REPORT OF THE FEDERAL TRADE COMMISSION ON ACTIVITIES IN THE OIL AND NATURAL GAS INDUSTRIES

REPORTING PERIOD JULY-DECEMBER 2011

The Federal Trade Commission ("Commission" or "FTC") is pleased to submit this report to the Congressional Appropriations Committees ("the Committees") in response to the Report of the Senate Committee on Appropriations on the Financial Services and General Government Appropriations Bill for Fiscal Year 2010 (incorporated by general reference in continuing resolutions). In that 2010 Report, the Committee expressed its concern "with the potential for market manipulation and anticompetitive behavior in the oil and natural gas industries," encouraged the FTC "to continue its investigations and other activities related to these concerns," and directed the agency "to keep the Committee apprised of findings made regarding fuel prices, as well as other planned activities and investigations regarding the oil and gas industries."[1]

Overview

The Commission pursued a number of significant activities involving petroleum and natural gas during the second half of calendar 2011, demonstrating that the FTC considers the protection of American consumers from potentially anticompetitive practices in the energy sector to be one of its major responsibilities. The Commission continued to pay close attention to the energy sector during this six-month period. The FTC and its staff focused on mergers and acquisitions, possible anticompetitive conduct, and other activities involving pricing or competition in the petroleum and natural gas industries. The Commission expects this vigorous activity to continue through 2012 and beyond.

Memorandum of Understanding with the CFTC

As discussed in our last semiannual report, the FTC and the Commodity Futures Trading Commission ("CFTC") signed a Memorandum of Understanding ("MOU") in April 2011 that is intended "to foster further cooperation between the two agencies by helping them share

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[1] Committee on Appropriations, United States Senate, Report 111-43, on the Financial Services and General Government Appropriations Bill, 2010, S. 1432, at 85 (July 9, 2009), *available at* http://frwebgate.access.gpo.gov/cgi-bin/getdoc.cgi?dbname=111_cong_reports&docid=f:sr043.111.pdf. As the Commission noted in previous reports to the Appropriations Committees, because this is a public report, it is drafted to exclude sensitive details of ongoing investigations, which the Commission is prohibited by law from revealing.

nonpublic information."[2] By facilitating the sharing of such information in investigations of wholesale oil and gasoline markets, the MOU was expected to help each agency carry out its authority to detect and prevent manipulation in those markets. During the second half of 2011, the FTC and the CFTC have exchanged information pursuant to the MOU on multiple investigations.

Law Enforcement Activities

The Commission's work in the oil and natural gas sector also involves the analysis of mergers and acquisitions. Since July 1, 2011, the Commission has received premerger filings under the Hart-Scott-Rodino Act for 59 proposed transactions in these industries. The agency reviewed each of these premerger filings, and also monitored the industry for nonreportable transactions that might raise antitrust concerns.

In July, the Commission announced the issuance of a final consent order stemming from the acquisition by Irving Oil Ltd. and Irving Oil Terminals, Inc., of terminal and pipeline assets from ExxonMobil Corp. in the South Portland and Bangor/Penobscot Bay areas of Maine. The consent order, which required Irving to relinquish rights to certain terminal and pipeline assets, is intended to prevent the acquisition from leading to higher gasoline and diesel fuel prices for consumers.[3]

The Commission also investigated other mergers and acquisitions that raised significant competition issues. These investigations involved refined petroleum product terminals, pipelines, and bulk supply; gasoline retailing; liquefied petroleum gas (propane); natural gas liquids transportation, storage, and marketing; and natural gas gathering, processing, transportation, distribution, and retail sales. A number of these matters involved the cooperation of state attorney general offices, which the Commission always welcomes.

In November, the Commission acted on an application by ConocoPhillips to reopen and modify an FTC consent order that stemmed from Conoco's 2002 merger with Phillips. That order required ConocoPhillips to grant a ten-year exclusive license to Holly Corporation, giving Holly exclusive use of the "Phillips" and "Phillips 66" brands in Utah, Idaho, Wyoming, and Montana. The Commission's modification removed the exclusivity provision from the original order (as it pertained to Wyoming and Montana) two years early, which allows ConocoPhillips itself to use the brands in those two states. The Commission also approved a seven-year extension of the license agreement, on a nonexclusive basis, in all four states.[4]

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[2] *See* http://www.ftc.gov/opa/2011/04/ftccftc-mou.shtm (press release); http://www.ftc.gov/os/2011/04/110412ftccftc-mou.pdf (text of the MOU).

[3] *See* http://www.ftc.gov/opa/2011/07/competition.shtm.

[4] *See* http://www.ftc.gov/os/caselist/0210040/111611conocoorder.pdf. Holly, which submitted a supporting affidavit, concurred in ConocoPhillips's request for the modification and

The Commission's enforcement activities also included examinations of possibly anticompetitive conduct in the petroleum and natural gas industries. Crude oil and refined petroleum product prices and profit margins increased substantially earlier this year. As recounted in the last semiannual report, last spring the Energy Information Administration ("EIA") reported that U.S. refiners' refining margins had increased more than 90 percent between the beginning of 2011 and early May, while those refiners were using only 81.7 percent of their capacity in early May (a seven percent reduction from the same period in 2010). Those and other developments led the Commission to open an investigation – including the use of compulsory process – to determine whether certain oil producers, refiners, transporters, marketers, physical or financial traders, or others have engaged or are engaging in anticompetitive or manipulative practices or have provided any federal department or agency with false or misleading information related to the wholesale price of crude oil or petroleum products.[5] The investigation seeks information that may include, but is not limited to, utilization and maintenance decisions, inventory holding decisions, product supply decisions, product margins and profitability, and capital planning.

The FTC also has examined other types of conduct by firms in the oil and natural gas industries, including inquiries related to propane and investigations of possibly anticompetitive or possibly deceptive conduct involving other petroleum products and fuel-saving devices.[6] Some of this work involved contacts with local law enforcement officials.

Petroleum Market Manipulation Rule

As mentioned in previous reports, the Commission established a process in November 2009 to monitor compliance with the Petroleum Market Manipulation Rule,[7] which prohibits manipulation in wholesale markets for crude oil, gasoline, or petroleum distillates. Staff in the Bureau of Competition's Office of Policy and Coordination received no communications regarding the Rule from the public since July 1, 2011, but the Commission stands ready to examine closely any complaints or other communications that it receives regarding the Rule, and

approval of the extension.

[5] *See* "Information To Be Publicly Disclosed Concerning the Commission Petroleum Industry Practices and Pricing Investigation," File No. 111 0183 (June 20, 2011), available at http://www.ftc.gov/os/2011/06/110620petroleuminvestigation.pdf.

[6] For example, the Commission recently announced that it had "reached a settlement putting a stop to the phony claims of marketers who told consumers their fuel economy device could boost automobile gas mileage by at least 50 percent and 'turn any vehicle into a hybrid.'" *See* "FTC Stops Marketers from Selling Phony Fuel Economy Devices" (Dec. 20, 2011), *available at* http://www.ftc.gov/opa/2011/12/dutchman.shtm.

[7] The Commission issued this Rule under the authority of Section 811 of the Energy Independence and Security Act of 2007, 42 U.S.C. § 17301.

to take action as appropriate.[8]

Oil and Gas Price Fraud Working Group

The interagency cooperation typified by the FTC-CFTC MOU assumed a broader form in light of last spring's increase in oil and gasoline prices. As described in our last semiannual report, the Attorney General established the Oil and Gas Price Fraud Working Group, which consists of federal and state law enforcement agencies with oversight of oil and gasoline markets. In a series of meetings, the member agencies discussed their respective expertise in the oil and gas sector and explored ways to share information and complaints received from the public. The Working Group has enhanced the possibilities for cooperative information-sharing among the member agencies, and various agencies' investigations in the petroleum sector – including those by the FTC – may benefit from information gleaned from the Working Group process. As one of the co-chairs of the Working Group, the Commission helps ensure that American consumers are not harmed by unlawful conduct.

Gasoline and Diesel Price Monitoring

During the relevant period, the FTC also continued a decade-old project that has provided valuable information in connection with the agency's efforts to police conduct in the petroleum industry. Begun in 2002, the Gasoline and Diesel Price Monitoring Project involves monitoring by the Bureau of Economics of the wholesale and retail prices of gasoline and diesel fuel in order to help detect possible anticompetitive activities and determine whether a law enforcement investigation is warranted. This project continues to track retail gasoline and diesel prices in 360 cities across the nation and wholesale (terminal rack) prices in 20 major urban areas. The staff of the Bureau of Economics receives daily data from the Oil Price Information Service (except on Sundays) and reviews other relevant information that the Commission might receive directly from the public or from other government agencies or Members of Congress. The staff reviews the data and uses an econometric model to determine whether current retail and wholesale prices each week are anomalous in comparison with historical data. This alerts FTC staff to unusual changes in gasoline and diesel prices so that further inquiry can be undertaken expeditiously. When price increases do not appear to result from market-driven causes, the staff consults with the EIA. FTC staff also contacts the offices of the appropriate state attorneys general to discuss

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[8] The "Guide to Complying with Petroleum Market Manipulation Regulations" that the Commission issued in November 2009 (http://www.ftc.gov/os/2009/11/091113mmrguide.pdf) provides addresses – including an email address – to which the public may send complaints of possible Rule violations. Complaints that evidence a serious possibility of a Rule violation are referred to the FTC litigation units that specialize in maintaining competition in energy industries. Complaints that concern activity in futures markets are shared with the CFTC (through the FTC's working relationship with that agency), to ensure that consumers are protected against fraud and deception in whatever form they take. In addition, as described elsewhere in this report, FTC litigators and economists continue to employ additional techniques to monitor prices and other activity in petroleum markets.

the anomaly and appropriate potential actions, including the opening of an investigation. The Commission expects to continue this important activity.

Outer Continental Shelf Leasing

The FTC has an ongoing responsibility to provide an antitrust review of proposed oil and natural gas leases on the Outer Continental Shelf, pursuant to the Outer Continental Shelf Lands Act Amendments of 1978. The Commission undertook one such review during the second half of 2011 and advised the Assistant Attorney General for Antitrust regarding its views of the proposed lease sale.

Economic Analysis of Oil and Gas Issues

In September, the Commission's Bureau of Economics issued a staff report that examined trends in the petroleum industry and how they have affected gasoline prices between 2005 and early 2011.[9] The report concludes that although a broad range of factors influence the price of gasoline, worldwide crude oil prices continue to be the main driver of what Americans pay at the pump. Building on prior Commission and staff reports that informed the public and policymakers about petroleum industry issues (including gasoline prices in particular), the new report updates FTC work on gasoline price factors and on mergers, structural changes, and antitrust enforcement in the petroleum industry. The report also reviews and comments on academic and other research regarding the rate at which gasoline prices adjust to price changes further up the petroleum supply chain, as well as evidence regarding regional variations in the patterns of these adjustments.

Congressionally Mandated Reports

On December 1, 2011, the Commission approved the seventh annual *Report on Ethanol Market Concentration*. The Commission's ethanol reports, issued pursuant to Section 1501(a)(2) of the Energy Policy Act of 2005 (45 U.S.C. § 7545(o)), entail an analysis of ethanol industry concentration to determine whether there is sufficient competition among ethanol industry participants "to avoid price-setting and other anticompetitive behavior."[10]

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[9] FEDERAL TRADE COMMISSION, BUREAU OF ECONOMICS, GASOLINE PRICE CHANGES AND THE PETROLEUM INDUSTRY: AN UPDATE (2011), *available at* http://www.ftc.gov/os/2011/09/110901gasolinepricereport.pdf.

[10] In its 2011 ethanol report, *available at* http://www.ftc.gov/os/2011/12/111213ethanolreport.pdf, the Commission concluded that "[r]egardless of the particular measure of market share or the market share allocation method used to calculate concentration, the low concentration levels that characterize the U.S. ethanol production industry have persisted." The industry dynamics described in the report – including potential entry by new firms and the possibility of ethanol imports – "make it extremely unlikely that a single ethanol producer or marketer or a group of such firms could exercise market power

FTC Personnel Involved in Oil and Gas Activities

During the second half of 2011, personnel from many parts of the Commission continued their involvement in the agency's activities in the oil and natural gas industries. The Commission's Associate General Counsel for Energy engaged in virtually all aspects of the agency's work in these industries. Personnel from the Mergers III division of the Bureau of Competition (which is devoted primarily to petroleum and natural gas issues) and from a number of other Bureau divisions have been involved in addressing oil and natural gas issues as well.[11] In addition to the Bureau of Competition, one division of the Commission's Bureau of Economics bore major responsibility for conducting competition analysis of pricing and other competitive issues in the petroleum and natural gas industries. Staff from the Commission's Office of the General Counsel, the Bureau of Consumer Protection, the Office of Congressional Relations, the Commissioners' offices, the FTC's Regional Offices, and other FTC organizations also contributed to oil and natural gas matters during the second half of 2011.

Conclusion

The Commission has maintained its intensive antitrust and consumer protection scrutiny of the energy sector during the second half of 2011. In view of the fundamental importance of oil, natural gas, and other energy resources to the overall vitality of the United States and world economy, we expect that FTC review and oversight of the oil and natural gas industries will remain a centerpiece of our work for years to come.

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to set prices or coordinate on price or output levels."

[11] Additional Bureau of Competition offices whose staff participated in oil and gas matters during the second half of 2011 include the Office of the Director, the Division of Compliance, the Mergers II and Mergers IV divisions, the Office of Policy and Coordination, the Division of Technology and Information Management, the Division of Operations, and the Office of Premerger Notification.