease certain OCS blocks (CX 1040Z-4-Z-11). Relying on geological and geophysical information in their possession, companies bid for these leases (Tr. 843). Bids may be submitted by a single company; sometimes one or more groups of companies submit joint bids. MMS evaluates the bids submitted and may award the block lease to the highest bidder (CX 1040Z-4-Z-8).

<sup>3</sup> Hereafter, blocks will be referred to by name and number only, *e.g.*, "East Cameron 264."

23. Leases are awarded for an initial period ranging from five years to ten years. The longer leases are awarded to encourage exploration and production in areas where the water is unusually deep or where other unusual adverse conditions exist so that additional time is needed to develop the block (CX 1040Z-11, Z-87). A lease for a tract that is not yet producing gas is said to be in its primary term. Once oil and gas is produced from the tract, the lease is extended indefinitely until production ceases (CX 1038W).

*b. Production And Development*

24. After securing a lease, a company proceeds with exploration. Exploration includes drilling one or more exploratory or wildcat wells to determine whether or not commercial volumes of oil or gas exist in reserves under the block (Tr. 843, 922). After evaluating the results of exploratory activity, the lessee must decide whether to proceed with development (Tr. 845, 923). Developing a tract may involve the construction of platforms and the drilling of development wells. If the decision to produce is made, a production platform is installed from which production will take place, and production wells are drilled. The largest single cost item [8] associated with offshore development is installation of the production platform; the drilling of the wells themselves is the second most costly (Tr. 847). During the production process, there is frequent opportunity for further exploration, most likely in the form of deeper drilling. Both the decision to develop a block initially and the decision to proceed with further development during the production stage are influenced by the anticipated prices for natural gas (Tr. 409, 686-87, 846, 927).

25. The OCS is one of the most attractive basins for oil and gas discoveries in the lower 48 states (Tr. 867; CX's 36N, 148M; *see also* Tr. 936-37). According to a 1984 MMS survey, the industry ranked the central and western Gulf as first and second on a list of all 24 MMS OCS planning areas for interest in exploration and development (CX 1040"O"). Of particular interest is exploration activity in the deep water of the Gulf of Mexico (CX 1040Z-17-Z-18; *see also* CX 1040Z-11-Z-16). Companies have invested heavily in leasing OCS blocks and drilling on OCS prospects (CX 1040Z-12, 1047M).

*c. Future Production In The Alleged  
Relevant Geographic Markets*

26. The testimony of Edward H. Feinstein, a FERC petroleum

engineer, during rate case hearings for Sea Robin and Stingray detailed various reserve projections for the areas served by these pipelines. The models described by Mr. Feinstein showed substantial additional reserves available to both Sea Robin and Stingray (CX's 36C-Q, Z, Z-8, 169G-O, Z-55).

27. A 1983 study prepared by Trunkline, operator of Stingray, projected that during the next decade 182 developed leases would be available for connection to Stingray (CX 35I). A NGPL official, commenting upon the Trunkline study pointing out Stingray's "advantageous location," found the Trunkline document to be "somewhat conservative" in its estimates (CX 35B).

28. In 1984, NGPL studied the future gas supply in an area currently served by HIOS and Stingray and projected deepwater extensions of these two systems. In that study, NGPL forecast the connection of 235 new fields during the ensuing ten years (CX 105F).

29. In 1985, ANR, the operator of HIOS, prepared a long-range plan in which substantial additional reserves were forecast for shipment through this system (CX 399C).

30. There are 929 unconnected blocks in the alleged relevant geographical markets (Tr. 984; CX's 1107A-B, 1108A-B). Included in this figure are 288 blocks that are in their primary term (CX 1108A-B). These blocks have been awarded after [9] companies paid substantial sums of money for the right to develop the block. Winning bids have frequently been in the millions of dollars (CX 904). Producers bid with the expectation of recouping their investment. Dr. Uri, complaint counsel's economic expert, testified that the fact that producers are "voting with their money" indicates that it is likely that natural gas exists under some of these blocks (Tr. 986).

31. Although no pipelines exist in the Garden Banks deepwater area of the alleged geographic market and there is no natural gas being produced in this area (Tr. 692, 1716; RX 2004), it is of interest to both producers and pipelines because of its potential for development (Tr. 868-69). There has been increased bidding, leasing, and exploration activity in Garden Banks (*see* CX 399F, H, Q, T, U), as there has been in other deepwater areas of the Gulf (Tr. 860; CX 1040Z-11-Z-18). Over 100 Garden Banks blocks are in their primary term (CX 1108A).

32. There are no pipelines in the Garden Banks area, but several pipelines have considered connecting Garden Banks 236 (CX's 71A-F, 504, 512A-G, 513A-F), and, as recently as June 1986, Trunkline considered developing a pipeline system to serve future transportation needs of several large Garden Banks area producers (*see* CX 638A).

33. Thus, while Garden Banks is only a potential future market (Tr. 1468), it is possible that this area, as well as non-producing blocks in other areas in the alleged geographic markets, will experience future production of natural gas.

### 3. The Sale And Transportation Of OCS Natural Gas

#### a. Pipelines

34. After gas is produced, it is transported to various destinations via pipelines (Tr. 847). There are two types of pipelines: laterals and trunklines. A lateral is a relatively small diameter pipeline which carries gas from a production platform to a trunkline (Tr. 160). A lateral can be connected to a trunkline either at a platform constructed at the end of the trunkline or at valves installed at intervals along the trunkline (Tr. 161). Laterals deliver gas to a main trunkline, a large-diameter pipeline. The trunkline moves the gas towards shore (*see* CX 903).

35. Gas flows from an area of high pressure to an area of low pressure. The greater the difference in pressure between the pipeline intake and the outlet points, the greater the quantity of gas that flows through a pipeline of a given diameter during any period of time. At a number of places along a route, pressure may be increased by using a compressor. This increases [10] the capacity of the pipeline (Tr. 165-66). Compression may also be used at the production platform as the well depletes and the natural pressure from the reservoir declines (Tr. 79-80).

#### b. The Sale Of OCS Natural Gas

36. A wellhead gas purchase contract contains the terms under which a producer sells production from natural gas reserves from a block which has not been previously connected to a trunkline (*see, e.g.*, CX's 196A-Z-26, 197A-Z-26, 1220A-Z-30). The contract is usually a long-term agreement, extending for 15 years or the estimated life of the reserves (*see, e.g.*, CX's 196Z-20, 197Z-12-Z-13, 1045F, 1220Z-24; 15 U.S.C. 3375(a)(3)). Long-term wellhead contracts assure each party that the large investment in production and transmission facilities will be recouped over time (CX 1045F). A producer would not sell gas on a short-term basis if it had to incur the cost of building a lateral (Tr. 673).

37. A gas purchase contract typically obligates the producer to sell to the purchaser the producer's share of the gas produced from

reserves located under a particular block (Tr. 662-63; CX's 196F, 197F, 1220G) and specifies the initial price and the formula by which the price will be determined over the life of the contract (Tr. 667-68; *see, e.g.*, CX's 197N-S, 1220W-Z-26). The gas purchase contract usually obligates a purchaser to take a quantity of gas expressed as a percentage of the well's deliverability on a daily, monthly or annual basis. A well's deliverability is determined by periodically conducting well flow tests and other engineering studies as specified in the contract (*see, e.g.*, CX's 1220M-V, 1971I-N).

38. Traditionally, the parties to a wellhead gas purchase contract were the producer, as seller, and an interstate natural gas pipeline company, as buyer. The pipeline company would purchase the gas at the production platform, transport the gas to some onshore destination and resell the gas either to the direct user (such as industrial concerns or electric utilities) or to a local distribution company ("LDC") (Tr. 294, 527, 672, 1653-54, 2460-61) which is a company engaged in the retail sale of natural gas to end-users, such as homeowners, commercial or industrial establishments (Tr. 1656, 1667). More recently, industrial customers, utilities, intrastate pipelines and LDCs have become purchasers under wellhead gas purchase contracts (Tr. 678, 801, 930-31). In such transactions, either the producer or the purchaser may be responsible for securing transportation of the gas on pipeline facilities owned by third parties (Tr. 294, 801-02, 932-33, 1674). [11]

### *c. The Transportation Of OCS Natural Gas*

#### 1. Types Of Transactions

39. Natural gas may be transported from the OCS in two ways: in the first, the purchaser is an interstate pipeline company that ships the gas to shore over its own pipeline system. In this case, there is no separately stated transportation charge (*see, e.g.*, CX 1038A-Z-85), but there is an implicit transportation margin for each unit of gas which is equal to the difference between the price the pipeline pays for the gas at the wellhead and the price at which it resells the gas (Tr. 992, 1003).

40. In the second case, where the shipper (the owner of the gas) and the transporter (a pipeline company) are different parties, they negotiate a transportation agreement (*see, e.g.*, CX's 178Z-70-Z-100, 701A-U, 702A-Y, 703A-V, 704A-Z, 705A-Z). This can occur even where the shipper owns an interest in the pipeline (CX 180C-Z-14).

## 2. The Transportation Agreement

41. The following terms are typically included in a transportation agreement.

### (aa). *Type Of Service*

42. A transporter may offer different priorities of service. Two of the most common classifications are referred to as firm service and interruptible (or "best efforts") service (CX 201W). A transportation agreement will state whether the service being offered is firm or interruptible or part firm and part interruptible (*see, e.g.*, CX's 640F-G, 703D). A customer with firm service is entitled to capacity in the pipeline in an amount up to its "contract demand," the daily quantity of gas that the transporter is obligated to accept from the shipper for transportation (CX 405D; *see also* CX 1014Z-60 (§ 284.8(a)). A customer entitled only to interruptible service can be displaced by a firm service customer up to the amount of the contract demand of the firm service customer if sufficient capacity is not available for both customers (Tr. 276-77, 2319-20). [12]

### (bb). *Demand And Commodity Charges*

43. A commodity charge is a charge per unit of gas transported (*see, e.g.*, CX 167E), and it is computed by multiplying the volume actually shipped by the commodity rate (Tr. 2346). Generally, an interruptible customer pays only a commodity charge (Tr. 1185, 2346; CX 705G-I).

44. A demand charge is a charge per unit of contract demand (*see, e.g.*, CX 167E), and it is computed by multiplying the contract demand by the demand rate (CX's 167E, 178Z-439). The shipper pays the demand charge, usually monthly, regardless of the actual volume shipped (Tr. 194-95, 355). A firm service customer usually pays a two-part charge: a commodity charge and demand charge (*see, e.g.*, CX 167Z).

### (cc). *Duration*

45. The duration of a transportation agreement may be stated as a primary term (initial term), with the right of renewal for subsequent time periods until cancelled by either party (*see, e.g.*, CX's 178Z-11, 405I-J).

46. A shipper generally wants the duration of a transportation agreement to match its contractual obligation to buy gas or the

expected time it would take to deplete the wells whose production is being transported (Tr. 95-96, 280, 396; CX 201Z-4-Z-5, Z-12-Z-13).

47. Prior to 1982, a shortage of natural gas existed in the interstate market (F.'s 57, 63) and during that period, Federal regulations encouraged long-term contracts (Tr. 556). Many of the transportation agreements signed in the late 1960's and 1970's contained long-term commitments on the part of shippers (Tr. 1149-50; *see* RX 1059A-F). Since 1982, however, shippers have shown increased desire to control costs by attempting to match the duration of the contract to the requirements of the particular block being connected (CX 201Z-27; *see also* Tr. 399).

(dd). *Contract Demand Levels And  
Contract Demand Reduction Options*

48. A shipper typically seeks to have the contract demand approximate the average maximum deliverability of the connected reserves over the initial three or four years of the transportation contract (CX 201Z-17-Z-18). Under some agreements, the shipper may elect periodically to reduce its contract demand (Tr. 96, 282-83, 1186; [13] CX's 178Z-51, 180Z-19-Z-20). This feature enables the shipper to adjust its monthly demand charge obligations as the volume of gas that can be produced from connected wells declines (Tr. 96-97, 283; CX 201Z-19-Z-20).

(ee). *Charges For Fuel And Gas Loss*

49. Shippers are charged for fuel use and gas loss. The charge is deducted by permitting the carrier to deliver less than it receives (*see, e.g.*, CX 764G). These charges account for gas that the carrier uses as fuel for compressors and other equipment and for any loss that occurs when gas escapes during transmission (Tr. 105-07). All of the contract provisions described above are negotiated by the shipper and the transporter (Tr. 279, 282-84, 293, 931-32).

(ff). *Capital Costs For Lateral Construction*

50. Usually a lateral must be constructed to move gas from the production platform to the trunkline. Negotiations between the parties determine who bears the cost of the lateral (Tr. 279-80, 857-58, 864-66, 874-75).

(gg). *Shipper Flexibility To Change Receipt Points*

51. A receipt point is the location at which a transporter will accept

gas from a shipper. Receipt points are specified in the transportation agreement (*see, e.g.*, CX's 167Z-9-Z-12, 178Z-61, Z-86). Most contracts require the shipper to get the transporter's approval to add new receipt points (*see, e.g.*, Tr. 91, 1764-65; CX's 29A-K, 167X, 180K).

#### 4. The Sale Of OCS Gas To Onshore United States Customers

52. Natural gas produced in the OCS is not consumed there but is shipped onshore to LDC's, which, in turn, sell the gas to "burner tip" or end-use residential, commercial and industrial customers (Tr. 360, 2461-62; RX's 1515-16).

53. LDC's are usually state-regulated public utilities that are given exclusive franchises by their regulators to serve particular geographic areas (Tr. 576, 1667). LDC's have historically purchased most of their natural gas from interstate and intrastate pipeline companies (Tr. 576). Sales to LDC's [14] occur in what are called "city-gate" markets where the interstate pipeline connects with, and transfers custody of its gas to, the LDC's distribution system (Tr. 359, 1668, 2463; RX 1516).

54. In the past, interstate pipeline companies have performed a "merchant" function by purchasing natural gas at the wellhead (Tr. 1656, 2490-92; RX's 2007-10), transporting it over their own or other facilities, and selling it to customers in city-gate markets (described as "bundling" by Dr. Hall, respondents' expert economist) (Tr. 1654, 2460-61). The sales price included the cost of the gas at the wellhead and the cost of transporting it from wellhead to city-gate (Tr. 2173-74). Both NGPL and UGPL have performed this merchant function (Tr. 1653, 1812, 1814).

55. FERC policies during the 1970's encouraged pipelines to perform the merchant function (Tr. 566), but in recent years, it has become common for LDC's and large end-users to purchase gas directly from producers and to purchase transportation services on an unbundled basis. A marketer or broker arranges these unbundled services (Tr. 2461, 2485-86).

#### 5. Regulation In The Natural Gas Industry

##### a. *Historical Perspective*

56. The federal government has regulated natural gas pipelines since 1938 when the Natural Gas Act, 15 U.S.C. 717-717w, was passed (Tr. 549, 1655, 2026). At first, natural gas pipeline companies

were regulated by the Federal Power Commission ("FPC"), which also, by virtue of the decision in *Phillips Petroleum Co. v. Wisconsin*, 347 U.S. 672 (1954), was required to regulate the wellhead price of natural gas that was delivered into the interstate market (Tr. 550).

57. The FPC's control of wellhead prices created significant shortages of natural gas in the 1970's because the prices it allowed were too low to stimulate enough production for the interstate market (Tr. 553, 1083-84).

58. Another consequence of federal wellhead price controls was that buyers in the intrastate markets purchased virtually all the new onshore gas supplies available because they were allowed to pay more than FPC-controlled prices. Intrastate companies, however, were effectively prohibited from buying OCS gas. In the 1970's, this market imbalance led to shortages on many interstate pipeline systems. Many pipelines could not meet their contractual obligations to deliver gas to all their customers and had to file curtailment plans with FERC (Tr. 1816-18; CX 506E). [15]

59. To encourage producers to explore for and develop gas supplies in the OCS in the early 1970's, interstate pipelines made interest-free loans (called "advanced payments" or "prepayments") to producers to enable them to explore specific OCS tracts. In exchange, producers agreed to commit all reserves discovered on these tracts to the pipeline that made the advance payments (Tr. 98-99, 818, 928-29, 1686-87, 1822-23; CX 197C).

60. Producers received maximum lawful prices for their OCS production throughout the gas-shortage period (Tr. 688, 920, 1825). Pipelines would accept delivery of the gas at the platform and pay for construction of a lateral (Tr. 672, 940). Contracts frequently had deregulation clauses which set a formula to determine price in the event wellhead price controls were eliminated (Tr. 1825). In the 1950's and 1960's, contracts would typically obligate a pipeline to take 50 percent or less of the well's deliverability. As the shortage developed, "minimum take" provision increased to 80 or 90 percent of deliverability (Tr. 1689). During the period of shortage, producers would bargain for, and frequently receive from purchasers, payment for a minimum quantity of gas, whether or not the purchaser actually took that volume. This became known as a take-or-pay provision (Tr. 1689).

61. In 1978, Congress passed the Natural Gas Policy Act of 1978 ("NGPA") (15 U.S.C. 3301-3432). The NGPA gave the Federal

Energy Regulation Commission ("FERC"), successor to the FPC, jurisdiction over the maximum price producers could charge for gas sold in either the intrastate or interstate markets. But the NGPA mandated the ceiling prices to be used and prescribed a phased decontrol of prices for most gas discovered after February 19, 1977 (so-called "new gas") (15 U.S.C. 3301-3331).

62. Under the NGPA, the price of some categories of gas was decontrolled immediately; the maximum lawful price of other categories of gas was permitted to escalate 10 to 15 percent a year (Tr. 1695). The NGPA deregulated most new gas on January 1, 1985 (Tr. 563). Congress chose to rely upon market forces to bring forth sufficient supplies to satisfy demand (Tr. 560).

63. The enactment of the NGPA was followed in 1979 by the quadrupling of oil prices by OPEC. These events led to a boom in drilling in the United States in 1979, 1980 and 1981. In 1980, for the first time since 1960, the nation found as much gas as it produced (Tr. 1695). A surplus of natural gas first appeared in late 1981-1982 (Tr. 610, 688-89, 1697) and it has continued through the winter of 1986-1987 (Tr. 409, 672). The surplus resulted from increased drilling, increased discoveries, and diminished demand (Tr. 1697). The surplus depressed natural gas prices so that the statutory wellhead price ceiling was no longer the effective constraint on wellhead prices (Tr. 562, 669-70). Contractual provisions reflected this surplus situation. New contracts did not set gas prices at the maximum lawful price (Tr. 691), costs for the construction of laterals were often [16] shifted from the purchaser to the producer (Tr. 672, 866, 925, 940), and some contracts gave purchasers the unilateral right to reduce the price below the contract price if the purchaser determined that the gas was not marketable in end-use markets at the contract price (so-called "market-out clauses") (Tr. 671). Some purchasers have exercised these market-out clauses since at least 1984 (Tr. 691). Some contracts permitted the buyer to deduct increases in third-party transportation costs from prices due the producer (Tr. 921).

64. During the 1970's, the wellhead price was generally the FERC-set maximum lawful price (Tr. 920) and transportation rates did not affect wellhead prices because the end-use market price for natural gas was below the price of competitive fuels (Tr. 859). The elimination of the maximum lawful price as a constraint on wellhead pricing led to wellhead prices being determined by a "netback" process (Tr. 346-859). The value at the wellhead became a function of what natural gas

sold for in end-use markets, less the cost of transportation to the market (Tr. 346, 859). Thus, if the cost of transportation changed, so did the value at the wellhead (Tr. 346, 411, 683-84, 878-79, 920-21; see RX 1040B, D; CX's 43A, 63A-B, 82A-B, 99A, 107A-C, 108A-B, 303B, F, 304B, 381A, 1220W, 1268, 1295C).

65. The elimination of binding wellhead price constraints also affected the type of buyer that a producer would seek out. During the period of wellhead controls, a producer received the FPC ceiling price for its gas regardless of who purchased it (Tr. 802). Under these circumstances, wellhead sales to interstate pipeline companies were preferred to sales of gas downstream to local distribution companies or to end-users (Tr. 802). The interstate pipeline companies generally bought gas in the producing area, owned the gas at every point while it was in the pipeline and then sold it to customers at the other end of the pipeline (Tr. 527, 2460-61). Historically, pipelines did not transport for producers (Tr. 674). After wellhead decontrol, wellhead values could vary (Tr. 919), and producers sought to achieve maximum wellhead value (Tr. 674). To achieve this goal, producers have sought to sell gas to firms in addition to interstate pipeline companies, the traditional purchasers. These firms include LDC's and end-users (Tr. 801). To effectuate these sales, producers and their customers sought transportation services from interstate pipelines (Tr. 290-301, 310-28, 677-78, 683, 801-02, 2461).

b. *FERC Regulation Of Transportation Services*

66. If an interstate pipeline company wishes to construct new facilities, extend existing facilities, provide new services or expand existing services, it must file a proposal with FERC and receive authorization from it (Tr. 564, 594, 2028). Once a particular service or facility is commenced or is in place, the [17] pipeline company must receive FERC authorization to discontinue or abandon the service or facility (Tr. 2026, 2089-90, 2331).

67. The procedures for filing a traditional Section 7(c) certificate for construction of new facilities consist of a pipeline filing a request for a certificate with FERC, FERC publishing a notice in the Federal Register of the proposed certificate, and interested parties filing intervention papers in the certificate proceeding. The FERC staff then makes a recommendation either to grant or not grant the certificate, or to set the case for a hearing. If the case is set for a hearing, all parties with an interest in the proceeding are allowed to appear before

an administrative law judge and argue why the certificate should or should not be granted (Tr. 595). Obtaining a traditional Section 7(c) certificate is obviously a lengthy process (Tr. 104-05, 596, 681, 804).

68. In some circumstances, FERC grants a "blanket certificate" which allows a pipeline company to engage in certain routine activities without the necessity of seeking a FERC certificate prior to each transaction. Transactions undertaken pursuant to a blanket certificate are nevertheless certificated activities. The FERC has merely given advance approval of certain kinds of transactions (Tr. 569-70, 588). This process is authorized by FERC Order 436 (Tr. 605) whose most significant feature is its provision for open access, nondiscriminatory transportation (Tr. 604-05, 2035). This order also has new provisions concerning how transportation rates must be determined (Tr. 606), but does not change the basic method (Tr. 2058). In particular, the Order 436 maximum rate must be "just and reasonable," and must be a fully allocated cost rate (Tr. 2056-57).

69. FERC must approve the abandonment (discontinuance) of a previously certificated transportation service. In making this decision, it would consider whether the reserves underlying the transportation agreement have been depleted and the desire of the shipper having the right to terminate the agreement (Tr. 2159-61). On the other hand, Order 436 transportation rights can be discontinued at the expiration of the contracts underlying the service (CX 1013G, J).

### *c. FERC Regulation Of Pipeline Construction*

70. Where a certificate for pipeline construction is required, three types are available: traditional Section 7(c) certificates, blanket certificates for minor projects, and optional expedited certificates (Tr. 570, 594-95, 641-43).

71. An applicant seeking a traditional certificate must submit an application which is processed in a manner similar to that of a traditional transportation certificate (Tr. 594-95). [18] An applicant for a traditional certificate must show that the project complies with environmental regulations and will be economically viable. HIOS, Stingray and Sea Robin are joint venture pipelines which required FERC approval before construction (RX's 1987A-P, 1989A-C, 1992A-X, 1993A-I, 1994A-B, 1995A-E, 1996A-C, 1997A-C, 1998A-N, 1999A-C).

72. FERC requires that those proposing a new offshore pipeline demonstrate that they have sufficient gas reserves in specific areas

under long-term purchase contracts with producers (Tr. 556, 2072), and that they prepare engineering studies to show how the reserves would be connected, their cost, and the cost of construction to consumers (Tr. 1838).

73. The application to construct Stingray was unusual in that while approximately three trillion cubic feet of reserves served as the basis for the application, only about 1.2 trillion cubic feet were under contract (Tr. 2072-73). Thus, FERC had to evaluate the estimated reserves in the Stingray area and assume that those reserves would be transported via Stingray regardless of who would purchase them (Tr. 2073). The reserves that served as a basis for Stingray were different from the reserves that served as a basis for Sea Robin (Tr. 2073). FERC rejected the idea of duplicative or competing pipelines to provide transportation from the offshore fields served by HIOS, Stingray, and Sea Robin (Tr. 2062-66, 2072-74).

74. FERC avoids inefficient duplication of facilities (Tr. 601, 2074) and would tend not to approve an application for construction of an offshore pipeline based on reserves that had been the basis for an existing offshore pipeline (Tr. 2074). To this end, FERC encouraged cooperation between several parties wishing to construct facilities in the High Island areas. The result of this cooperation was the HIOS joint venture (Tr. 2075). A study of reserves in the High Island area, done in 1975, was relied upon by FERC to justify its construction (Tr. 217). HIOS was based on an estimated five trillion cubic feet of reserves, largely not yet under contract. These reserves were different from the reserves on which the approval of Stingray was based (Tr. 2074-79).

75. FERC has made blanket certificates available for minor projects. Once a blanket certificate is secured, a company can construct, without prior notice to FERC, any facility that does not cost more than \$5,100,000. Any project costing less than \$14,300,000 may be constructed if no protests are filed within 45 days following publication in the Federal Register of a notice of the proposed project. Dollar limits for both automatic authorization and prior notice projects change annually with inflation (Tr. 570, 2108-09; CX 1011A-P). OCS laterals have been constructed under this blanket program (CX's 93C-G, M, 603B, 606B, 1027B, C n. 2). [19]

76. Facilities may also be constructed upon obtaining an Order 436 optional expedited certificate (*see, e.g.*, CX 1014Z-34-Z-43, Z-55-Z-58). Under this certificate, the applicant must bear the financial risk

of the project. Revenues from existing customers may not be used to subsidize the project if it turns out to be unprofitable (Tr. 641-43; CX 1014Z-34). In a proceeding for a certificate under the optional expedited procedures, the applicant does not have to prove economic viability; that burden is shifted to those challenging the issuance of the certificate (Tr. 641-43; CX 1014Z-56 (§ 157.104); CX 1013X).

d. *FERC Regulation Of Pipeline Rates*

77. Pipelines subject to FERC jurisdiction must file their rates with FERC and charge only those rates that are on file. FERC regulates rates charged for sales and transportation services to ensure that they are "just and reasonable" (Natural Gas Act § 4; 15 U.S.C. 717c).

78. FERC regulates the rates for gas sold by interstate pipelines for resale. It does not regulate the price of gas sold by the pipeline directly to end-users, such as industrial customers or electric utilities (Tr. 575). Nor does FERC regulate the price of gas sold by marketing affiliates of interstate pipeline companies (*see* Tr. 1861-63, 2384-85). Gas sold directly to end-users often is sold at a fixed price and not at the pipeline's weighted average cost of purchased gas ("WACOG") (*see* CX's 189A-Z-30, 190A-Z-42, 191A-Z-164, 192A-Z-176).

79. Over the years, FERC has developed a procedure for arriving at "just and reasonable" rates. The first step is the computation of costs which the company is entitled to recover. These include the expenses of operating and maintaining pipeline, storage, and related facilities; sales and administrative expenses; depreciation; and various taxes. Costs also include an allowance for return, which is a return (or profit) on the capital invested. The allowance for return is computed by multiplying the "rate base" (*i.e.*, the dollar amount of the company's assets valued at cost less depreciation) by a reasonable rate of return (Tr. 576-77, 2038-39).

80. FERC then determines the type of customer from which the company will collect certain costs. Costs are allocated between jurisdictional and non-jurisdictional customers, and by function (*i.e.*, gas procurement, transmission and storage). Jurisdictional customers include firms that transport gas and firms that buy gas for resale (*i.e.*, LDC's that supply residential and commercial end-users). Nonjurisdictional customers include firms that buy gas for their own use, *e.g.*, industrial customers. The FERC does not establish a rate for [20] nonjurisdictional customers, but will allocate costs among regulated and nonregulated enterprises when calculating rates (Tr. 577-78, 2038-43).

81. FERC then determines how revenue will be collected. For this purpose, costs are classified as demand costs or commodity costs. Demand costs can be collected through a demand charge, which is a payment for the customer's right to a certain quantity of pipeline capacity regardless of actual service used. Commodity costs must be collected, if at all, through a commodity charge, an amount based upon actual units delivered (Tr. 580-81, 2043).

82. Conceptually, fixed costs are recovered through a demand charge and variable costs through a commodity charge (Tr. 579). However, FERC, at various stages in its history, has adopted various formulas to allocate various elements of fixed costs between the demand charge and the commodity charge (Tr. 579-80). FERC's general current rule is that a pipeline's return on investment and taxes related to income shall be recovered through the commodity charge (Tr. 2046).

83. Finally, FERC computes the appropriate unit rates. Typically, the demand charge is calculated by dividing the demand costs by the total of the contract demands in customer contracts (Tr. 580, 2046). The commodity charge for a particular service (*e.g.*, transportation service) is calculated by dividing the commodity costs by the so-called "representative volume," the estimated total quantity of gas that will be delivered (Tr. 581-82, 2048-49).

84. The rate structure required for Order 436 self-implementing transportation must have both maximum and minimum rates (Tr. 287, 620; CX 1014Z-60). Maximum rates are based upon a pipeline's fully allocated costs (Tr. 621; CX 1014Z-60). Minimum rates are based on the level of variable costs and thus will be well below the maximum rate allowed by FERC (Tr. 288, 621, 2036). Rates actually paid by a shipper are set by negotiations between the shipper and the transporter and may be set at any level between the filed maximum and minimum without prior FERC approval (Tr. 621, 1784; CX 1014Z-60). Transporters may charge different customers different transportation rates (*i.e.*, price discriminate) within the band of allowable rates (Tr. 625-26, 631). This provides the transporter with the ability to meet a competitive situation without lowering its rates across the board to all customers or to all customers within a certain class of service (Tr. 620-26, 2036).

85. The extent to which a transporting pipeline will be able to discriminate between similarly situated shippers with regard to rates under Order 436 is an open question (Tr. 614, 1785). This issue is on

appeal to the United States Circuit Court of Appeals for the District of Columbia in a case challenging Order 436 (Tr. 1786, 2059). Order 436 applies to new [21] shippers and new transportation agreements only. Even if it is upheld, Order 436 will have no effect on the rates applicable under existing transportation contracts that have been approved under the traditional Section 7(c) certificate procedure (Tr. 1795) such as the currently existing long term transportation agreements in effect in the offshore (Tr. 2090-91).

86. Assuming that the selective discounting provisions of Order 436 are upheld, a pipeline that discounts might not earn the permitted rate of return. It could only maintain its rate of return by increasing throughout to a level above that on which the rates were predicated. Where a pipeline elects to discount and undercollects as a result, it cannot transfer those costs to a later rate period in order to recover them (Tr. 600, 622-23, 2059).

87. A pipeline that discounts its rates within the maximum and minimum rates approved by FERC must report such discounts to FERC within 15 days. A customer who believed a pipeline had unduly discriminated among customers in discounting would be able to file a complaint or protest with FERC (Tr. 625-26, 2060-61).

88. Both UGPL and NGPL are operating as open transporters pursuant to interim authority under Order 436 (Tr. 2376-77). They are seeking final settlement of the terms and conditions which will be included in their Order 436 tariff. Sea Robin is fully open now. Although its final tariff has not yet been issued, it is operating under an interim tariff and seeks no waivers of any provisions of Order 436. Although neither HIOS nor Stingray is operating as an Order 436 transporter, MidCon has asked its partners in those pipelines to consider opening the pipelines (Tr. 1750, 1780). Because NGPL and UGPL are shippers on both HIOS and Stingray, and because they are open access transporters, they are operating as open transporters on HIOS and Stingray (Tr. 1750, 1780, 2376-77).

89. FERC regulation is prospective: rates are set for a future time period. FERC rates do not compensate for underrecovery in past time periods or recoup excess revenues earned in past time periods. Thus, a pipeline company's actual revenues may be different from the amounts projected by FERC if the company's level of business varies from FERC projections. For example, if a company's deliveries exceed its representative volume, its total revenue can exceed its revenue requirement. If a company does not deliver its representative volume,

its revenues will fall short of its revenue requirement. During the time period that the particular rates are effective, the company may keep the excess revenue and will not be made whole for shortfalls. This is one of the features of FERC regulation that gives pipelines an incentive to compete for additional business: an increase in deliveries over the representative volume will increase the pipeline's profits (Tr. 582-84). [22]

e. *FERC And Competition*

90. FERC is required to consider competition in carrying out its mandate under the NGA, 15 U.S.C. 717-717W; *Northern Natural Gas Co. v. Federal Power Commission*, 399 F.2d 953 (D.C. Cir. 1968).

91. According to Mr. Malloy, a former employer of FERC, it has displayed a heightened awareness of the role of competition in the regulatory process (Tr. 563, 565). For example, in statements accompanying the issuance of its Order 380, FERC said:

... [A] minimum commodity bill can serve as a barrier to competition. A customer is not likely to purchase gas from an alternate supplier if it is required to pay for gas it does not take from the original supplier. As such, a minimum commodity bill may inhibit natural gas price decreases that could otherwise result from competitive forces.

\* \* \*

The commission therefore finds that utilization of minimum commodity bills to recover costs for gas not taken is fundamentally inconsistent with the increasingly competitive wellhead market mandated by the Congress in 1978. Congress intended that there be an opportunity for gas prices to increase or decrease—whichever the market demands. Implementation of the instant rule will further this Congressional intent by removing one obstacle that inhibits response to market demand (CX 1012B, G).

92. FERC also acted to expand competition by encouraging pipelines to transport for others (Tr. 554, 566). In a series of orders, the Commission permitted pipelines to obtain blanket certificates to transport gas for particular groups of end-users. These orders permitted pipelines to engage in these activities without the need for a certificate for each individual transaction (Tr. 566-68).

93. FERC's Order 436 was adopted to comport with the mandate of NGPA for greater competition (Tr. 611-13). In proposing to adopt Order 436, FERC stated: [23]

The competitive pressures caused by partial wellhead deregulation continue to grow and have become even more evident since January 1, 1985. Demand for transportation services to reflect the growing competition at both wellhead and burner tip can also be expected to increase. Greater customer access to alternate suppliers and/or transporters of gas is giving rise to innovative marketing strategies both by new entrants to the natural gas sales business as well as by traditional suppliers. Alterations in the way risks are shared, more open access to transportation and concomitant changes in service agreements, and new gas purchase policies are reflections of and responses to fundamental changes which have already occurred in the natural gas markets. These new ways of doing business in response to market forces have important implications for the way the industry is regulated, and have made necessary timely regulatory adjustments (CX 1013E (footnote omitted)).

In issuing Order 436, FERC wrote:

The NGPA certainly accomplished its primary goal of increasing competition and gas supplies at the wellhead. But the NGPA also aggravated price distortions between the city-gate and the wellhead. These price distortions have intensified competitive pressures on pipelines for new and lower-priced services. In turn, these competitive pressures require changes in the Commission's regulations if we are to fulfill statutory regulatory obligations over interstate pipelines in turbulent and fast-changing gas commodity markets (CX 1014M).

94. As justification for adoption of Order 436, FERC stated:

. . . [C]ompetition in the natural gas industry today is proliferating. In these circumstances, it makes little sense to withhold from pipelines the basic weapon other businesses have to wage the competitive battle: the ability to lower prices to beat the competition (CX 1014Z-20). [24]

f. *The Outer Continental Shelf Lands Act*

95. The Outer Continental Shelf Lands Act ("OCSLA"), 43 U.S.C. 1331-1356, requires that both the purchase and transportation of offshore gas be made on a nondiscriminatory basis (Tr. 2080; 43 U.S.C. 1334(e) and (f)). Pursuant to the OCSLA, the pipeline industry has considered itself obligated to both purchase and transport gas on a nondiscriminatory basis in the offshore (Tr. 2081). A witness from Texaco stated his belief that interstate pipelines have an obligation to move gas for individual companies in the offshore, and that offshore pipelines cannot unreasonably deny access if they have capacity available because of the OCSLA (Tr. 947), and Shell has filed a petition with the FERC alleging that Black Marlin Pipeline is unreasonably denying access to Shell and other producers in violation of the OCSLA (RX 2781, 2782A-U).

96. FERC's actions demonstrate a similar interpretation of the OCSLA. On June 12, 1978, it issued an order amending the original HIOS and UTOS certificates. This order provides: "In order to accommodate volumes attributable to non-affiliated shippers, HIOS and U-T will allocate their certificated capacity on a pro rata basis among all the shippers to be served. Both HIOS' and U-T's existing tariffs provide for the reduction in contract demand on a pro rata basis to accommodate new shippers" (Tr. 2081-82; RX 2760A).

#### E. *Natural Gas Pipeline Systems In The OCS*

##### 1. HIOS

97. Five companies participated in the proposal for constructing the HIOS system (Tr. 1858; CX 159Z-1). On June 4, 1976, the FPC issued a Section 7(c) certificate to the partnership (RX 1987A-P), and HIOS was placed in service on March 31, 1978 (Tr. 155, 1859; RX's 1987A-P, 2004).

98. HIOS begins in West Cameron 167, which is 25-28 miles from shore, and extends south into the High Island East Addition Area South Extension A-264 at which point three major legs were built, one going due south and back to the east to A-334 South Extension, the middle leg extending south through the A-573 area, and the west leg extending down to the A-563 area (Tr. 216, 1857; RX 2004).

99. HIOS' termination point in West Cameron 167 is the point at which it interconnects with two separate offshore pipeline systems (Tr. 157, 216, 394, 1746-47). At West Cameron 167, HIOS connects with UTOS and a segment of American Natural Resources' ("ANR") pipeline system [25] (Tr. 170, 217, 1746-47; RX 2004). UTOS delivers gas at Cameron Meadows, Louisiana; ANR's pipeline delivers gas at Grand Chenier, Louisiana (Tr. 170). Shippers send their gas through either UTOS or ANR's pipeline, depending on which system can get the gas back to their onshore systems (Tr. 1746-47).

100. Before the MidCon/United acquisition, HIOS was owned by five partners with equal 20 percent shares: ANR, a subsidiary of Coastal Corp. (and HIOS' operator); Texas Gas Transmission Co. ("Texas"); Transcontinental Gas Pipeline Co. ("Transco"); NGPL, and UGPL. MidCon, through its subsidiaries, NGPL and UGPL now owns 40 percent of HIOS. The other three venture partners own the remaining 60 percent (Tr. 145, 1718, 1743; CX's 159Z, Z-15).

101. The HIOS management committee controls all of its significant business decisions. These include whether to make rate filings or

submit rate proposals to FERC; whether to seek FERC approval to construct new expansions or extensions of the system and, if approved, whether to construct them; and, whether to enter into contracts or amend existing contracts. A majority vote controls decisions of the committee, and three votes constitute a majority. Each owner appoints one member to the committee. MidCon has appointed one person to vote for both NGPL and UGPL (Tr. 184-85, 219, 222-23, 1748; CX's 159Z-13-Z-14, Z-43, Z-46).

102. HIOS has long-term transportation contracts with five owner shippers and eight non-owner shippers (Tr. 206; RX 1059A-B; CX 167K-Z-419). The term of each firm transportation agreement is 15 years from the date of initial delivery, then continuing year-to-year thereafter until the shipper gives a one year notice to terminate the agreement (CX 167P, Z-17, Z-44, Z-69, Z-96 Z-123, Z-148, Z-174, Z-199, Z-224, Z-249, Z-275, Z-301, Z-327, Z-352, Z-377, Z-399; RX 1059A-B). These agreements were executed in 1977 and 1978 (RX 1059A-B). Since initial deliveries began in 1978, the primary term of these agreements will expire in 1993.

103. HIOS' 13 shippers have long term agreements which grant the right to ship specific quantities of gas without interruption (Tr. 172-73, 357-58; CX's 167G, Z-9-Z-12, Z-36-Z-38, Z-63-Z-64, Z-88-Z-90, Z-115-Z-118, Z-143, Z-172-Z-173, Z-194, Z-218, Z-244, Z-269-Z-270, Z-295-Z-296, Z-321-Z-322, Z-347, Z-372, Z-394, Z-419; RX 1059A-B). All of HIOS's certificated capacity that has been approved by FERC is currently contracted to shippers who have firm rights to transport gas on HIOS (Tr. 180, 1747; RX 1059A-B). If a new shipper desires capacity on HIOS, the partnership agreement provides that the existing capacity will be reallocated to include the new shipper (Tr. 1747, 2081-87; CX 159Z-6; RX 2760A-C).

104. Shippers on HIOS have the right to use their firm contract demand to transport gas for third parties (Tr. 219), and there is no significant difference in the transportation contracts between HIOS and its owner and non-owner shippers [26] (Tr. 2082-89; CX 167K-Z-419); these shippers use their capacity to provide interruptible transportation and exchange service to many other parties (TR. 2353-56; RX 1057D-N). HIOS is a transporter of OCS natural gas; it does not buy and resell that gas (Tr. 219, 698, 1280-82, 1657, 1789, 1858).

105. HIOS is required to file a FERC rate case biannually. The filings are prepared by the HIOS rate committee and submitted for approval of a majority of the HIOS management committee (Tr. 2189;

CX's 39, 159Z-14). Because NGPL and UGPL have one representative on the five-member HIOS management committee, MidCon could not force HIOS to take any action with respect to rates (Tr. 2189-90). ANR, HIOS' operator, represents it in FERC rate proceedings (Tr. 2197).

106. The current unit rate for transportation of natural gas on HIOS is 12.01 cents per Mcf, calculated on a 100 percent load factor basis (Tr. 2194-95; RX 2020A-B). The rate charged by HIOS to its primary shippers is not necessarily the same rate charged by the shippers to third-parties (Tr. 1794-95, 2092).

## 2. Stingray

107. The first leg of what is now the Stingray pipeline system was built by NGPL in the early seventies (Tr. 1721). In the early seventies, NGPL and Trunkline Gas Company ("Trunkline") proposed a joint venture extension of Stingray (Tr. 1721-22). The proposal was approved by the FPC in 1974. Construction was finished in 1975 and gas began flowing through the system in that year (Tr. 1723; RX 1992A-X).

108. The original 75-mile long Stingray was extended by further additions in 1976 and 1978 (Tr. 1726, 1728; RX's 1993E, 1994A-B). The system now extends from Cameron Parish, onshore Louisiana, to various blocks in the West Cameron area offshore and to High Island A-330 where it connects with HIOS (Tr. 1721-22, 1726-28).

109. Stingray does not build laterals to connect reserves; shippers or other interstate pipeline companies do this (Tr. 1533-35, 1715).

110. Before the MidCon/United acquisition, Stingray was owned equally by Trunkline, which is an affiliate of Panhandle Eastern Corporation, and NGPL. No change has resulted in Stingray's ownership as a result of the MidCon/United acquisition (Tr. 268-70, 1200, 1718; CX 177Z-3).

111. Stingray is controlled by a six-member management committee which consists of three members appointed by NGPL and three members appointed by Trunkline (Tr. 1730-31; CX 177I). Pursuant to the Stingray partnership agreement, all management [27] committee decisions must be carried by a concurrence of a majority of all members appointed by Trunkline and a majority of all members appointed by NGPL. Accordingly, a majority under the Agreement requires the agreement of two out of the three members from each of the companies (CX 177I-J). Therefore, in order for a proposal to be

approved by the management committee four out of the six management committee members must approve it, and as a practical matter, the decision must be unanimous (Tr. 1731).

112. The management committee makes all the major business decisions for Stingray. These decisions include whether to propose a rate change or make a rate filing with FERC, and whether to apply to FERC for permission to construct new facilities (Tr. 1731-32; CX 177I). According to the Stingray Partnership Agreement, neither party can block the construction of a lateral to connect new reserves to Stingray if the proposed construction does not impair the operation and capacity of Stingray (Tr. 1735).

113. Trunkline has operated Stingray continuously since its construction. As operator of the pipeline, Trunkline's responsibilities include the day-to-day running of the pipeline to make sure that gas received at each of the platforms is properly measured, moves through the system, is properly brought to the terminus of the system, dehydrated or separated, remeasured, and then allocated to the receiving pipeline or pipelines. Trunkline is also responsible for the maintenance, ongoing operation, major repairs, and new construction of the system as designated by the management committee. In addition, it is responsible for the accounting, day-to-day cash management, and development of rate filings and rate proceedings (Tr. 1737-38; CX 177N-Q).

114. Three interstate pipeline systems, NGPL, UGPL and Trunkline, have firm transportation agreements which grant shipping rights in the Stingray pipeline system (Tr. 272, 1736, 1743; RX 1059D; CX 180G-Z-52). The initial term of these agreements extends 20 years from the date of initial receipt and delivery and thereafter from year-to-year until a 12-month written notice of intent to cancel is given by one of the parties (CX 180Q, Z-25). Since Stingray began initial delivery of gas in 1975, the initial term of these contracts runs until 1995 (Tr. 1723). Each of the parties has a contractual right to move a specified amount of gas through the system each day without interruption (Tr. 272, 1743; RX 1059D). The parties may lease their contract demand capacity to third parties (Tr. 355, 1743). Stingray transports gas for its shippers; it has never purchased gas (Tr. 1654).

115. The Stingray rate committee reviews the rate filing prepared by Trunkline, subject to the approval of the management committee. NGPL and Trunkline must agree on any action with respect to rates (Tr. 2190; CX 177I-J). [28]

116. Stingray's current unit rate for transportation of natural gas (which is not necessarily the same as that charged by its contracting shippers to other parties), calculated on a 100 percent load factor basis, is 12.72 cents per Mcf. Its profit per Mcf of gas is approximately 2 cents (Tr. 2195-96).

### 3. Sea Robin

117. The initial Section 7(c) construction application for Sea Robin was filed as a joint venture by UGPL and Southern Natural Gas Company ("Southern Natural"). It was intended to transport gas bought from producers in the East Cameron, South Marsh Island, and Eugene Island areas of the OCS (Tr. 1840-43; RX 1995A-E).

118. In considering the application, the FPC questioned whether Sea Robin would duplicate another offshore system proposed by Texas Eastern, but decided that duplication would not occur (Tr. 1843-44; RX 1995C).

119. Additional construction by Sea Robin of a 26-mile extension from Eugene Island 206 to Ship Shoal 222 was authorized in January 1970 (Tr. 1846; RX 1997A). Extensions of Sea Robin's east and west legs were authorized in February 1977 (Tr. 1847; RX 1998A), the FPC noting that the west leg extension would be in the vicinity of a then recently-authorized extension of the Bluewater System (RX 1998C-D). The FPC determined that connection of the blocks in the area where the two pipelines would cross to the proposed Sea Robin extensions would be quicker and cheaper than connection to Bluewater (RX 1998D).

120. A further 11.3 mile lateral extension of Sea Robin to connect Vermilion 228 to Vermilion 190 was authorized in February 1977 (RX 1999B).

121. Unlike HIOS and Stingray, Sea Robin purchases gas for resale to its two owners, NGPL and Southern Natural. Sea Robin also transports natural gas for its owners and other shippers (Tr. 1752, 2303; CX 178A-Z-634; RX 1059E-F).

122. The Sea Robin joint venture agreement permits either owner to contract for reserves and build laterals to move the reserves without the consent of the other owner (Tr. 1849; CX 179P).

123. Before the MidCon/United acquisition, Sea Robin was owned equally by Southern Natural and United. As a result of the acquisition, MidCon owns half of Sea Robin, as does Southern Natural (Tr. 1663, 1751; CX 179T). [29]

\* 124. Sea Robin is controlled by a management committee which is comprised of an equal number of members appointed by each joint venturer. The Sea Robin joint venture agreement requires the concurrence of a majority of all the members appointed by each joint venture to approve decisions (CX 179C-D). In addition, the Sea Robin rules and regulations require an affirmative vote of each of the joint ventures to transact any business (CX 179Z-7). Thus, the agreement of both United and Southern Natural is needed to make any decision regarding Sea Robin (Tr. 1752-53; CX 179D, Z-7). The Sea Robin management committee makes all significant business decisions related to the operation of Sea Robin, including decisions regarding the purchase of gas and gas purchase contracts (Tr. 1753; CX 179C).

125. UGPL, the operator of Sea Robin, has the following duties: (a) representing Sea Robin in FERC rate proceedings; (b) negotiating and administering Sea Robin's transportation contracts; and (c) overseeing Sea Robin's certificate applications (Tr. 2197-98, 2301-02; CX 179I-L). Southern Natural reviews and must approve both the transportation and exchange activities and the certificate activities of Sea Robin (Tr. 2302-03; CX 179L).

126. Sea Robin has firm transportation agreements with ten primary shippers (CX 178B-C, Z-7-Z-8; RX 1059E-F). Generally, these agreements continue in effect from year-to-year after their initial terms unless cancelled by either party by at least six months' written notice (CX 178Z-51, Z-73, Z-105-Z-106, Z-170, Z-263, Z-287, Z-311, Z-387, Z-412, Z-438-Z-439, Z-468, Z-543 (one year notice), Z-555, Z-578). These transportation agreements grant the shipper the right to ship specific quantities of gas in Sea Robin each day without interruption (CX 178Z-61, Z-86, Z-106, Z-170, Z-216, Z-237, Z-258, Z-263, Z-287, Z-311, Z-412, Z-434, Z-467, Z-516, Z-555 Z-578; RX 1059E-F).

127. Sea Robin's rate filings at FERC are prepared by its rates committee, subject to the approval of its management committee. Sea Robin's owners must agree on any action with respect to rates (Tr. 2191-92). Sea Robin's current unit rate for transportation of natural gas is 9.45 cents per Mcf, calculated on a 100 percent load factor basis (Tr. 2194; RX 2020A-B). The rate charged by Sea Robin to its primary shippers is not necessarily the same rate charged by the shippers to third-parties (Tr. 1794-95).

#### 4. Other Natural Gas Pipelines In The OCS

128. Before and after the MidCon/United acquisition, over 20 major

singly-owned and joint venture pipeline systems operated in the OCS, offshore from Texas and Louisiana (RX 2004). These offshore pipeline systems operate as gathering lines or segments of interstate pipeline systems to provide transportation from [30] producing areas in the Gulf of Mexico for ultimate delivery to city-gate and burner tip markets. The offshore pipelines interconnect with other offshore and onshore pipelines to provide a transportation system to move gas from offshore wellhead markets to city-gate and burner tip markets throughout virtually the entire United States. The offshore pipeline systems are owned entirely or partially by interstate pipeline companies with extensive onshore pipeline systems serving various city-gate markets. Many non-owner shippers on offshore pipelines also have extensive onshore pipeline systems serving various city-gate markets. Other non-owner shippers include producers, LDC's and end-users (F.'s 129-142).

129. ANR purchases gas from the offshore Gulf of Mexico and transports it to its city-gate markets in Michigan, Illinois, Minnesota, Wisconsin and Iowa (Tr. 211-12, 1679-80; RX's 2004, 2005). ANR owns several pipeline systems in the offshore, one that starts in West Cameron Blocks 167 and 238 and connects with ANR's main onshore transmission line in Eunice, Louisiana (Tr. 151-52; RX 2004). ANR also owns an offshore pipeline system beginning in the Eugene Island, Vermilion, South Marsh Island and Ship Shoal areas offshore Louisiana which connects with ANR's main line at Patterson, Louisiana (Tr. 151-52; RX 2004). ANR also has a one-fifth ownership interest in HIOS (F. 7). From offshore, ANR's pipeline system extends into the Oklahoma and Texas Panhandle area and extends north into southeastern Illinois, Minnesota, Iowa and Wisconsin (Tr. 212, 1679; RX 2005). The city-gate markets served by ANR are in the upper midwest, primarily Michigan and Wisconsin (Tr. 143-44). ANR transports gas owned by third parties through ANR's offshore lines. ANR also purchases gas in areas where it has no major facilities in the offshore. ANR has entered into transportation and exchange arrangements (F.'s 158-159) with other pipelines to receive the gas and deliver it back to ANR's facilities, onshore and offshore, for ultimate delivery to its city-gate and burner tip markets (Tr. 1679-80; RX 1055A-C, D-H).

130. Columbia Gulf and Columbia Gas are affiliated corporations. Columbia Gulf purchases gas from the offshore and transports it to Mississippi, Tennessee and Kentucky (RX's 2004, 2005). Columbia

Gulf owns offshore pipeline facilities beginning in the East Cameron and Vermilion areas which extend through Louisiana, then run northeasterly through Mississippi, Tennessee, Kentucky, and Ohio where it connects with Columbia Gas' system (RX's 2004, 2005). Columbia Gulf also has an ownership interest in Bluewater joint venture pipeline system (RX 2004). Columbia Gas is a non-owner shipper on HIOS, as well as other pipelines in the offshore (RX 1059A). Columbia Gas has pipelines that start in the Gulf Coast area, and extend through Louisiana, across Mississippi, into Tennessee and Kentucky, and then into Ohio, Pennsylvania and New York (Tr. 212; RX 2005). Columbia Gas has extensive gathering and distribution facilities in Ohio and Pennsylvania; its system ends in New York State and serves the greater New York area as well as lower New England [31] (Tr. 1745; RX 2005). Columbia Gas purchases gas in the offshore, but because it has no offshore facilities it has entered into transportation agreements to have the gas delivered for ultimate delivery to its city-gate and burner tip markets (RX 1055S, Z-8, Z-13, Z-15, Z-39, Z-41, Z-43, Z-47).

131. Consolidated Gas is a non-owner shipper on HIOS, as well as on other pipelines (RX 1059A). Consolidated Gas is headquartered in Clarksburg, West Virginia and owns pipeline facilities in Ohio, West Virginia, Pennsylvania and New York (Tr. 213, 384; RX 2005). Consolidated Gas has no transmission facilities from the offshore to its facilities in West Virginia, Ohio, Pennsylvania, and New York (Tr. 1745; RX's 2004, 2005). The gas purchased by Consolidated Gas in the Gulf is transported by various offshore pipelines to interconnections with Texas Gas and Texas Eastern for ultimate delivery to Consolidated Gas and its city-gate and burner tip markets (Tr. 393-95, 420, 1745, 2353-54).

132. El Paso is a non-owner shipper on HIOS with firm shipping rights which it utilizes to transport gas it purchases in the offshore (Tr. 214; RX 1059A-B; RPF 178). El Paso serves California and the western parts of the United States (Tr. 1746; RX 2005). Its pipeline system starts in the Permian Basin of Texas, runs west along the Rio Grande River, has an extension that runs through New Mexico and Arizona, and is tied together and terminates at the California border (Tr. 213, 1746; RX 2005).

133. Florida Gas has firm shipping rights on HIOS and numerous other offshore pipelines (RX 1055V, Z-10, Z-13, Z-23, Z-40). Florida Gas owns no offshore transmission facilities (RX's 1347A-I, 2004).

Florida Gas' pipeline system begins in the southeastern portion of Mississippi; traverses into the panhandle of Florida; extends throughout Florida to the cities of Jacksonville, Orlando, Daytona, Tampa, and Sarasota; and runs south along the east coast of Florida to the Florida Keys (RX 2005).

134. National Fuel Gas Supply Corporation is a non-owner shipper on HIOS (CX 167Z-323-Z-347; RX's 1055V, 1059A-B). National Fuel Gas Supply Corporation owns no major transmission facilities in the offshore (RX 2004). National Fuel Gas Supply Corporation owns onshore pipeline facilities starting in the northeastern portion of Pennsylvania and extending into the eastern portions of the State of New York, supplying gas to the cities of Erie, Pennsylvania and Buffalo, New York (RX 2005).

135. Northern Natural has firm shipping rights on HIOS which it uses to transport gas it purchases in the offshore (RX 1057D). Northern Natural's system starts in the Permian Basin and the panhandle of Texas, and brings gas north across Kansas into Nebraska, and then north into the Minneapolis-St. Paul area (Tr. 1682; RX 2005). It also has a leg that runs across into Illinois and southern Wisconsin (Tr. 1682). [32]

136. Southern Natural purchases gas from the offshore Gulf of Mexico and transports it to its market areas in Alabama, Georgia and Mississippi (Tr. 1746; RX's 1059A-B, 2005). Southern Natural owns offshore pipeline facilities which begin in the Eugene Island, Main Pass, West Delta and South Pass areas in the Gulf of Mexico, extend north into Mississippi, and then split into two legs, one going further north then east into northern Alabama and Georgia, and the other going east into central Alabama and Georgia (Tr. 1751-52; RX's 2004, 2005). Southern Natural also has a one-half ownership interest in Sea Robin (Tr. 1751; CX 179T). Southern Natural transports gas owned by third parties through its offshore lines. Southern Natural also purchases gas in areas where it has no major facilities in the offshore (RX's 1347A-I, 2004). Southern Natural has entered into transportation and exchange arrangements with other pipelines to receive the gas and deliver it back to its facilities, onshore and offshore, for ultimate delivery to its city-gate and burner tip markets (RX 1057Z-13, Z-23).

137. Tennessee Gas purchases gas from the offshore Gulf of Mexico and transports it to its markets in Ohio, Pennsylvania and New York (Tr. 213, 1680-81; RX 2005; RPF 251). Tennessee Gas owns offshore

pipeline facilities beginning in the Sabine Pass area, the West Cameron and East Cameron areas, Vermilion area and South Marsh Island area which all connect to a main transmission line onshore in southwest Louisiana (RX 2004). Tennessee Gas also has offshore pipelines in the South Timbalier area, South Pass area, and the West Delta area which connect to main transmission lines onshore in southeast Louisiana (RX 2004). Tennessee's system begins in the offshore and joins with another leg from Texas at the northern border of the State of Tennessee, at which point the system continues north to Ohio, Pennsylvania and New York (Tr. 213, 1680-81; RX 2005). Tennessee Gas has an ownership interest in the Bluewater offshore joint venture pipeline system. Bluewater extends south from Vermilion Parish, offshore Louisiana into the southern border of the Vermilion area, then east through South Marsh Island, Eugene Island and the Ship Shoal areas, then north through the South Pelto area to an onshore connection at Terrebonne Parish, Louisiana (RX 2004). Tennessee Gas also has firm shipping rights on HIOS and Stingray, as well as other pipelines in the offshore (Tr. 2353; RX 1055D-E, S-T, U, W, Z-6, Z-11, Z-30, Z-49). Tennessee Gas transports gas owned by third parties through its offshore lines. Tennessee Gas also purchases gas in areas where it has no major facilities in the offshore (RX's 1347A-I, 2004). Tennessee Gas has entered into transportation and exchange arrangements with other pipelines to receive the gas and deliver it back to Tennessee Gas' facilities, onshore and offshore, for ultimate delivery to Tennessee Gas' city-gate and burner tip markets (RX 1057T).

138. Texas Eastern purchases gas in the offshore Gulf of Mexico and transports it to city-gate markets in New York, Philadelphia and Pittsburgh (Tr. 69). Texas Eastern owns the [33] Cameron offshore pipeline system (Tr. 69-70). The Cameron system begins in the East and West Cameron areas offshore (Tr. 70; RX 2004). The Cameron system extends north and connects with Texas Eastern's main transmission lines in Beauregard Parish, Louisiana (RX 2005). From this point, the main transmission line traverses southwest along the Texas Gulf coast to the Mexican border. The main transmission line also travels in a northeasterly direction through Mississippi, Alabama, Tennessee, Kentucky, Ohio, New Jersey, into New York and Pennsylvania. Texas Eastern also owns offshore pipeline facilities beginning in the Main Pass area, and travelling through the Breton Sound Area into onshore Louisiana and connecting to the main transmission line

near Francisville, Louisiana (Tr. 69; RX 2005). Texas Eastern transports and exchanges gas owned by third parties through its offshore lines (RX 1055Z-28-Z-32). Texas Eastern also purchases gas in areas where it has no major facilities in the offshore (RX's 1347A-I, 2004). Texas Eastern has entered into transportation and exchange arrangements with other pipelines to receive the gas and deliver it back to Texas Eastern's facilities, onshore and offshore, for ultimate delivery to its city-gate and burner tip markets (Tr. 116-18, 127-29; CX 805A-Y; RX's 2064A-Z-14, 2065A-Z-59, 2138A-T).

139. Texas Gas has a one-fifth ownership interest in HIOS (F. 7). Texas Gas' onshore system begins onshore Louisiana, then goes north through Mississippi, Tennessee, and Kentucky; then one leg travels into Indiana and the other leg travels into Ohio (RX 2005). Texas Gas transports its own and other parties' gas through lines on which it has shipping rights, such as HIOS (RX 1057D).

140. Transco purchases gas in the offshore Gulf of Mexico and transports it to its city-gate markets in New Jersey, New York and Pennsylvania (Tr. 211; RX 2005). Transco owns extensive pipeline facilities in the offshore (Tr. 211, 1744; RX 2004). Transco has offshore pipelines beginning at Vermilion Block 215, Vermilion Block 331, Eugene Island Blocks 206 and 208, Ship Shoal area blocks 108, 223, 246, 268, and 239, and South Pelto area blocks 12 and 13, which all connect to its main transmission line in Terrebonne Parish, Louisiana (RX's 2004, 2005). Transco also has offshore pipelines beginning at Mustang Island area blocks 619, Brazos area blocks A-19, A-17, and A-1 which connect to Transco's main transmission line in Texas (RX's 2004, 2005). Transco has an offshore pipeline beginning at Galveston area block 241 and High Island block 179 and another pipeline beginning at West Cameron block 110 which connects to the main transmission line in western Louisiana (RX 2004). Transco also has a one-fifth ownership interest in the HIOS joint venture offshore pipeline system and a one-third ownership interest in UTOS (Tr. 1718; CX's 159Z, 182C, K). Transco's main transmission line extends north from offshore Louisiana and Texas and east to New Jersey, New York and Pennsylvania (Tr. 211; RX 2005). Transco transports gas owned by third parties through its offshore lines (RX's 1055T, Z-33-Z-43, 1057J-L). Transco also [34] purchases gas in areas where it has no major facilities in the offshore (Tr. 817; RX's 1347A-I, 2004). Transco has entered into transportation and exchange arrangements with other pipelines to receive the

gas and deliver it back to Transco's facilities, onshore and offshore, for ultimate delivery to Transco's city-gate and burner tip markets (RX's 1057D, U, Z-3, Z-8).

141. Trunkline and Panhandle Eastern Pipeline Company are both subsidiaries of Panhandle Eastern Corporation (Tr. 268-69). Trunkline purchases gas from the offshore Gulf Coast as well as from South Texas and Louisiana and transports it to its markets in Illinois, Indiana and Michigan (Tr. 269). Trunkline owns the Terrebonne offshore pipeline system (Tr. 271). The legs of Trunkline's Terrebonne system begin in the Eugene Island, South Timbalier and Grand Isle areas and traverse through the South Pelto area, the Ship Shoal area, and South Marsh Island area (RX 2004). Another leg begins in the North Addition of the South Marsh Island area and connects with the main trunk of the Terrebonne offshore system near the shoreline (RX 2004). The Terrebonne system connects with Trunkline's main transmission system in Louisiana (RX 2004). The main line travels north to the city-gate markets it serves in Indiana, Michigan and Illinois (Tr. 269; RX 2005). In addition, Trunkline has a one-half ownership interest in the Stingray joint venture offshore pipeline system (Tr. 268-69; CX 177Z-3). Trunkline interconnects with Panhandle Eastern Pipeline in Tuscola, Illinois (Tr. 269). Trunkline transports gas owned by third parties through its offshore lines (RX 1055Z-44-Z-45). Trunkline also purchases gas in areas where it has no major facilities in the offshore (RX's 1347A-I, 2004). Trunkline has entered into transportation and exchange arrangements with other pipelines to receive the gas and deliver it back to Trunkline's facilities, onshore and offshore, for ultimate delivery to Trunkline's city-gate and burner tip markets (Tr. 350).

142. Panhandle Eastern has an extensive onshore pipeline system (Tr. 1681; RX 2005). It buys gas in the Hugoton and Anadarko Basin field in Kansas and Oklahoma and the West Panhandle field in Texas and parts of Oklahoma (Tr. 268). Panhandle Eastern's system extends from the Panhandle of Texas to the Permian Basin, across Kansas and Missouri into Illinois, and across Indiana into Detroit (Tr. 1681). It serves the Indiana market, the central Illinois market and part of the Missouri market (Tr. 1681; RX 2005). Panhandle Eastern transports gas for resale to customers in five states: Michigan, Indiana, Ohio, Illinois and Missouri (Tr. 268). Panhandle Eastern purchases gas in the offshore, but because it has no offshore facilities it has entered into transportation agreements to have the gas delivered to Panhandle

Eastern for ultimate delivery to its city-gate and burner tip markets (RX's 1055U, 1057E, K, Z-22). [35]

*F. Natural Gas Producers In The OCS*

143. Natural gas producers operating in the OCS explore for, drill for and produce natural gas throughout this area, as well as onshore (Tr. 2468-69; RX 1341A-Z-50; CX 1212A-V).

144. Some of the more important producers in the OCS are:

145. Amerada Hess, which holds leasehold interests in offshore blocks stretching from the Viosca Knoll area on the far eastern side of the Gulf to the Matagorda Island area on the far western side of the Gulf (RX 1341C).

146. Amoco Production Company, which owns offshore leasehold interests stretching from as far east as Viosca Knoll to as far west as Mustang Island and the Brazos area (RX 1341D).

147. ARCO, which has offshore leasehold interests stretching from as far west as the Matagorda Island area to as far east as the Viosca Knoll area and as far out as the Garden Banks area (RX 1341G).

148. Chevron USA, Inc., which holds offshore leasehold interests throughout the Gulf (RX 1341K).

149. Conoco, Inc., which has offshore leasehold interests stretching from the far eastern side of the Gulf including the Viosca Knoll area, the South Timbalier area and the Mississippi Canyon area to as far west as the Brazos area (RX 1341N).

150. CNG Producing Company, whose offshore operations extend from the South Timbalier area to the High Island area (Tr. 413; RX 1341M).

151. Elf Aquitaine Inc., which has leasehold interests all across the Gulf (RX 1341Q).

152. Exxon Corp., which also holds leasehold interests across the Gulf (RX 1341T).

153. Kerr McGee Corporation, which owns leasehold interests stretching from the far east side to the far west side of the Gulf (RX 1341X).

154. Pennzoil, which has sold gas in virtually every area in the OCS where there is production (Tr. 710-11).

155. Shell, which has extensive leasehold interests in the Gulf (RX 1341Z-18).

156. Standard Oil, which hold leases in Alaska, the continental United States, and in hundreds of thousands of acres from the far west to the far east of the Gulf (Tr. 840; RX 2004). [36]

157. Texaco, USA, which is involved in the domestic exploration and development of oil and natural gas throughout the continental United States, the Gulf and the Atlantic and Pacific oceans. Texaco has interests in approximately 60 leases within the alleged geographic markets (Tr. 916-17; RX 1341Z-43-Z-44).

#### G. *Natural Gas Purchasers In The OCS*

##### 1. Transportation And Exchange Agreements

158. Through transportation and exchange agreements, pipeline companies can purchase natural gas in areas where they have no facilities (Tr. 2470, 2478; RX 1348A-Z-97). In transportation agreements, one pipeline company agrees to transport gas for another one, the first company agreeing to receive gas into its system, transport it to an interconnect point between the two systems, and deliver the gas to the second pipeline at the interconnect (Tr. 153, 2235-36; RX 1629A-Z-26).

159. An exchange agreement is a type of transportation agreement. The difference between them is that in a transportation agreement, consideration is received for moving the gas whereas in an exchange agreement, pipeline A which has a gas supply near pipeline B, and B which has a supply near pipeline A, agree to transport gas for each other without charge (Tr. 2237; RX 1742A-V). These agreements, which involve no costs because equal volumes of gas are exchanged, are thought to be more desirable than transportation agreements (Tr. 119, 1675, 2247).

##### 2. Purchases By Interstate Pipeline Companies

160. Transportation and exchange agreements allow pipeline companies to purchase gas throughout the OCS even though their physical facilities are located only in parts of this area (Tr. 246-72, 1674; RX's 1341A-Z-50, 1348A-Z-97).

161. Thus, NGPL, UGPL, Sea Robin, and virtually every other interstate pipeline company purchase gas both near their existing transmission facilities and away from those facilities. Gas purchased by NGPL, UGPL, or Sea Robin which is not directly connected to the wholly-owned facilities of these pipeline companies is moved through transportation or exchange agreements negotiated with other pipeline companies (Tr. 1917-18, 2303, 2309, 2471; RX's 1347A-I, 1348M-N, Z-4-Z-5, Z-19-Z-20, Z-35-Z-36, Z-49-Z-50, Z-64-Z-65, Z-78-Z-79, Z-93, 2001, 2004). [37]

162. Other interstate pipelines operating in the OCS purchase off-system gas and gas located near their systems: ANR (Tr. 1925-26; RX's 1347A-I, 1348B-C, Z-9-Z-10, Z-46, Z-76, 2004); Arkla (RX's 1347C-D, 1348D, Z-11, Z-40, Z-70, 2004); Columbia Gas (RX's 1347A-J, 1348F-G, Z-13-Z-14, Z-41-Z-42, Z-71-Z-72, 2004); Consolidated Gas (RX's 1347, 1348H, Z-15, Z-43, Z-73, 2004); El Paso (RX's 1347, 1348I, Z-16, Z-44, Z-74, 2004); Florida Gas (RX's 1347A-I, 1348J, Z-17, Z-45, Z-75, 2004); Mid-Louisiana Gas Company (RX's 1347A-I, 1348K, Z-18, Z-48, Z-77, 2004); Northern Natural (RX's 1347A-I, 1348"O"-P, Z-21-Z-22, Z-51-Z-52, Z-80-Z-81, 2004); Sea Robin (RX's 1347G, 1348R, Z-24, Z-54, Z-83, 2004); Southern Natural (RX's 1347A-I, 1348S-T, Z-25-Z-26, Z-55-Z-56, Z-84-Z-85, 2004); Tennessee Gas (RX's 1347A-I, 1348U-V, Z-27-Z-28, Z-57-Z-58, Z-86-Z-87, 2004); Texas Eastern (RX's 1347A-I, 1348W-X, Z-29-Z-30, Z-59, Z-88, 2004); Texas Gas (RX's 1347A-I, 1348Y, Z-31, Z-60, Z-89, 2004); Transco (Tr. 817, 870-71; RX's 1347A-I, 1348Z-1-Z-2, Z-32-Z-33, Z-61-Z-62, Z-90-Z-91, 2004); Trunkline (RX's 1347A-I, 1348Z-3, Z-34, Z-63, Z-92, 2004); West Lake Arthur Corporation (1981-1984) (RX's 1348Z-66, 2004).

#### H. *The Relevant Product Market*

163. There is no record evidence that any method of transportation other than pipelines was considered by producers or is being used to move gas from the producing blocks offshore to the ultimate purchasers. The only practical method of transporting gas from the OCS is through pipelines designed for that purpose (Oil pipelines are not reasonable substitutes, Tr. 400, 695, 817), and Dr. Uri, complaint counsel's expert witness, concluded, therefore, that although natural gas passes through a sequence of markets before it is consumed (Tr. 1011), since market power can be exercised at the origin end of the pipeline (Tr. 996-97), the relevant product market in which to assess the competitive effects of this merger is the transportation of natural gas via pipeline out of the producing areas (Tr. 1010).

164. Respondents' expert witness, Dr. Hall, views the product market much more expansively, arguing that since the demand for transportation of gas derives from the demand for gas at the burner tip, the product market extends from the wellhead to the point of consumption (Tr. 2460-61, 2467).

165. Purchasing practices in the industry lend some support to a broad definition of the product market for pipeline companies (Tr.

360, 1754-55), end-users and local distribution companies (RX 1057C, F-L, Z-1, Z-4-Z-6, Z-0) and producers (Tr. 294, 829-30), all arrange for transportation from wellhead to burner tip. They are not concerned simply with transportation [38] from an offshore producing field to the shoreline of Texas or Louisiana because consumers are not located there (Tr. 830, 1486-87, 1826-27).

166. After analyzing the evidence and the testimony of the experts, I conclude that while the overall product market may be viewed as the transportation of natural gas from the wellhead to the city-gate or the burner tip, since market power can be exercised at various stages within this market where separate transactions occur (Tr. 1014), there are product submarkets, including the transportation of natural gas out of the producing areas. In fact, Dr. Hall testified in another case, *Colorado Interstate Gas Co. v. NGPL*, that a relevant market was “the transportation of gas out of Wyoming” (Tr. 2613-17).

### I. *The Relevant Geographic Market*

#### 1. Introduction

167. According to Dr. Uri, a geographic market exists if a hypothetical monopolist controlling the producing assets can exercise market power within that area (Tr. 1069-70).

168. A hypothetical price increase postulated by Dr. Uri to define his geographic market could be a uniform price increase or a discriminatory price increase. On a gas pipeline, a uniform price increase would be a rate increase over the entire pipeline for all shippers. A discriminatory price increase would occur over only a portion of the pipeline, such as a single leg, or for connection of an individual block (Tr. 1072-73). In cases where one can define a relevant geographic market based on selective price changes (price discrimination), Dr. Uri testified that there may be more than one geographic market in which to analyze the competitive effects of the merger (Tr. 1073-74). Where price discrimination is possible, the geographic market will be smaller in scope than if price increases are uniform (Tr. 1073).

169. In this case, because of the supposed ability of pipelines to price discriminate, Dr. Uri proposed several geographic markets (Tr. 1073-76): (1) the area identified in paragraph 20 of the complaint as amended; (2) the portions of the paragraph 20 area that are east of the north-south line that runs through the eastern boundary of West Cameron block 596 and that are north of the east-west line that runs

through the northern boundary of Garden Banks block 284; (3) the portions of the paragraph 20 area that are west of the north-south line that runs through the eastern boundary of West Cameron block 596 and that are north of the east-west line that runs through the northern boundary of Garden Banks block 270; and (4) individual blocks within the paragraph 20 geographic area (Tr. 1074-75 (referring to CX's 1125, 1082)). Although he could identify additional [39] geographic markets, Dr. Uri concluded that defining additional markets would add little to the inferences that he drew regarding the competitive effects of the acquisition (Tr. 1075-76).

170. Dr. Uri's theory relies, in part, on the fact that pipeline systems in the proposed relevant geographic markets are substitutes for the connection of new blocks in some cases (F.'s 180-195).

171. New blocks have been connected to pipelines that are 10, 20 or more miles from a block (CX 1116A-B). For example, CX 93A-H identifies nine blocks connected to HIOS, Stingray or Sea Robin by laterals more than ten miles long: High Island 480 (12.9 miles); High Island 568 (10.63 miles); High Island 447 (10.76 miles); High Island 414 (14.17 miles); High Island 309 (10.07 miles); West Cameron 630 (12.0 miles); Vermilion 369 (20.45 miles); West Cameron 331 (11.2 miles); Galveston 131 (19.18 miles). CX 94A-Z-13 identifies seven laterals which are longer than ten miles: East Cameron 32 (19.08 miles); Eugene Island 57 (10.34 miles); High Island 171 (26.55 miles); High Island 139 (26.82 miles); Mustang Island (16.7 miles); Vermilion 340 (10.05 miles); West Cameron 436 (13.74 miles).

172. Industry members sometimes consider pipelines that are even further from a block to be viable connection alternatives for that block. Trunkline looked at blocks within a 15 mile radius of Stingray in estimating future reserves and connections available to Stingray (CX 35G). Other pipeline reserve studies assess areas of comparable or further distance from the pipeline (CX 105A-H (Stingray), CX 399A-V (HIOS)). NGPL prepared several gas supply evaluations positing construction of laterals more than 10 miles in length (*see, e.g.*, CX 1400A-D (16.7 miles), CX 1402A-C (25.62 miles)). Mr. Hahn of Texaco viewed the Columbia lateral connected to the Bluewater project to be a viable alternative for Texaco blocks West Cameron 654 and 663 (Tr. 936). A review of an OCS map shows that this lateral is over 12 miles from the blocks (West Cameron 654/663 to West Cameron 616) (*see* CX 904). Trunkline proposed to transport gas on Trunkline-owned pipelines from blocks that were substantial distances

from its system. CX 606 is a proposal to connect East Cameron 185 to Stingray, a distance of 23 to 24 miles (CX 606B). A proposal to connect South Timbalier 292 to Trunkline's Terrebonne system involved a distance of 22.5 miles (CX 605B).

173. Analyzing unconnected blocks located within the paragraph 20 market, Dr. Uri found several within 10 or 15 miles of more than one pipeline (Tr. 1047-48, 1249; CX's 1105A-C, 1106A-C) and he concluded that more than one pipeline is likely to be a viable alternative for many blocks (Tr. 1050). In fact, some blocks are connected to more than one pipeline (Tr. 1051-53; CX 1114). [40]

174. Dr. Uri also considers the fact that pipelines cross a confirmation that these pipelines are sufficiently close in some areas to be substitutes for new blocks (Tr. 1042-43). Stingray and Sea Robin cross each other at three points, in East Cameron 265, 278 and 297 (see CX 904). There is an additional point of intersection in East Cameron 264 where a lateral off Sea Robin crosses Stingray (see CX's 807, 904). Similarly, Sea Robin crosses the 601 project once (East Cameron 334) and Texas Eastern three times (East Cameron 248, 263 and 265) (see CX's 807, 904). Stingray crosses the 601 Project in three places (East Cameron 293 and 314, Vermilion 263), and Texas Eastern in 12 (West Cameron 241, 277, 433, 459, 483, 484, 565, East Cameron 263, 280, 281, 286 and Vermilion 263) (see CX's 807, 904). Stingray connects to the West Cameron 616/601 lateral in West Cameron 616 and crosses the lateral in West Cameron 607 (CX's 807, 904).

175. In deepwater areas and other areas far from any pipeline, pipelines even further than 10-20 miles from a block may be alternatives. For example, NGPL extended its pipeline system 53 miles to connect blocks in the Matagorda Island area (CX's 904, 1369A-C, 1370A-C; RX 2004). # [IN CAMERA] # There has been consideration of connection of Garden Banks blocks to pipeline systems in the market. NGPL considered three options for connecting Garden Banks 236, a 18.4 mile lateral to Columbia Gulf, a 15.5 mile lateral to Stingray, and a 19.3 mile lateral to Stingray (CX 1355A-C). HIOS considered extending toward the Garden Banks to compete with Stingray (CX 399Q). Trunkline evaluated a pipeline to connect blocks in the Garden Banks to Stingray (CX 638A-B). Northern Natural has worked with Columbia to connect Garden Banks 236 to Bluewater (CX 502T; see also CX 105A-G (portions of Garden Banks within NGPL study area for expansion of HIOS and Stingray); CX 141E

(HIOS extension to access Garden Banks reserves); CX 149C (17 blocks under exploration in Garden Banks for potential HIOS transport)).

176. Other record evidence convinced Dr. Uri that pipeline companies within the alleged relevant geographic markets are substitutes for one another.

177. Pipelines that interconnect are substitutes, in his opinion, for transporting gas from blocks near the point of interconnection and for gas flowing to the interconnection point (Tr. 1043-44). HIOS and Stingray interconnect at High Island A-330 (Tr. 1043; CX 1125) and gas from the "state line laterals" can flow into either HIOS or Stingray (Tr. 171-72, 2431). Thus, for blocks connected to the state line laterals, both HIOS and Stingray are easily accessible (Tr. 1043). An ANR document noted that if Trunkline would not transport gas from West Cameron 536 [41] and 542 on Stingray, the volumes could be transported on HIOS by displacement even if the blocks were connected to Stingray (CX 385B-C). NGPL has shifted shipments between HIOS and Stingray based on the rates charged by these pipelines (Tr. 2432-33; CX 48A). NGPL shifted volumes from HIOS to Stingray in order to avoid the UTOS commodity change (Tr. 2433; CX's 133A, 143A-B, 202B). This evidence suggests to Dr. Uri that HIOS and Stingray are sufficiently close together to be substitutes for new blocks, particularly those near the state line laterals (Tr. 1045-46).

178. Blocks are often connected to pipelines that are not the closest pipelines, which indicates to Dr. Uri that more than one pipeline can be a substitute for a block and that spatial competition can and does occur among OCS pipelines (Tr. 1034). CX 1117 shows examples of blocks that were connected to pipelines that were not the closest to the block. Where a more distant pipeline connects a block, this indicates that the cost disadvantage created by the longer distance has been outweighed by lower cost of other elements of the transportation charge (*see* Tr. 1034-37).

179. Purchasers of gas at the wellhead often indicate a preference for connecting a block to their own pipeline systems even where other closer pipelines exist (Tr. 1031-34; CX's 371A, 711A). For example, one NGPL evaluation proposed connecting the block to Transco's system via a 1.8 mile lateral, but requiring payment to Transco of 17 cents per Mcf in transportation charges (CX 1403A-C). A second NGPL evaluation proposed building 25.62 miles of lateral to connect

the block to its own system, which could be achieved at a lower overall cost than the Transco option because no transportation charges had to be paid to a third party (*Compare* CX 1402A with CX 1403A; Tr. 2391). NGPL built the 25.62 mile lateral to High Island 139 (CX 902; RX 2004). ANR considered three alternative routes to connect reserves in Eugene Island 284 to its own pipeline (CX 377A-C), while Sea Robin passes directly through the block (CX's 377C, 904). ANR also proposed to connect reserves from West Cameron 169 and 170 to its own system via a 1.1 mile lateral, while noting that Stingray was closer (CX 378).

## 2. Connections Of Individual Blocks In The Paragraph 20 Area

180. The following analysis of individual blocks located in the paragraph 20 area reveals that in some instances more than one pipeline was considered as an alternative connection.

181. West Cameron 566 and 570: Texas Eastern considered connecting gas it purchased in West Cameron 570 and 566 to HIOS, Stingray or its own Texas Eastern Cameron system (Tr. 82-87) and it connected these blocks to the Texas Eastern system with a 20.1 mile lateral (CX's 314A-B, 1024A-Z23), although HIOS was 11 miles [42] from the block and Stingray was 1.8 miles away (Tr. 82-85; CX's 807, 809A-D). Other potential purchasers and transporters of the West Cameron 566/570 gas also considered alternative connections for this block. For example, Texas Gas evaluated connections to HIOS or Stingray (CX 852). Trunkline proposed to connect the gas on behalf of the producers and transport it through Stingray (Tr. 299-301; CX 601A-D). CNG Producing Company considered HIOS, Stingray and Texas Eastern as viable alternatives for connecting its gas from this block (Tr. 390). # [IN CAMERA] # In evaluating the purchase of these blocks, NGPL concluded that Stingray was the best transportation alternative (Tr. 2402; CX 1381A-D).

182. High Island A-289: Texas Eastern evaluated HIOS and Stingray as substitutes for transporting gas it purchased in High Island A-289 (Tr. 87-91; CX 811A-D). Texas Eastern determined that there would be a lower cost of service for it to connect High Island A-289 to Stingray and utilize a pre-existing transportation and exchange agreement with NGPL on Stingray (Tr. 88; CX 811A). United, the other purchaser of High Island A-289 gas, preferred to connect the gas to HIOS (Tr. 91; CX 309A). HIOS intervened, claiming that the proximity of the block to HIOS indicated connection

to HIOS rather than Stingray (CX 87B, F). Texas Eastern ultimately connected High Island A-289 to Stingray via an NGPL lateral (Tr. 87).

183. West Cameron 556: Tennessee Gas Pipeline considered the Stingray, Texas Eastern and Bluewater systems as substitutes for the connection of gas marketed by Amerada Hess in West Cameron 556 (CX 755). Koch proposed to connect the block "to one of three pipelines in the area: Stingray, Sea Robin or Texas Eastern" (CX 1200A). Trunkline proposed to transport West Cameron 556 reserves through its capacity on Stingray on behalf of the producers (Tr. 310-14; CX 603A-J). Sea Robin evaluated connection of West Cameron 556 reserves to its own system (CX 315A-K). ANR assessed a lateral connection to the Texas Eastern system for West Cameron 556 reserves (CX 379C). Finally, Transco constructed the connecting pipeline from this block to Texas Eastern (Tr. 373; CX 1291B; RX 2004), after also evaluating an alternative connection to the Stingray system (CX 610A-C).

184. East Cameron 299: CNG considered Stingray, Sea Robin, Bluewater and Texas Eastern as viable alternatives to transport gas it planned to market from East Cameron 299. Texas Eastern bought the gas and connected the block to its Cameron system (Tr. 387-88). Sea Robin had evaluated the feasibility of transporting these reserves on its system (CX 329B).

185. West Cameron 597: United evaluated as alternative connections for West Cameron 597 both Stingray and Columbia Gulf's pipeline system (CX 316A-F). [43]

186. West Cameron 494: An NGPL gas supply evaluation proposed to connect reserves in West Cameron 494 to HIOS (Tr. 2403-04; CX 1420A-C). This block has been connected to the Texas Eastern Cameron system (Tr. 2404; CX's 807, 904).

187. West Cameron 464: United conducted two studies for the connection of reserves in West Cameron 464, one with a proposed connection to HIOS (CX 113A), and a second with a proposed connection to Stingray (CX 113B-D). This block has been connected to the Texas Eastern Cameron system (*see* CX's 807, 904).

188. East Cameron 280: Tennessee initially proposed to connect reserves it purchased in East Cameron 280 via a lateral to Texas Eastern in East Cameron 281. Tennessee then proposed to connect the block to Stingray (CX 327). Texas Eastern and Stingray intersect in this block (CX 904).

189. East Cameron 281: United conducted an analysis of connecting reserves in East Cameron 281 to Texas Eastern, Stingray or Sea Robin (CX 324C-F). NGPL and Trunkline preferred to connect this block to Stingray (CX 328). Stingray and Texas Eastern intersect in this block, and the block is connected to Texas Eastern (CX's 328, 904).

190. West Cameron 610 and 615: Columbia proposed to connect reserves from West Cameron 610 and 615 to the Bluewater project, "thus precluding transportation in either Stingray or HIOS" (CX 401).

191. High Island 365 and 375: ANR evaluated a joint lateral project with Trunkline to connect reserves from High Island 365 and 376 to a pre-existing lateral to Stingray (CX 375A). ANR had previously considered connecting these reserves to the east leg of HIOS (CX 375B). The block has been connected to the east leg of HIOS (*see* CX 904).

192. High Island A-350: United sought to connect reserves in High Island A-350 to the HIOS/Stingray interconnect in High Island A-330 which would enable it to transport the gas through its space on either HIOS or Stingray (CX's 18, 26B). Gas delivered to the interconnection can flow in either direction, to HIOS or to Stingray, allowing a shipper to obtain transportation on either of the two pipeline systems (Tr. 170-72, 2431-32; CX 362A).

193. Garden Banks 236: NGPL evaluated connecting reserves from Garden Banks 236 to Stingray or to Columbia Gulf (CX's 71C-D, 72A-C). Northern Natural conducted detailed analyses of a joint project with Columbia to build an 18.5 mile lateral to the Columbia Gulf system for this block (CX's 502A-T, 513A-F). [44] Trunkline investigated opportunities to build a pipeline off of the Stingray system into the Garden Banks area (Tr. 335-37; CX's 624A-B, 638A-B).

194. West Cameron 654 and 663: Mr. Hahn of Texaco identified HIOS, Stingray and Columbia as viable alternatives to transport gas from leases Texaco holds for West Cameron 654 and 663 (Tr. 936).

195. West Cameron 552: Texas Eastern investigated connecting gas reserves in West Cameron 552 to its Cameron system (CX 803A-B), noting that Transco and United had plans to build pipelines from this area to HIOS (CX 802). This block has been connected to the Stingray system (CX 904).

### 3. Connections Of Individual Blocks In The OCS Outside Of The Paragraph 20 Area

196. The examples described below reveal that pipelines outside of the paragraph 20 areas were sometimes considered as alternative connections to the same block.

197. West Cameron 330: Sonat had a "choice between Stingray and HIOS" for connection of its gas in West Cameron 330 (CX 81A). NGPL planned to take its gas from this block to the Tidal system, seven miles to the east (CX 713C).

198. West Cameron 253: Sea Robin evaluated alternative connections for gas from West Cameron 253 to the Stingray or Texas Eastern systems (CX 321D-E). NGPL also considered a Stingray option and a Texas Eastern option for connecting these reserves (Tr. 2393-94; CX 52A-B). NGPL recommended connection to Stingray (CX 52B); the block has been connected via a lateral to the Texas Eastern Cameron system (CX 807).

199. West Cameron 294: ANR prepared an evaluation comparing connection costs for reserves in West Cameron 294 to HIOS or to ANR's own pipeline system (CX's 382B-C, 392A). NGPL wanted to bring this gas to shore on its own Pelican system (CX 118A-E).

200. West Cameron 169 and 170: ANR prepared a cost analysis for connection of reserves in West Cameron 169 and 170 to ANR's offshore system, noting that Stingray and Natural also had facilities in the area (CX 378). NGPL in fact connected the reserves to Stingray (CX 124D).

201. West Cameron 192: Phillips developed a marketing strategy with other producers of reserves in West Cameron 192 based on the fact that "[b]oth Texas Eastern and Tennessee Gas [45] have lines in the immediate vicinity of our wells" (CX 1292). ANR also developed cost of service estimates for connection of this block to Tennessee or Texas Eastern (CX 397H-M).

202. West Cameron 318: An ANR document proposed connecting reserves from West Cameron 318 to HIOS (CX 387). An NGPL gas supply evaluation recommended connecting this block to the Pelican pipeline (Tr. 2405; CX 1374A-B). HIOS is closer to this gas source than the Pelican system, and in fact HIOS traverses the block (Tr. 2405-06; CX 904).

203. West Cameron 115 and 116: NGPL's System Design department prepared "an economic comparison of two possible methods of

connecting West Cameron Blocks 115/116," namely a connection to UTOS versus a connection to the Tidal system (Tr. 2395-96; CX 92A).

204. West Cameron 211 and 212: Northern Natural proposed to connect reserves in West Cameron 211 and 212 to its own system or to UTOS in negotiating with Arco for the purchase of these reserves (CX 1217A-B). NGPL prepared a gas supply evaluation for this gas based on proposed connections to Stingray or to the Pelican system (Tr. 2398-99; CX 1371A-B).

205. West Cameron 64 and 192: ANR considered connections to Tennessee or its own system for reserves in West Cameron 64 and West Cameron 192 (CX 397B-G). ANR chose its own system for West Cameron 64 and Tennessee for West Cameron 192.

206. High Island 116: ANR considered three pipeline system alternatives for transporting gas from High Island 116: NGPL, Transco and Tennessee (CX 390A-B).

207. High Island 139: NGPL prepared three separate gas supply evaluations to evaluate the attachment of reserves from High Island 139 (Tr. 2391-93). Two of these gas supply evaluations proposed a connection to the Transco system (CX's 1402A-C, 1416A-C), while the third recommended connecting the block to NGPL's system (CX 1403A-C).

208. High Island 68: Arco evaluated connection of High Island 68 to Transco, NGPL and UTTCO (CX 1210A-D).

209. Matagorda Island 652, 681 and 682: ANR assessed the costs to connect reserves in Matagorda Island 652, 681 and 682 to both the Matagorda Offshore Pipeline System and a Transco pipeline (CX 391T-W).

210. Eugene Island 336: ANR considered alternative pipeline connections to its own system and to Sea Robin in evaluating a potential purchase of reserves in Eugene Island 336 (CX 374A-C).

[46]

211. Eugene Island 284: ANR prepared cost estimates comparing "three alternatives for the potential connection" of Eugene Island 284 reserves to its own system some three to five miles away (CX 377A-B). Sea Robin traverses this block (CX 377C; *see* CX 904).

212. Eugene Island 182: In assessing "the prospect for obtaining a market for Exxon gas to be produced from a new platform to be installed at Eugene Island 182," Exxon noted that "four pipeline companies have pipeline capacity within seven miles or less of the new platform's location" (CX 1261A). The four pipelines were ANR (two

miles), Sea Robin (3.5 miles), and two Transco pipelines, both seven miles away (CX 1267A).

213. Eugene Island 172: ANR reviewed a competing proposal to connect reserves from Eugene Island 172 to Sea Robin in preparing its own proposal to connect this block to its own system (CX's 389A-D, 1331B-C). Tenneco considered five pipeline systems as alternatives to connect this block: Transco, TGP, Bluewater, Sea Robin and ANR (CX 1331R-T). Tenneco chose the Transco option after comparing costs for each alternative: "The economics shown reflect only expenses (transportation charges), capital requirements for this project and deliverability projections. This was done to highlight the economic differences among the options" (CX 1331J).

214. South Marsh Island 144, 160, 161 and 174: In its assessment of reserves in the South Marsh Island area including blocks 144, 160, 161 and 174, ANR prepared an "economic evaluation [that] compares gathering and transporting 110 MMcf/d from subject area to onshore Louisiana by Michigan, Wisconsin in competition with United Gas Pipeline" (CX's 350A, 367A-E). ANR determined that connection to its own system, via a 19.4 mile lateral, was more economical than a 11.7 mile lateral to United (CX 367C).

215. Natural also prepared a gas supply evaluation for connection of these reserves to the ANR pipeline (CX 1377A-F). Sea Robin proposed to connect these reserves as "[t]he area . . . holds the greatest potential at this time for justifying an expansion of the Sea Robin system . . . ." (CX 334C).

216. Ship Shoal 322 and 323: # [IN CAMERA] [47] [IN CAMERA] #

217. Vermilion 220 and 221: NGPL conducted an economic evaluation comparing costs to connect gas from Vermilion 220 and 221 to the Stingray, Texas Eastern or Bluewater systems (CX 65A-B). NGPL connected these reserves to the Stingray system via a 13.3 mile lateral, even though Texas Eastern and Bluewater were closer (CX 65A-B). NGPL rejected the Texas Eastern option because Texas Eastern was competing with NGPL for gas reserves, and rejected the Bluewater option because of higher transportation fees (CX 65B).

218. Vermilion 315: ANR used three alternative potential pipeline connections in its negotiations with Amoco for the purchase of reserves in Vermilion 315: Gulf Oil pipeline, Transco or Trunkline/NGPL (Stingray) (CX 386A-I). The Stingray connection, which required the longest lateral of the three options, would have the

“lowest rate to shore if Amoco [the producer] agrees to absorb the cost of the connection” (CX 386B).

219. Vermilion 318: CNG’s first choice was the Gulf Oil pipeline and Stingray for the connection of reserves in Vermilion 318; once Gulf Oil refused to provide transportation for third parties, CNG connected the block to Stingray (Tr. 391-93). NGPL also conducted a project evaluation for a connection of this block to Stingray (Tr. 2400; CX 1353A-B).

220. Vermilion 372: NGPL prepared an economic evaluation for the connection of Vermilion 372 reserves to Stingray (Tr. 2401; CX 1417A-C). This block has been connected to ANR’s pipeline system (CX 904).

221. South Timbalier 205, 206, 292 and 295: Trunkline presented a proposal for transportation on its Terrebonne system to Transco for Transco’s reserves in South Timbalier 205, 206, 292 and 295 (Tr. 318-19; CX 605A-F). Transco, a “competitor” of the Terrebonne system, was also considering an alternative connection to its own system (Tr. 324). Transco requested in writing a reduction in Trunkline’s 100-mile haul rate (CX 604A), and after Trunkline refused the request, Transco rejected the Trunkline option (Tr. 329-30).

222. Ship Shoal 188, 189, 210 and 211: Trunkline negotiated with Shell for the connection of Ship Shoal blocks 188, 189, 210 and 211 to the Terrebonne system while Shell was [48] “considering alternatives which would result in extension of a pipeline to a competitor in the area that was further away than the Terrebonne system” (Tr. 332-34; CX’s 645A-H, 646, 647A-B).

#### 4. Individual Blocks As Relevant Geographic Markets

223. Dr. Uri testified that if pipelines can engage in price discrimination, areas smaller than the total area served by a pipeline may be a relevant geographic market—in this case, areas as small as individual blocks (Tr. 1073-75) and that price discrimination is possible if a pipeline can offer a discount from a transportation charge without needing to lower rates on existing or future contracts (Tr. 1057-58, 1067).

224. According to a FERC document:

In a workably competitive market, because of consumer mobility and the inability of firms to prevent resale, the ability of the firm to selectively discount is limited except where [sic] the transaction cost of discovering prices is relatively high. Once the

workably competitive firm posts a price discount, this discount is available to all in that market. However, this firm may not choose to lower its price in all the markets in which it competes. Thus, a price inelastic customer gains the benefits of price discounting only in the market in which prices have been lowered. Natural gas transmission companies possess market power over some customers in some of their geographical markets. These captive customers are not mobile and they are not generally capable of benefiting from resale. The pipeline, unlike many workably competitive firms, can more easily price discriminate among customers . . . . (CX 1014Z-20).

225. FERC Order 436 increases the flexibility to offer selective discounts and reduces FERC procedural obstacles to discounting (Tr. 621-22). FERC has, in fact, determined that selective discounting under Order 436 does not violate the undue discrimination prohibitions of the Natural Gas Act (CX's 1014Z-18-Z-21, 1016Z-3-Z-4). The purpose of the selective discounting provisions of Order 436 is to permit pipelines to compete: **[49]**

. . . [C]ompetition in the natural gas industry today is proliferating. In these circumstances, it makes little sense to withhold from pipelines the basic weapon other businesses have to wage the competitive battle: the ability to lower prices to beat the competition (CX 1014Z-20).

226. It is unlikely that FERC will reject this policy, for it is consistent with FERC's encouragement of competition in the industry (F.'s 90-94).

227. Considering the above, Dr. Uri concluded that individual blocks within the paragraph 20 geographic market are relevant geographic markets (Tr. 1073).

## 5. Larger Areas As Relevant Geographic Markets

### a. *The Paragraph 20 Area*

228. Complaint counsel argue that complaint paragraph 20 defines a relevant geographic market because other pipeline systems are not close enough to this area to prevent the exercise of market power by the five systems which transport gas produced in the area (HIOS, Stingray, Sea Robin, Texaco Eastern, Bluewater) (Tr. 1083, 1088). The following evidence is cited in support of this argument:

1. No blocks in the area have ever been connected to pipelines other than HIOS, Stingray, Sea Robin, Texas Eastern, or Bluewater or laterals connected to those systems (*see* CX's 123, 1118).

2. Documents assessing connection of blocks in the area do not discuss connections with systems outside of the area (F.'s 181-195).

3. A gap between the pipelines serving the paragraph 20 area and the closest ones outside the market which, they claim, is greater than the gaps among pipelines in the area (Tr. 1083-86, 1088, 1090-91, 1595; CX's 902, 1118A-B; RX 2004).

4. Some of the closer pipelines outside the area have diameters that are substantially smaller than pipelines in the area (TR. 1086-88; CX's 904, 1118A, 1681C). [50]

b. *The Eastern And Western Regions*

230. Two submarkets—the eastern and western regions—within the paragraph 20 area, are also proposed for the following reasons:

1. Gas produced in the eastern region is transported through Stingray, Sea Robin, Texas Eastern or Bluewater, and other pipeline systems are too far away to prevent these systems from exercising market power (Tr. 1094). The northern and eastern boundaries of the eastern region are the same as those of the paragraph 20 market (CX 1125). The southern boundary of the eastern region is further north than the southern boundary of the paragraph 20 market because, as one moves further south, the pipeline systems in the eastern region lose their comparative advantage over the systems in the western region (*see* Tr. 1095-96). In either case, there are no pipelines south of the southern boundary (*see* CX 903). To the west, the closest pipeline system is HIOS (Tr. 1093; *see* CX 904). HIOS is approximately 18 miles from the boundary of the eastern region at its closest point and further from points inside the eastern region and is not close enough to prevent the exercise of market power (*see* CX 904).

2. Gas produced in the western area is transported through one of four pipeline systems: HIOS, Stingray, Texas Eastern or the Bluewater project (Tr. 1095; CX 1109E-G). Other pipeline systems are too far away to prevent these pipeline systems from exercising market power (*see* Tr. 1091-94). The northern and western boundaries of the western region are the same as those of the paragraph 20 market (CX 1125). The southern boundary of the western region is further north than the southern boundary of the paragraph 20 market because, as one moves further south, the pipeline systems in the western region lose their comparative advantage over the systems in the eastern region (Tr. 1095-96). In either case, there are no pipelines south of the southern boundary (*see* CX 903). To the east, the closest pipeline

system is Sea Robin (*see* CX's 904, 1125). Sea Robin is approximately 16 miles from the boundary of the eastern region at its closest point and further from points inside the western region and it is not close enough to prevent the exercise of market power (Tr. 1094-95; CX's 904, 1125). [51]

3. Evidence that pipelines outside the paragraph 20 market have not transported gas from any blocks inside that area shows that such pipelines have not transported gas from any blocks in the eastern region and western region, and the fact that no blocks in the eastern region have been connected to HIOS or any blocks in the western region have been connected to Sea Robin (*see* CX's 325, 363, 904, 1008, 1113B-G).

*c. The Gulf of Mexico*

231. Although respondents agree that individual blocks in the OCS may be viewed as relevant geographic markets, they argue that complaint counsel have not established any areas broader than those blocks but smaller than the entire Gulf as relevant markets.

232. Supportive of respondents' claim is the fact that the industry does not view the alleged markets as having any significance for business purposes (Tr. 1471-73, 1915, 2378).

233. For example, gas sales representatives employed by natural gas producers often operate without regard to particular geographic sales areas (Tr. 1914-15). Pennzoil has one gas sales representative whose responsibility is the sale of gas throughout the entire Gulf (Tr. 700-01). Pennzoil has never divided the Gulf for purposes of gas sales into any areas smaller than all of offshore Texas or all of offshore Louisiana (Tr. 701). Shell's Natural Gas Department, is organized into three marketing groups according to geographic regions of the country (Tr. 823). These groups are the Eastern Marketing Group, the Western Marketing Group and the Central Marketing Group (Tr. 823). Each regional group sells gas to pipelines serving the corresponding geographic areas (Tr. 823). Each regional group is responsible for selling gas produced both offshore and onshore to the pipelines in its region (Tr. 823-24).

234. Gas buyers for natural gas pipeline companies frequently work on a project-by-project basis without regard to the geographic location of the gas (Tr. 1912-15). No gas supply representative at either Florida Gas or Mid-Louisiana Gas Company was responsible solely for purchases of offshore gas (Tr. 1914).

235. Other evidence which suggests, as Dr. Hall claims, that areas smaller than the entire Gulf of Mexico might not capture all the supply and demand forces affecting the transportation of natural gas (Tr. 2472-73) includes: **[52]**

1. Producers operate throughout the Gulf of Mexico and do not confine their exploration and production activities to any particular areas (F.'s 144-157).

2. Pipeline companies purchase gas throughout the Gulf (F.'s 129-142).

3. Gas purchase contracts entered into with producers by NGPL and UGPL that relate to gas fields in the alleged geographic markets have purchase price provisions pegged to prices paid for gas throughout the offshore and even nationwide (Tr. 1897-98; RX 2700A-Z-377).

4. Pipeline companies buy gas in the Gulf far from pipeline facilities that they own, and they rely on a web of transportation and exchange agreements between them to transport gas from the Gulf to delivery points and without regard to whether the gas is produced in or outside of the alleged geographic markets (F.'s 158-162).

236. Dr. Hall's theory would be acceptable if the issue in this case were the effect of the challenged acquisition on consumers of gas, but complaint counsel's injury scenario is much more modest. They claim only that the effect of the acquisition will increase transportation rates with respect to the connection of new blocks, and restrict access to pipelines, in the alleged relevant geographic markets, thus injuring producers by transferring wealth from them to the pipelines (CPF 9.62-9.63). Confining the issue to this narrow injury scenario, one does not need to consider all of the supply and demand forces in the transportation of natural gas from the wellhead to the end users. The real issue is: to which pipelines, as a practical matter, can producers of natural gas turn as alternatives for transportation of their gas?

## 6. Conclusion

237. After considering all of the evidence and the testimony of Drs. Uri and Hall, I agree with respondents that complaint counsel have not established that the paragraph 20 area, or its eastern and western divisions, are relevant geographic markets. **[53]**

238. All of the evidence leads to the conclusion, instead, that individual producing blocks are the areas where decisions affecting producers' shipments of natural gas will be made. Complaint counsel's pretrial brief, at 40, recognizes this fact:

[T]he potential for competition occurs in determining which pipeline will connect to a new block and transport the gas from the block under a relatively long term contract . . . . This case focuses on competition to obtain connections of new blocks.

Dr. Uri also testified to this effect:

We have talked previously about the nature of competition. The competition is not for existing blocks that are currently hooked up to a pipeline. Rather, competition occurs for new hookups (Tr. 1294-95).

239. It is true that in several blocks in the alleged geographic markets, and in the OCS in general, producers may turn to more than one pipeline for connections. It is equally true, however, that for many blocks in the alleged markets, only one pipeline affords a connection. In fact, CX 1105, on which complaint counsel rely, proves this point beyond dispute.

JUDGE PARKER: But out of these seven randomly selected blocks, five of them indicate that only HIOS was ever a potential competitor or a competitor, a possible outlet. So, in competing with nobody, it didn't merge with a competitor?

THE WITNESS (Dr. Uri): That's right . . . .

JUDGE PARKER: . . . So, if you multiply it to the universe, or something like 75 percent of the blocks, HIOS never competed with Stingray.

THE WITNESS: If you want to expand it out . . . . (Tr. 1257; *see also* Tr. 1431-35).

Dr. Uri had previously testified that CX 1105 was a representative sample of the unconnected blocks in the alleged markets (Tr. 1257).

[54]

240. Dr. Uri also identified some circumstances in which only one viable connection would exist:

Q: Do you agree with the statement in complaint counsel's pretrial brief, I believe found at page 48, to the effect that if a block has a relatively small quantity of reserves and is much closer to one pipeline than another, the closest pipeline may, in those circumstances, be the only viable option for connection?

A. I would agree with that, certainly (Tr. 1431).

241. Blocks that have no viable connection alternatives are obviously not areas of effective competition under complaint counsel's theory. The MidCon/United acquisition could have no impact in these blocks, as Dr. Uri conceded (Tr. 1256-57).

242. There are many instances in which blocks have no viable connection alternatives. For example, from 1978 through 1986, NGPL

prepared 75 gas supply evaluations that evaluated potential gas supplies in the offshore Gulf of Mexico (Tr. 2393, 2395, 2435; CX 52A-B; RX 2710). Six of the seventy-five offshore gas supply evaluations evaluated the same gas supply as another gas supply evaluation pertaining to the same field (Tr. 2389-93). Of the 69 substantially different gas supply evaluations performed by Natural for offshore gas supply sources from 1978 through 1986, 13 of the gas supplies evaluated were within the alleged geographic markets (Tr. 2273, 2436-37; CX 52A-B; RX 2710). Of these 69 substantially different gas supply evaluations, only eight considered more than one possible pipeline connection (Tr. 2435-37; CX 52A-B; RX 2710). Three of the eight evaluations which considered more than one pipeline connection involved different means of connection to the same major transmission system (Tr. 2273-74; CX's 1350A-C, 1378A-C, 1411; RX 2710).

243. None of NGPL's gas supply evaluations considered HIOS and Stingray and Sea Robin, or HIOS and Sea Robin as connection alternatives for any offshore block either inside or outside the alleged geographic markets (Tr. 2275, 2445-46; CX 52A-B; RX 2710).

244. Complaint counsel criticize the methodology of these evaluations and the inferences which can be drawn from them, as do respondents with respect to complaint counsel's analysis which reveals that in some cases, blocks in the alleged relevant geographic markets were or could be connected to different pipeline systems (F.'s 181-195). [55]

245. These analyses may have some problems but there can be no doubt that they confirm that which is evident: If two or more pipelines are equally near a producing or a potentially producing block, or if some other factor such as different transportation rates overcomes a difference in distance, they can compete for hookup to the block. The opposite is equally clear: In many cases, because only one pipeline is near enough to a block, only that pipeline is a viable connection to a particular block.

246. Indeed, as respondents emphasize, of the well over 100 blocks connected to a pipeline within the paragraph 20 area before the acquisition, complaint counsel have identified only 11 blocks for which HIOS, Stingray and Sea Robin, in some combination, were allegedly considered by some party as potential transportation substitutes. *See* CPF's 6.27-6.30, 6.34, 6.36-6.39, 6.41-6.42 (F.'s 181-184, 187, 189-192, 194-195). Thus, for 90 percent or more of the blocks connected

to a pipeline within the paragraph 20 area before the acquisition, complaint counsel do not even contend that HIOS, Stingray or Sea Robin were substitutes for each other. Of the 96 blocks within the alleged market that were actually connected to HIOS, Stingray or Sea Robin before the acquisition, complaint counsel only contend that three involved competition between or among these pipelines. See CPF's 6.28, 6.38, 6.42 (F.'s 182, 191, 195). The examples cited by complaint counsel from outside of the paragraph 20 area do not, of course, establish that HIOS, Stingray and Sea Robin actually competed within the paragraph 20 area (F.'s 197-222).

247. Despite this evidence, Dr. Uri's theory assumes that, within his markets, all blocks can be served by all of the pipelines which are included in his concentration charts.

248. This is clearly incorrect and leads to inconsistent conclusions as to the nature of competition in the three alleged relevant geographic markets. In the paragraph 20 area, the concentration charts (CPF 7.31, Tables I and II) conclude that HIOS, Stingray and Sea Robin are competitors. Yet, in the eastern region (which is a subsection of the paragraph 20 area) (CPF 7.32, Table III), HIOS is not treated as a competitor of Stingray and Sea Robin, while in the western region (which is also a subsection of the paragraph 20 area) (CPF 7.33, Tables IV, V, VI), Sea Robin is not treated as a competitor of HIOS and Stingray.

249. Complaint counsel do not explain why HIOS, Stingray and Sea Robin are treated as competitors in the broad paragraph 20 area, while HIOS and Sea Robin are excluded as competitors in, respectively, the eastern and western regions of the broad area.

250. This inconsistency not only destroys the validity of Dr. Uri's conclusions with respect to the paragraph 20 area, but also those with respect to the eastern and western areas, for it [56] is unquestioned that within these areas there are many blocks where all but one pipeline is too far away to be a viable connection possibility.<sup>4</sup>

251. To explain away these problems, Dr. Uri developed a "capacity

<sup>4</sup> The very reason why HIOS and Sea Robin are excluded, respectively, from the eastern and western regions of the paragraph 20 area:

See CPF 6.99-6.100: "Gas produced in the eastern region geographic market is transported through one of four pipeline systems: Stingray, Sea Robin, Texas Eastern or the Bluewater project. Other pipeline systems are too far away to prevent these systems from exercising market power . . . ."

"Gas produced in the western region geographic market is transported through one of four pipeline systems: HIOS, Stingray, Texas Eastern or the Bluewater project. Other pipeline systems are too far away to prevent these pipeline systems from exercising market power . . . ."

interaction" theory in support of his claim that the relevant geographic market could be broader than individual blocks. I reject this theory.

Q: So your testimony, then, you begin with an individual field as the area within which competition occurs, and then in some fashion build out from that by use of this capacity interaction notion, perhaps as far as the Gulf?

A: Well, the capacity interaction is not the exclusive consideration. It is one of the considerations.

Q: What other considerations would indicate that one ought to examine something larger than an individual field or block?

A: Well, if we're going to look at collusive behavior, it might be convenient to have a collusive arrangement that covers more than an individual field. So you're asking [57] what other factors might be relevant. Well, the convenience consideration is another factor.

Q: Are there any other factors?

A: None that come to mind right now (Tr. 1464-65).

252. Dr. Uri's theory, which is not supported by any record evidence, is that one pipeline's success or failure in competing against a second pipeline to connect a particular block could affect the first pipeline's competition with a third pipeline to connect some other block (Tr. 1465-66). Taken to its logical conclusion, this theory could support the claim that the entire Gulf of Mexico is the relevant geographic market (Tr. 1464).

253. Dr. Uri could give only one example of "capacity interaction" (Tr. 1595-97) and this involved an onshore interconnection (Tr. 1595-97; CX 808B), well outside the alleged relevant geographic markets.

254. Dr. Uri's theory that it would be more "convenient" to have a conspiracy among pipelines in the alleged markets as opposed to the entire Gulf does not prove that his markets exist.

255. Finally, Dr. Uri includes in the paragraph 20 market, a part of the Garden Banks area in the deep water of the Gulf of Mexico where no pipelines exist (Tr. 1716; RX 2004), and where there is no natural gas production (Tr. 692). Dr. Uri testified:

Q: Wouldn't it therefore be really just a matter of speculation as to when pipelines might be built in that area?

A: Well, it's a matter of speculation to the extent we don't really know what's going to happen in the natural gas market in the future. I've spent a lot of time in the forecasting business when I was at the Department of Energy and, based on my experience there, there's an awful lot of uncertainty.

And so, given the attendant uncertainty with regard to the future of the natural gas market, there will be considerable uncertainty attendant with the development in that area. [58]

Q: Given that uncertainty about the natural gas market, then it's possible that no pipelines will be built in the Garden Banks for five or ten years? Is that possible?

A: It's possible that a sustained period might occur before pipelines are built into that area (Tr. 1469-70).

256. Dr. Uri admitted that in these circumstances the Garden Banks area was not an area in which competition presently exists:

Q: Is it fair to characterize the Garden Banks, then, as a potential future market, but not a present market, for the sort of competition you've analyzed for purposes of this case?

A: With regard to the kind of competition I considered, that's a fair characterization (Tr. 1468).

257. After analyzing all of the evidence relevant to the issue,<sup>5</sup> I conclude that complaint counsel have not established that the paragraph 20 area or the eastern and western regions of that area are relevant geographic markets. I also reject respondents' claim that the Gulf of Mexico is a relevant geographic market.

258. Complaint counsel, respondents and I agree that individual blocks are relevant geographic markets, but complaint counsel's argument that the acquisition will substantially lessen competition (CPF's 7.01-7.68) does not, except for unsupported claims,<sup>6</sup> rely on injury to competition as to individual blocks; [59] instead, complaint counsel's concentration charts in their proposed findings relating to the open access (Tables I-VI) and closed access scenarios (Tables VII-XII) rely on the theory that the paragraph 20 area and its eastern and western regions are relevant geographic markets. Since I reject these proposed markets, I necessarily must reject, as irrelevant, all proposed findings relating to concentration and the competitive effects of the acquisition under both scenarios (CPF 7.01-9.68).

### III. CONCLUSIONS OF LAW

#### A. *The Relevant Product Market*

Under Section 7 of the Clayton Act, a product market is defined "by the reasonable interchangeability of use or the cross-elasticity of demand between the product in question and products which are reasonable substitutes for it." *United States v. Continental Can Co.*,

<sup>5</sup> Including statements of some industry members that pipelines compete which I do not find significant since they do not relate to the alleged relevant geographic markets proposed by complaint counsel. Furthermore, Dr. Uri testified that he was unaware of any instance where HIOS, Stingray or Sea Robin set transportation rates in reaction to each other's rates (Tr. 1531). Ordinarily, one would expect this to occur if these pipelines were competitors (Tr. 1532).

<sup>6</sup> CPF 7.38 argues that "the acquisition is likely to lead to a merger to monopoly for some blocks" but does not identify those blocks.

378 U.S. 441, 449 (1964). On the supply side one considers whether producers of other products or services can readily switch facilities to the product or service in question. If so, then those producers must be included in the market. See *Brown Shoe Co. v. United States*, 370 U.S. 294 (1962); *Coca-Cola Bottling Co. of New York, Inc.*, 93 FTC 110, 204-05 (1979).

The evidence reveals that, despite some differences in quality or pressure characteristics, pipelines compete with one another in transporting gas from the OCS to the burner tip (F.'s 52-55). Furthermore, since there are no substitutes for pipelines, the only feasible method of transporting gas from the OCS to the end-users is the pipeline. Finally, oil pipelines are not a practical alternative for transporting gas out of the OCS to end-users (F. 163).

The only disputed issue on this point is the extent of the product market: whether, as complaint counsel claim, it is for the transportation of gas from producing fields or, as claimed by respondents, it extends from the OCS to the city-gate or burner tip.

Respondents are correct that the demand for the product—the transportation of natural gas—is derived from the demand for gas at the city-gate or burner tip. No customer of a pipeline or OCS producer is concerned with transportation only from the OCS to onshore, for consumers exist far beyond that point, and it is their demand which the pipelines exist to satisfy (F. 165).

Thus, the overall product market is the transportation of gas from the wellhead to the city-gate or burner tip, but a submarket also exists, *i.e.*, the transportation of gas from [60] producing blocks in the OCS (F. 166). See Hansen, *U.S. Oil Pipeline Markets*, 39-40 (1983). Referring to the oil pipelines, Hansen states:

Another difficulty lies in the definition of the relevant product. Very little consideration has been given to the definition of the product offered by oil pipeline companies, generally it reflects transportation services of crude oil 'between given producing areas and given refining areas.' It is occasionally noted, for example, that there are at least eighteen possible products pipeline routes between St. James, Louisiana, and Toledo, Ohio, implying that this might be a relevant market (transportation services over this distance being the relevant product). Yet, upon reflection, it seems unlikely that consumers in Toledo would care much about whether they received petroleum products from refineries in Louisiana or in Michigan. With few exceptions the origin of petroleum products is irrelevant to the consumer. We may conclude, therefore, that products shipped by pipeline from the gulf to Toledo compete with products shipped by pipeline from Chicago as well as with products from local

Toledo refineries. Realistically, there are at least two different products in two different markets being offered by a pipeline connecting the gulf coast with Toledo.

First, the pipeline offers a service that might be called 'a means of getting the petroleum out of the gulf coast area.' In this market the pipeline competes with other pipelines that carry the same products from the gulf coast whether they are going to Toledo or to some other market. Second, the pipeline offers a product that might be called 'a means of getting petroleum to Toledo.' In this market the pipeline competes with all other carriers that ship the same product to Toledo whether the shipments originate in the gulf or some other area (including products refined in Toledo).

Thus, in both crude oil and petroleum products pipelines there are four different types of markets: the markets where crude pipelines gather oil from producers, the markets where crude pipelines distribute oil [61] to refineries, the markets where products pipelines gather petroleum products from refiners, and the markets where products pipelines deliver products to distributors.

In any event, the dispute between the parties is of little practical significance, for the issue of controlling importance is the relevant geographic market, for if complaint counsel's claimed geographic markets do not exist, then whatever the product market may be, they cannot argue that the acquisition will lessen competition.

#### *B. The Relevant Geographic Market*

The purpose of defining a geographic market in a Section 7 proceeding is:

. . . [T]o establish a geographic boundary that roughly separates firms that are important factors in the competitive analysis of a merger from those that are not.

*DOJ Merger Guidelines*, § 2.31, 2 CCH Trade Reg. Rep. ¶ 4,492 at 6,879-10 to 11.

Respondents correctly point out that before one can define the relevant geographic market, one must determine what competitive activity might be suppressed by the challenged acquisition (Respondents' Post Trial Brief, at 32). Respondents argue that the competitive activity in this case which might be suppressed is the transportation of gas from points of production to points of consumption. If this is true, then Dr. Hall's theory that the relevant geographic market extends at least throughout the Gulf is correct, for competitive activity of this kind exists throughout the Gulf (F. 128).

However, complaint counsel take a much narrower view of the nature of competition in this case, and since they have the burden of establishing the relevant market, their claim as to the validity of that

market (or markets) must be tested in light of their definition of competition—the substitutability of pipelines to connect new reserves.

The test which should be applied to determine the commercial reality of complaint counsel's geographic market is simple: "Where, as a practical matter, can the purchaser turn for alternatives." *FTC v. Food Town Stores, Inc.*, 539 F.2d 1339, 1344 (4th Cir. 1976). [62]

In this case, the purchasers are future producers of natural gas in individual blocks within the alleged relevant geographic markets (F. 238). According to complaint counsel, the five pipelines in the paragraph 20 area or, alternatively, the four pipelines in the eastern and western regions are the suppliers of services to which the producers may turn for transportation from individual blocks.

Although some reference to individual blocks as relevant geographic markets is made in their proposed findings, complaint counsel's theory of competitive injury relies on their charts depicting concentration increases in the paragraph 20 area and its eastern and western regions (F. 258), and it is the validity of their choice of these areas as relevant geographic markets which must be tested.

The basic assumption of the concentration charts is that extrapolating from the few instances where there was competition for hookups, competition for new hookups will occur among all of the pipelines throughout the selected areas and that undeveloped blocks in the selected areas are potentially commercially productive. Complaint counsel have not satisfied me that this is true; in fact, their claim is refuted by the construction history of HIOS, Stingray, and Sea Robin. Given the enormous construction costs of these pipelines, it would have been folly to place them so that they would serve the same blocks, and FERC avoided inefficient duplication of pipeline services when it authorized their construction (F.'s 73-74, 118). Thus, there is little doubt that if these pipelines are extended into the Garden Banks area (F.'s 255-256), FERC will not authorize them to serve the same blocks and they will not be competitors.

Despite FERC's philosophy, in some cases within the alleged geographic markets, producers have been able to choose among different pipelines for connection (F.'s 181-195) but there were many instances where only one pipeline was a feasible connection possibility (F.'s 242-243, 246) and Dr. Uri conceded that in these cases these blocks were not areas of effective competition (F.'s 239-241).

In fact, analysis reveals that in the vast majority of cases involving connections made in the paragraph 20 area, HIOS, Stingray and Sea Robin were not considered as alternatives (F. 246).

Furthermore, complaint counsel's claim that five pipelines, including HIOS, Stingray and Sea Robin, compete within the paragraph 20 area is belied by their contradictory claims that in the eastern region of this area, HIOS is not a competitor, while in the western region, Sea Robin is not a competitor (F. 248).

The reason given by complaint counsel for their exclusion of HIOS and Sea Robin is that they are too far away to prevent pipelines which are competitors from exercising market power [63] (F. 250), but this is precisely the reason why I find that the markets selected by complaint counsel do not reflect commercial reality, and that, given complaint counsel's theory of competition, only the individual OCS blocks are relevant geographic markets.

Complaint counsel also point to the fact that blocks in the paragraph 20 area are not connected to pipelines outside the area (F. 228), but this is true with respect to pipelines in the area, as complaint counsel concede when they argue that HIOS and Sea Robin do not compete in the eastern and western regions.

Dr. Uri's "capacity interaction" theory was apparently designed to avoid problems presented by the fact that many OCS blocks have only one connection possibility, but if I were to accept it, there is no reason why it could not justify the inclusion of all blocks in the OCS as the relevant geographic market (F.'s 251-252). In fact, this theory seems to be similar to respondents' which posits a Gulf-wide relevant geographic market because of the web of commercial relationships between producers and pipelines in that area (F.'s 128-161).

Other indications that the geographic markets proposed by complaint counsel are artificial are the lack of industry recognition of them as relevant markets (F.'s 232-234), see *Brown Shoe Co. v. United States*, 370 U.S. 294, 326 (1962), and the absence of any evidence of significant price competition between Stingray, HIOS and Sea Robin within the alleged markets (F. 257, n. 5). Generalized statements by FERC (F.'s 90-94) and industry members about pipeline competition do not establish the validity of complaint counsel's proposed markets, for those statements refer to overall competition for the consumer's business from the producing fields to the burner tip.

While the DOJ Merger Guidelines require only that the proponent of a relevant geographic market establish that it "roughly" separates competing firms from non-competing ones, the market must be measurable in other than hypothetical terms. *Consul, Ltd. v. Transco*

*Energy Co.*, 1986-2 CCH Trade Cas. ¶ 67,347 (4th Cir. 1985), and it must "correspond to the commercial realities of the industry and be economically significant." *Brown Shoe Co. v. United States*, 370 U.S. 294, 336-37 (1962). Complaint counsel's proof does not satisfy these standards.

Since complaint counsel have failed to meet the burden of proving that the relevant geographic markets which support their claim of probable injury to producers of natural gas exist, I reject their proposed findings relating to the effects of the acquisition, and find that they have failed to establish that the acquisition may substantially lessen competition for the transportation of natural gas out of the producing basins and fields in certain areas of the OCS off the coasts of Texas and Louisiana. Therefore, [64]

#### IV. ORDER

*It is ordered*, That the complaint be, and it hereby is, dismissed.

#### OPINION OF THE COMMISSION

BY CALVANI, *Commissioner*:

##### I. INTRODUCTION

##### A. *Procedural History*

MidCon Corp. ("MidCon") acquired United Energy Resources, Inc. ("United") through a cash tender offer in 1985. The Commission's complaint, issued September 19, 1985, charges that this acquisition may substantially reduce competition in the transportation of natural gas out of producing fields and basins in certain areas of the Gulf of Mexico Outer Continental Shelf ("OCS"),<sup>1</sup> in violation of Section 7 of the Clayton Act and Section 5 of the Federal Trade Commission Act. The administrative trial began November 4, 1986 and concluded February 26, 1987.<sup>2</sup> The record was closed on November 27, 1987, and after briefing, Administrative Law Judge Lewis Parker issued an initial decision February 2, 1988, dismissing the complaint. Complaint counsel has appealed. For the reasons described below, the complaint is dismissed.

<sup>1</sup> The second count of the complaint, charging that the acquisition also produced anticompetitive effects in onshore natural gas transportation and sale, was settled by a consent order at the same time the complaint was issued. *Midcon Corp.*, 107 FTC 48 (1986).

<sup>2</sup> After MidCon sold United LaSalle Energy Corporation on June 30, 1987, MidCon moved to dismiss the complaint. The Commission denied that motion on November 16, 1987.

### B. Summary of Facts

MidCon and United transport and sell natural gas. Each, through subsidiaries, has interests in pipelines that transport gas from producing platforms in the OCS to the shore. The OCS pipelines at issue here are High Island Offshore System ("HIOS"), U-T Offshore System ("UTOS"), Stingray Pipeline Co., and Sea Robin Pipeline Co. These pipelines are highlighted on the map attached to this [2] opinion.<sup>3</sup> The interests in these lines of MidCon, United, and their other owners are summarized in the following table, which shows the owners' percent shares and identifies the pipeline's operator.

Owner	Share of Ownership or Control			
	HIOS	UTOS	Stingray	Sea Robin
MidCon	20	33 $\frac{1}{3}$	50	
United	20	33 $\frac{1}{3}$		50*
Transco	20	33 $\frac{1}{3}$		
Texas Gas	20			
ANR	20*			
Trunkline			50*	
Southern Natural				50

\*Operator of pipeline

Thus, the acquisition gave MidCon a 40 percent interest in HIOS, 50 percent in Stingray, 50 percent in Sea Robin, and 66 $\frac{2}{3}$  percent in UTOS, which is functionally an extension of HIOS.

These OCS pipelines transport gas from producing fields in the Gulf to onshore points of connection with other pipelines. The OCS pipelines are "trunklines", connected to the gas production platforms by smaller diameter pipes called "laterals". The producing platforms are located in "blocks" of the OCS, areas usually three miles square defined by the Department of the Interior for assigning mineral leases. Gas producers bid for these leases, which convey the right to explore for gas and, if exploration is successful, to produce the gas and sell it. During the five- to ten-year period during which the winning bidder has the right to explore, before actual production begins, the lease is said to be in its "primary term". A lease will be extended indefinitely once production starts.

HIOS, Stingray, UTOS, and Sea Robin are joint ventures (although some OCS pipelines are not). For each, the management, operation,

<sup>3</sup> Derived from CAB, Appendix A, Map 3.

and owners' rights are controlled by the terms of a joint venture agreement. On some joint venture pipelines, although not any of these four, each owner has the right to use its share of the capacity independently, so that, to the extent of that share, each owner acts as an independent competitor. On others, the pipeline is run as a single venture, with the owners acting together to manage it. For each of the joint venture pipelines at issue here, there is a management committee whose members are nominated by the owners in proportion to ownership shares. Although substantial management authority is delegated to the pipeline's operator, a majority vote of the managing committee is required for decisions concerning expansion and rate changes. Thus, for HIOS, with no owner controlling a share over 40 percent, no single owner can control or veto decisions. For Stingray and Sea Robin, each of the 50-percent owners has an effective veto over those decisions that require majority votes.

The theory of complaint counsel's case is that this acquisition, by adding veto power over decisions by Sea Robin to MidCon's existing veto power over decisions by Stingray and by increasing MidCon's influence in HIOS (and UTOS), may substantially lessen competition among these pipelines [3] and others for connecting new gas supplies. Complaint counsel's analysis presumes that the acquisition amounted to a merger of these lines.<sup>4</sup>

The principal issue on appeal is the proof of the relevant geographic market. The complaint alleges that four areas of the Gulf of Mexico, defined by terms used in describing lease blocks, and "any relevant submarket" of any of these four areas are relevant "sections of the country". Complaint counsel elected to focus the case on the area described in Paragraph 20 of the complaint (slightly modified) and smaller areas within it called the "western" and "eastern" regions.<sup>5</sup> The Paragraph 20 region, which covers several thousand square miles of the Gulf, begins about 60 miles offshore and extends out over the continental shelf and beyond, south of the Louisiana-Texas state line. The western region and eastern region are, roughly, the Paragraph 20 region's northwestern and northeastern quadrants. These regions are highlighted on the map attached to this opinion. Stingray extends into the center of the Paragraph 20 region, HIOS enters it from the west, and Sea Robin enters it from the east. UTOS does not itself reach this

<sup>4</sup> See CAB p. 19, CRB pp. 35-44.

<sup>5</sup> The areas defined in Paragraphs 17-19 of the complaint were abandoned and dismissed with prejudice. See record, p. 1385. The Paragraph 20 market is essentially the same as that described in Paragraph 17 plus two areas to the south of it.

region, but it connects HIOS to the shore. In addition to these large regions, complaint counsel also contends (and MidCon agrees, in principle) that individual blocks could be relevant geographic markets.

Judge Parker found that complaint counsel had failed to prove that the Paragraph 20 regions were relevant geographic markets, and that, although individual blocks could in principle be relevant markets, complaint counsel had not carried its burden of proving those markets.<sup>6</sup> We agree with [4] Judge Parker that complaint counsel failed to show that there was a substantial likelihood of anticompetitive effects in a section of the country.

## II. PRODUCT MARKET

### A. *Natural Gas Transportation*

Traditionally, interstate pipelines bought gas from producers at or near the wellhead, transported it across the country, and then resold it to local distribution companies ("LDCs") or large industrial consumers. Natural gas transportation was thus only one of a pipeline company's internal operations. Since the onset of deregulation, it is increasingly common for LDCs, industrial consumers, and companies that simply market gas to purchase gas directly from producers and then arrange for pipelines to transport it for them. Thus the transportation function is becoming identifiably separate from the business of buying and selling gas. Judge Parker found, and we agree, that transportation of natural gas from wellhead to the burner tip is a market.<sup>7</sup>

A relevant product market, within the broadly conceived market for natural gas transportation, is transportation from producing areas. The complaint alleges that a relevant line of commerce is the

<sup>6</sup> On appeal, complaint counsel alleges that Judge Parker made the following errors:

1. Finding that complaint counsel had failed to show how concentration would increase and competition decline in individual block markets.
2. Finding that a region (such as the Paragraph 20 region and the western and eastern regions within it) could not be a geographic market unless each competitor in it could compete with each other competitor in every part of the region.
3. Misunderstanding the extent of interpipeline competition and ignoring changing conditions favoring increased competition in the future.
4. Failing to make findings on concentration and other factors.

Rather than address the issues in the particular order of complaint counsel's stated issues on appeal, we set out here our own views on the geographic market questions, the nature of industry competition and the need for specific findings about concentration and other factors affecting competition.

<sup>7</sup> ID p. 59.

transportation of natural gas from producing fields and basins.<sup>8</sup> Judge Parker found that this term described a separate stage or transaction at which market power might be exercised.<sup>9</sup> That finding is supported in the record. Even MidCon's economic expert, although arguing in this case for a broad market, previously testified in another case that this separate stage of transportation was itself a relevant market.<sup>10</sup> For the purpose of this appeal, neither complaint counsel nor respondents dispute Judge Parker's finding that transportation from producing areas is a relevant product market.

### B. Regulation and Competition

Natural gas transportation has historically been highly regulated, first by the Federal Power Commission and now by its successor, the Federal Energy Regulatory Commission ("FERC"). FERC approval is required to construct new interstate pipeline facilities and again to abandon them. FERC regulates the prices pipelines charge for gas sold to LDCs (but not for direct sales to industrial users or sales by pipeline marketing affiliates), and regulates transportation rates pipelines may charge other shippers. For many years, FERC regulated wellhead natural gas prices.

But the industry's record of close regulation does not portend a future without meaningful competition. Over the last ten years, the industry has been evolving toward greater reliance on the forces of competition, led by initiatives from Congress and FERC. The Natural Gas Policy Act of [5] 1978<sup>11</sup> started decontrolling prices. FERC in 1985 adopted Order 436,<sup>12</sup> permitting pipelines to become "open access" transporters, free to engage in many transactions without specific prior FERC approval. Order 436 permits rate structures with maximum and minimum rate levels within which the pipeline may set prices to individual customers. FERC has announced that Order 436 is intended to encourage price discounts in response to competition.<sup>13</sup> After the court's ruling on appeal of Order 436,<sup>14</sup> FERC modified

<sup>8</sup> Complaint, 16.

<sup>9</sup> ID p. 38, 166, and p. 59-61.

<sup>10</sup> Id 166, citing Tr. 2613-17.

<sup>11</sup> 15 U.S.C. 3301-3432.

<sup>12</sup> FERC Order No. 436, Docket No. RM85-1-000, 50 Fed. Reg. 42,408; see CX 1013, CX 1014, CX 1016, CX 1017.

<sup>13</sup> Under Order 436, a pipeline's maximum rate is based on total costs, and the minimum rate is based on variable costs. One witness gave an example of the range of an Order 436 pipeline transportation rate, from \$.15 to \$1.00 Tr. 620-21.

<sup>14</sup> *Associated Gas Distributors v. FERC*, 824 F.2d 981 (D.C. Cir. 1987).

some of the Order's details, but reaffirmed its basic purpose.<sup>15</sup> The industry is recognizing and adapting to these new competitive realities. Sea Robin has already become an open access pipeline under Order 436, as have two of the respondents' major pipeline subsidiaries, Natural Gas Pipeline Company of America and United Gas Pipe Line Company. FERC has now decided that all OCS pipelines should be open access pipelines subject to Orders 436 and 500, and has ordered HIOS, Stingray and UTOS (as well as others) to take necessary steps to do so.<sup>16</sup>

In examining this market's likely future, we assume that the changes in regulatory attitude at FERC, as reflected in Order 436, will persist. The initial decision recognizes,<sup>17</sup> and we agree, that FERC is unlikely to reverse its pro-competitive direction. Basing analysis on the new environment, rather than the environment in which many of the events described on the record took place, would be consistent with the Commission's general approach to post-acquisition evidence. For one thing, the changes in regulatory climate are not post-acquisition events. The move toward greater reliance on market forces in the transportation of natural gas began many years before this acquisition, and one of FERC's most significant changes in transportation regulation, Order 436, coincided with it. The Order 436 rulemaking process began in December, 1984, the detailed proposal was put out for comment in May, 1985, and the order, issued on October 9, 1985, became effective in October and November, 1985.<sup>18</sup> Meanwhile, the premerger filing for this acquisition was made August 13, 1985, and MidCon acquired a majority of United's shares by the end of September, but MidCon did not complete the acquisition until December, after Order 436 had become effective.<sup>19</sup> In addition, even if the regulatory changes had post-dated the acquisition, post-acquisition changes [6] in competitive conditions brought about by changes in law can be considered in analyzing an acquisition's likely effects. *American Medical International*, 104 FTC 1, 212 (1984). The government's announcement of new laws and regulations, and the market's response, are not the kinds of exculpatory self-help by respondents under investigation of which the Commission and the courts have long been skeptical. See *United States v. General*

<sup>15</sup> FERC Order No. 500, 52 Fed. Reg. 30,334.

<sup>16</sup> FERC Order No. 509, 53 Fed. Reg. 50,925 (December 19, 1988). The Commission grants MidCon's January 6, 1989 motion, which complaint counsel does not oppose, to take official notice of this FERC decision.

<sup>17</sup> ID 226; see also ID 90-94.

<sup>18</sup> CX 1013, CX 1014.

<sup>19</sup> RPF 41.

*Dynamics Corp.*, 415 U.S. 486, 504-05 (1974); *Hospital Corp. of America*, 106 FTC 361, 473 n. 10 (1985), *aff'd*, 807 F.2d 1381 (7th Cir. 1986), *cert. denied*,—U.S.—(1987).

*C. Focus of Competition: Transporting New Supplies*

In the market for transportation from producing areas, the competition is to connect new sources of production rather than to divert existing production away from current transportation outlets. Transportation contracts in the OCS are usually long-term and the physical facilities that transport natural gas are expensive and immobile. FERC policy would discourage building a new pipeline to transport gas already being transported by another pipeline, at least if that gas had been part of the basis for granting the old pipeline's original certificate.<sup>20</sup> There is no evidence of a producer cutting off a block's connection to one pipeline in order to connect it to another pipeline. This is not to say that it could never happen. Supply contracts for these pipelines, entered during the era of tight regulation, are still in their initial term; what will happen when they expire in a new, more competitive environment is unknown. But even if past trends continue, so that a producer will not change a block's connection from one pipeline to another, there is substantial evidence that producers already can and do choose between different pipelines in deciding how to connect a block that is beginning production.

Respondents are wrong in asserting that there is little inter-pipeline competition for new supplies. Instead, there is ample evidence that developers of new sources can and do choose among alternative pipelines.<sup>21</sup> That a producer ultimately chose one of the alternatives as best does not necessarily mean that the others were "noncompetitive". In addition to the basic transportation rate, criteria for deciding which pipeline to choose include factors such as the cost of building a lateral (which is usually proportional to distance), and contract terms such as contract demand requirements, receipt points, and others. A customer may prefer to connect to a pipeline that can deliver most directly to the customer's ultimate consuming location. Choices are different at different locations, and for some locations realistic possibilities may be limited, perhaps to only one. But there are enough opportunities for competition to reject the argument that competition

<sup>20</sup> See *Id* 72-76. The FERC decisions described in this record were made ten or fifteen years ago, when these pipelines were originally approved. The record is silent about how FERC would now treat such an application, especially if the construction costs of the existing pipeline had already been recovered.

<sup>21</sup> *Id* 180-222.

is an aberration, a geographic accident that misrepresents the true nature of the marketplace. Moreover, there is likely to be additional new production in the future for which there will be competition for transportation service. Exploration and development of potential new gas supplies in the Gulf of Mexico continues. [7] The pipelines expect that new supplies will be developed in the future<sup>22</sup> and that they will be competitors for connecting new supplies.

### III. GEOGRAPHIC MARKET

Geographic market definition identifies the suppliers to consider in predicting competitive effects. The goal is to “roughly separate [ ] the firms that are important factors in the competitive analysis” from those that are not.<sup>23</sup> But where it is difficult to distinguish or identify who is in and who is out of the market, it will be difficult to predict competitive effects confidently.<sup>24</sup>

#### A. Range of Service

A threshold issue in defining a geographic market is how close a trunkline must be to a production platform to provide it with transportation service. The question in geographic market analysis is, “Where, as a practical matter, can the purchaser turn for alternatives?” *FTC v. Food Town Stores*, 539 F.2d 1339, 1344 (4th Cir. 1976). Here that question implies another: How far is practical? How long a lateral can be depends on how the cost of building and operating it compares to the expected revenues and profits from selling the gas it will carry. In general, the larger the reserves under a block, the longer and more expensive the lateral to it can be. There is evidence roughly quantifying the relationship between reserve size and lateral length. The estimates vary, from 4 Bcf (billion cubic feet)

<sup>22</sup> See ID 26-33.

<sup>23</sup> Department of Justice, Merger Guidelines, 2.31 (June 14, 1984) (“DOJ Guidelines”). The DOJ Guidelines characterize an area as a market if firms in the area could impose a “small but significant and nontransitory” price increase without losing significant sales to firms in other areas.

<sup>24</sup> The discussion assumes that “blocks” in the OCS are “customers”, an assumption that is not strictly correct. Producing wells are located at places conveniently designated by their block “addresses”. But the customer looking for transportation service may not be the lessee producer. MidCon argues that a customer—a production company, an interstate pipeline, an LDC, or an end user—may have interests (of different kinds) in production from several different locations, so that focusing on individual blocks misses competitively important relationships. Complaint Counsel simplifies its case by treating each OCS lease block as a distinct customer, thus assuming that, no matter what the other commercial interests of the firm with rights to that block’s gas, the demand for transportation at that block is independent of transactions at or affecting fields under other blocks. This simplification is consistent with complaint counsel’s theory of anticompetitive effect, which is concerned about anticompetitive reductions in wellhead prices (and thus reductions in the incentive to discover more gas). See ID 236.

of gas reserves per mile of lateral up to 10 Bcf per mile, with most around the middle of this range, at 7-8 Bcf per mile.<sup>25</sup> At that 7-8 Bcf per mile rate, a producing field containing about 75 Bcf of gas reserves (typical of those already discovered and connected in [8] the OCS) could justify building a lateral about ten miles long. Using the higher and lower rates would imply feasible laterals for such a field from 7 to nearly 20 miles long. A larger field could justify a longer lateral. These rough approximations are consistent with observed practice; there are a number of laterals from 10 to 15 miles long, and some even longer.<sup>26</sup> The assumption used by complaint counsel's expert, that pipelines within a range of 10 to 15 miles from a location could be competitive (all other things being equal), is supported in this record.

MidCon's argument that the feasible lateral length is so short that for any producing well or block there is usually only a single feasible trunkline connection—that, therefore, competition is essentially impossible—is rejected. MidCon's claim is a generalization from the lengths of existing laterals. These include the laterals to the blocks connected when the trunklines were first built, which may be "unusually" short because the trunklines were located in part to serve these blocks and presumably to minimize the costs of connecting them. Thus the lengths of all existing laterals may imply little about the feasible length of laterals connecting new producing wells or blocks to an existing pipeline. The most useful estimate of relevant lateral length might have been the "average" length of laterals constructed to connect new supplies to existing lines. A systematic estimate of this average was apparently not done, but the record cites many examples of laterals to newly connected blocks that are 10 to over 20 miles long.<sup>27</sup> The existence of these longer laterals supports the conclusion that a large enough new supply of gas might have many possible pipeline options—depending on just where it is.

#### B. *The Entire Gulf As a Market*

If we assume that geographic price discrimination is not possible, the entire Gulf of Mexico appears to be the smallest relevant geographic market. This conclusion follows from an analysis of supply

<sup>25</sup> See CPF 6.09. Judge Parker evidently rejected this proposed finding, without explanation. See ID p. 3. But it is supported by the exhibits in the record, respondents did not object to it, and Judge Parker's findings that there are laterals ten and even twenty miles long, ID 171, are consistent with it.

<sup>26</sup> ID 171-72.

<sup>27</sup> ID 171 identifies laterals to new blocks ranging from 10 to 27 miles long.

elasticity similar to that set out in the DOJ Guidelines. Begin where the respondents' pipelines can supply transportation service. Those locations would include each point along the pipelines' length at which gas supplies could be connected, plus the area on either side of the pipeline swept out by the length of a feasible lateral. Because of the pipelines' extension across the Gulf, and because of their owners' interests in other lines, the initial region identified is likely to extend through a large part of the Gulf.<sup>28</sup> Next hypothesize a monopolist trying to impose a non-transitory, [9] uniform price increase along the length of each of its pipelines.<sup>29</sup> Can the customer turn to suppliers elsewhere in response to that increase? The pipelines and the producing platforms are stationary; they cannot literally move themselves. But, can existing pipelines build laterals, or can new pipelines be built, into the region from elsewhere?<sup>30</sup> If so, expand the region to include the additional locations and repeat the process, ending only when no feasible outside source is found.

A customer seeking to connect a new well located equidistant from the hypothetical monopolist's location(s) and another pipeline at a different location could presumably choose either.<sup>31</sup> An equidistant, or crossing, pipeline, by not going along with the monopolist's price increase, could prevent the monopolist from raising the price. If the monopolist does not price discriminate and therefore the increase must be uniform for the entire pipeline, blocking the increase at one point means blocking it for the entire pipeline. The entire length of both pipelines must then be included in the market. Because the interlock-

<sup>28</sup> Lines in which Midcon had an interest before the acquisition (HIOS, UTOS and Stingray) reach regions extending from High Island South Addition in the west to the Vermilion region in the east, and from a point on the shore in the West Cameron region to the Garden Banks—roughly, a triangle 90 miles on a side. Lines in which United had an interest before the acquisition (HIOS, UTOS and Sea Robin, and UGPL itself) stretch even farther, over a trapezoidal area from High Island South Addition in the west to the Ship Shoal and Eugene Island South Addition regions on the east, a distance of roughly 130 miles, and from the Garden Banks to a 90 mile stretch of the shore extending from the West Cameron region to the Eugene Island region. Lines owned by the other partners in the lines in which Midcon or United had interests are found in virtually every region of the Gulf from southern Texas (Transeo) to the mouth of the Mississippi (Southern Natural).

<sup>29</sup> This could take the form of a change in base price or a uniform change in pricing policy. A pipeline's basic transportation rate may either be uniform at every point along the pipeline ("postage stamp") or vary based on mileage; thus, it is possible to conceive a uniform increase in that rate, affecting every customer. However, other provisions of supply contracts might differ between particular connections, resulting in different effective prices. To avoid complications based on such circumstances, a proxy for a uniform price increase might be a system-wide surcharge or elimination of discounts.

<sup>30</sup> A customer might be able to get equivalent value or service elsewhere, but this is not an option if the goal is to transport gas from a specific producing well. But possibility not developed in the initial decision is that a customer could shift production to a different part of the Gulf where the pipeline rates are better, all other things being equal. Complaint counsel did not address this, because its "modest" competitive effects claims were limited to effects on netbacks and drilling incentives; thus, the concern indeed was moving particular physical parcels of gas.

<sup>31</sup> ID 245.

ing network of pipelines extends across the Gulf, when we posit a uniform price increase, the market could not be limited to any smaller region.

*C. Paragraph 20 Regions As Markets*

If we assume the possibility of geographic price discrimination, relevant geographic markets smaller than the entire Gulf of Mexico are possible. Regions such as the Paragraph 20 area, the "eastern" and "western" regions within it, or other collections of blocks—even perhaps individual blocks—could be relevant geographic markets. To the extent that a region is geographically isolated from other pipelines, no transportation alternatives would exist to defeat a hypothetical increase in transportation rates within the region. There are some examples in this record of areas so isolated that a single pipeline may be the only feasible transportation available. For example, producing blocks in the southwestern corner of the High Island, South Addition area are more than 50 miles from any pipeline except HIOS.

For the paragraph 20 region (or its eastern or western regions) to be a relevant geographic market under this analysis, the pipelines that serve it must have the power to set prices within the region independently of the prices they set outside it, without fear of competition from other [10] pipelines that do not now serve the region. Because basic transportation rates for these pipelines are uniform for their entire length, outside these regions as well as inside them, differences in pricing would have to be accomplished by differences in discounts or other terms.

The Administrative Law Judge decided that the Paragraph 20 area could not be a relevant geographic market on the theory that the pipelines in the area do not compete.<sup>32</sup> In his view, "FERC avoided inefficient duplication of pipeline services when it authorized their construction," and FERC will not authorize the pipelines to compete with respect to any extensions to unconnected reservoirs of gas.<sup>33</sup> We disagree. Although FERC may have authorized the pipelines to serve different gas reserves, in fact the pipelines in the Paragraph 20 area are located so that they are transportation alternatives for some producing blocks. The pipelines are located close to one another, Stingray, Sea Robin, Bluewater and Texas Eastern intersect at

<sup>32</sup> I.D. at 61-62.

<sup>33</sup> I.D. at 62.

several points and HIOS and Stingray are connected at one point to facilitate shipments through either of them. The record shows that gas producers and shippers can and do consider pipeline alternatives when they are available. We can infer that adjacent and intersecting pipelines will be available alternatives for transportation out of the area for some producing blocks. The conclusion that the pipelines do not and cannot compete is, therefore, incorrect.

No evidence about price sensitivity between the Paragraph 20 region and other areas was offered. We do not know whether or how prices for transportation in these regions have been, are, or will be affected by or related to prices for transportation elsewhere. To be sure, in the past close regulation may have disguised or even overwhelmed any interregional pricing relationships; moreover, because the separate market for transportation services was nearly nonexistent, there would have been little evidence about separate prices for those services. The market is changing, and there is as yet little experience of actual pricing for transportation services. The briefs only speculate about actual pricing practices under the newly allowed selective discounts under Order 436. Whether prices in the future will demonstrate close relationships, or no relationships, is speculative.

The evidence of actual shipping patterns establishes that gas produced in this region has only been transported on pipelines in this region. Although evidence about shipment patterns can demonstrate the existence of geographic market, it must not be used uncritically, especially when there is little or no evidence about price correlations tending to show that a region is competitively isolated. The fact that producers in this region have always connected to pipelines in this region could be consistent with the existence of a much larger geographic market, in which competitive pressure from pipelines outside this region forces those within it to offer prices so attractive that producers do not choose to go outside. If that were the case, then those other pipelines should be considered to be in the market, not outside it.

Examining the map<sup>34</sup> and applying the kinds of benchmarks used by complaint counsel's expert witness discloses some apparently arbitrary inclusions and exclusions. Some blocks within the [11] alleged Paragraph 20 market, at its northwestern edge, are more than 15 miles from any large pipeline, whether inside the region or outside

<sup>34</sup> CV 804

it; the same is true of blocks in the Garden Banks to the south. Presumably, these blocks are included in the alleged market on the theory that, if any pipeline could serve them, it would be one that serves the Paragraph 20 region. But any pipeline serving these blocks would be well over 15 miles away, farther than the expert's 10- and 15-mile benchmarks.<sup>35</sup> The inclusion of these more distant blocks in the alleged market implies that pipelines more than 15 miles from a producing well could be considered feasible transportation alternatives in some circumstances.

On the southern edge of the eastern and western regions of the alleged market, other blocks are more than 15 miles from any pipeline. Some of these blocks are about the same distance from the pipelines within the alleged market as they are from an ANR pipeline only 14 miles outside it. Complaint counsel would exclude the ANR line because its diameter is only 12 inches,<sup>36</sup> but just five miles farther away that 12-inch line connects to a 24-inch line, one that is larger than the nearby legs of Stingray (22 and 16 inches) and Texas Eastern (12 inches and 16 inches) inside the Paragraph 20 region. Complaint counsel would also exclude the two 20-inch diameter Transco legs that come within 20 miles of the eastern edge of the region. But lines that are included in the Paragraph 20 region, or laterals from them, reach to within just three miles of these two Transco lines. Just outside the Paragraph 20 region is a block, Vermilion 369, connected by a 20-mile lateral to a pipeline inside it; that block is 15 miles from ANR and less than 20 miles from Transco.<sup>37</sup> Are the Transco lines too small or far away to matter, especially given the evidence that laterals are sometimes as long as 20 miles, or even longer? Complaint counsel has done little more than assert that other lines not physically within the Paragraph 20 region are either too small or too distant.

Even assuming the ability of pipelines to price discriminate on a geographic basis, on balance it is not entirely clear that pipelines outside the Paragraph 20 area are too far away to provide transportation alternatives for producing blocks in the area, so that the Paragraph 20 region as a whole could be considered a relevant geographic market. But the availability of nearby pipelines as

<sup>35</sup> Complaint counsel's expert witness used the 10- and 15-mile benchmarks to identify blocks that might be affected by the acquisition. By implication, those benchmarks would, under the expert's analysis, also measure the range of feasible alternative pipeline connections.

<sup>36</sup> CPF 6.96.

<sup>37</sup> ID 171; CX 904.

transportation alternatives for some producing blocks at the edges of the alleged Paragraph 20 market would not defeat the ability to exercise market power, if any exists, in more distant parts of the area. Judge Parker was incorrect in suggesting that a region cannot be a geographic market unless each firm located in the market competes in every part of it. The fact that HIOS and Sea Robin are too far from each other to compete directly with respect to particular producing blocks does not, by itself, defeat the existence of the larger Paragraph 20 market. HIOS and Sea Robin could be in the same geographic market, even if they are too far apart to compete with each other directly, if each of them competes with Stingray or some other pipeline or pipelines. Stingray in fact intersects with every other pipeline in the alleged market: HIOS, Sea Robin, Texas Eastern, and the Bluewater [12] extension. Thus complaint counsel's delineation of the alleged eastern and western region markets is not necessarily inconsistent<sup>38</sup> with a geographic market that encompasses both.

The evidence supporting the Paragraph 20 regions as geographic markets is not strong. Because the argument ultimately depends on the ability to price discriminate, it may be more fruitful to examine the implications of such price discrimination at the level of individual blocks or collections of blocks, rather than attempt to determine whether the theory supports defining the somewhat arbitrary Paragraph 20 regions as "markets".

#### *D. Individual Blocks As Markets*

A collection of blocks could also describe a relevant market if price discrimination is possible at particular block locations. As a theoretical proposition, this was found by Judge Parker and is admitted by respondents. If a hypothetical monopolist could impose a discriminatory increase at isolated locations within a larger market, then it is appropriate to collect those locations into a separate market for assessing competitive effects. In considering possible markets defined under this theory, there is a danger of implicitly assuming the conclusion. It is important to consider how significant the price discrimination might be to determine whether Section 7's requirement of "substantial" lessening of competition would be met in such "markets".

Here, the possibility of economic discrimination—differences in price not based on differences in cost—has been established more in

<sup>38</sup> See I.D.F. 249 & 250.

theory than in fact. Regulated uniformity of price has been the industry's traditional practice. FERC has announced that it will now permit more price variation to encourage greater price competition. Whether the effect of permitting greater variation will be to increase, or restrict, the range of options available to producers is conjectural. The evidence offered to show past price discrimination shows only price differences. It includes special deals some customers have negotiated allowing them to reduce contract demand, and one example of a flatly different rate for one customer.<sup>39</sup> Differences in the contracts' dates and other circumstances make comparison difficult. The record does not clearly demonstrate that the differences between the contracts reflect economic discrimination.

Complaint counsel's chief evidence for the possibility of price discrimination, other than the fact of geographic isolation,<sup>40</sup> is the wide gap between maximum and minimum prices permitted [13] under Order 436.<sup>41</sup> But permitting pipelines to grant deep discounts on transportation rates to capture new business could expand the range at which they can offer service.<sup>42</sup> The availability of a lower transportation rate, for example, could make it economical to build a longer lateral, all other things being equal. Thus, although geographic isolation in principle could encourage discriminatory treatment, permitting pipelines to offer non-uniform pricing could reduce the importance of that isolation. The net effect is, at the moment, speculative. The industry is adapting to the new regulatory environment, and FERC, while interested in encouraging selective discounting as a form of competition, still has the statutory obligation to prohibit undue discrimination. Because the experience under Order 436 is limited, predictions of future effects should be made cautiously.

We do not require proof of actual price discrimination in the past to use the possibility of price discrimination to define a market in a Section 7 case. Section 7 addresses likely future effects on competition, so proof of likely future discrimination could support the necessary market definition showing. The ability to price discriminate in the future is an open question in this industry, because prices

<sup>39</sup> CPF 6.83.

<sup>40</sup> Complaint counsel also asserts that arbitrage is difficult: the "same" transportation service cannot be shifted to any other place, because contracts restrict the customers' right to nominate or change delivery points. Such a shift might be made indirectly, by reselling, not the transportation, but gas produced where the favored transportation rate is available, to a customer who wants to avoid paying a higher rate. Whether such indirect arbitrage is a realistic possibility is not developed in the record.

<sup>41</sup> CPF 6.14; see note 12 *supra*.

<sup>42</sup> *Id.*

historically have been regulated and because some future price regulation is likely. For example, under Order 436, FERC regulates minimum and maximum prices, and unduly discriminatory prices are prohibited. We do not require waiting until market power is established and is being exercised before taking enforcement action. Thus the possibility of price discrimination might in appropriate circumstances be enough to justify concern about anticompetitive effects. But "possibilities" can be a weak foundation for a prediction of "likely", "substantial" competitive effects.

#### IV. COMPETITIVE EFFECTS

To demonstrate the extent of the acquisition's competitive effects, complaint counsel's expert witness used a simple sampling method, analyzing the transportation choices available at each of a number of blocks selected at random, on the assumption that only pipelines within 10 to 15 miles of a block were feasible. This analysis disclosed some blocks in the Gulf where the number of pipeline alternatives was limited, and where that number would be reduced if this transaction were treated as a merger.<sup>43</sup>

Other assumptions, in addition to the assumption that price discrimination is possible, are necessary to infer an effect on competition for connecting new supplies at the blocks identified by the expert. Some of these assumptions are plausible and some are not. One plausible assumption is that gas in commercial quantities will probably be found at some unconnected blocks. The fact that a particular block is not leased (and is therefore unexplored) may not demonstrate that no gas will ever be produced there, but the fact that a block has been leased, explored and abandoned may be some evidence that gas is not available in that block in commercial quantities. That the amount of gas below each block is unknown is not critical. It may be plausible to assume that some commercial [14] quantities will be found in some of the identified blocks. This assumption is supported by findings that additional reserves will be connected in the OCS, from blocks now leased in primary term if not from the never-leased or abandoned orphans.<sup>44</sup> The assumption that pipelines more than 15 miles from a block are not feasible alternatives is a defensible estimate, but not a clearly demonstrated fact. The feasible length of a lateral to a particular block depends on the size of

<sup>43</sup> The locations found by the sampling method are not contiguous, but that fact is not fatal: it is conceivable that, in an industry like this one, a "Swiss cheese" pattern could have been shown to be a relevant market.

<sup>44</sup> ID 26-33.

its reserves, something that is unknown. Longer laterals in the OCS suggest that at least some customers might have transportation options at distances greater than 15 miles. Moreover, there is little experience under the newly permitted deep discounts; it is conceivable that pipelines might offer service at even greater ranges under the new regulatory scheme.

Complaint counsel sets out an "existence" proof, a sample undertaken to determine whether there are potential new gas supplies for which competitive choices could be affected by the acquisition. The concrete showing is limited. For about three-quarters of the 42 blocks in the sample, competition is presumably possible because there are already two or more pipelines within 15 miles. About two-fifths of those 42 blocks have been leased, and two MidCon-affiliated lines are within the benchmark distance. The sample contains two blocks that most clearly fit complaint counsel's scenario of competitive effect, because this acquisition allegedly left those two blocks, High Island 390 and Garden Banks 140 (which are virtually adjacent), with no alternatives other than MidCon-affiliated lines. High Island 390 is unleased. Both blocks are at the southwestern part of the western region, reasonably close to HIOS and some 15-20 miles from Stingray. But the claim that MidCon-affiliated pipelines are the only transportation alternatives within the benchmark distance is belied by the map: these two blocks are about as close to Bluewater as they are to Stingray.<sup>45</sup>

Complaint counsel would extrapolate from this sample to a conclusion that this acquisition would affect competition in hundreds of blocks in the Paragraph 20 region. They do so simply by multiplying the proportions from the sample by 929, the number of unconnected blocks in the region. The detailed extrapolations now urged from the sample are unpersuasive. A large number of the blocks allegedly affected by the acquisition would be in the still-undeveloped Garden Banks, where predictions for gas reserves and transportation alternatives are most uncertain and where only a few blocks are within 15 miles of any pipeline. Few of these blocks are represented in the sample, although it is intended to be representative of all of the blocks. Some of the arguments made here demonstrate how extrapolations from the sample can be unreliable. By Judge Parker's reckoning, based on the lack of transportation alternatives for 5 out of 7 blocks, 75 percent of the blocks in the alleged Paragraph 20 market

<sup>45</sup> See CX 904.

would not be affected by the acquisition because they already had no transportation alternatives.<sup>46</sup> To counter that extrapolation, complaint counsel argues that shifting the boundary six miles to change the sample would yield the opposite conclusion: that *all* of the blocks *would* be affected.<sup>47</sup> Complaint counsel thus demonstrates that the value of projections from its sample is questionable. Thus, although we agree that there are likely to be more blocks affected [15] than the particular ones identified by the sample, we are much less confident that there will be hundreds of them.

We do not demand that each affected block be identified, any more than we would typically require that every affected customer be identified in any other merger case. But the sample here, which turned up only a few examples of blocks where customers might suffer the alleged anticompetitive effects, is insufficient to show substantial anticompetitive effects.<sup>48</sup>

The Commission does not rule out the possibility that mergers among OCS pipelines could violate Section 7 of the Clayton Act. There is evidence that OCS pipelines have been considered competitors with each other in the past and that they are likely to have more opportunities to compete in the future. A merger that is proven to be likely to substantially lessen that competition will be found illegal. But complaint counsel has failed to make that proof here.

#### V. CONCLUSION

The complaint is dismissed for failure to prove the likelihood of substantial lessening of competition in a section of the country.

<sup>46</sup> ID 239.

<sup>47</sup> CCAB p. 53 n. 35.

<sup>48</sup> Judge Parker apparently found that complaint counsel failed to show anticompetitive effects because no concentration data were presented for "block" markets. I.D.F. 258. But detailed concentration data are not always necessary in a Section 7 case (and the initial decision is in error to the extent it suggests otherwise) if other evidence shows the likelihood of anticompetitive effects. Here, it is not obvious that the changes in ownership from this acquisition would cause a significant change in concentration or competition at alleged "block" markets. The isolated examples of alleged "merger to monopoly" are two blocks where, pre-acquisition, the nearest pipelines were HIOS (20 percent controlled by Midcon), Stingray (50 percent controlled by Midcon), and Bluewater. The increase in Midcon's interest in HIOS to 40 percent does not self-evidently pose a competitive threat to these blocks.

Opinion

APPENDIX A



## FINAL ORDER

This matter having been heard on the appeal of complaint counsel from the initial decision and on briefs and oral argument in support of and in opposition to the appeal, for the reasons stated in the accompanying opinion, the Commission has determined to deny the appeal. Accordingly,

*It is ordered,* That the complaint is dismissed.  
Commissioner Machol not participating.