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

REPORTING PERIOD JANUARY-JUNE 2010

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. That Report expressed the Committee's 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]

The Commission's significant activities involving petroleum and natural gas during the first half of calendar 2010 demonstrate that protecting American consumers from potentially anticompetitive practices in the energy sector remains one of our most important responsibilities. The Commission continued to pay very close attention to the energy sector during this six-month period. After the agency's Final Rule against manipulation in wholesale markets for crude oil, gasoline, or petroleum distillates took effect in November 2009,[2] the staff has received and closely examined 10 communications from the public regarding the Market Manipulation Rule. In addition, the FTC and its staff also continued to focus on mergers and acquisitions, possible anticompetitive conduct, and other activities involving pricing or competition in the petroleum and natural gas industries. The Commission expects its vigorous activity to continue throughout 2010 and beyond.

During the first six months of 2010, personnel from many parts of the Commission continued to be involved in law enforcement, economic analysis, and rule- or policy-related activities in the oil and natural gas industries. The Commission's Associate General Counsel for Energy remained involved 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

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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.

[2] The Commission issued this Rule under the authority of Section 811 of the Energy Independence and Security Act of 2007, Pub. L. No. 110-140.

primarily to petroleum and natural gas issues), from that Bureau's front office, and from a number of other Bureau divisions have been involved in addressing oil and natural gas issues as well.[3] In addition to the Bureau of Competition, one division of the Commission's Bureau of Economics also bore major responsibility for conducting competition analysis of pricing and other competitive issues in the petroleum and natural gas industries. Other staff involved in oil and natural gas matters during the first half of 2010 came from the Commission's Office of the General Counsel, the Office of Congressional Relations, the Office of Policy Planning, the Commissioners' offices, and other FTC organizations.

Pursuant to the process that the Commission established in November 2009 to monitor compliance with the Market Manipulation Rule, staff in the Bureau of Competition's Office of Policy and Coordination have examined all communications to the FTC regarding the Rule, including complaints about Rule violations.[4] Complaints that evidence a serious possibility of a Rule violation are referred to FTC litigation staff who specialize in maintaining competition in energy industries. Complaints that concern activity in futures markets are shared with the Commodity Futures Trading Commission (through the FTC's working relationship with that agency), to ensure that consumers are protected against fraud and deception in whatever form they take.[5]

The Commission's work in the oil and natural gas sector also involves the analysis of mergers and acquisitions. Since January 1, 2010, the Commission has received premerger filings under the Hart-Scott-Rodino Act for 34 proposed transactions in these industries. The agency reviewed each of these transactions, and also monitored the industry for nonreportable transactions that might raise antitrust concerns. For transactions that raised such concerns, the Commission investigated further. During the relevant period, the Commission has investigated a number of transactions involving petroleum or natural gas, including acquisitions involving crude oil and natural gas exploration and production, refined petroleum products pipelines and terminals, refined products wholesaling, retail gas stations, sales of long-haul diesel fuel,

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[3] Additional Bureau of Competition offices whose staff have participated in oil and gas matters during the first half of 2010 include the Office of the Director, the Mergers II division, the Division of Anticompetitive Practices, the Division of Compliance, the Division of Technology and Information Management, the Office of Policy and Coordination, the Division of Operations, and the Office of Premerger Notification.

[4] The "Guide to Complying with Petroleum Market Manipulation Regulations" that the Commission issued last November (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.

[5] As described in more detail below, FTC litigators and economists also continue to monitor prices and other activity in petroleum markets.

liquefied petroleum gas (propane), and certain lubricant oils.[6] On June 30, the Commission announced its acceptance of a consent agreement stemming from Pilot Travel Center's contemplated acquisition of Flying J Inc.'s travel center business. To resolve the Commission's allegations that the acquisition would have lessened competition in the over-the-road sale of diesel fuel to long-haul trucking fleets, Pilot agreed to sell 26 travel centers to Love's Travel Stops and Country Stores, allowing Love's to compete for long-haul customers who otherwise would have been harmed by Pilot's acquisition of Flying J.[7]

During the relevant period, the FTC also continued a longstanding project that has provided valuable information in connection with the agency's efforts to police conduct in the petroleum industry. Since 2002, the Gasoline and Diesel Price Monitoring Project has involved monitoring by the Bureau of Economics of the wholesale and retail prices of gasoline 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 some 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 Energy Information Administration. FTC staff also contacts the offices of the appropriate state attorneys general to discuss the anomaly and appropriate potential actions, including the opening of an investigation. The Commission expects to continue this important activity.

The tragic oil spill in the Gulf of Mexico precipitated FTC activity during this six-month period. For example, the Commission posted a consumer alert on its website entitled "FTC Warns of Oil Spill Scams," warning consumers and businesses to be on the lookout for fraudulent activity – such as false fundraising claims or phony offers of remediation services –

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[6] The Commission's activities involving oil and natural gas also have included the examination of possibly anticompetitive conduct by firms in those industries, including an ongoing investigation of conduct in the propane business.

Over the years, some inquiries concerning gasoline prices have involved close cooperation between the FTC staff and state attorney general offices. For example, the FTC staff continues to evaluate the concerns raised by one state attorney general concerning gasoline prices in a particular part of a state. During the relevant period, the staff has also worked cooperatively with other state attorneys general or local officials in investigating both mergers and potentially anticompetitive conduct involving various petroleum products.

[7] *See* http://www.ftc.gov/opa/2010/06/flying.shtm for the FTC's press release announcing the Pilot/Flying J settlement.

stemming from the Deepwater Horizon explosion and the resulting spill.[8]

FTC staff began preparations to draft the Commission's sixth annual *Report on Ethanol Market Concentration*, which will be due at the beginning of December 2010. 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)), involve an annual analysis of ethanol industry concentration to determine whether there is sufficient competition among ethanol industry participants "to avoid price-setting and other anticompetitive behavior."[9]

Another ongoing responsibility is the FTC's 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 two such reviews during the first half of 2010 and advised the Assistant Attorney General for Antitrust regarding its views of the proposed lease sales.

Finally, the Bureau of Economics released several working papers pertaining to petroleum. In Working Paper No. 300, entitled *Petroleum Mergers and Competition in the Northeast United States*, the Bureau reported on a retrospective evaluation of two consummated transactions – Sunoco's 2004 acquisition of El Paso's New Jersey petroleum refinery and

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[8] *See* http://www.ftc.gov/bcp/edu/pubs/consumer/alerts/alt058.shtm.

[9] The Commission's 2009 ethanol report, *available at* http://www.ftc.gov/os/2009/12/091201ethanolreport.pdf, concluded that the dynamics of the industry in 2009 – including a continuing "industry trend toward less concentration," an increase in ethanol production capacity, potential entry by new firms, and the availability of ethanol imports – "make it extremely unlikely that a single ethanol producer or marketer or a small group of such firms could wield sufficient market power to successfully engage in price-fixing or other anticompetitive behavior."

A number of reports prepared by the FTC or its staff that predate the period covered by the current report to Congress also demonstrate the Commission's commitment to delving deeply into key competition and consumer issues in the energy sector and sharing its expertise with Congress and the public. *See, e.g.*, FEDERAL TRADE COMMISSION, REPORT ON SPRING/SUMMER 2006 NATIONWIDE GASOLINE PRICE INCREASES (2007), *available at* http://www.ftc.gov/reports/gasprices06/P040101Gas06increase.pdf; FEDERAL TRADE COMMISSION, REPORT ON GASOLINE PRICE MANIPULATION AND POST-KATRINA GASOLINE PRICE INCREASES (2006), *available at* http://www.ftc.gov/reports/060518PublicGasolinePricesInvestigationReportFinal.pdf; FEDERAL TRADE COMMISSION, GASOLINE PRICE CHANGES: THE DYNAMIC OF SUPPLY, DEMAND, AND COMPETITION (2005), *available at* http://www.ftc.gov/reports/gasprices05/050705gaspricesrpt.pdf; FEDERAL TRADE COMMISSION, BUREAU OF ECONOMICS, THE PETROLEUM INDUSTRY: MERGERS, STRUCTURAL CHANGE, AND ANTITRUST ENFORCEMENT (2004), *available at* http://www.ftc.gov/os/2004/08/040813mergersinpetrolberpt.pdf.

Valero's 2005 acquisition of Premcor's Delaware refinery. The authors found that, aside from some mixed evidence regarding unbranded rack prices, both transactions "were largely competitively neutral." Working Paper No. 302, *Asymmetric Pass-Through in U.S. Gasoline Prices*, presented new evidence that upward cost shocks are passed through more quickly than downward cost shocks in United States gasoline prices. Working Paper No. 303, *Edgeworth Price Cycles in Gasoline: Evidence from the U.S.*, used multiple methods to identify price cycles in retail gasoline and diesel price and found Edgeworth price-cycling behavior in a small number of cities in certain contiguous upper Midwestern states.[10]

Conclusion

The Commission has maintained its intensive antitrust scrutiny of the energy sector during the first half of 2010. 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.

[10] Working Papers No. 300, 302, and 303 are available at, respectively, http://www.ftc.gov/be/workpapers/wp300.pdf, http://www.ftc.gov/be/workpapers/wp302.pdf, and http://www.ftc.gov/be/workpapers/wp303.pdf.