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FTC Turns Up the Pressure on Oil and Gas M&A

Transacting parties should be aware of five recent trends in oil and gas merger enforcement and prepare for more arduous regulatory reviews.

US antitrust enforcement in oil and gas transactions has spiked in the last year. The Federal Trade Commission (FTC) recently announced an increased focus on closely scrutinizing transactions in the industry, and that scrutiny has resulted in many recent oil and gas transaction investigations and deal challenges. Oil and gas producers and midstream and downstream operators need to take into account this shifting antitrust enforcement framework as they negotiate transaction agreements and formulate antitrust clearance strategies.

A Heightened Focus on Oil and Gas Transactions

Over the course of the last year, the FTC has made clear that it intends to increase scrutiny of the oil and gas sector — both in public statements and through its enforcement actions.

In August 2021, FTC Chair Lina Khan wrote a letter highlighting her concern "that the Commission's approach to merger review in recent years has enabled significant consolidation" in the oil and gas industry.[1] Chair Khan announced a three-pronged approach to address these concerns, including identifying "additional legal theories to challenge retail fuel station mergers," seeking to deter certain oil and gas mergers from even being proposed or attempted, and asking FTC staff to "investigate abuses in the franchise market."[2]

Shortly thereafter, in September 2021, the Director of the FTC's Bureau of Competition, Holly Vedova, issued a statement underscoring that "the Bureau of Competition is redoubling its commitment to police unfair methods of competition in wholesale and retail gasoline and diesel sales."[3]

In November 2021, President Biden sent a letter to Chair Khan seeking to call attention to the "mounting evidence of anti-consumer behavior by oil and gas companies."[4] President Biden asked that the FTC further strengthen its oversight of the industry and of transactions within the oil and gas sector.

This increased focus can also be seen in the significant number of investigations conducted by the FTC since the beginning of 2021; for example:

- In May 2021, midstream operator Energy Transfer received a "Second Request" (an in-depth request for documents and information that prolongs the statutory review period of a proposed transaction) for its acquisition of Enable Midstream.[5]

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- In June 2021, 7-Eleven and Marathon Petroleum agreed with the FTC to divest hundreds of fuel outlets after a protracted investigation of their transaction.[6]

- In July 2021, Berkshire Hathaway Energy (BHE) and Dominion Energy agreed to terminate the proposed acquisition of Dominion's Questar Pipeline by BHE due to concerns about the ability to obtain clearance from the FTC.[7]

- In the fall of 2021 and into 2022, several additional transactions underwent lengthy Second Request investigations, including HollyFrontier's purchase of Sinclair Oil,[8] Vertex Energy's sale of motor oil collection and re-refining assets to Safety-Kleen Systems,[9] and EnCap Investments' acquisition of oil and gas producer EP Energy.

Newly Emerging Oil and Gas Industry Antitrust Enforcement Trends

There are several recent trends in FTC enforcement in Hart-Scott-Rodino (HSR) Act investigations that parties should be aware of when analyzing and evaluating potential transactions, negotiating transaction agreements, and projecting the timeline for regulatory review.

1. More Second Request Investigations and a Less Accommodating FTC

As noted above, this past year has seen a marked uptick in the number of in-depth Second Request investigations of transactions in the oil and gas sector, including a heightened focus on both upstream and midstream deals. Under the HSR Act, the FTC may launch a Second Request investigation if it cannot resolve potential competition concerns about a transaction within the initial 30-day (or 60-day with a pull-and-refile) HSR Act waiting period. These lengthy investigations involve onerous requests requiring the production of large volumes of documents, detailed information, and data extending back multiple years. Second Request investigations often consume nine to twelve months, and in some cases extend to fifteen months or more.

In addition to a larger number of Second Request investigations, the burden and associated compliance timeline for completing these investigations has increased. There has been a general trend toward lengthier investigations at the FTC.[10] This trend stems from a variety of factors, including the agency's reluctance to grant the transaction parties' requests for accommodations to reduce the burden of complying with the Second Request, and its demands for lengthier decision-making timeframes beyond what the agency is permitted by the HSR Act. For example, new policies require more onerous privilege logging, and more scrutiny of the technical specifics of how the parties seek to comply with the Second Request. The FTC is also asking for more time to reach a decision after the parties have complied with the Second Request, often an extra three months in addition to the one month that the HSR Act provides.

Transaction parties need to take the timing, burden, and cost impacts of these challenging trends into account. This includes ensuring that their transaction agreements have the necessary covenants, conditions and timing provisions to allow the parties to successfully address a lengthy investigation process. The parties need sufficient time built into the "outside date" of their transaction agreement to allow them to respond to an investigation and, if necessary, negotiate a remedy or litigate a challenge of the deal.

2. More Demanding Requirements for Remedies Including Prior Approval Requirements and Constraints on Divestiture Buyers

The transaction parties may elect to propose a "remedy" to address the FTC's concerns about a transaction. This often takes the form of a divestiture of assets or businesses in the area where the FTC

claims to have identified competitive harm. The terms of the remedy are negotiated, agreed, and memorialized in a consent decree with the FTC. As of October 2021, the FTC has taken the position that consent decrees must now contain "prior approval" provisions. These provisions typically require the post-transaction entity to obtain, for 10 or more years following the consummation of the transaction, affirmative approval from the FTC before any future transaction that involves the relevant market(s) implicated by the competitive harm that the FTC alleges, even when such a transaction is not otherwise HSR-reportable. The FTC has indicated that it may consider expanding the scope of prior approval provisions on a case-by-case basis to include products or geographies beyond the scope of the specific relevant markets at issue.[11] While the precise contours of enforcement of these provisions remains to be seen, the FTC's statement could conceivably open the door to an indefinite review period for transactions that fall below the HSR-reportability threshold, significantly expanding the scope of the FTC's review authority.

Notably for the oil and gas sector, the FTC highlighted in its September 2021 statement that it would consider imposing prior approval requirements that go beyond the overlapping product and geographic markets implicated by the underlying transaction where circumstances so justify, noting that "[o]il and gas mergers are prime candidates to require this tougher extra relief."[12]

In addition to prior approval requirements, the FTC has also recently required the purchaser of the divestiture assets or businesses — an unrelated third party that has agreed to acquire the divestiture business or assets as part of the remedy process — to obtain FTC prior approval for the sale of those assets or businesses for up to 10 years post-closing, depending on the characteristics of the proposed buyer. This significant imposition is likely to have a chilling effect on potential divestiture buyers, for fear of acquiring assets or businesses that cannot be easily transferred if necessary or financially desirable for several years post-acquisition.

These new requirements mean that transaction parties must consider both (i) the potential impact of the prior approval provisions on the buyer's go-forward business and (ii) the possibility that the divestiture buyer restrictions could make finding a party willing to agree to those constraints difficult. Taken together, these considerations could mean that transactions become more difficult to resolve through a remedy, and transaction parties could be forced to litigate an FTC challenge and/or revise, restructure or abandon their deal.

3. Bad Documents Significantly Impacting Merger Investigations

The content of parties' transaction-related and ordinary-course documents have had an increasingly important impact in the current enforcement environment. Certain documents relating to the proposed transaction and topics around competition, markets, sales growth and synergies are required to be submitted to the agencies along with the notification form pursuant to the HSR Act. These documents, known as Item 4(c) and 4(d) documents, are reviewed closely by the agencies, and any references to dominance, potential post-transaction price increases or output reductions, or a discussion of high combined market shares or limited competitive constraints, can significantly increase the likelihood that the agency opens an investigation into the transaction.

Further, as part of an in-depth Second Request investigation, the parties are required to produce thousands of employee emails, internal business documents, text and chat messages, and various other materials to the FTC. Discussions in these documents about a concentrated market or the post-transaction entity having market power, dominance, or the ability to charge higher prices can greatly influence the course of the investigation and can lead the FTC to challenge a deal, even if the economics do not necessarily align with statements made in those documents. For example, the recent FTC

complaint in the EnCap-EP Energy transaction cites several of buyer's internal business documents and notes that the buyer's "internal, high-level analysis and strategy documents acknowledged the likely competitive effects from the Acquisition."[13] These statements included a discussion of the buyer "taking out 1 of 4 major producers" in Utah's Uinta Basin, and using a cartoon of "Pinky and the Brain" with the tagline "Try to Take Over Utah."[14]

Companies should take steps early in a transaction process to ensure that company personnel and outside advisors understand the risks associated with creating documents that misrepresent the impact of the transaction or use exaggerated, hyperbolic language when discussing competitive dynamics or market structure.

4. Commission Approval Delays

Transaction parties may also need to account for the risk of FTC Commission approval delays. The recent Marathon/7-Eleven transaction highlights these risks. In that transaction, the agreement was signed in August 2020 and within a few months, it was reported that the parties were intending to divest several hundred gas stations to address overlaps between 7-Eleven and Speedway stores.[15] The parties entered into a timing agreement with FTC Staff, which was extended four times.[16] The last amendment reflected the parties' intention to close on May 14. As of the end of April 2021, the parties had agreed to a remedy with FTC Staff to divest 293 fuel outlets, and FTC Staff recommended that the FTC Commissioners approve the remedy. However, on May 11, two Commissioners requested a further extension for more time to review the remedy. The parties declined to provide the additional extension and closed the deal on May 14, but continued to operate in accordance with the terms of the remedy proposal. Two Commissioners issued a statement condemning the consummated transaction as illegal and stating that they were extremely troubled by the parties' decision to close without having finalized the consent decree with the Commission.[17] The parties continued to work with FTC Staff on the terms of the remedy following the closing, and on June 25, the FTC announced that the Commission had approved the remedy, which required the divestiture of 293 stores and prohibited 7-Eleven from enforcing any non-compete provisions as to franchisees or employees.[18]

This situation, while anomalous, shows that parties must be prepared for a lengthy and unpredictable review process and potential delays on the part of the Commission to reach a decision. For transactions with overlaps that may attract regulatory scrutiny, transacting parties should consider at the deal negotiation stage how they would proceed in the event of FTC inaction, and tailor the provisions in the transaction agreement to accommodate that potential outcome.

5. "Close at Your Own Risk" Letters

The FTC and DOJ recently began delivering letters to transaction parties in certain deals at the end of the initial HSR waiting period (even without any direct contact with the parties), after the parties "pull and refile" their HSR filing in order to give the agencies an additional 30 days to review the proposed transaction, or at the conclusion of a Second Request investigation and subsequent additional waiting period. These letters, colloquially known as "close at your own risk" letters, state that although the waiting period will soon expire, the agency's investigation is ongoing and, while the parties may choose to consummate the transaction, they do so at their own risk of a future challenge.[19] These letters highlight the ability of the FTC and DOJ to challenge transactions before *or* after their consummation and underscore that parties cannot avoid an enforcement action by consummating the transaction.

Parties negotiating a transaction agreement may consider expressly addressing the receipt of a "close at your own risk" letter in the agreement. Some transaction agreements include specific language on this issue in the relevant closing conditions.

Conclusion

Given the heightened antitrust focus on the oil and gas sector and a recent shift toward more onerous investigations, greater uncertainty and more protracted delay, parties should consult antitrust counsel early in the process when considering a potential transaction and should keep counsel involved at each step along the way. These trends underscore the importance of taking account of different potential outcomes when negotiating transaction agreements and working with counsel to navigate the regulatory review process.

If you have questions about this *Client Alert*, please contact one of the authors listed below or the Latham lawyer with whom you normally consult:

Jason D. Cruise
jason.cruise@lw.com
+1.202.637.1033
Washington, D.C.

Lindsey S. Champlin
lindsey.champlin@lw.com
+1.202.637.2122
Washington, D.C.

Caitlin N. Fitzpatrick
caitlin.fitzpatrick@lw.com
+1.202.637.3358
Washington, D.C.

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Endnotes

[1] https://www.whitehouse.gov/wp-content/uploads/2021/08/Letter-to-Director-Deese-National-Economic-Council.pdf

[2] *Id.*

[3] https://www.ftc.gov/enforcement/competition-matters/2021/09/protecting-americans-gas-pump-through-aggressive-antitrust-enforcement

[4] https://int.nyt.com/data/documenttools/ftc-gas-prices/92d93dca9793b8b4/full.pdf

[5] https://investors.enablemidstream.com/news/news-details/2021/Enable-Midstream-Announces-Second-Quarter-2021-Financial-and-Operating-Results/#:~:text=On%20May%2012%2C%202021%2C%20Enable,Hart%2DScott%2DRodino%20Act. The transaction ultimately closed in December 2021 without an FTC enforcement action.

[6] https://www.ftc.gov/news-events/news/press-releases/2021/06/ftc-orders-divestiture-hundreds-retail-stores-following-7-eleven-incs-anticompetitive-21-billion. The details of that investigation are discussed further below.

[7] The FTC thereafter issued a statement that the merger was "representative of the type of transaction that should not make it out of the boardroom." https://www.ftc.gov/news-events/news/press-releases/2021/07/statement-regarding-berkshire-hathaway-energys-termination-acquisition-dominion-energy-incs-questar

[8] This transaction closed in March 2022, seven months after it had been announced in August 2021.

[9] In January 2022, the parties announced that they had mutually agreed to terminate the proposed transaction, citing the "prolonged" FTC review process and "the considerable time and resources required to support what has become a costly and time consuming regulatory review." https://www.sec.gov/Archives/edgar/data/890447/000158069522000012/ex99-1.htm

[10] See the FTC's September 28, 2021 blog post describing new changes to the Second Request investigation process, including making merger reviews "more comprehensive and analytically rigorous." https://www.ftc.gov/enforcement/competition-matters/2021/09/making-second-request-process-both-more-streamlined-more-rigorous-during-unprecedented-merger-wave

[11] https://www.ftc.gov/system/files/documents/public_statements/1597894/p859900priorapprovalstatement.pdf

[12] https://www.ftc.gov/enforcement/competition-matters/2021/09/protecting-americans-gas-pump-through-aggressive-antitrust-enforcement

[13] https://www.ftc.gov/system/files/ftc_gov/pdf/2110158C4760EnCapEPEComplaint.pdf

[14] *Id.*

[15] https://www.reuters.com/article/seveni-hldgs-speedway-idUSL1N2HL312

[16] https://corp.7-eleven.com/corp-press-releases/05-14-2021-7-eleven-inc-response-to-ftc-commissioner-statement

[17] https://www.ftc.gov/news-events/news/press-releases/2021/05/statement-ftc-acting-chairwoman-slaughter-commissioner-chopra-7-elevenspeedway-merger

[18] https://www.ftc.gov/news-events/press-releases/2021/06/ftc-orders-divestiture-hundreds-retail-stores-following-7-eleven

[19] The FTC published a blog post describing this new practice, along with a form of the letter as an example. https://www.ftc.gov/enforcement/competition-matters/2021/08/adjusting-merger-review-deal-surge-merger-filings. During a February 2022 panel, FTC Commissioner Noah Phillips indicated that the FTC has sent at least 50 such letters so far. *See* https://www.law360.com/articles/1468528/ftc-s-phillips-sees-no-path-to-return-of-early-termination.