THE EXXON-MOBIL MERGER

HEARINGS

BEFORE THE

SUBCOMMITTEE ON ENERGY AND POWER

OF THE

COMMITTEE ON COMMERCE

HOUSE OF REPRESENTATIVES

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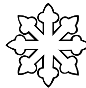

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THE EXXON-MOBIL MERGER

WEDNESDAY, MARCH 10, 1999

HOUSE OF REPRESENTATIVES,
COMMITTEE ON COMMERCE,
SUBCOMMITTEE ON ENERGY AND POWER,
Washington, DC.

The subcommittee met, pursuant to notice, at 10:02 a.m., in room 2123, Rayburn House Office Building, Hon. Joe Barton, (chairman) presiding.

Members present: Representatives Barton, Largent, Burr, Rogan, Shimkus, Wilson, Bryant, Ehrlich, Bliley (ex officio), Hall, McCarthy, Sawyer, Markey, Gordon, and Wynn.

Also present: Representatives Engel and Jackson-Lee.

Staff present: Cathy VanWay, majority counsel; Ramsen Betfarhad, majority counsel, Donn Salvosa, legislative clerk; Rick Kessler, minority professional staff member, and Sue Sheridan, minority counsel.

Mr. BARTON. The Subcommittee on Energy and Power of the Commerce Committee hearing on the Exxon-Mobil merger will come to order.

I would like to welcome everyone to today's hearing on the recently announced merger between Exxon and Mobil. As everyone knows on December 1, 1998, Exxon, the Nation's largest domestic oil company, agreed to buy Mobil Oil for $77 billion.

This merger, if approved, would represent the largest industrial merger in history, exceeding the $54 billion acquisition of Amoco by British Petroleum. Exxon-Mobil Corporation would have a combined 1998 revenue of $170 billion.

It would create the largest non-state-owned integrated oil and gas company in the world. It would have a market capitalization of over $240 billion. The new company will have a work force of 122,700. Approximately 40 percent of which would be based in the United States.

A very important fact is that this merger, if approved, is just one of several energy mergers that have been announced or completed in the last 2 years. Because of the size and scope of the transaction, it is important that this subcommittee, which has jurisdiction over the oil and gas industry in the United States, find out more about this merger, what is driving it, and its impact on consumers.

This is not a confrontational hearing. It probably could be said that it's not even controversial. But it is an important hearing because, if there is a problem in this merger, it needs to be put before the American people. It would be irresponsible of this subcommittee and the full committee, which has jurisdiction for the House of

Representatives, to not assure ourselves and the American public that consumers at a minimum will not be harmed and, hopefully, will benefit from the merger, again, if it's approved.

It's important to put this merger into context. The major integrated oil companies are operating in an increasingly competitive and an increasingly global marketplace. As we speak, world oil prices have languished at record lows for several months. Every oil company, large or small, is looking for ways to cut costs, eliminate duplication, and increase efficiency.

New international opportunities for oil exploration and production require ever larger capital and resources in order to compete for these new sources of oil and gas. When we look at the globalization of the oil market, mergers such as Exxon-Mobil appear to be a natural way of life.

While we say that and while we can appreciate the market factors that drive such a merger, we must assure ourselves that they do not have anticompetitive impacts for the American consumer. Service station dealers, jobbers, and independent refiners have raised concerns about certain aspects of the merger. None of the parties have argued that the merger should not go forward, but all believe steps may need to be taken to assure that their subsets of the oil industry do not get harmed in the interim.

We will hear from those witnesses or representatives of those witnesses tomorrow. Today we are going to hear from the Federal Trade Commission, the Energy Information Administration, and the Securities and Exchange Commission about how they look at mergers in general and the impact of these mergers. I hope today's testimony will create a framework for us to ask questions of the companies' representatives tomorrow and the other interested parties tomorrow that will appear before this subcommittee.

I want to note that today's hearing will just be the first of a number of hearings the subcommittee intends to undertake on the domestic oil and gas industry.

Today's low oil prices may pose a risk to our national energy security because, if they continue, they will discourage domestic production, domestic exploration, and threaten to make the independent oil and gas producer a thing of the past.

The United States is now dependant for over 50 percent of its oil from foreign sources and that dependance is likely to grow if today's low oil prices persist. This is an issue that should be addressed and will be addressed by this subcommittee.

I want to welcome our witnesses today. We look forward to your testimony. I am sure that we will find it very informative.

I would like to recognize Mr. Bliley, the chairman of the full committee, for an opening statement.

Chairman BLILEY. Thank you, Mr. Chairman, and I would like to commend you for holding this timely hearing on the merger between Exxon and Mobil, two of our Nation's largest integrated oil companies.

I think this hearing is timely because it gives us an opportunity to explore not only what is happening in the oil industry, but what is happening in the larger energy industry as it becomes more competitive.

The past 2 years have been record-breaking in terms of the number and size of mergers being announced and completed across the energy industry. Oil companies are merging with oil companies like the recently completed British Petroleum-Amoco merger. Electric companies are merging with electric companies as in the American Electric Power Central and Southwest proposal. Electric and gas companies are merging with each other as in the recently announced acquisition of CNG by Dominion Resources. Importantly, everyone thinks this trend will continue.

So I believe it is important that we take a look at these mergers, what is driving them, and how they will impact consumers and U.S. global competitiveness. It is clear in the global economy in which business now operates that they must be as efficient as possible. Some of these companies clearly believe being efficient also means being big, but this is not necessarily bad.

As a general rule that efficiency benefits consumers as they see lower prices in the goods they purchase. Consumers also benefit because companies focus more on customer service and adding value for their customers. The consumer benefits of competition is, in fact, the reason why I support customer choice for electricity. However, mergers can become harmful when companies use their size or market power to restrict competition.

Today the Federal Trade Commission will tell us about some of the things we should look at in evaluating whether a merger is benign or harmful. Tomorrow we will hear from Exxon and Mobil and other interested parties about how this merger, in particular, stacks up against the FTC's standards.

While I think it is important that we look closely at these mergers, I do not start, as some do, from the assumption that all mergers are bad. I believe each needs to be judged on its own merits.

Again, Mr. Chairman, I commend you for holding this hearing. I look forward to hearing the testimony of the witnesses as well. Thank you very much.

Mr. BARTON. I thank the full committee chairman. We would now recognize the distinguished senior member from Massachusetts, Mr. Markey, for an opening statement.

Mr. MARKEY. Thank you, Mr. Chairman, very much, and I would like to begin by commending you for holding the first of two oversight hearings on this proposed merger of Exxon and Mobil. I think it is altogether appropriate that we have created this winter wonderland outside as a nostalgia day, remembering what winters used to be like in the United States when oil companies were really big and supply was limited and $30-a-barrel oil escalating up to $90-a-barrel oil was predicted. It is kind of like a nostalgia day here, remembering the way it used to be and oil companies as a result are going to come in and argue that they should be able to merge, to deal with this pressing issue of the fact that we don't have winters any longer.

But, of course, the fact that we don't have winters any longer doesn't have anything to do with the greenhouse effect, either, they will testify. So we will leave that as kind of a mystery to be resolved at another hearing unrelated to this one.

The merger of Exxon, our Nation's largest domestic oil company, and Mobil, the Nation's second largest domestic oil company, would

represent the largest industrial merger in history. Exxon's buyout of Mobil in a nearly $80 billion stock deal dwarfs BP's $54 billion acquisition of Amoco and would create the world's largest private corporation.

It has been said that current trends in the domestic and global oil and gas markets, persistent low prices, and increased exploration and production costs are driving the current trend toward concentration in the oil industry. The recent wave of mergers, we are told, has been driven by the need to achieve the savings and the synergies made possible by combining assets and resources.

All of this may be true and there may be a compelling business and economic rationale for a consolidation in the oil industry, but a transaction of this size and scope clearly merits very serious scrutiny by our Nation's antitrust regulators. For in allowing Exxon and Mobil to merge, we must carefully guard against recreating Standard Oil, one of our Nation's most notorious monopolies.

In 1911 the courts approved the breakup of John D. Rockefeller's giant monopoly into 34 independent companies. We have now seen BP, the acquirer of Standard Oil of Ohio, the original Rockefeller company, take over Amoco, the successor to Standard Oil of Indiana. Now we have before us a proposal to merge Exxon, the successor to Standard Oil of New Jersey, with Mobil, the successor to Standard Oil of New York.

If we allow these mergers to proceed without assuring that appropriate safeguards are established that protect against anticompetitive actions, including requiring divestiture of assets, where appropriate, consumers may find that the synergies and efficiencies resulting from these deals amount to little more than higher prices at the gas pump.

So while I am very sympathetic to the notion that the consolidation in the industry that the Exxon-Mobil represents may make a great deal of sense in order to facilitate more efficient exploration and production, I believe it is absolutely essential for the FTC to look very carefully at the impact of the proposed merger on regional wholesale and retail markets in the United States.

During today's hearing I will be particularly interested in hearing whether the FTC plans to look at market concentrations in the Northeast, and whether it intends to move aggressively to address any potential anticompetitive effects on our markets.

I thank you, Mr. Chairman, for calling this hearing and I look forward to the testimony from our witnesses.

Mr. BARTON. I thank the gentleman from Massachusetts. I personally don't remember $90-a-barrel oil but maybe we had it for half a day in Massachusetts——

Mr. MARKEY. Would the gentleman yield?

Mr. BARTON. [continuing] and I just missed that.

Mr. MARKEY. Would the gentleman yield?

Mr. BARTON. I will be happy to yield.

Mr. MARKEY. The nuclear utility executives who ordered 200 nuclear power plants in the 1970's premised upon $90-a-barrel oil. At this time they remember it because they no longer——

Mr. BARTON. Oh, "premised upon." I am glad for that clarification. I am glad for that clarification. I do remember $14 an MCF

natural gas. Those were the good old days in the natural gas market.

I would now recognize the distinguished ranking member from Texas, Ralph Hall, for an opening statement.

Mr. HALL. You go back to talking about 5 cent cotton while you are getting into there that I remember and I think we just charged those folks around Boston that 90 bucks a barrel.

I thank the chairman for convening these hearing. I think, of course, it is important that we do so. All of us, I suppose, have emotions. I can't say that they are even mixed emotions, but I think the enormity of it requires the hearing that the chairman has called, and I thank you for calling it.

I have pretty much of an open mind on it. It probably would be very good for stockholders, for employees, and may not raise significant competitive issues or at least none that can't be resolved before the deal is done.

I am extraordinarily interested in the factors that drive this merger. Certainly one of them has to be the historic low oil prices. Never have I seen the concern in my district—and, yes, the fear in my district—shown by the leaders of the independent petroleum industry there in Texas. I have the oil patch in my district, Tyler, Longview, Bladewater, Kilgore in that area.

A viable domestic onshore petroleum industry represents a very best defense that we could have against the possibility of skyrocketing oil prices in the future. Yet, producers are leaving the business daily, and the associated businesses that provide the infrastructure for producers really is melting away. It is atrophying away.

What we don't realize is that the same infrastructure that supports oil producers also supports the continued exploration and development of natural gas reserves in the country. This administration and industrial America has bet an awful lot on the continued availability of natural gas at reasonable prices, and I know we had the Fuel Use Act in the late 1980's. I think that was Mr. Carter's, and it was passed on the basis that we were out of natural gas. Of course, that was not true. What we were out of was out of incentive to look for it and reward for finding it.

I think if the producers and the infrastructure that's required to get natural gas out of the ground and deliver it to where it is consumed, if that disappears, then I really fear that the country is in for a rude awakening when, and not if, the prices for these products sudden spike upward.

I guess like a lot of other people, like the current low prices at the pump, but I realize that the consequences for huge economic disruptions when prices rise sharply, they rise sharply upward, could be very great, indeed.

So I hope, Mr. Chairman, with your cooperation, to actually review this proposed merger, we will convene some more hearings to take a serious look at the causes and effects of unstable and fluctuating oil prices.

We probably need to make a Paul Revere's ride through the country and begin to warn people, particularly in the non-producing States, those 40 States that use energy and don't produce any

of it, that they, too, need to join with us now to help dampen the effects of future price spikes.

In closing, Mr. Chairman, I welcome our witnesses here today and I thank you for the time you give us here today and the time it has taken to get ready to come with us. We need to understand better the criteria by which these present-day mega-mergers are being judged. Yours in not an easy job and we appreciate what you do to protect the public interest.

With that, Mr. Chairman, I yield back the balance of my time.

Mr. BARTON. I thank the gentleman from Rockwell and say that the subcommittee could not have a better member who knows more about the oil and gas industry at this point in time than Mr. Hall.

I would recognize the gentleman from California, Mr. Rogan, for a brief opening statement.

Mr. ROGAN. Mr. Chairman, thank you. I thank you for calling this hearing. I ask unanimous consent to allow my opening statement be made a part of the record.

Mr. BARTON. Without objection.

Mr. ROGAN. Thank you. I yield back.

[The prepared statement of Hon. James Rogan follows:]

PREPARED STATEMENT OF HON. JAMES ROGAN, A REPRESENTATIVE IN CONGRESS FROM THE STATE OF CALIFORNIA

I thank the Chairman for holding this hearing today. And I thank the panel for being here to discuss the largest merger in history. I am glad to have the opportunity to learn directly from them how this transaction will impact business owners and consumers in California.

As we hear your testimony, it is my hope that we can all concentrate on the primary focus for the hearing: The merger of the Exxon Corporation and the Mobil Corporation.

Some may have interest in discussing legislation and policies that may impact the companies in this merger, but not the merger itself. It would be refreshing, Mr. Chairman, if we all could pledge to keep our eye on the ball today and tomorrow.

One issue I hope the witnesses will discuss concerns the fact that we have an outflow of oil in California. As you know, given this condition, it is a challenge for independent refiners in the Golden State to acquire crude oil to refine.

Many refiners in California are concerned that the Exxon/Mobil Merger will generate such a strong upstream demand for oil that the smaller refiners will be negatively impacted.

I am eager to hear how this problem for our small refiners can be mitigated. The Exxon/Mobil merger is an exciting byproduct of a healthy global economy. I am pleased to have the opportunity to learn of the good things to come from this merger, and look forward to Teaming more about how our interests in California will be enhanced by this merger.

Mr. BARTON. Is that the only statement you wish to make at this point in time.

Mr. ROGAN. Just unless you are inviting further commentary.

Mr. BARTON. No, no, no. I am just giving you an opportunity.

Mr. ROGAN. Mr. Chairman, as we say back home, that will do it.

Mr. BARTON. I recognize the gentleman from Ohio, Mr. Sawyer, for an opening statement.

Mr. SAWYER. Thank you, Mr. Chairman, and I thank you and our witnesses for your attention to this issue today.

I do not have an extended opening statement, but I would just like to make an observation and that is that I come from Akron, Ohio. I represent a community that has been known by its signature industry, the tire and rubber industry, for the largest part of this century.

In recent years we have seen exactly the same kind of phenomenon globally in the tire industry that we are seeing evidenced here in the hydrocarbon industry. It is probably only coincidental that the rubber industry is a heavy user of hydrocarbon feedstocks in the production of synthetic rubber.

But it is remarkable to me, and I think to most Americans, when they realize that, despite the enormous number of brand names, that the actual number of producers globally in the tire industry, the major producers are probably just about four with most other producers affiliated, with those four major producers, and only one real American producer of any size. Fortunately, that American producer is very powerful in the market and is a strong provider of portable products.

Our only concern at this point is to assure that we have the same kind of capacity to provide for American consumers and the capacity to have access to global resources in an industry where the competition for those resources is fierce. The capacity to market into this country is every bit as important as the ability of those who are domiciled here to be able to have a substantial portion of that market.

With that, Mr. Chairman, I yield back the balance of my time and look forward to the testimony both today and tomorrow.

Mr. BARTON. I thank the gentleman from Ohio. The Chair would recognize the gentleman from Illinois, Mr. Shimkus, for an opening statement.

Mr. SHIMKUS. Thank you, Mr. Chairman. I am going to be following these hearings the next 2 days very closely, focusing on the consumers of this Nation, the station owners, small independent producers of oil.

As many people may know, Illinois is the 11th largest oil-producing State and the two largest fields are in my district.

I have two primary concerns with the low prices today, and that is the decision that many of these marginal oil producers are making in going out of business, which obviously affects my district just as a means of production and employment.

But the second issue that I have been trying to trumpet since becoming a Member of Congress is energy security of our Nation. I think these marginal wells play an important role in energy security, and my question will be—and I will try to listen to answers—how is this merger going to affect our energy security as a Nation?

With that, Mr. Chairman, I appreciate you taking time for these hearings and I yield back the balance of my time.

Mr. BARTON. The Chair is going to recognize the gentlelady from New Mexico for a brief opening statement and then we will come to the gentleman from New York.

Mrs. WILSON. Mr. Chairman, in the interest of time, I will ask unanimous consent that my opening statement be put in the record.

Mr. BARTON. I thank the gentlelady. Does the distinguished gentleman from New York wish to make a brief opening statement? Not at this time, all right. The gentleman from Tennessee, Mr. Bryant.

Mr. BRYANT. I thank the chairman for calling this hearing and I thank the very distinguished panel that we have before us today.

I look forward to hearing their testimony and also reading their statements, and with that, I will also pass.

Mr. BARTON. Does the gentlelady from Missouri, Ms. McCarthy, wish to make a brief opening statement?

Ms. MCCARTHY. Thank you very much, Mr. Chairman, no, not at this time.

Mr. BARTON. All members being present and having been given the opportunity to make an opening statement, for all members not present we ask unanimous consent that they be given the requisite number of days to put their statement into the record.

Hearing no objection, so ordered.

[Additional statement submitted for the record follows:]

PREPARED STATEMENT OF HON. CLIFF STEARNS, A REPRESENTATIVE IN CONGRESS FROM THE STATE OF FLORIDA

Thank you, Mr. Chairman. I appreciate this opportunity to learn more about the Exxon-Mobil merger. As a member of this Subcommittee, my interests regarding this merger lie in the areas of national energy policy, impact on consumers, and interstate commerce.

I understand that, if we were here 20 years ago having this discussion, a merger between Exxon and Mobil would have been nearly impossible. It would have been much more difficult due to the companies' larger global market share. However, with the nationalization of crude-producing assets and the growth of state-owned oil companies, major oil companies were reduced.

Thus, the present Exxon and Mobil combined production accounts for less than 4 percent of the world production, and a merger between these two companies is now possible.

Exxon and Mobil seem to be following a trend in the industry of consolidation—recently, we saw the merger of BP and Amoco. However, despite their reduced production, these two companies will still produce the largest industrial merger ever and will create the largest private oil company worldwide.

With such a large merger, the implications for our national energy policy, consumers, and interstate commerce are not immediately clear. How will our panel members, in their various capacities, evaluate the merger with respect to these areas? I look forward to learning the opinions of our panel members today, as they speak on behalf of the FTC, the SEC, and DOE. Thank you.

Mr. BARTON. The Chair now wishes to recognize our panel for the opening of today's hearing. It is a distinguished panel. Representing the Federal Trade Commission we have Mr. William Baer, who is the Director of the Bureau of Competition; representing the Energy Information Administration we have the Administrator, the Honorable Jay Hakes; is that correct?

Mr. HAKES. Yes, sir.

Mr. BARTON. And representing the Securities and Exchange Commission we have Mr. Michael McAlevey; is that correct?

Mr. MCALEVEY. "McAlevey."

Mr. BARTON. McAlevey, who is the Deputy Director of the Division Corporate Finance.

We are going to recognize Mr. Baer, and because this is the only panel that we have today we will recognize each of you gentleman for as much time as you may consume. We will put your entire written statements into the record and then at the conclusion of your oral testimony we will have a question period.

So the Chair is glad to welcome Mr. William Baer for his statement.

STATEMENTS OF WILLIAM J. BAER, DIRECTOR, BUREAU OF COMPETITION, FEDERAL TRADE COMMISSION; JAY HAKES, ADMINISTRATOR, ENERGY INFORMATION ADMINISTRATION, DEPARTMENT OF ENERGY; AND MICHAEL MCALEVEY, DEPUTY DIRECTOR, DIVISION OF CORPORATE FINANCE, SECURITIES AND EXCHANGE COMMISSION

Mr. BAER. Thank you, Mr. Chairman. Good morning and good morning to members of the subcommittee.

We appreciate the opportunity to appear to discuss the FTC's role in enforcing the antitrust laws to make sure that consumers of petroleum products are fully protected.

We at the agency appreciate that a viable and competitive energy sector is vitally important to the economic health of the United States and to the world. At the same time, our job at the FTC is to make sure that consolidations in the energy field do not put consumers at risk of higher prices, namely, paying more for gasoline at the pump and other fuels, and the consequent harm that those higher prices would cause to our economy, both specific regions of the economy and the Nation as a whole.

Mr. Chairman, as you noted, this merger, the largest industrial merger ever, creates the largest private oil company worldwide and the largest U.S.-based company of any type on the basis of its revenues.

Today, Mobil and Exxon face each other at just about every level of the industry, exploration and production of crude, refining of crude into petroleum products, manufacture of petrochemicals and lubricants, and the transportation and marketing of gasoline and other fuels in many parts of the United States, in particular the Northeast, the Gulf Coast, and California. Exxon and Mobil combined would likely be the largest or one of the largest players in each of these sectors of the American economy.

Obviously, a transaction of this size alone merits our attention. As antitrust enforcers, we need to consider whether Exxon-Mobil's size, or other attributes, will somehow change for the worse the competitive dynamics of the industry.

While I cannot comment in any detail on the specifics of a pending non-public law enforcement investigation, I can, by referring to what we have done in the past, give you some sense of the process the FTC follows and the issues that are likely to be important to us as we examine the Exxon-Mobil transaction.

As I noted, this merger doesn't occur in a vacuum, but appears to be part of an ongoing trend of consolidation and concentration in the industry. In recent months we have seen the merger of British Petroleum and Amoco, until now the largest industrial merger in history, and the combination of the refining and marketing businesses a year or so ago of Shell, Texaco, and Star Enterprises. That created the largest refiner and marketer of petroleum products in the United States. Other transactions are either proposed, as the chairman indicated, or rumored to be on the drawing boards.

Our job at the FTC is to review these transactions carefully and where appropriate to intervene to prevent the merger from significantly reducing competition in any sector of the industry that affects the U.S. or its citizens. This is the basic goal of antitrust and it is particularly vital with respect to the petroleum industry,

where even very small prices increases can have a direct and lasting impact on the entire economy.

Now in the past we have looked at a number of mergers and sought relief where we thought it appropriate. In the British Petroleum-Amoco deal, which was consummated earlier this year, we preserved local competition in 30 retail markets across the United States by requiring divestiture of retail business and also terminals, the terminals that supply the retail outlets.

A little over a year ago in the Shell-Texaco joint venture we worked to protect competition in the western part of the United States, where we were concerned with an undue concentration the joint venture would have, an undue market share they would have at the refining level. We remedied that by insisting that the parties, as a condition of merging, divest a refinery in Washington State, a refinery that served the northwestern part of the United States, as well as making CARB II gasoline, the specially formulated gasoline that is sold uniquely in California.

We also were concerned about transportation of refined product from the Gulf Coast up to the East Coast along the Colonial and Plantation pipelines and required divestiture of interests there to make sure that those pipelines continued to compete aggressively with each other to offer as low a tariff as possible for the transportation of refined product.

We also were concerned that the transaction would adversely affect consumers in local markets in California, particularly San Diego, as well as in Hawaii, and required divestitures there as well.

In recent years we've also seen smaller deals like Shell and Exxon's proposed merger of assets in Guam. A company called PRI and Shell in Hawaii also proposed to consolidate their assets. We threatened to go to court to enjoin those transactions because we could not see any legitimate pro-competitive functions served by them and saw considerable risks to consumers as well. Both transactions were abandoned.

Now how do we go about doing our job? What do we look at when we are confronted with a transaction? One thing we look at is the trend toward concentration in an industry. Where we find evidence that an industry is consolidating, i.e., there are fewer players, the risk to consumers that those fewer players will behave anticompetitively over time grows. We also want to know whether the merger will yield efficiencies that might counteract the anticompetitive effects the merger would otherwise threaten.

Just claiming cost savings is not enough to allow an anticompetitive merger. So cost savings must be real; they must be substantial. They should not result from reductions in input and they must counteract the merger's anticompetitive effect, not merely be cost savings that flow to the shareholders' bottom line and result in higher consumer prices.

Now where we find problems, we do not, as I have indicated, automatically seek to block a transaction. Where we can isolate the problem, as we did in the Shell-Texaco merger and in other mergers, we seek to require divestiture of the assets, assets sufficient to restore the status quo-ante, to ensure that competition remains healthy in the sectors of the economy where we thought there could

be a problem. But where we have an anticompetitive concern that infects so much of the deal that there's no practical way of working out a negotiated solution, we go to court and ask the court to enjoin the transaction.

In the petroleum industry we do our job by looking at each level of production separately, from exploration and production down to refining, and finally, to local markets. In the exploration and production sector upstream we observe that the crude oil market is for most purposes worldwide, and we recognize that there have been some major changes since the 1970's with lots of producing nations being more of a significant factor in the marketplace than they had been at the time of the Arab oil embargo.

And we have not, in reviewing prior transactions, found problems of undue concentration at the exploration and production level. That doesn't necessarily mean that further consolidation is harmless, but it does mean that we need to look carefully and cautiously at that aspect of this proposed transaction.

Refining is the second sector we look at closely, and that has been an area where we have had concerns in various parts of the county over time. The Nation's principal refining market, the Gulf Coast, not only serves that immediate area, but sends substantial amounts of its product by pipeline to the Midwest, to the Southeast, and the Northeast, and it is vitally important for nearly all of the country east of the Mississippi to maintain a competitive Gulf Coast market.

The two firms, Exxon and Mobil, have considerable refining capacity in the Gulf Coast, and we need to look at whether combining those assets potentially puts consumers at risk. If you go west of the Rockies, there are fewer refineries and less competition and, not surprisingly, there tends to be higher prices for gasoline and other fuels west of the Rockies. That's why in the Shell-Texaco matter we required divestiture of a significant refinery in the Pacific Northwest to make sure that there would be remaining competition for the Shell-Texaco joint venture and the other firms operating in the northwestern United States.

California refining markets are an area of concern to the Commission. Mr. Hakes of the Energy Information Administration has studied the supply situations in California, where the market is so concentrated that even a little bit of a change in supply can have a significant affect on prices.

According to press reports, there was a terrible fire at Tosco's Avon refinery last month. That refinery only provided 6 percent of California's product, but having that refinery out of business for a short while raised prices 30 percent.

So while a fire taking a refinery out, is an act of God, doesn't raise antitrust concerns, the ability of firms in a concentrated market to take a little bit of capacity out of the market and drive prices up is the sort of thing we look at carefully in performing our antitrust analysis.

Gasoline marketing is another area of concern. On several occasions we blocked mergers or required divestitures where we thought there was going to be undue concentration at the marketing level. We are concerned not only that one firm might be a near monopolist in a local market, but in places like San Diego even re-

ducing the number of firms from 6 to 5 or 5 to 4 can cause a reduction in the intensity of price competition and allow prices to be higher than they otherwise would, and that is why, in looking at the Shell-Texaco joint venture, the Commission ordered divestiture of a substantial number of retail gas stations in California.

Mr. Chairman, what we have learned from our investigations is that competition is critical to this industry and that concentration, as well as increases in concentration, can have serious adverse affects on competition.

We are at a very early stage in our investigation of the Exxon-Mobil merger. We have made no conclusions about the nature and extent of any problems we might find. The attorneys general of many States are highly interested in this deal. We are working closely with them as well as with our counterparts overseas.

I can assure you, sir, that the Commission will do its job as thoroughly and as expeditiously as we can. We have received pledges of full cooperation from both Exxon, and Mobil and we intend to rely on those pledges in making sure we get our job done right and done quickly.

Thank you, Mr. Chairman.

[The prepared statement of William J. Baer follows:]

PREPARED STATEMENT OF STATEMENT OF WILLIAM J. BAER, DIRECTOR, BUREAU OF COMPETITION,[1] FEDERAL TRADE COMMISSION

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

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

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

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

As many have noted, this merger does not occur in a vacuum, but appears to be part of an ongoing trend of consolidation and concentration in this industry. In recent months, we have seen the merger of BP and Amoco—which was the largest

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

industrial merger in history until Exxon/Mobil was announced—and the combination of the refining and marketing businesses of Shell, Texaco and Star Enterprises to create the largest refining and marketing company in the United States. In addition, Tosco acquired Unocal's California refineries and marketing business; Ultramar Diamond Shamrock acquired Total's North American refining and marketing operations; and Marathon and Ashland combined their refining and marketing businesses. We also have seen the worldwide combination of the additives businesses of Shell and Exxon. Other combinations, such as the pending combination of the refining and marketing businesses of Ultramar Diamond Shamrock and Phillips (which we are currently examining), likely will follow. These consolidations and joint ventures are not limited to the United States: BP and Mobil have combined their refining and marketing operations in Europe, and Total and Petrofina have recently announced their own merger plans.

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

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

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

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

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

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

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

tated to seek to block mergers, in this industry and elsewhere, where other remedies were insufficient.[4]

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

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

Refining. Mergers involving oil refineries have long been a matter of intense interest to the Commission. The nation's principal refining market, the Gulf Coast, not only supplies that immediate area, but also sends substantial amounts of gasoline by pipeline to the southeast, the northeast and the midwest. It is vitally important for nearly all of this country east of the Mississippi to maintain a competitive Gulf Coast refining market. Similarly, we must ensure that the pipelines that deliver Gulf Coast product to these markets remain competitive. In the 1980s, the Commission acted to preserve competition in Gulf Coast refining in connection with Standard of California's merger with Gulf by requiring the divestiture of a Louisiana refinery and an interest in the Colonial Pipeline, one of the two pipelines that carries gasoline and other fuels from the Gulf Coast to southeastern and northeastern markets. When Shell and Texaco combined their refining and marketing arrangements, the Commission required a similar pipeline divestiture.[7]

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

Thank you.

Mr. BARTON. We have two 15-minute votes pending on the floor. We have a 15-minute journal vote and then there's a 15-minute recorded vote. We are going to have to take a recess.

So my question to Mr. Hakes, is your oral statement less than about 10 minutes? If it's less than 10 minutes, we will hear you right now. If it's more than 10 minutes, we will go vote and hear you in about 35 minutes.

Mr. HAKES. My schedule is flexible, but I think it is less than 10 minutes.

Mr. BARTON. Then if you would proceed, and then at the conclusion of your oral statement we will take a recess to go vote.

STATEMENT OF JAY HAKES

Mr. HAKES. Thank you, Mr. Chairman, and members of the committee. I am pleased to testify today on the proposed merger of the Exxon and Mobil Oil companies.

The Energy Information Administration cannot answer all the questions affecting the wisdom of this merger, and I am glad that the Federal Trade Commission and the Security and Exchange Commission are also here at today's testimony. But I think our agency does have some relevant data that can assist the subcommittee and others in their deliberations.

What I would like to do is start by talking about the global ramifications. It may be helpful to start with the role of major oil companies in the global production of oil.

As figure 1 in my testimony shows, the picture has changed dramatically since the early 1970's, and you can seen before you a color version of that graphic. In the early 1970's many major oil-producing countries nationalized many of the assets of private oil companies. The results of this action can been seen in table 1 and figure 1.

In the early 1970's many major oil-producing countries nationalized many of the assets of private oil companies. The results of this action can be seen in table 1 and figure 1 of my testimony.

In 1972 Exxon was still the world's largest oil-producing company and Mobil ranked seventh. Together they accounted for about 16 percent of world oil production.

You can see there, the orange part of that pie reflecting 1972, national oil companies were only 6 percent of the world situation. Exxon alone was almost twice as much as those national oil companies.

But if we turn over to the pie graph on the right side we see a different situation. The five largest companies in oil production in 1997 were the national companies of Saudi Arabia, Iran, Venezuela, Mexico, and China, each larger than a combined Exxon and Mobil.

The share of world oil production coming from these two majors had dropped from 16 percent down to 4 percent. By 1997, despite an expansion of the world's oil markets, the combined production of Exxon-Mobil was less than Mobil alone in 1972. Of course, what is clear from the graphic is the orange part has expanded dramatically from 6 percent to 52 percent.

The nationalization of a major share of world oil production tended to leave the major private companies with areas of high-cost production. As a result of this development and a competitive market, there has been great emphasis in the industry on lowering costs. Adoption of new technologies, restructuring, and downsizing have been important parts of this process.

As seen in figure 2 of my testimony, the major oil companies dropped about 60 percent of their employees worldwide from 1980 to 1997. Although the decline seemed to have slowed in 1997, the low oil prices of 1998 may accelerate the descent again. Announced cutbacks resulting from the Exxon-Mobil merger are estimated to be about 9,000 people. With or without the merger, there will likely be a continuation of downsizing pressures in all areas of energy production and generation.

Now I would like to turn to refining and marketing. Major oil companies do a lot more than produce oil, and consumers may be more concerned about their activities downstream in areas such as refining and marketing.

A merger of these activities could raise competitive concerns. These will be addressed by other Federal agencies. EIA does, however, collect data that will be relevant for any investigation.

In the United States the major oil companies have been shifting out of the refining, and in 1997 they accounted for less than 60 percent of the capacity, as independent refiners and foreign producing countries have grown in importance. In 1997 Exxon and Mobil together controlled about 12 percent of U.S. refining capacity.

As table 2 of my testimony indicates, there is considerable regional variation, however, in the extent to which refining by Exxon and Mobil overlap. The overlap is largest in the Gulf Coast region, by far the largest of the refining regions. Their share of refining in the Gulf Coast would constitute about 18 percent.

In 1997 Mobil and Exxon together controlled about 9 percent of U.S. branded retail stations. Again, however, there are regional differences in overlap, as can be seen in figure 3, which we also have with us upfront.

In the States of the Northeast marketing area, there is a green area here that sort of stops at Pennsylvania and West Virginia, where it turns into dark blue, and all the way up to Maine, absent Rhode Island. All those States are over 15 percent Exxon-Mobil stations.

Mr. BARTON. What year is that? Is that 1998 or 1997?

Mr. HAKES. That's 1997.

Mr. BARTON. 1997?

Mr. HAKES. 1997, and within those individual States it ranges from about 14 percent in Rhode Island to as high as 35 percent in some jurisdictions. Elsewhere in the country, once you get outside of that dark blue area into the rest of the country, the share ranges from zero percent in some States to 14 percent.

In conclusion, I would be glad to furnish any additional data requested by the committee. I have also been testifying before other committees on the causes of low oil prices. So I would be glad to answer questions on that and certainly any questions that the members have this morning.

[The prepared statement of Jay Hakes follows:]

PREPARED STATEMENT OF JAY HAKES, ADMINISTRATOR, ENERGY INFORMATION ADMINISTRATION, DEPARTMENT OF ENERGY

I wish to thank the Committee for the opportunity to testify today on impacts of the proposed merger between Exxon and Mobil. As Administrator for the Energy Information Administration (EIA), which is an independent analytical and statistical agency within the Department of Energy, I will focus on the business environment leading up to the BP-Amoco and Exxon-Mobil merger announcements and highlight several areas where large overlap of operations occur.

Exxon-Mobil Merger Recombines Two Standard Oil Spin-Offs

Exxon and Mobil were two of the seven largest companies that were spun off from the Standard Oil Company breakup by the Supreme Court in 1911. The seven companies are known today as Exxon, ARCO, Conoco, Amoco, Mobil, Chevron, and BP America.

Prior to the Arab Oil Embargo in 1973, mergers between British Petroleum and Amoco and between Exxon and Mobil would have been unthinkable due to the sheer sizes of these entities in the global market (Figure 1). In the upstream or exploration and production business segment, Exxon ranked first in world production, supplying almost 11 percent of the world's crude oil. Mobil ranked seventh and produced about 5 percent of the world's oil supply. Had BP-Amoco and Exxon-Mobil merged in 1972, the two resulting organizations would have controlled almost 28 percent of world oil production.

Up until the early 1970's, virtually all non-communist areas in the world had been open to U.S. major oil companies.[1] But in the late 1960's and early 1970's, many of the major oil companies' producing assets abroad were nationalized, and state-owned oil companies were formed to carry on the production. Private oil companies not only lost assets, but also access to some of the world's lowest-cost producing areas. North America and Europe are high-cost regions in which to explore and produce.

In 1997, state-owned or national oil companies represented the world's top 6 producers. Exxon ranked number 7 with 2.4 percent of the world's production (1.6 million barrels per day), and Mobil was down to number 18, producing only 1.4 percent (0.9 million barrels per day) of the world's supply (Table 1). The combined production of both Exxon and Mobil (2.5 million barrels per day) is only slightly more than Mobil's crude oil production was alone in 1972 (2.3 million barrels per day).

Exxon and Mobil combined share of world oil reserves is much smaller than their share of production, since a very large share of the world's reserves lie outside of the private sector in the Middle East. In 1997, the two companies accounted for 1

[1] Major oil companies are the U.S.-based companies required to report to EIA's Financial Reporting System (FRS). Included U.S. companies must be among the top 50 worldwide oil producers and account for 1 percent or more of U.S. production or reserves of oil, gas, or coal, U.S. refinery capacity, or U.S. refined product sales. In 1997, 24 companies were included in the FRS.

percent of world reserves (10.7 billion barrels), down from about 2.6 percent in 1973. Their U.S. share of reserves in 1997 was just under 12 percent of total.

Strongly limited access to low-cost foreign areas continued until the time around the oil price collapse in 1986, when some countries again began to open to private investment. The new opportunities in these foreign areas have attracted oil company interest. Between the oil price drop in 1986 through 1997, more than 40 percent of the growth in exploration and development expenditures of the major oil companies has been in countries outside of North America and Europe. In spite of the majors refocusing in these foreign areas, over three-quarters of the majors' current oil and gas production is from relatively high-cost United States, Canadian, and North Sea properties.

Participation by the majors in world refining has also changed over the years, but to a lesser extent than exploration and production. Many more national oil companies own refining capacity now than 25 years ago. Today, 9 out of the largest 20 refiners are state-owned companies. In the United States, the major oil companies have been shifting out of refining, and in 1997 they accounted for less than 60 percent of capacity as independent refiners and foreign producing countries have grown in importance. Mobil and Exxon have also participated in this shift. In 1993, Exxon sold its Bayway, New Jersey, refinery to Tosco; in 1997, Mobil sold a 50 percent interest in its Chalmette, Louisiana, refinery to the Venezuelan state-owned company, PDVSA; and in 1998, Mobil sold its Paulsboro, New Jersey, refinery to Valero. In 1997, Exxon and Mobil together controlled almost 12 percent of U.S. refining capacity, and just under 9 percent of U.S. branded retail stations.

Average Performance and Low Oil Prices Drive Oil Company Actions in the 1980's and 1990's

Many U.S. major oil companies were already cutting costs and rationalizing after deregulation in 1981, but after the oil price drop in 1986, companies engaged in further cost cutting in an attempt to improve performance. Figure 2 shows evidence of the cost reductions in the steady loss of personnel from the major oil companies alone through the 1980's and 1990's. The majors dropped about 60 percent of their employees worldwide between 1980 and 1997. Although the decline seemed to have slowed in 1997, the low oil prices in 1998 may accelerate the descent again. The announced cutbacks resulting from both the Exxon-Mobil and BP-Amoco mergers amount to 15,000 people (9,000 from the Exxon-Mobil merger), which represents about 3 percent of the worldwide employees of the majors and about 1 percent of total oil industry employment in the United States.

The low prices since 1986 and pressure to improve performance have resulted in application of new technologies that have reduced costs both to produce oil and to add new reserves. In the downstream we have seen closure of many small inefficient refineries and a trend toward increasing volume throughput of gasoline stations to gain economies of scale. Refineries have changed hands, with the majors selling U.S. refineries to growing independent refiners as companies re-position themselves for growth in the future. We also have seen a number of joint ventures formed between U.S. refiners and producing countries that can provide the U.S. partner with additional financial resources and crude oil supply agreements. More recently, a wave of mergers, acquisitions, and alliances began, even before the most recent price decline.

Overlaps in Refining and Marketing Vary by Region

EIA data can provide information on areas in U.S. refining and marketing in which Exxon and Mobil overlap, but EIA does not make determinations about the competitive implications of these overlaps. Competitive issues arising from major oil company acquisitions are largely the responsibility of the Federal Trade Commission (FTC), and sometimes involve the Antitrust Division of the Department of Justice. EIA data may suggest where the FTC reviews are likely to be concentrating.

Table 2 shows that the U.S. areas in which Exxon and Mobil overlap in refining are on the West Coast (PADD 5) and the Gulf Coast (PADD 3). Gulf Coast refineries are the major supply sources for markets east of the Rocky Mountains. These refineries processed 56 percent of the crude oil used in PADDs 1 through 4 in 1997. While Exxon and Mobil account for less than 12 percent of U.S. capacity, they control 18 percent of the Gulf Coast capacity. This 18-percent share is comparable to the combined BP-Amoco share of refining capacity in the Midwest (PADD 2).

Exxon and Mobil are also strong players on the West Coast (PADD 5). The Exxon Benicia refinery serves the Northern California area, and the Mobil Torrance refinery serves the Los Angeles area. The refinery outputs may not pose a problem since refineries in northern and southern California tend to serve different regions. Furthermore, Equilon, the joint venture between Shell and Texaco, has about as much

capacity in PADD 5 (250 thousand barrels per calendar day) as do Exxon and Mobil combined. We have no data on local domestic crude purchasing issues.

Gasoline is the most visible petroleum product to consumers and is the focus of many concerns over the impacts of mergers. Figure 3 shows that Mobil and Exxon have the largest overlap in marketing areas in the Northeast. This figure is based on branded retail station counts, but it is consistent with the regional concentration of EIA volume sales data as well.

This concludes my testimony before the Subcommittee. I would be glad to answer any questions at this time.

Table 1. Worldwide Crude Oil Production of 20 Leading Companies, 1972 and 1997
(Thousand Barrels per Day)

1972			1997, pre-mergers			1997, post-mergers		
Company	Production	Percent of Worldwide Total	Company	Production	Percent of Worldwide Total	Company	Production	Percent of Worldwide Total
Exxon Corp	**4,968**	**10.8%**	Saudi Arabian Oil Co.	9,052	13.6%	Saudi Arabian Oil Co.	9,052	13.6%
British Petroleum	**4,664**	**10.1%**	National Iranian Oil Co.	3,755	5.7%	National Iranian Oil Co.	3,755	5.7%
Royal Dutch/Shell	**4,169**	**9.0%**	Petroleos de Venezuela	3,424	5.2%	Petroleos de Venezuela	3,424	5.2%
Texaco, Inc.	**3,777**	**8.2%**	Petroleos Mexicanos	3,410	5.1%	Petroleos Mexicanos	3,410	5.1%
Chevron Corp.	**3,232**	**7.0%**	China National Petroleum	2,884	4.3%	China National Petroleum	2,884	4.3%
Gulf Oil	**3,214**	**7.0%**	Kuwait Petroleum Corp.	1,976	3.0%	***Exxon Mobil***	***2,526***	***3.8%***
Mobil Corp	**2,316**	**5.0%**	**Exxon Corp.**	**1,599**	**2.4%**	Kuwait Petroleum Corp.	1,976	3.0%
Communist Bloc[a]	1,301	2.8%	Nigerian Nat'l Petroleum	1,417	2.1%	***BP Amoco***	***1,888***	***2.8%***
CFP (Total - France)	977	2.1%	**Royal Dutch/Shell**	**1,328**	**2.0%**	Nigerian National Petroleum	1,417	2.1%
Sonatrach (Algeria)	925	2.0%	Sonatrach (Algeria)	1,318	2.0%	**Royal Dutch/Shell**	**1,328**	**2.0%**
Amoco Corp	**815**	**1.8%**	Abu Dhabi National Oil Co.	1,310	2.0%	Sonatrach (Algeria)	1,318	2.0%
ARCO	**652**	**1.4%**	Libya National Oil Co.	1,259	1.9%	Abu Dhabi National Oil Co.	1,310	2.0%
DuPont (Conoco)	**594**	**1.3%**	**British Petroleum**	**1,251**	**1.9%**	Libya National Oil Co.	1,259	1.9%
USX Corp. (Marathon)	**453**	**1.0%**	Iraq National Oil Co.	1,248	1.9%	Iraq National Oil Co.	1,248	1.9%
Petroleos Mexicanos	440	1.0%	**Chevron Corp.**	**1,071**	**1.6%**	**Chevron Corp.**	**1,071**	**1.6%**
Occidental Petroleum	**443**	**1.0%**	Pertamina (Indonesia)	1,028	1.6%	Pertamina (Indonesia)	1,028	1.6%
Getty Oil	**443**	**1.0%**	Lukoil (Russia)	1,024	1.5%	Lukoil (Russia)	1,024	1.5%
Sun Co.	**369**	**0.8%**	**Mobil Corp.**	**927**	**1.4%**	Petrobras	916	1.4%
Unocal Corp	**365**	**0.8%**	Petrobras	916	1.4%	**Texaco Inc.**	**833**	**1.3%**
Phillips Petroleum	**337**	**0.7%**	**Texaco Inc.**	**833**	**1.3%**	Elf Aquitaine	795	1.2%
Top 20 Total	34,434	74.6%	**Top 20 Total**	41,030	61.9%	**Top 20 Total**	42,462	64.0%
Worldwide Total	46,170	100.0%	**Worldwide Total**	66,317	100.0%	**Worldwide Total**	66,317	100.0%

[a] For 1972, only non-Communist world oil production and Communist bloc (including China) exports to the non-communist world are included, while 1997 includes total world production. Sum of components may not equal totals due to indpendent rounding. Shares were calculated based on unrounded data.

Sources: Company data 1972: Jacoby, Neil H., *Multinational Oil* (New York, 1974, pp. 192-193) and company annual reports.

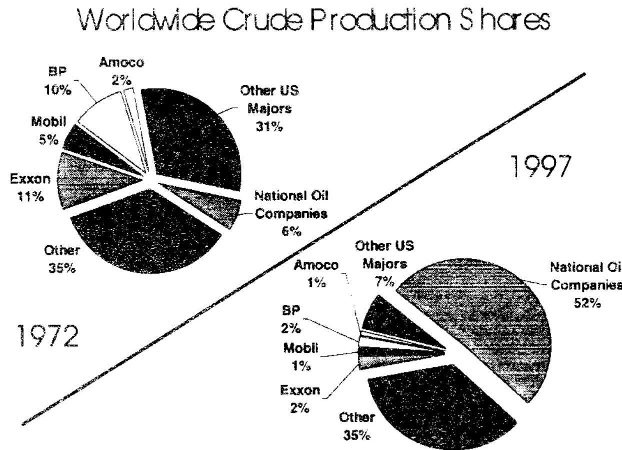
Table 2. Refining Capacity
(Thousand Barrels per Calendar Day)

	Exxon	Mobil	Combination of Exxon and Mobil	Total	Percent of Total
U.S. Refining Capacity					
Total U.S.	1,017	952	1,969	15,827	11.5
PADD 1		0	0	1,637	0.0
PADD 2		200	200	3,444	5.8
PADD 3	843	470	1,313	7,293	18.0
PADD 4	46		46	520	8.8
PADD 5	128	130	258	2,932	8.8
Foreign Refining Capacity					
Total Foreign	2,747	1,312	4,059	62,325	6.5
Europe	1,625	368	1,993	16,425	12.1
Asia-Pacific	642	751	1,393	17,595	7.9
Other	480	193	673	28,305	2.4

Note: PADD—Petroleum Administration for Defense Districts. Mobil's PADD 3 capacity includes the 50 percent interest of PDVSA in the Chalmette, LA refinery. Chalmette has 159 thousand-barrel-per-calendar day capacity.

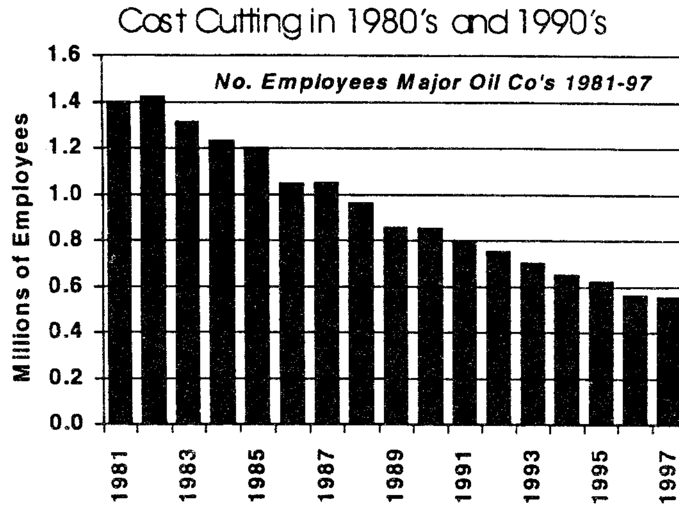
Sources: Company information: 1997 annual reports and statistical Supplements; U.S. totals: Energy Information Administration, **Petroleum Supply Annual 1996 Volume 1,** Tables 37 and 40, with Tosco Trainer and TransAmerican Norco refineries added; Foreign totals: British Petroleum, **BP Statistical Review of World Energy** (June 1998), p. 16.

Figure 1



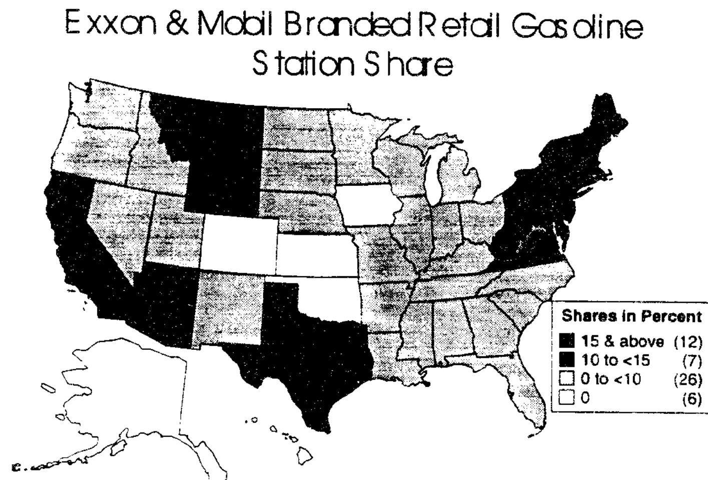
Source: Company data 1972: Jacoby, Neil H., *Multinational Oil* (New York. 1974, pp. 192-192) and company annual reports.

Figure 2



Source: Energy Information Administration, Financial Reporting System

Figure 3



Note: The numbers in parentheses are the numbers of states in each share category. The District of Columbia is also included.
Source: National Petroleum News, 1997 Data

Mr. BARTON. Thank you, Mr. Hakes. We are going to take a recess to go vote. We have this vote and then one other vote. I would think we could be back over here by about 11:10.

So the committee stands in recess until 11:10.

[Brief recess.]

Mr. BARTON. The subcommittee will reconvene, a quorum being present.

We now hear from our last witness for the day, Mr. McAlevey for such time as you may consume.

STATEMENT OF MICHAEL R. MCALEVEY

Mr. MCALEVEY. Mr. Chairman, members of the subcommittee, my name is Michael McAlevey. I am the Deputy Director of the Division of Corporation Finance at the Securities and Exchange Commission. I am pleased, on behalf of the Commission, to testify today.

While I recognize that the focus of this hearing is the proposed Exxon-Mobil merger, those companies have not publicly filed with the Commission a document soliciting shareholder approval of the deal. Consequently, my statement will discuss generally the SEC's role in regulating mergers of public companies and the procedures that we employ in reviewing merger filing.

The Federal Securities laws are designed to protect investors by requiring full and fair disclosure of all material information about publicly traded securities. Full disclosure ultimately benefits both investors and the capital markets. By enhancing investors' confidence in the completeness and accuracy of information about pubic companies, these full disclosure requirements encourage investor participation in the capital markets.

It is important to bear in mind that the Commission does not have the authority to approve or disapprove a security or transaction on its merits. Rather, the Commission's job is to ensure that the company fully discloses material information about a transaction or a security, so that investors can make informed investment decisions.

Ordinarily, when a company proposes to merge with another company, it is required to obtain shareholder approval of the transaction. If shareholder approval is required, the Federal security laws require a public company to deliver a proxy statement to its shareholders. This document discloses the material terms of the transaction to shareholders, so that they can make an informed decision when they vote on the transaction.

In addition, when a public company proposes to issue stock in a merger transaction, it must register the offer and sale of that stock under the Securities Act. The registration statement that covers that offer and sale includes a prospectus that discloses material information about both the companies and the proposed transaction.

Information about the transaction is always included in the prospectus itself. Information about the companies, however, may be incorporated by reference into the prospectus from the companies' Exchange Act reports if the companies meet certain requirements.

While the entire registration statement must be filed with the SEC and is publicly available, only the prospectus must be actually delivered to investors who will receive stock in the transaction. The

prospectus also serves as the proxy statement for the company's solicitation of shareholder approval of the transaction.

After drafting the proxy statement prospectus, the companies file it with the Commission. The proxy rules allow companies to file preliminary proxy statements relating to merger transactions confidentially, so that the proxy statement prospectus is not available to the public when it is initially filed.

The Commission's rationale, when it adopted this position, was that it wanted to allow companies to go through the review and comment process without prematurely disclosing confidential information to the market about merger transactions. The document only is made available to the public when the final proxy statement that will be delivered to shareholders is filed.

When a filing is made with the Commission, it is routed to the appropriate industry group for processing. We do not have sufficient resources to review all registration statements and other filings that are made with the Commission. Therefore, we use a selected review process by which we review some, but not all, of the filings that are made with the Commission.

A filing is screened to determine if it will be subjected to full financial and legal review, a partial review for specific issues only, or no review. In order to preserve the integrity of the selective review process, we do not publicly disclose our screening criteria. If the filing is selected for full review, a staff attorney and an accountant are assigned to examine the filing. Senior-level staff is also assigned as a second level of scrutiny. If necessary, the filing also is referred to special offices within the Division of Corporation Finance for an additional level of specialized review. For example, mining or gas and oil filings are referred to a mining or petroleum engineer.

A filing is reviewed to determine whether it complies with the requirements of the security laws and regulations and that it fully discloses all required material information.

Much of this review involves us stepping into the shoes of a potential investor and asking questions that investors might ask on a reading of the document.

All of the comments that the staff members generate on the filing are incorporated in one comment letter to the company. The company then responds to the letter by sending us a responsive letter and revising the document in accordance with our comments.

When we receive the company's response and revised filing, we review them to make sure the company has complied with our comments. We issue additional comments, if necessary, until all material concerns are resolved. The company then requests that the registration statement be declared effective so that the transaction can proceed. If all material concerns are resolved, the Commission, through delegated authority to the Division of Corporation Finance, issues an order declaring the registration statement effective.

The review of the Exxon-Mobil filing generally would follow the procedures outlined above. Our concern with respect to this transaction, as with any transaction, is that the companies make full and fair disclosure of all material information that they are required to disclose. The determination of the merits of the transaction will be left to the shareholders.

Mr. Chairman, this concludes my oral statement. I am happy to answer any questions that you or other members of the subcommittee have. Thank you.

[The prepared statement of Michael R. McAlevey follows:]

PREPARED STATEMENT OF MICHAEL R. MCALEVEY, DEPUTY DIRECTOR, DIVISION OF CORPORATION FINANCE, SECURITIES AND EXCHANGE COMMISSION

Mr. Chairman, Members of the Subcommittee: My name is Michael McAlevey. I am the Deputy Director of the Division of Corporation Finance at the Securities and Exchange Commission. I am pleased, on behalf of the Commission, to have the opportunity to discuss our role in regulating mergers of public companies. I want to state at the outset that the Commission does not, nor is it charged with, determining the merits of mergers or regulating the terms of transactions. In the context of the merger of two public companies, the federal securities laws require that the companies disclose all material information about the proposed merger so that investors can make a fully informed decision about the proposed transaction. In general, this disclosure appears in filings with the Commission and in a prospectus that is publicly available. I will outline the procedures that the SEC employs in reviewing merger filings. These procedures will apply to the proposed merger between Exxon Corporation and Mobil Corporation.

1. THE ROLE OF THE SECURITIES AND EXCHANGE COMMISSION IN REVIEWING FILINGS

The Commission is responsible for administering the federal securities laws. These laws are designed to protect investors by requiring full and fair disclosure of all material information about publicly traded securities. Full disclosure ultimately benefits both investors and the capital markets. By enhancing investors' confidence in the completeness and accuracy of information about public companies, these full disclosure requirements encourage investor participation in the capital markets.

The Commission's Division of Corporation Finance has primary responsibility for overseeing disclosures by issuers of securities. The Commission does not have authority to approve or disapprove a security or a transaction on its merits. If a transaction appears to involve a high degree of risk to investors or if a company involved in a transaction is experiencing financial difficulty, we do not, and we can not, stop the transaction from proceeding on that basis. Rather, the Commission's job is to ensure that the company fully discloses these risks and fully informs investors of its financial condition so that investors can make informed investment decisions. This system is designed to maintain market transparency. It allows market forces rather than regulatory controls to determine what transactions will proceed and at what prices a company's securities will trade. In this way, even small companies and companies with financial difficulties may have access to the public capital markets on an equal footing with larger, or more financially secure companies. Full and fair disclosure allows markets to assign an appropriate value for the securities of all public companies.

Under the securities laws, public companies file registration statements, periodic reports and other disclosure documents with the Commission. All registration statements are subject to review by the staff of the Division of Corporation Finance. Given the volume of filings each year, we fulfill this obligation by selectively reviewing registration statements and other documents that companies file when they engage in public offerings and other transactions in publicly traded securities. These filings include documents concerning mergers and acquisitions. We also selectively review periodic reports that public companies are required to file with the Commission. These reports are designed to keep investors apprised of the companies' financial condition on a continuing basis.

The Division's role in the registration process is to use reasonable means to encourage companies to make full and fair disclosure to investors of all material information. Our principal means of accomplishing this is through dialogue with the companies. This makes sense because the companies themselves possess the information that they are required to disclose. When we review a registration statement, we ask the company about any disclosures that are: unclear, incomplete, inconsistent with disclosures elsewhere in the document or in other publicly available materials, or do not comply with the specific disclosure standards in the federal securities laws and regulations.

The company then responds to our questions by amending the document or supplying us with information to respond to our concerns. Registration statements will not be declared effective—permitting the sale of the securities—until we have no reason to believe that the disclosure is not materially complete, accurate and mean-

ingful. I will discuss this process, which we call the "review and comment" process, in greater detail below. We rely on the company's responses to our comments and on the company's legal obligations to respond to us in a truthful manner. In addition, the legal, financial and accounting professionals who are involved in preparing and/or auditing the company's disclosures have professional obligations and may be subject to legal liability if the disclosures contain material misstatements or omit material information.

The Division of Corporation Finance does not independently audit the company or its operations. If we have significant concerns or become aware of information that suggests that a company may have violated the securities laws, we may refer the matter to the Division of Enforcement. The Division of Enforcement has broad authority to investigate possible violations of the securities laws and may bring actions against a company if information in its registration statement proves to have been materially false or misleading.

2. PROCEDURES THAT THE DIVISION OF CORPORATION FINANCE EMPLOYS IN REVIEWING MERGER FILINGS

A. The companies file the proxy statement/prospectus with the SEC

Ordinarily, when a company proposes to merge with another company, it is required to obtain shareholder approval of the transaction. Whether shareholder approval is required in a particular situation depends on the significance of the merger to the company and the requirements of the state of incorporation or the stock exchange or market on which the company's shares are traded. If shareholder approval is required, the federal securities laws require a public company to deliver a proxy statement to its shareholders. This document discloses the material terms of the transaction to shareholders so that they can make informed decisions when they vote on the transaction.

In addition, when a public company proposes to issue stock in a merger transaction, it must register the offer and sale of that stock under the Securities Act. For example, assume that company A, a publicly traded company, proposes to merge with company B, also a publicly traded company. The companies have negotiated to exchange company A's stock for company B's stock. Before company A can offer its shares to company B's shareholders, it must file a registration statement with the SEC. The registration statement includes a prospectus that discloses material information about the companies and the proposed transaction. In addition to the prospectus, the registration statement contains exhibits, which include, among other filings, the company's articles of incorporation and bylaws, opinions of counsel and material contracts to which the company is party.

While the entire registration statement must be filed with the SEC and is publicly available, only the prospectus must actually be delivered to investors who will receive stock in the transaction.[1] The prospectus also serves as the proxy statement for the companies' solicitation of shareholder approval of the transaction.[2] As a result, we usually refer to the disclosure document that the companies distribute to shareholders as the proxy statement/prospectus. The disclosure about each company must include, among other things, a description of: its business, its property, any material threatened or pending legal proceedings against the company, historical financial results, and a textual discussion of the company's financial condition and historical results of operations.

If the companies have a reporting history with the Commission, are current in their reports, and have at least $75 million in market capitalization held by the public, they can incorporate their Exchange Act reports by referring to them in the registration statement.[3] These reports include quarterly and annual reports and special reports, which typically are used to announce unusual developments or events. Incorporation by reference can reduce the length of the document and the burden on the companies to disclose information that is already available in the companies' periodic reports. The reasoning behind this accommodation is that larger companies with reporting histories generally are followed sufficiently closely by the markets so that information about them is already publicly available. Further, the markets usually will have absorbed the public information about these companies

[1] The prospectus that is delivered to investors also includes the merger agreement as an appendix.

[2] Rule 14a-6(j) under the Securities Exchange Act allows companies to use the same document as the proxy statement for purposes of soliciting shareholder proxies, and the prospectus for purposes of offering and selling the securities in the transaction.

[3] A Company may also incorporate its Exchange Act reports by reference if it has been subject to the reporting requirements for three years, has been timely for the last year, and sends the incorporated Exchange Act reports with the prospectus. This option is rarely used.

and used it to establish a fair trading price in their securities. Therefore, receiving delivery of full information about such companies generally is not as important to investors as is information about smaller companies or companies without solid reporting histories. When companies incorporate their periodic reports by reference, they still are liable for the information in the reports that they incorporate by reference in the same manner as they would be if they included all of the information from the reports directly in the registration statement itself.

In addition to this information about the companies, the disclosure in the proxy statement/prospectus also must include material information about the proposed merger including: any material risks associated with the proposed transaction, pro forma financial information for the combined company after giving effect to the merger, the material terms of the proposed transaction, a discussion of how the companies negotiated the transaction, any material contracts between the two companies, information about the proposed management of the combined company after the transaction is completed, and a description of how shareholders' rights will change if the merger is completed.

After drafting the registration statement, the companies file it with the Commission. The proxy rules allow companies to file preliminary proxy statements related to merger transactions confidentially, so the proxy statement/prospectus is not available to the public when it is initially filed.[4] The Commission's rationale when it adopted this position was that it wanted to allow companies to go through the review and comment process without prematurely disclosing confidential information to the market about merger transactions. The document only is made available to the public when the final proxy statement that will be delivered to shareholders is filed. Domestic companies are required to electronically make all of their non-confidential filings and, as a result, the final, or definitive, proxy statement/prospectus is available on the Internet in the SEC's EDGAR database generally within 24 hours after it is filed. Companies are required under state law to deliver the proxy statement to shareholders sufficiently in advance of the meeting to allow them time to consider the information before voting on it. The specific amount of time that the company must give shareholders varies by state.

B. The staff's review of the filing

1. *Routing to the appropriate industry group*—The Division of Corporation Finance is divided into 12 industry groups, each of which is headed by an Assistant Director. Each industry group is responsible for reviewing filings in one or more related industries.[5] This system allows members of the staff to develop expertise in their industries and to better identify issues that are of particular concern within an industry. When a filing is made with the Commission, it is routed to the appropriate industry group for processing.

2. *Selective review process*—The Division does not have sufficient resources to review all registration statements and other filings that are made with the Commission. Therefore, in 1980, we implemented a "selective review" program by which we review some, but not all, of the filings that are made with the Commission. When a filing is made and routed to the appropriate industry group, it is then "screened" to determine if it will be subjected to a full financial and legal review, a partial review for specific issues only, or no review. We conduct a full review of all initial public offerings. In order to preserve the integrity of the selective review process, we do not publicly disclose our screening criteria for other filings.

3. *Assignment of filing to staff*—If the filing is selected for full review, a staff attorney or financial analyst and an accountant are assigned to examine the filing. Senior level staff are assigned as a second level of scrutiny to review the filing and the comments drafted by the examining attorney or financial analyst and accountant. This second level of review helps us to ensure the thoroughness of our reviews and the consistency of our comments across filings. If necessary, the filing also is referred to special offices within the Division for an additional level of specialized review. For example, mining or oil and gas filings are referred to a mining or petroleum engineer, international filings may be referred to a separate international office in the Division of Corporation Finance, and some complex mergers, acquisitions and tender offers are referred to a separate mergers and acquisitions office within the Division.

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[4] SEC Release No. 34-30849. 57 FR 29564 (June 24, 1992).

[5] The industry groups are: (1) health care and insurance, (2) consumer products, (3) computers, (4) natural resources, (5) transportation and leisure, (6) manufacturing and construction, (7) financial services, (8) real estate, (9) small business, (10) electronics and machinery, (11) telecommunications, and (12) new products and structured fiance.

4. *Examination of filing to staff*—The attorney or financial analyst and accountant who examine the filing review it to determine whether it complies with the requirements of the securities laws and regulations, that it fully discloses all required material information, and that the disclosure is meaningful to investors. Much of this review involves stepping into the shoes of a potential investor and asking questions that investors might ask on reading the document.

As a result, some comments that we issue in the review and comment process are quite common and others are unique to the particular filing under review. For example, today, we commonly ask companies to expand their discussion of the risks associated with the Year 2000 problem. Often, companies make only generic disclosures indicating that they may have liability if their computer systems are non-compliant. We often ask companies to discuss specifically what they have done to evaluate and address their Year 2000 problem, what the costs associated with the Year 2000 problem are, what special risks are presented by the Year 2000 issue, and what contingency plans the company has established.

Some other comments that we issue are unique to the company's industry, the company itself and the filing. In oil and gas filings, the petroleum engineer assigned to the filing typically will request from the company underlying documentation to support its calculation of reserve estimates. This documentation often includes detailed reserve reports prepared by the company's independent engineering experts. The staff engineer then will issue further comments if any disclosures in the proxy statement/prospectus are not materially consistent with the underlying reserve reports. Similarly, if a company is doing business in a politically unstable part of the world, we might ask it to disclose the risks associated with doing business there. If a company incurred a large, unexpected expense, we might ask for disclosure of the impact that expense has had on other planned capital expenditures. If the disclosure of the transaction or the companies is unclear or if important questions are left unanswered, we would ask the company to revise the document to clarify it. The range of possible comments is practically limitless and depends on the issues that arise in the particular filing.

One important focus of the staff's review is in ensuring that the prospectus is clear and readable. As of October 1, 1998, our rules require that prospectuses be written in plain English. We want investors to be able to pick up the prospectus and understand the material information about the transaction on first reading. They should be able to do this without a legal dictionary, without diagramming the transaction, and without having to flip back and forth to different parts of the document to decipher the disclosure. We have made significant efforts to enforce this rule and are finding that prospectuses now are significantly more user friendly.

5. *Issuance of comment letter*—All of the comments that the staff members generate on the filing are incorporated in one comment letter to the company. The company then responds to the letter by sending us a responsive letter and revising the document in accordance with our comments. The staff often also discusses any of the company's questions with the company and its legal, accounting, engineering and other advisors.

6. *Comment clearance*—When we receive the company's response and revised filing, we review them to make sure that the company has complied with our comments. If we have further comments, we issue additional comment letters until all material concerns are resolved.

7. *Declaring the registration statement effective*—The company then requests that the registration statement be declared effective so that the transaction can proceed. At that point, the Assistant Director of the group conducts a final review of the filing and makes a public interest finding that he or she has no reason to believe that the disclosure is not complete, accurate and meaningful. If the Assistant Director is unable to make such a finding, he or she will issue further comments. When all material concerns are resolved, the Commission, through delegated authority to the Division, issues an order declaring the registration statement effective. This allows the company to proceed with the transaction.

3. THE PROPOSED MERGER OF EXXON CORPORATION AND MOBIL CORPORATION

The review of the Exxon/Mobil filings generally will focus on the same substantive issues outlined above. Our concern with respect to this transaction, as with any transaction, is that the companies make full and fair disclosure of all material information that they are required to disclose. We will not scrutinize the transaction to make an independent assessment of whether its terms are fair or whether the merger would benefit shareholders. That determination will be left to shareholders, after they have received full and meaningful disclosure of the material terms of the transaction.

Mr. BARTON. Thank you. The Chair is going to recognize himself for the first 5 minutes of questions.

Could we put the chart up that shows the percentage of oil markets that are controlled by that national oil companies from 1972 to 1997? It was either the first or second chart.

Thank you. The Chair recognizes himself for 5 minutes.

My first question, and it is primarily to Mr. Baer, but possibly to Mr. Hakes, historically, when we have looked at mergers in the United States, the private entities that are looked at from the FTC or the SEC are domestic companies that are manufacturers or retailers and they are selling in the domestic market. In this case we have a situation where, according to the EIA information in 1997, 2 years ago, national oil companies controlled 52 percent of the world oil market. So the Exxon-Mobil merger is not just competing against Texaco and Royal Dutch, Shell, and Arco, but you are competing against Aramco and the Venezuelan oil company and the Mexican oil company and the Chinese oil company.

So my first question is to Mr. Baer: How did the FTC evaluate such a merger when you are really looking more internationally than nationally, and when you look internationally, you are really looking at state-owned competition as opposed to the privately owed competition?

Mr. BAER. It is a great question, Mr. Chairman.

Mr. BARTON. Thank you. Give me a great answer.

Mr. BAER. And the answer is a little complicated. The fact that a market is international does mean, first of all, we need to take into account all the folks overseas who are doing energy exploration and production. In order to assess competitive effect, you need to figure out how many players there are and how aggressive they are going to be. Will a merger such as Mobil-Exxon reduce the number of players unreasonably?

Where it gets more complicated is where you do have national oil companies in the mix. On the one hand, if they are out there competing to generate as much revenue as they can for themselves, if they are competing aggressively, they ought to have some of the same competitive instincts private firms have, that is, to bid their price of oil low enough so that they make the next sale. At the same time sometimes State interests do change that behavior a little bit and we need to factor it in.

There's another concern here that is raised by Mr. Hakes' chart, and it is the second part of my answer to your question. That is, what do we do if this 52 percent behaves not as a bunch of different firms, but as a bunch of nations that might, as we had back in the 1970's, decide they had a common interest, either by engaging in an embargo for political or other reasons, or by deciding that the way to maximize their return is to behave as a cartel, and so you have over 50 percent of the market raising price? We need to assess the likelihood those sorts of things would happen, and those are issues we consult with our sister agencies who know more about international issues and trends than we do at the FTC.

But, also, what is the likely competitive impact of this merger if the market were to change dramatically and we were confronted with an international model of a cartel? Would having a firm the size of a combined Exxon-Mobil give them an undue percentage of

the remaining market in the event of an embargo? Could they do more with price then, and should that be of concern to us?

So those are the sorts of issues we are going to be working through in the course of our investigation.

Mr. BARTON. Could one conclude that you actually need such a hat is being proposed in order to give an economy of scale to compete against a State-owned oil company or against a collection of State-owned oil companies in a cartel like OPEC? I mean, is it possible that the conclusion could be, for national security interests, you want a privately owned mega-merger because it gives the economies of scale to participate and to prevent the cartelization of world oil markets?

Mr. BAER. That certainly could be a legitimate efficiency or overall economic benefit for a merger that needs to be factored into the analysis. I agree with that, Mr. Chairman.

Mr. BARTON. Now, Mr. Hakes, again in this chart—my time has expired, so this will be my last question—we just show one big orange slice of pie that says 52 percent. Within that orange slice, which is the biggest State-owned oil company, and approximately what is its market share and its revenue?

I would assume it would be Saudi Aramco?

Mr. HAKES. That is correct, Mr. Chairman. Their share is about 14 percent.

Mr. BARTON. So the single largest State-owned oil company, if Exxon-Mobil goes through, Exxon-Mobil would be slightly smaller than Saudi Aramco; is that correct?

Mr. HAKES. It would be substantially smaller. Their production worldwide would be about 4 percent. So they would be below also Iran, Venezuela, Mexico, and China.

Mr. BARTON. So they would be in the same league, but they would be at the bottom of the standings, not at the top of the standings?

Mr. HAKES. Well, there are a lot of producers. So there would be a lot of companies and countries below them, but they would be in between China and Kuwait.

Mr. BARTON. The Chair would recognize Mr. Hall for 5 minutes.

Mr. HALL. Mr. Chairman, I am going to hold my questions and probably present them in writing. I think they are in the review process and there would be a lot of things that you could not comment on now, except to say what you have done before in the same or similar situation. We will present questions to you in writing, if that is all right, and you can timely answer them.

Mr. BARTON. The Chair would recognize Mr. Shimkus for 5 minutes.

Mr. SHIMKUS. Thank you, Mr. Chairman. I'm trying to make sure I get the names right.

For the FTC, Mr. Baer, what effect will the prospects of a long period of lower oil prices have on your merger analysis in the energy industry? Will that play any role in your analysis?

Mr. BAER. It will, sir. To the extent that current depressed prices for oil are a reflection of intense competition at the production and exploration level, that would tend to suggest that a merger of two big companies is unlikely to have an impact on what is, for purposes of hypothetically speaking, an intensively competitive mar-

ket. So if the market is competitive and two guys are merging and it is unlikely to change the competitive dynamic, that would tend to be a reason not to intervene on antitrust grounds to block a transaction.

Mr. SHIMKUS. And in analyzing the retail gasoline markets, how local is local?

Mr. BAER. Well, we look at a metropolitan area, you know, city by city. In San Diego, as I indicated, in the Shell-Texaco joint venture, we looked at that market, and realized that there are only a few majors present there. There was not a lot of independent competition. San Diego is a tight market in terms of real estate. So the prospect that someone would enter and replace lost competition was quite slight. So we required divestiture of a significant number of retail gas stations.

Ultimately, ironically, Exxon came in and bought them up and maintained what was, I believe, a five-firm presence in that market, ensuring that we would not have lessened competition as a result of that transaction.

Mr. SHIMKUS. And in your opening statements you talked about the State attorney generals. Can you explain to me the role between you all and the State attorney generals and what impact they have or they do not have?

Mr. BAER. Fair enough. Most States have their own antitrust laws which they can apply under principles of federalism to transactions that affect constituents in their States.

Over the last 10 years or so, to avoid balkanization of antitrust enforcement, we have developed a terrific working relationship with the State attorney generals. They try to act collectively in consultation either with the FTC or for mergers over at the Antitrust Division, the Justice Department, to make sure we are coordinating our requests for information from the parties, so we aren't unnecessarily burdening them.

But, ultimately, each State may have an interest. In the Northeast, for example, as Mr. Markey commented, whether there would be an undue increase in concentration; we would work together to identify the concerns. To the extent we share a view, we would approach the companies collectively in an effort to see if we cannot work out a disposition that would address those competitive concerns on a State-by-State basis.

Mr. SHIMKUS. Is that process done through their association or their coordination with the State attorneys general? Is that basically done through the national association?

Mr. BAER. It is done generally under the auspices of NAAG, but what they do is they have a buy-in process where States in a particular merger who have an interest let each other know through—they've got an efficient e-mail system—and they appoint one State to be the lead and then we end up working both with that one State and with the group collectively to make sure we are focused and as efficient as we can be in pursuing our common goals.

Mr. SHIMKUS. Thank you very much. Mr. Chairman, I yield back my time.

Mr. BARTON. The gentleman from Illinois yields back the balance of his time. The Chair recognizes the gentleman from Maryland, Mr. Wynn for 5 minutes.

Mr. WYNN. Thank you, Mr. Chairman. Mr. "Baer," is it?

Mr. BAER. Yes, sir.

Mr. WYNN. I am not sure if this has been covered and it may be somewhat tangential. But what I would like to know is whether or not the FTC is going to take into consideration the effect of this merger on dealers, any rights that they may have with respect to their stations and their contractual relationships with Exxon-Mobil in evaluating this merger. Any comments you could share about that I would appreciate.

Mr. BAER. Sure, I could perhaps, Mr. Congressman, put my answer in the context of the BP-Amoco deal which we worked through in late December and January. We have a process where we consult with dealers and with jobbers to understand their sense of the competitive picture and also make sure we understand any unintended consequences that might flow from our effort to preserve competition. Our job is to make sure that somebody doesn't get too big as a result of the deal and have the ability to raise consumer prices.

But in terms of designing remedies, part of our job as well is to avoid unduly disadvantaging folks who are caught in the middle. We have gotten some comments in the BP-Amoco consent decree where we have a formal comment period, from dealers expressing some concerns about whether they ought to have a right—these are dealers who are lessees of BP or Amoco—whether they ought to have the right to go in and buy out BP or Amoco on a station we required BP or Amoco to divest. Those are legitimate, important issues. I realize that you have got some legislation you are introducing, sir, to address that issue.

We are hopeful we can work with the dealers to understand their concerns and figure out if there is a way, in terms of making sure we get the relief we think consumers need, that we adequately protect legitimate interests of local dealers.

Mr. WYNN. Can I interpret what you said to indicate that with the BP merger there were some problems with respect to individual dealers who were not accorded a right of first refusal?

Mr. BAER. They expressed concern that, if the station which they operated, but didn't own, was going to be sold, that our divesture order did not give them a right to buy out that station. What our order required is that BP-Amoco find a buyer for all the divested stations in a particular market, and the rationale for that was you have five firms in a market today, and after BP-Amoco, it is down to four. What you want to do is have some other significant flag carrier, you know, a Texaco, whoever, to come in and fly that flag on all of the stations to be divested, so you have a significant competitive presence.

What my understanding is, lessee dealers have filed some formal comments with us which are on the public record—which is why I can talk about them—where they expressed those concerns. We have met with them and are going to continue to talk to them to see if there is a way to accommodate those concerns. I do not have an answer for you yet other than to say that we are working with them to see whether we can get there.

Mr. WYNN. One follow up question: Do you believe it is within the purview of the Commission's jurisdiction to provide that right of first refusal by way of consent decree or some other mechanism?

Mr. BAER. We don't have the right to interfere with pre-existing contract rights. We have the right to insist that, as a condition of settling a deal, allowing their transaction to go, that BP and Amoco take certain actions.

The question we need to work through is whether the conditions we have imposed—that is, divestiture to a single buyer—is a condition that we really need in order to protect consumers or whether allowing there to be buyouts from the lessee dealers is something that would make sense from the antitrust point of view, as well as give those understandably concerned lessee dealers an opportunity to pay fair price for the station they have invested in.

Mr. WYNN. Thank you very much. Mr. Chairman, I relinquish the balance of my time.

Mr. BARTON. Thank you, Congressman. The Chair recognizes Mr. Largent of Oklahoma for 5 minutes.

Mr. LARGENT. Thank you, Mr. Chairman.

Mr. Hakes, most industry analysts have said that, as a result of this merger, there could be possibly 9,000 to 12,000 jobs lost. How many of those would be jobs in the United States? Do you have any idea?

Mr. HAKES. I don't have a breakdown on that, I don't believe. That does reflect international numbers. So it would not all be domestic. I am sorry, we don't have that broken down.

Mr. LARGENT. And would the total number of employees be after the merger before they let people go, around 122,000? Is that what I read?

Mr. HAKES. I don't know if we have that number. We have tracking systems for overall employment in the industry. We don't collect that information, I don't believe.

Mr. BARTON. I can answer that. The current number is 122,700.

Mr. LARGENT. Mr. Hakes, let me ask you another question. What percentage of the world's oil production is currently controlled by OPEC, currently, as opposed to what it controlled in the 1970's?

Mr. HAKES. OPEC, I don't remember the exact number. It is less than it was in the 1970's. We are importing more oil than we were in the early 1970's. The latest figure is 43 percent is produced by OPEC and 28 percent in the Persian Gulf.

One of the problems that OPEC had after prices ran up in the 1970's and early 1980's was they sort of priced themselves out of the world market a little bit, and so their share has gone down. However, since the late 1980's, it has been creeping back up, and most of our projections suggest that the OPEC share and the Persian Gulf share will rise in the coming decades, but right now it is lower than it was in the 1970's.

Mr. LARGENT. And what percent of the oil do we currently import in this country?

Mr. HAKES. If you use net imports, it is a little bit over half. If you use gross imports, it is somewhat higher than that. But, again, our forecasts indicate that, if current trends continue, we could be up to 60 percent in the not-too-distant future.

Mr. LARGENT. And does that create national security concerns?

Mr. HAKES. Well, I think, yes, it does. I mean, as we saw during the Persian Gulf War, it is possible for major supplying areas to be taken off the world market and depending on a lot of other things that are going on at the same time, that could have a big impact or a huge impact. At the time of the Persian Gulf War there was a lot of excess capacity in Saudi Arabia, so the interruption was not as big in its impact as it might have been. But I think everybody is always concerned about possible interruptions of supply, particularly from regions of the world that are unstable.

Mr. LARGENT. One of the things that is going on, as you are probably aware, in oil patch States like Oklahoma and Texas, and many others, is that, because of the low cost of oil today, it is driving many of the independent producers out of business. What do you view as being a price per barrel that is needed to sustain a domestic production industry?

Mr. HAKES. Well, I think that varies a lot. I mean, clearly, these low prices have had a big impact. When the quarterly figures for the end of last year came out, we showed a drop of production of 500,000 barrels a day over the year previously and that is a sizable drop in domestic production.

Onshore you tend to have stripper wells which have a high cost and offshore they seem to be able to sustain this a little better.

I don't know exactly the answer to that question. For West Texas Intermediate we consider the normal range for that has normally been in the $17 to $21 range. Probably 15 is a number that a lot of people use to make investment decisions.

But these numbers are a little bit misleading because West Texas Intermediate is a good quality of oil and some of the producers have actually been getting as low as $6 a barrel for heavy oils. So they would have to be higher than they are now, I think, certainly, for onshore producers to be able to continue to produce.

Mr. LARGENT. Mr. Baer, I wanted to ask you one question, and that is, in your statement you talked about that moderate concentration levels in this industry may have substantial adverse effects on competition. My question is, why would that be true or maybe that is true in any industry, but from your comments I thought you were saying that perhaps this industry is a little unique in that the moderate concentration would have adverse effects?

Mr. BAER. Mr. Largent, you read my comment accurately. That is, we do think that our experience in the petroleum industry suggests that the ability of firms at retail-wholesale and refining to price in what we call an interdependent fashion. That is not an allegation of an illegal cartel, but simply refers to the ability of the firms to be very conscious of each other's firm price is setting their own prices, and therefore, maybe work price up a little bit.

That tends to be a factor we see more in certain markets, certain industries than others. Petroleum is what we call an undifferentiated product. Gas is gas. Heating oil is heating oil. They may add a little additive to it, and differentiate it in their advertising, but essentially it is a commodity, a commodity product. Where you have commodity products and published prices, there is a tendency for firms, when there are fewer of them, to be able to price a little less aggressively against each other.

So the concern is with consolidation in petroleum, and we have seen this in our prior investigations in some markets where you have five firms, which might be enough to make a market competitive in some industries, may not be enough, depending on the market shares, in some other industries. That is what I was trying to suggest. This is one of those industries where we tend to get to a concern level a little earlier.

Mr. LARGENT. I see. Thank you, Mr. Chairman.

Mr. BARTON. Thank you, Mr. Largent. The Chair recognizes Mr. Burr of North Carolina for 5 minutes.

Mr. BURR. I thank the chairman, and I apologize to the witnesses that I have not been here for the majority of it. It is not because of lack of interest. I am going to try to limit my questions to you, Mr. Hakes, because I am not sure what I can and cannot ask the other ones. But if they have some relevant answer, I will be happy to take it.

Tell me, if you will—I was curious with your comment about the 30 percent increase in cost after a fire at a refinery in California. What made that happen? Was that supply?

Mr. HAKES. Well, in the California market it is a more isolated market as opposed to the East Coast, where there are a lot of refineries and they can trade back and forth easily. In California they have different clean air standards, and therefore, it is difficult to move product in and out of there. So when a refinery goes down in California, it has a much stronger impact on price there than, say, a refinery elsewhere in the country if it went down.

Mr. BURR. But there are clearly refineries that refine California fuel elsewhere other than California?

Mr. HAKES. Yes, ultimately, that is the case. So, you know, the market has self-corrective mechanisms for a lot of these things. In the short term there is a price runup. That usually is a signal to the market that California needs product and it is possible to produce it elsewhere.

Mr. BURR. So it is really the structure of the refinery network in total, the time that it takes to get from one that is not in California to California?

Mr. HAKES. Right, and to make sure they are adapting to the kind of gasoline that they use in California.

Mr. BURR. So, using that analogy, we should not be concerned, then, that this merger would cause a price spike for a refinery reason?

Mr. HAKES. Well, I think I agree with the point you are making in that you have to look at sort of the transportation infrastructure, and one of the reasons petroleum is attractive as a fuel is it is relatively easy to transport from one area to another. I mean, it can be imported from Europe, if need be, to offset a shortage. So I am certain that transportation is one of the things that would be taken into account for looking at competition, and petroleum does tend to be a competitive fuel, more than some other commodities, because it is so easy to transport.

Mr. BURR. From where you observe this, does this merger make sense?

Mr. HAKES. The Energy Information Administration has sort of earned its credentials over the years by providing information to

the Congress and administration. We try not to take a position on policy issues. I think it keeps our data a little cleaner that way. I would like to be able to answer that question.

Mr. BURR. I will let you maintain that neutral setting, but, clearly, from some of the things that we have looked at with production and retailing and refinery, though the size of the merger in dollars is not necessarily replicated in market share, and I think that is the disconnect that a lot of us have, because it is very small in proportion to the rest in totality of what you accumulate.

But let me ask you about job loss specifically. Have you broken job loss down by the different sectors within these businesses, i.e., exploration and production, refinery, and retail?

Mr. HAKES. I don't have that certainly available today. I might be able to get it for you.

[The following was received for the record:]

EIA's data on employment within the major oil companies and the potential job losses resulting from the mergers come from publicly available information provided by the companies. EIA revisited that information, but we can find no breakdown of how the Exxon-Mobil merger-related job losses may be distributed across the companies.

For your information, in 1997, Exxon employed about 29,700 in the United States and 50,300 internationally. Mobil employed about 20,500 people in the United States, and another 22,200 abroad. Mobil also publishes a distribution of its employees across business segments as shown in the table below. One logical target area for reductions is corporate overhead and staff support, which seems to be a large part of Mobil's 1997 "Other" category. The "Other" category accounts for 3,000 employees in the U.S. and represents almost 15 percent of Mobil's U.S. force.

Mobil Oil Corporation Employee Statistics 1997

	US	International	Total
Exploration & Production	1,800	4,200	6,000
Marketing & Refining	7,300	14,300	21,600
Chemical	2,600	1,300	3,900
Technology	1,700	100	1,800
Other*	3,000	1,300	4,300
Salaried Service Station & Other Non Regular Employees	4,100	1,000	5,100
Total	**20,500**	**22,200**	**42,700**

*Includes operations of Real Estate and Mining and Minerals (both businesses substantially divested in 1996), Corporate Administration, and other activities. Staff support groups are reported in Other as well.
Source: Mobil's Financial Fact Book (available on Mobil's Web Site)

Mr. BURR. In your capacity do you believe that these companies, were they not to merge, would have job reductions within their companies to meet the changes in the marketplace and the pressures that are in the market today?

Mr. HAKES. Yes, there has been a long-term trend in all the energy industries to reduce employment. If you look at the electricity industry or the coal industry, and certainly the oil and gas industry, there has been a pretty consistent trend now since the early 1980's to reduce the number of employees, and again, we project that trend as likely to continue into the future. So, with or without mergers, there are downsizing pressures on all these firms to reduce costs.

Mr. BURR. So we can safely expect that there would be some job loss with the merger because of the duplication of jobs, but even if we didn't have the merger, we would likely trend toward fewer

jobs within these two companies without the merger just from the market?

Mr. HAKES. I think that is a likely assumption, yes.

Mr. BURR. Let me ask one final question with the chairman's indulgence: Tell me, if you will, how will oil prices be affected by this merger?

Mr. BARTON. So we can go out and invest in the market when you give us the answer. We are hanging on every word here.

Mr. HAKES. Most of what we do is on an aggregate national and international level, and I am not sure there is anything here that would cause us to change our price forecast.

As has been suggested in other testimony, the issues may be more regional and local in nature. I mean, if you look at some States, they have not had one station from Amoco, BP, Exxon, or Mobil, and you get into some other area and over half the market would include those particular companies. So I think from an aggregate level it might be hard to find, and I think most of the tension will probably be focused on more regional and local issues.

Mr. BURR. Can I ask it in a slightly different way? Does this merger increase or decrease our reliance on imported oil?

Mr. HAKES. There may be some indirect effects, but I wouldn't see any direct effects that come immediately to mind.

Mr. BURR. I thank the three of you, and I yield back, Mr. Chairman.

Mr. BARTON. The Chair would recognize the distinguished gentleman from Tennessee, Congressman Bart Gordon, for 5 minutes for questions, if he so wishes.

Mr. GORDON. I will pass at the moment and reclaim my time later if that is possible.

Mr. BARTON. Sure. All members present of the subcommittee have had an opportunity to ask questions. By an agreement with the minority leadership, Mr. Dingell and Mr. Hall, the Chair would recognize the gentlelady from Houston who is not a member of the committee, but who has an interest in the issue, Congresswoman Sheila Jackson-Lee for 5 minutes.

Ms. JACKSON-LEE. I thank the chairman very much, my colleague from Texas, and I will be brief in my question to the Director of the FTC.

We have come to understand that all bigness is not bad. There are some concerns, of course, as we watch the prevailing impact of low price per barrel on various companies with downsizing.

My question to you, on your ongoing investigation on this merger, what are the other criteria other than business, if you want to cite two or three or four, that are extremely singular in their importance in your analysis? And my question goes to the ultimate impact on the consumer, how you look at these factors as you move toward your conclusions.

Mr. BAER. Thank you, Congresswoman. The simple answer is, first of all, we agree with you that bigness does not necessarily imply badness, but bigness can be bad if it is big in a relevant market, and that is really what we look at.

We look at, if I start from the place closest to the consumers heart, the retail pumps. Will a few firms, as a result of this transaction, control in a local community a significant percentage of the

gas stations? If so, there is a risk that either one company acting alone or two companies being a little less aggressive with each other could raise prices a penny, two cents, three cents. It doesn't sound like much until you multiply it out, and it obviously matters to the individual consumer.

As you go further up the distribution chain, there are regional areas where there are terminal networks, and if somebody basically is in control of an undue percentage of the terminal, the storage facilities, they can raise the price that the jobbers who come and pick up the gas, and transport it to the stations must pay. So there is a potential anticompetitive effect there. I am not saying there is in this transaction, but just that is what we look at.

If you go up to pipelines, where I mention in my opening statement that Texas and the Gulf Coast has an undue percentage of the refining capacity, and they need to get that to the country some way. One way is through pipelines, and if one or two firms controlled an undue percentage of the pipelines they potentially could raise the tariff rates and extract, what we call, a monopoly rent, but basically raise prices and injure consumers a little bit indirectly but ultimately injure consumers. Going up one more level to the refining level, if one firm or a few firms control an undue percentage of the refining in any particular area of the country.

We analyzed that in the Shell-Texaco joint venture. We were concerned that the firms would combine four refineries, I believe it is, on the West Coast with potential for them to have some impact both on prices for what they call the CARB II gasoline that is used exclusively in California, but also for the more standard gasoline and aviation products used elsewhere on the West Coast.

We required a divestiture of one of the four refineries to make sure that there in fact would be significant competition after the fact.

Then, finally, we go all the way up to exploration and production, both domestic, Gulf, Alaska, and elsewhere around the world, to see whether there is a potential impact there.

At any level if somebody is too big or a few firms are too big, that is the mechanism by which prices can get raised to consumers' detriment. Long-winded answer.

Ms. JACKSON-LEE. Not at all. Thank you very much and thank you, Mr. Chairman, for allowing me this time. I yield back my time.

Mr. BARTON. I thank the gentlelady. The Chair would now recognize Mr. Gordon of Tennessee for his 5 minutes.

Mr. GORDON. Thank you. In the past we have seen where world events, whether they be the Mid-East or potentially I guess they could even occur in Venezuela, Mexico, that have an impact on prices and consumers. What is your opinion as to this type of merger having either benefiting or being a detriment to consumers as a result of international activities? When I said, "international activities," crises or bad happenings.

Mr. BAER. It is a fair question. As one who is an antitrust lawyer and not either a diplomat or an international specialist, we go to our sister agencies and ask them to help play out that scenario and then——

Mr. GORDON. I think we can assume something is going to happen. We may not know when or where, but we know there is going to be an international problem, and we know that, ultimately, it will have some impact on the production of oil.

Mr. BAER. There are two possible outcomes—one procompetitive, one anticompetitive, and I believe Mr. Largent suggested a possible procompetitive outcome.

If the national oil companies engaged in a cartel or withhold product entirely, as they did in the Arab oil embargo, it may well be that having a couple of big U.S. firms with the resources to exploit opportunities overseas independent of nationally owned oil companies will be a net benefit to competition, because in the event of a national emergency, we will have exploited or developed resources we otherwise wouldn't. I think the companies fairly see that as an upside for America from this deal.

At the same time it is——

Mr. GORDON. It's better to have one than two in those types of circumstances?

Mr. BAER. I think they would say that—and they will be in tomorrow; you can ask them—that the scale of investing overseas is such that there is an upside from having one firm at the scale needed to invest. That's a factual question that we would need to investigate in any merger.

The flip side, sort of the bad scenario for consumers, is that if somehow an embargo takes a lot of production off the market, are you going to have one firm with 15, 20, 25, 30 percent of production that is imported into the United States, and if so, is that going to increase the likelihood that that firm could manipulate supply, manipulate price in a way that would injure consumers? Those are the sorts of questions we try to work through in our analysis.

Mr. GORDON. Now if you had a situation where you had a national oil cartel that got together and then we had a large American-based firm, what is your opinion as to them putting their country above their shareholders?

So in other words, if the world market went up to whatever, $25 a barrel, and it was $18 just a month before and it is artificially up to $24, are they going to say that they don't have a responsibility to their shareholders to maybe take it up to a dollar less rather than keep it down below so that the U.S. economy can keep purring?

Mr. BAER. We assume for antitrust purposes that companies are going to be profit maximizing; that they are going to take advantage of every opportunity that they have to make the next dollar, and that is not a pejorative statement; it is just, I think, a statement of how our American economy operates and should operate.

The way antitrust comes into the picture is to say, all right, now is a particular transaction going to actually give somebody the ability to get price artificially high? If so, we ought to stop that deal or restructure that deal so that eventuality cannot happen. That is how we factor in. We assume that people are going to act in the best interest of their companies and in the best interest of their shareholders and we just got to make sure that is not inconsistent with the American consumers' interest.

Mr. GORDON. Thank you.

Mr. BARTON. Does that conclude your questions?

The Chair recognizes the distinguished gentleman from Tennessee, Mr. Bryant for 5 minutes.

Mr. BRYANT. I thank the chairman.

Mr. Hakes, I am over here on the end.

Mr. BARTON. We have two gentlemen from Tennessee.

Mr. BRYANT. I wanted to ask you, Mr. Hakes, if I could, if you see a trend in energy mergers to form combinations that cut across product lines, for example, natural gas and electric mergers, and if so, what do you think would be behind this trend?

Mr. HAKES. Well, I think there is a tendency to say that the customer at the end of the purchase wants to buy energy and they don't sort of care what it is. For instance, when you are heating your home you may heat it with gas or with electricity, and there may be some reason for one company to be able to offer a customer the choice between natural gas and electricity. So, historically, that has not been the way those industries have operated, but it is the way they may operate in the future.

Oil went through a fairly early restructuring of the laws governing competition. So it has been operating in a competitive market for some time. Electricity and gas are in a way still going through this. Gas is further along. This is leading to a lot of restructuring in how products are offered to consumers.

I don't really pretend to be an expert on the motivations for mergers. I am sure there are a lot of reasons companies have, but I think there is a sense in energy to see that fuels are to some extent interchangeable and you probably want to be aware of and be able to operate in several different fuel areas.

Mr. BRYANT. Thank you. Mr. Baer, sort of a followup to that question: Is oil a separate product market from natural gas, and do petrochemicals also represent a separate product market?

Mr. BAER. Mr. Bryant, I think for most purposes the answer would be yes. I didn't mention this in my prepared remarks, but, for example, petrochemicals, if you look down the food chain, consumers, ultimately—if oil additive prices were raised, there is no substitute for them. So they really are the sort of separate market we would look at.

We had a transaction involving Exxon and Shell involving viscosity improvers, oil additives. We thought the merger in many respects didn't have problems. However, with respect to that separate product market, the VIs, the Commission concluded that a divestiture was appropriate in order to prevent anticompetitive effects.

So the short answer is, yes, we look at them separately.

Mr. BRYANT. Another question, Mr. Baer, a little bit bigger picture here from a historical standpoint: When specifically looking at the oil industry mergers, what countervailing efficiency considerations has the FTC identified that might mitigate against the anticompetitive impact of such a merger?

Mr. BAER. In the past, Mr. Bryant, we have taken a look at claims that by combining two oil companies they will be able to invest overseas, have the resources, the capital to invest that they might not otherwise have.

It tends to be a very factual-specific question and it gets to the question of: How big is big enough? Are they competing effectively

already? Do you really need this? Those are the sorts of questions we work through in a transaction.

You can see efficiencies in refining. For example the refineries on the West Coast that split their output between regular West Coast product and CARB II formulated for California.

Sometimes firms have come in and explained that by rationalizing how they would run a group of refineries they actually can reduce their cost. So we look at those sort of claims and credit them where we think factually they bear out.

At the same time you still have to weigh those claims of efficiency gains against the increase in concentration, and if the efficiency, the lowered cost, is occurring in a merger to monopoly, for example, the monopolist will have the ability to take price up, and it may well be that ultimately the efficiencies are modest and the price risk is high, in which case we tend to discount the efficiency.

Where you have the possibility that the market is sufficiently competitive, that the firm's cost savings will be competed down to consumers in some substantial measure, then under our guidelines we tend to weigh those efficiencies and stay out of the way.

So our analysis tends to be case-by-case, fact-specific, always considering the efficiencies in light of the competitive harms that we might be able to identify.

Mr. BRYANT. Mr. Chairman, I see my time is out. I just have probably three or four or five other questions. Could I submit those in writing to the FTC?

Mr. BARTON. You can certainly submit them in writing or we are going to have a second question round, at least I am. So if you want to wait another 10 minutes, you can probably ask them. It is whatever your preference is.

Mr. BRYANT. Thank you.

Mr. BARTON. The Chair would recognize the gentleman from Massachusetts, Mr. Markey, for 5 minutes.

Mr. MARKEY. Thank you, Mr. Chairman, very much.

Mr. Baer, on page 9 of your testimony you note that the FTC has on several occasions blocked mergers or required divestitures to prevent the elimination of competition at the terminal or tank farm level, thus, ensuring that there are competitive sources of supplies to local marketers.

Now I understand that in Boston there are six terminals through which gasoline, home heating oil, and other fuels must pass on the way to reaching their local markets, Exxon, Mobil, Gulf, Citgo, Global, and Irving. Exxon and Mobil, however, reportedly control the only two real deep water terminals in Boston Harbor that are capable of accommodating the largest tanker ships. The other four terminals reportedly can accommodate only smaller ships, and therefore, have higher costs, reportedly of up to 1 cent per gallon. Of these four, I understand that one is in the process of being closed down.

In the course of the FTC's review of this merger, will the FTC be examining the transaction's impact on competition at the terminals in Boston?

Mr. BAER. I am committed not to getting into the details of where we are going to look and how we are going to look, but I can assure you, Mr. Markey, that those are the very sorts of issues that

we are obligated to look at, and look at carefully. Six going to five in any market may be benign, but it also may be there are special characteristics of a market that make it much less than benign and worthy of your consideration.

Mr. MARKEY. And as you look at it generically, "B" is at the top of the alphabet and, as a result, would probably be one that you will look at?

Mr. BAER. As one who had the nuns calling him frequently because he had a "B" to start his last name, I am sensitive to those issues.

Mr. MARKEY. I see.

Mr. BAER. And the priorities that——

Mr. MARKEY. You are so right, you know, people whose name begins in "M," we are in the best of situations because even when Sister decided that she had overdone the "A," "B," "C's" she always said, well, let me go now to you, Mr. W; you know, "R" and the "M's" were always protected. We never got the first question in class. It was a nice place to be.

Now I understand that oil companies frequently enter into agreements with what are called through-puts or exchanges in which they supply one another with fuel. If the combined Exxon-Mobil were not to renew such agreements following the merger or raise the price they charged other oil companies for such through-puts or exchanges, might they raise anticompetitive concerns with the Federal Trade Commission?

Mr. BAER. The possible price increases resulting from a transaction in any merger are the sorts of things we look at. What you look at is the real risk that would happen, and if somebody was faced with that kind of price increase, would they have alternatives to go to? If they don't have sufficient alternatives, then there is a real antitrust concern.

Mr. MARKEY. So you will be looking at those contractual relationships?

Mr. BAER. I am not promising to look at anything. I am trying to stay out of the specifics of this transaction. I am saying, Mr. Markey, that those are the sorts of issues it is our job to look at.

Mr. MARKEY. Okay; good. Now I also understand that, in the course of reviewing the BP-Amoco merger and the Shell-Texaco joint venture, the FTC required those companies to divest themselves of a number of retail gas stations. In addition, in the BP-Amoco case the FTC also ordered the companies to allow their wholesale customers, both open dealers and so-called jobbers, to switch their gas stations to other brands.

Mr. Hakes' testimony suggests on page 6 that Mobil and Exxon have the largest overlapping marketing areas in the Northeast. In fact, it is my understanding in the Northeast Exxon and Mobil has a combined market share of between 15 and 27 percent of the branded gas stations in the region.

Will the FTC be closely examining the local market impact of the merger in this region to determine whether divestiture of gas stations or facilitating switching by open dealers or jobbers might be needed to assure competition?

Mr. BAER. Local impact is a critically important issue for us to look at in any petroleum company merger, including this one.

Mr. MARKEY. Now a December 4, 1998, article in the Wall Street Journal reports that in Massachusetts Mobil has 511 branded gas stations while Exxon has a much smaller presence in the State. According to this article, this is in part because Exxon is known to charge dealers much higher rents. The article reports that, quote, "A Mobil station, for instance, might carry $4,000 or $5,000 rent while an Exxon station pumping the same amount of fuel might pay monthly rent of $10,000 or $12,000."

Would the FTC be at all concerned if this merger transaction lead to more than doubling of the rents that local dealers must pay, given the fact that those costs most likely would be passed right along to consumers in the form of higher gas prices?

Mr. BAER. Our job is to be concerned about any price change that might ultimately affect consumers and limit competition, sir.

Mr. MARKEY. Mr. Chairman, I have 20 seconds of a question left. I would beg your indulgence.

Mr. BARTON. Sure.

Mr. MARKEY. Thank you.

Finally, I have heard that one business practice now taking place in the retail gasoline marketplace is that the major oil companies are refusing to allow their existing distributors to build any new gas stations within 30 to 35 miles of any big city or metropolitan area that would use their brands. Instead, the major oil companies are limiting new stations that they own themselves.

Does this practice raise any potential anticompetitive concerns on the part of the FTC? Would you expect that the FTC might examine such practices in the course of reviewing the merger?

Mr. BAER. The antitrust laws give a manufacturer or distributor of a product some ability to choose how it will go to market, that is, through company-owned retailers or through independent retailers and to some extent those decisions, as long as there is not a long-term anticompetitive consequence from it, are not the sort of things we normally are empowered under the law to go after.

There are circumstances where if, for example, one or two firms dominate a particular market, their ability to impose that kind of restriction can have a long term anticompetitive effect, and in those circumstances we are able to act. So it would depend on the facts we found in our inquiry, sir.

Mr. MARKEY. Mr. Chairman, I am a big admirer of Mr. Baer and the other two witnesses, and I thank you so much for your good work. Thank you.

Mr. BARTON. Thank you, Mr. Markey. The Chair is going to recognize himself for a few questions. I may not have time to do them all because we have two pending votes.

Mr. McAlevey, you sit there somewhat neglected. I don't think anybody has asked you a question.

Mr. MCALEVEY. I have an "M" in my name. There it is.

Mr. BARTON. There you go. Well, I have a "B" in my name, and I am going to ask you a few here.

You gave us a pretty straight forward text book synopsis about what the SEC does when mergers are presented that have stockholder investment. Is it random whether you look, as you put it, look at the file, or the bigger, the greater likelihood it is that the file will be looked at?

Mr. MCALEVEY. It is not random. We participate in a process known as selective review because we don't have enough resources to single filing that comes——

Mr. BARTON. But there is a high likelihood that your agency will look at the largest merger in the history of the United States of America?

Mr. MCALEVEY. That may be a consideration that we take into account. As a matter of policy, we don't disclose what the selective review criteria are for a number of reasons. But a merger, size and magnitude would be something that we may take into account.

Mr. BARTON. Well, be prepared to have the Chairman of the SEC come back before this committee if this one is not looked at. I will put it that way.

Mr. MCALEVEY. I will bring that message home.

Mr. BARTON. You can send that message.

I want to go back to some of the global implications of this. Is OPEC today an effective cartel, either Mr. Baer or Mr. Hakes?

Mr. HAKES. Well, I think in the mid 1980's it was evidenced that OPEC had lost some of its ability to control the world market, and I think since that time there has been a continuation of their influence to erode. I think some of the members actually compete against each other on production and distribution and sometimes they have difficulty getting people to comply with the quotas. I still am of the judgment, however, that they are a factor in setting the world oil prices and prices might be different if the cartel wasn't there. But particularly countries like Venezuela have begun acting much more independently in recent years.

Mr. BARTON. Mr. Baer, we do have a cartel called OPEC. You are aware of that. That has to play some role in the evaluation of this merger.

Is the FTC aware that recently several CEOs of major privately owned oil corporations have been invited to private meetings with the Saudi minister here in the United States and on at least several occasions their CEOs have also been invited to Saudi Arabia to have private meetings with Saudi Aramco?

Mr. BAER. We are generally aware that, based on published press reports, that there have been some discussions and that there is some consideration on the part of some national oil companies to inviting the private U.S. oil companies back into markets in which they had a significant presence back in the 1970's and before. So we are aware of that.

To the extent that your question raises a concern about whether there might be a collusive concern, coordinated behavior by firms resulting from that, that is the sort of thing we look at. In an investigation, any investigation, we want to find out what contacts merging parties have had with other players in the industry and whether there is any evidence that people have behaved in a coordinated fashion.

Mr. BARTON. Well, the potential exists that, if you have a cartel, admittedly, the cartel has not been very effective in the recent past in coordination of its production policies. But the fewer the number of players in the private sector, the more likelihood that there could be an effort between the cartel and the private sector to collude in a way that would be detrimental to the consumer. So I

would hope that that would be a consideration that the FTC would look at.

My last question because of time I am going to ask again, and primarily to Mr. Baer, this merger is between two integrated oil companies. They are vertically integrated. Is there any one particular phase of the chain that is a greater potential for a bottleneck which would, if the merger were to occur, would result in an anticompetitive nature?

In other words, is the retail level more likely to present a bottleneck or the distribution level or the refiner level or the production level in terms of the way the FTC looks at this?

Mr. BAER. It is a question that I need to answer generically without regard to what we are finding, or expect to find, with respect to the Exxon-Mobil merger.

But if you look at the history of our investigations of mergers in this industry, we have found problems at the refinery level that concerned us and have ordered divestitures in the late 1970's and most recently involving the Shell-Texaco transaction. We found problems with pipeline transportation and have required companies to divest ownership interest in pipelines, so that they cannot straddle two pipelines and manipulate prices there. We have found problems at terminaling and at retail. We have also found problems with respect to the byproducts, the chemicals that are made out of the refining process. So at each of those levels a transaction, if both firms are present in that market, potentially raises concerns. So we need to be alert really across the waterfront.

Mr. BARTON. We are going to have a number of questions for the record. I know Mr. Bryant of Tennessee said he would have some questions. Mr. Hall said he was going to present his questions for the record.

So we are going to recess this hearing until tomorrow morning at 10:30. We do thank you, gentlemen, for attending. You will have questions. We hope you will reply in the very timely fashion. Tomorrow at 10:30 we will have the two CEOs of Mobil and Exxon Corporation.

The hearing is recessed until 10:30 in the morning.

[Whereupon, at 12:20 p.m., the subcommittee recessed, to reconvene at 10:30 a.m., Thursday, March 11, 1999.]

THE EXXON-MOBIL MERGER

THURSDAY, MARCH 11, 1999

HOUSE OF REPRESENTATIVES,
COMMITTEE ON COMMERCE,
SUBCOMMITTEE ON ENERGY AND POWER,
Washington, DC.

The subcommittee met, pursuant to notice, at 11:38 a.m., in room 2123, Rayburn House Office Building, Hon. Joe Barton (chairman) presiding.

Members present: Representatives Barton, Stearns, Shimkus, Pickering, Fossella, Bryant, Hall, McCarthy, Sawyer, Markey, Gordon, and Wynn.

Staff present: Cathy VanWay, counsel; Ramsen Betfurhad, counsel; Donn Salvosa, legislative clerk; Rick Kessler, minority professional staff member; and Sue Sheridan, minority counsel.

Mr. BARTON. If the subcommittee could come to order.

We have had a series of votes on the House floor which has delayed our 10:30 hearing until just now. I am going to wait a few more minutes to see if the ranking Democratic member, Mr. Hall, will be in attendance. I saw him leaving the floor the same time I did, so I want to give him the courtesy of coming. If he is not here in about 2 minutes, we will go ahead and start, but we are going to start very shortly.

[Brief recess.]

Mr. BARTON. The subcommittee will come to order. We are going to convene the second day of hearings on the merger of Exxon and Mobil. This is a continuation of a series of hearings that we started yesterday where we heard from the Federal Trade Commission, the Energy Information Agency, and the Securities and Exchange Commission.

Today we have two panels. On our first panel, we have Mr. Lee Raymond, who is chief executive officer of Exxon Corporation. And with him, we have Mr. Lucio Noto, who is the chairman and chief executive officer of the Mobil Corporation.

The second panel, we will have a representative of the Petroleum Industry Research Foundation, a gentleman who represents an analytical firm, and a gentleman who represents the Service Station Dealers of America.

I want to point out to the audience, this is an open, public hearing. Everyone is welcome, but we do expect that the rules of the decorum, in terms of committee meetings, be adhered to.

[Additional statements received for the record follow:]

PREPARED STATEMENT OF HON. CLIFF STEARNS, A REPRESENTATIVE IN CONGRESS FROM THE STATE OF FLORIDA

Thank you, Mr. Chairman. I appreciate this opportunity to learn more about the Exxon-Mobil merger. I am interested to hear from today's two panels about how they view the impact of this merger on national energy policy, consumers and interstate commerce.

Exxon and Mobil seem to be following a trend of consolidation in the industry—recently, we saw the merger of BPAmoco and Shell-Texaco. However, despite their reduced production, Exxon and Mobil will still produce the largest industrial merger ever and will create the largest private oil company worldwide.

The companies are targeting a 10 percent reduction in annual spending. Exxon and Mobil have stated that as a result, 9000 jobs will be lost in to the merger. 'How many of these cut jobs will be in the US? Will the number be closer to 12,000 employees, as some observers suggest? I would like to here more from our first panel about this projected job loss.

The CEO's of both Exxon and Mobil have indicated that to secure FTC approval of the $77 billion merger, the companies will be required to divest some assets. This means that they may sever contracts with more than 1,000 gas stations and sell one or more refineries. This problem is significant in the Northeast and Middle Atlantic states, where the two companies have significant market share. I expect our second panel will have much to tell us about their view of these divestitures.

With such a large merger, the implications for our national energy policy, consumers, and interstate commerce are not immediately clear. I look forward to hearing from our panels today to help us understand the Exxon-Mobil merger's effects. Thank you.

PREPARED STATEMENT OF HON. EDWARD J. MARKEY, A REPRESENTATIVE IN CONGRESS FROM THE STATE OF MASSACHUSETTS

Thank you, Mr. Chairman. I would like to begin by commending you for calling this second oversight hearing to review the proposed merger of Exxon and Mobil.

As the Subcommittee heard yesterday, the merger of Exxon, our nation's largest domestic oil company, and Mobil, the nation's second largest domestic oil company, would represent the largest industrial merger in history. The testimony we heard from the Federal Trade Commission at our last hearing indicated that presently Exxon and Mobil face each other at just about every level of the oil and gas industry—from the exploration for and production of crude oil, to the refining of crude oil into gasoline, home heating oil, or other petroleum products, to the manufacture of petrochemicals and lubricants, to the marketing of gasoline and other fuels to the consumer. We also heard that this proposed merger is not occurring in a vacuum, but appears to be part of a larger ongoing trend of consolidation and concentration in the oil and gas industry. The FTC noted, and I agree, that the existence of a trend towards concentration in an industry is highly relevant in examining the consequences of a merger and compels us to carefully consider the consequences of further concentration.

Today we will be hearing directly from the Chairman and Chief Executive Officers of Exxon and Mobil. We will be examining the trends in the domestic and global oil and gas markets—such as persistent low prices and increased exploration and production costs—that are said to be driving the current trend towards concentration and consolidation in the oil industry. We will be hearing about the potential benefits that the proposed merger could produce in terms of the increased savings and synergies that could accompany the combination of the assets and resources of these two industry leaders.

As I indicated yesterday, I am willing to accept the proposition that there may be a compelling business and economic rationale for a consolidation in the oil industry, particularly in the areas of exploration and production. But I also believe that a transaction of this size and scope clearly merits serious attention and scrutiny by our nation's antitrust regulators to assure that it does not stifle competition or result in higher prices for consumers purchasing gas at their local service station or heating oil for their homes. It is therefore absolutely essential for the FTC to look very carefully at the impact of this proposed merger on regional wholesale and retail markets in the United States. The new company to be created out of this merger reportedly will be called Exxon-Mobil. It is our duty to assure that its real name does not become "Standard Oil"—a name synonymous in this country with excessive monopoly power.

During today's hearing, I will be particularly interested in hearing from both Exxon, Mobil, and the other witnesses about how we can assure that merger, if ap-

proved, can be structured to address any potential anti-competitive effects on regional wholesale and retail markets, particularly in the Northeast. Thank you, again, Mr. Chairman, for calling today's meeting. I look forward to hearing the testimony from our witnesses.

Mr. BARTON. I want to welcome our first panel. Your entire statement is in the record in its entirety, that has been presented to the subcommittee.

I am going to recognize Mr. Raymond for such time as you may consume to elaborate on your statement, and then Mr. Noto, and then obviously the subcommittee will have questions.

Gentlemen, welcome.

Mr. Raymond, you are recognized for an opening statement.

STATEMENTS OF LEE R. RAYMOND, CHIEF EXECUTIVE OFFICER, EXXON CORPORATION; AND LUCIO A. NOTO, CHAIRMAN AND CHIEF EXECUTIVE OFFICER, MOBIL CORPORATION

Mr. RAYMOND. Thank you, Mr. Chairman.

I think, in the interest of time, I would just like to add a few comments in addition to the material that we have submitted for the record.

Fundamentally, the driving force that is behind this merger is the very competitive nature of the oil and gas industry, both in this country and around the world. If anything, the competitive forces over the last several years have continued to intensify and become even more difficult in terms of being able to provide an adequate return to our shareholders, while at the same time providing the kinds of goods and services that we think are important for our customers.

Of course, the competitive landscape in our business started to change significantly some 25 years ago with the arising of state-owned oil companies and the nationalization of many interests that we and other companies had, both in Latin America and the Middle East. Those companies, of course, have developed and continued to grow their businesses and, as a matter of fact, some of them are major competitors of ours in the downstream operations in this country today.

But, of course, the fundamental point that is behind all of this is the direct link between economic growth and availability of competitive energy supplies to our economy, as well as to all the economies of the world. There is no question that this country continues the need to have a strong and viable energy industry. Without it, the engine of economic growth, which is access to energy, simply won't be there, and eventually that will become a significant problem for the country.

But from my point of view, in terms of managing a company in that industry, success in this environment means we have to manage the factors over which we have control, which are costs. I think the events of the last 18 months, in terms of what has happened to the variability of crude price and the volatility, illustrate once again—and even more so than in the past—that for our company to continue to be successful, means we have to more and more focus on those activities where we have the control and that, primarily, is focused on costs.

Those companies that can control costs and have access to potential resources are the ones that will be able to meet future energy demand and will be successful in the longer term. But what this calls for, of course, is efficiency, quality people, strong finances, development of leading-edge and applying leading-edge technology, and economy of scale. In that sense, mergers help capture these benefits, in the short term, through savings and efficiency steps, and in the longer term, in more effective use of capital.

We think the Exxon merger with Mobil will, first of all, create synergies and efficiencies that will enable the new company to provide high-quality products to our consumers at more competitive prices, provide to us and our shareholders a more diverse business portfolio which we think is essential in the volatile environment that this industry has to operate in. And, last, it will allow the new entity, which is a combination of two strong American oil companies, to compete more efficiently with foreign-based multinationals and the very large state-owned oil companies.

With that, Mr. Chairman, I would really like to move to try and be able to respond to questions that the committee may have.

Mr. BARTON. Thank you, Mr. Raymond.

We would now recognize Mr. Noto.

Again, your statement is in the record in its entirety, and we will give you such time as you may consume to elaborate on it.

For members who weren't here yesterday, we did opening statements by members yesterday. Any member present today that wishes to put an opening statement in the record, it will be put into the record at the beginning of the hearing process.

Mr. Noto, you are recognized.

STATEMENT OF LUCIO A. NOTO

Mr. NOTO. Thank you, Mr. Chairman. Thanks for the opportunity to be in front of your subcommittee today.

Mr. BARTON. You need to put the microphone closer to you, sir——

Mr. NOTO. Sorry.

Mr. BARTON. [continuing] so that the recording clerk can hear you.

Mr. NOTO. Is that better?

Mr. BARTON. That's better.

Mr. NOTO. Thank you.

Mr. BARTON. Yes, sir.

Mr. NOTO. It is a pleasure to be with you today. Thank you very much for giving us this opportunity to testify.

I think Lee has given you a picture of the new industry for us—much more competitive, dealing with projects that are much more complex. A lot of the "easy oil"—if you will let me use that expression—has been found, and it is being produced. The world is going to need more energy in the future, notwithstanding the fact that right now there is a surplus. The combination of Mobil and Exxon is certainly going to be better poised to be able to develop more diverse sources of energy for U.S. and worldwide consumers than they would on separate companies.

These projects are complex; they are technologically demanding. They are in, frankly, riskier places—the Caspian, the Middle East,

West Coast of Africa. Even a company the size and with the experience that Mobil has, is having difficulties managing its programs right now, wanting to do enough of these new projects and develop new energy in the future and still manage its existing business, and still keep its shareholders happy with dividends. We did this, recognizing that we had a history of 130 years as a separate company, and a proud history.

We are absolutely convinced that being part of this combination is going to be better for our shareholders, better for our customers, and, ultimately, better for the people who consume our products. From a shareholder point of view, I think it is obvious. From a customer point of view, the efficiencies that we are talking about generally get flowed into the marketplace in the form of lower prices. Some of our major competitors have put their businesses together here in the U.S.—BP and Amoco, Shell and Texaco. They expect—and I suspect—that they will be able to realize savings in the hundreds of millions of dollars. That exceeds the amount of money that I am making in the U.S. downstream, and my U.S. downstream is a good business. So for me to stay competitive, and for me to be able to satisfy my shareholders and my customers, I am going to need a level playing field. I'm going to have to be able to accomplish the same kind of savings.

We have done a lot in the last 7 years on our own. Regrettably, we have shaved about one-third of our manpower. We have sold billions of dollars of assets that weren't producing the right kind of returns. And we got to the point where further cost savings will not be easy to accomplish. So far, we put $4 billion of savings on the books. We got to the point now where we are talking about muscle and not fat. We are getting to the point now where if we try to take hundreds of million dollars out of our business, we are really going to impact our ability to grow in the future, so this merger for us represents a very, very important step.

We think our customers are going to be better off. We will be able to be fully competitive. I am—we are committed to do this merger. We want to try to do it in an expeditious fashion. And we would be very happy to try to answer any of the questions that you might have today.

Thank you.

[The joint prepared statement of L.R. Raymond and Lucio A. Noto follows:]

JOINT PREPARED STATEMENT OF L.R. RAYMOND, CHAIRMAN AND CHIEF EXECUTIVE OFFICER, EXXON CORPORATION AND LUCIO A. NOTO, CHAIRMAN AND CHIEF EXECUTIVE OFFICER, MOBIL CORPORATION

Mr. Chairman, we appreciate this opportunity to appear before the subcommittee to discuss the proposed merger between Exxon and Mobil and to answer any questions you may have.

For a number of reasons, we believe this merger is compelling for our two companies, our customers and our shareholders. In addition, we believe it to be an important step in strengthening the ability of American industry to compete in an increasingly challenging global business environment.

The principal driving force behind this proposal is the intensely competitive nature of our industry. We will outline the elements of the environment in which we are operating, discuss why mergers are an appropriate response to that environment, then turn to the specific advantages of the Exxon-Mobil merger.

Petroleum Industry Environment

The key characteristics of the current environment are intense competition and a changing business landscape, compounded by an imbalance between oil supply and demand. Oil demand showed essentially no growth over the past year while supplies rose, creating an increase in inventories. The reasons include the Asian economic crisis and mild winters as well as increased production by OPEC countries, including the near-doubling of production from Iraq in 1998.

In the upstream—or exploration and production sector—of the energy business, one of the most significant developments has been the growth of state-owned oil companies and their expansion beyond their traditional boundaries. The nationalization of assets of private oil companies by OPEC countries in the 1970s established for many of these state-owned companies a significant concentration of productive capacity and reserves, especially in the Middle East, with the competitive advantage of relatively low development and operating costs. As outlets for their production, many state oil companies have established refining and marketing operations in other countries, including the United States.

In some countries that are net importers of oil, government companies have been aggressively acquiring foreign reserves to improve the security of their supplies.

During this period, private companies have focused on using advanced technology in existing non-OPEC producing areas such as Alaska, the North Sea, the Gulf of Mexico and Canada. However, as fields in these areas have matured, exploration efforts have shifted to prospects in more remote and challenging areas such as the deep waters off West Africa and Brazil. The opening of the former Soviet Union, and in particular the Caspian region, has created additional opportunities for private investment, but at higher cost and increased levels of risk. Overall, the trend has clearly moved in the direction of higher-risk, geographically remote, and technically challenging production opportunities in politically sensitive areas. Competition for these new prospects is intense, as is the need for technology advancements that will deliver lower finding and recovery costs. This is critical in a business where the cost of single projects can run into *billions* of dollars.

To the consumer, perhaps the most visible change has been the increased competition in the downstream—or refining and marketing business—particularly at the retail level. Independents have established a growing presence in the marketplace, as have non-traditional retailers such as "hypermarkets," whose core business may be food or general retail, but who provide fuelling facilities as a way of attracting customers to their stores.

Refining capacity has continued to grow because of expanded production from existing facilities and the start-up of idle capacity. Finished product imports from Europe, the Middle East and Latin America are now competing for the consumer's dollar. The relatively low returns and weak margins in the refining and marketing sector have forced many companies to take steps to improve financial performance—steps such as consolidation, joint ventures, restructuring and divestitures. Cost control, manufacturing efficiency and yield maximization remain industry priorities.

Another major issue in the refining and marketing business has been the emergence of low-cost, highly competitive independent refiners and marketers as industry trend-setters, often acquiring and effectively operating facilities that major oil companies considered non-core assets. Independents' share of retail gasoline sales in the U.S. has grown from around 41% to over 45% since 1992. Independent marketers have experienced similar rapid growth in many other countries.

Looking ahead, over the near term, supply and demand should eventually come back into balance as Asian economies recover and surplus inventories are drawn down. With the eventual restoration of a more balanced market, the industry will be better able to finance new oil and natural gas developments, but there will still be intense competition for the more attractive exploration and production opportunities, continued downward pressure on costs and the need to apply increasingly sophisticated technology. There is more than adequate refining and marketing capacity to meet consumer needs, for the next few years at least, but the industry will need to invest large sums for increased fuel quality.

The longer-term outlook is governed by the unarguable link between energy demand and economic growth and the vital role of fossil fuels in meeting future energy needs. With continued expansion of world economies, oil consumption is projected to grow at an average annual rate of about 2 percent over the next 20 years. Much of this growth will be in the transportation sector, especially in less developed countries, where there is no practical alternative to oil.

Natural gas demand is expected to grow even faster—at roughly 3 percent annually on average—spurred by electricity market deregulation in developed countries and the increasing electrification of developing nations.

Industry's principal challenge will be to find economically viable sources of oil and gas. As production from mature fields declines, replenishment of reserves coupled with growing demand will require the application of technologies not yet developed and the deployment of best industry practices for operational efficiency and cost effectiveness. Wise choices in investment selection and management in this capital-intensive business will be essential.

This is increasingly important as the United States' dependence on oil imports continues to grow. We need energy to support economic growth, but we can't solve the import-dependence problem simply by stopping imports. The solution is to manage the risk by seeking additional diversification in our own sources of supply. This means that we must encourage the development of resources and production capacity from diverse areas of the globe, in addition to the Middle East. A significant portion of the world's future oil and gas supplies will come from remote, politically sensitive regions involving projects that require technological advances and large amounts of investment capital.

In the downstream, large investments will be required to meet ever-tighter environmental requirements—such as reducing sulfur in gasoline—higher product quality standards, and the need for research in developing the fuels of the future.

Managing an Energy Company in the Current Environment

The energy business has always been challenging, but today companies seeking to supply their customers at a competitive price and deliver an appropriate return to their investors face new difficulties.

The petroleum business is inherently unpredictable and always full of surprises. We have no control over basic raw material costs. And we cannot know when the economic rebound will occur in Asia or whether a supply disruption is on the horizon—nor can we make any safe assumptions about the specific impact of such events on oil markets.

In other words, the industry must deal with a high level of uncertainty and volatility. Combine that with the fact that the energy business is very capital-intensive and involves projects that take many years to develop and repay their investments, and it becomes clear that any company hoping to do its job must have its house in order. It must, in other words, consistently strive to do its business in the most efficient manner possible.

A truly efficient company has:

Economies of scale. Large energy projects require large organizations for two reasons. One is the magnitude of physical, financial and technological resources they can bring to a job. The other is their ability to use their size to lower operating costs as well as justify the development and use of the most advanced technology in order to be competitive.

Financial strength. To compete and to meet its commitments to customers and shareholders, a company must have the requisite financial resources: both substantial cash flow and a strong credit rating. These assets keep financing costs low, provide the reach to consider a spread of opportunities around the world to better manage risk, and make it possible to fund the research needed to develop new technology.

Operating synergies. Simply put, this entails finding ways to combine elements of different operations in a way that yields more product, cost savings, service, profits or other benefits than could be achieved by the individual operations themselves. This helps create a far more competitive company, able to serve customers more efficiently and at lower cost.

Investment selectivity. Investment decisions are often challenging, but it is essential to develop a broad range of investment options and to rigorously test them against a wide range of scenarios, then move ahead decisively with commitments that make the most economic sense.

Quality portfolio of exploration and production investment opportunities. In today's environment, it's essential to assemble project opportunities that offer the highest return at the lowest cost. There is simply no room or reason for maintaining marginal prospects.

Cutting-edge technology. Technology has long played a key role in the energy business, which is one of the world's highest-tech industries. For example, developing an oil discovery in very deep water, at a cost that makes the project economic, has required major technological advances. In addition, today's environmentally sound fuels and high-performance lubricants have required major technical advances in refining.

Talented people. For all the material resources a successful energy company requires, none of them matter without intelligent, well-educated, highly motivated people of integrity to put them to work.

In sum, the energy industry must today work vigorously to adapt to increasingly difficult conditions. A logical and positive part of that adaptation process is a phenomenon we have seen increasingly in recent years: the merger.

The Value of Mergers

The driving imperative in succeeding in today's energy business is to manage those factors over which we have some control, as opposed to oil prices, which are set by the marketplace. There is much that can be done to manage costs and future capital programs. This is essential if a company is to be competitive, profitable and able to make the large investments needed to ensure future customer energy demand can be met. Mergers are an excellent way to enhance the ability to manage costs better and be a more efficient competitor. And in the case of combining two American companies, a merger creates an entity able to compete on a level playing field with the largest global firms in the industry.

Mergers can lead to a new entity that can do a better job of supplying energy, and at a lower cost, than the two original companies could on their own. Combining redundant operations, for example, creates significant opportunities to achieve improved efficiencies—efficiencies that result in lower costs and ultimately benefit the consumer.

Moreover, where the merger parties have complementary operations, mergers enhance the important business advantages of functional and geographic diversity as well as financial strength—all of which are essential to succeeding in a highly volatile price environment.

More broadly, the rationale for mergers encompasses both near-term and longer-term benefits.

In the early years following a merger, cost savings can be expected from improved organizational efficiency, the high-grading of programs throughout the business, optimal use of raw materials and intermediate products, implementation of each company's most effective and efficient operating practices and optimizing procurement activities across the two companies' supply, refining and chemicals networks.

Capturing these near-term advantages is important, but we believe the key driver in many oil industry mergers is the longer-term opportunity to improve capital productivity—to get the most out of invested dollars in an industry where time horizons can be quite long.

More specifically, the merged company will be able to choose from an extensive portfolio of investment options in all parts of its business. It can also benefit from improved investment selectivity by realizing comparable or higher earnings contributions from lower annual capital expenditures than the two companies could have realized separately.

In addition to these prospective investment opportunities, the combined company should also benefit from continued application of a systematic and disciplined asset management program.

The Exxon-Mobil Merger

We believe the Exxon-Mobil merger will create synergies and efficiencies enabling the new company to provide high-quality products to consumers at more competitive prices. It will also allow us to provide shareholder value to the hundreds of thousands of people who invest in Exxon and Mobil directly and the many more who have an indirect stake in our performance through mutual funds and pension plan investments.

It's important to note that both companies share a large number of common values.

First and foremost, Exxon and Mobil share a common resolve to maintain the highest standards of safety, health and environmental care.

Both companies also have a long-term commitment to creating shareholder value and to meeting the needs of our customers as efficiently as possible.

Most important, we have the high-quality people necessary to get the job done right.

In other words, the two companies line up very well with each other and make what we believe to be an excellent fit.

As is not unusual in cases such as this, the Exxon-Mobil merger will have an impact on the combined worldwide staffing of both companies, currently about 123,000. At this point in time, we estimate a surplus of about 9,000 employees worldwide. Transition teams composed of representatives from both companies are carefully evaluating the staffing needs of the new organization.

On the issue of jobs, we believe it's important to bear in mind that staffing reductions have occurred continually over the past two decades in the oil and gas indus-

try and are likely to remain a part of the ongoing industry rationalization process, whether or not mergers occur.

The merger will provide the new company with a more functionally and geographically diverse business portfolio, which is essential in a highly volatile industry environment. In many of the most promising areas around the world, our existing assets are very complementary. For example, Exxon's deepwater exploration position in West Africa will combine with Mobil's existing production in Nigeria and Equatorial Guinea. In the Caspian, Exxon's presence in Azerbaijan will combine with Mobil's presence in Kazakhstan and Turkmenistan. And Mobil's position in liquefied natural gas should complement Exxon's involvement in this high-growth clean fuel business, both in traditional pipeline sales and in gas-to-liquids technology.

This proposed merger of two American companies, with headquarters in the United States, will allow the new entity to compete more efficiently with the foreign-based multinational oil companies and the very large state-owned oil companies that are rapidly expanding outside their home bases—both geographically and functionally. Unless we are able to compete on the same scale as these other recently merged companies, they may lock in a cost advantage that will not be passed on to consumers. The merged company's larger resources—financial, technological and human—will increase our ability to participate in more of the difficult and risky new opportunities in the global oil and chemical business. This broader resource base will help ensure that we are able to make the very large investments needed to meet the energy needs of our customers in the next century.

Another key reason for the merger is the opportunity to increase the company's competitiveness through business synergies, or savings. Those synergy benefits come as a result of the merger and would not be available to either Exxon or Mobil individually. Put another way, this is a case of the whole being greater than the sum of the parts.

Anticipated savings fall broadly under two categories—near-term synergies and capital productivity steps.

We expect to achieve substantial annual synergies from a diverse set of initiatives ranging from organizational efficiencies to more efficient and profitable product manufacturing—what we call "molecule management." They include expense reductions as well as revenue enhancements.

The new company will also have a larger, more diverse asset base, which will provide opportunities to optimize capital productivity. It is the opportunity to improve capital productivity that drives the merger rationale longer-term—and ours is a very long-term business. Combined with expected cost savings, these synergies will help the combined company compete for the consumer's business even in a prolonged low-price environment. Only by operating as efficiently as possible will we be able to carry out the costly and complex projects and continue to develop and apply the cutting-edge technology needed to provide additional energy supplies in the next century.

Past experience in both our organizations would suggest there is plenty of room in a merged Exxon and Mobil for an active asset management program, in discrete steps, over a period of years.

Looking to the future, we expect to benefit from enhanced investment selectivity, which should allow the combined company to operate more efficiently than the two on a stand-alone basis.

The merger will provide the combined companies with a more complete portfolio of petroleum and petrochemical operations around the world.

It will significantly improve the new company's ability to compete with other shareholder-owned companies, as well as state oil companies, both of which are strong competitors.

It will enhance the new organization's financial, technological and human resources, which will improve its ability to take on new challenges.

These factors add up to running the business in a way that is significantly more cost-effective and makes the most productive use of the organization's capital. This is a plus for the company's shareholders, but it's also a major benefit to consumers because it gives the company the means to deliver its products to the public more efficiently and at lower cost.

The merger will also mean that the Exxon Mobil company will be able to compete on the same scale as the largest foreign firms. The U. S. energy industry is one of America's most important strategic resources. In order to remain viable and to continue to meet society's needs, it must have the flexibility to adapt as times change and circumstances dictate.

Mr. BARTON. Thank you, Mr. Noto.

The Chair is going to recognize himself for the first 5 minutes of questions, and we will go in alternating order. And, obviously, we may need more than one round, so if members have numerous questions, you will be given at least two opportunities.

So, the Chair recognizes himself for the first 5 minutes.

My questions are going to be general to both of you, so which ever one of you wishes to take it, it is directed at both.

When the Energy Information Agency was here yesterday, they put a little pie chart up that showed that in 1997, 52 percent of the world oil market was controlled by state-owned oil companies like Saudi Aramco and the Venezuelan company, Pemex, and the like. So when we look at Exxon-Mobil, obviously, if the merger goes through, it is the world's largest privately owned oil company, but you are only in the top five, in terms of oil companies worldwide.

So, my first question is, how big does a company need to be in order to compete in the world market, given the economies of scale that you are not competing against other private companies as much as you are competing against state-owned, and in some cases, monopoly companies?

Mr. RAYMOND. Well, I don't think there is an answer that you can give to that from the standpoint—I'll say it, from a top-down point of view.

I think that the only way you can begin to answer that question is if you look at companies like ours—and Lou can speak for Mobil—all we can do is look at the position we have relative to our competitors. And in the case you are talking about now is in the upstream business, because these companies are largely in the upstream, although in some cases, they are in the downstream, too. But they are in the exploration and production business.

And the question is, as we look at the kinds of opportunities we have and the kind of risk management we think we need to undertake, in order to continue to have a strong and viable company, that is the only measure we can use. And the conclusion we have come to is that by putting Mobil and Exxon together, that, particularly in the upstream, we will have a portfolio of upstream activities around the world which will diversify our asset base to the point where we think we can be a more effective competitor than we are now.

That doesn't answer your question, "Are we absolutely able to compete on an absolute basis?" But we know that if we do this, we will be much more effective than we would be if we do not do it.

Mr. BARTON. Well, here is my concern. We have an obligation to provide an open marketplace for the American public—we, the Congress, and the executive branch. You have got an obligation to provide the highest rate of return possible to your shareholders and to provide products that are quality and competitively priced in whatever markets you participate in, which are not just in the United States, but overseas.

But if you look at the domestic—as you put it—downstream market, the market that most impacts the average Americans, is the gasoline market, and you go to the gas station to get gas. And most people know Citgo. Citgo is owned by Venezuela.

Mr. RAYMOND. That is correct.

Mr. BARTON. It is a state-owned oil company, competing at the retail level in the United States. Saudi Arabia has a Aamco; they have a 32.5 percent stake in a company called Motiv, which is a joint venture between Texaco and Shell, and they have 14,000 gas stations in the United States.

So, I think the Congress has an obligation, not only to look and insist that there is competition in the marketplace, but that it is of such a nature that it is the classic so-called "private" competition. If we get to where the only gas stations on the corners in our neighborhoods are owned by state-owned oil companies overseas, I don't think they necessarily have the best interest of the American consumer at heart.

So, that is what I am trying to get to, is, you know, when you look at this merger at first glance, you think, "My, God, why does Exxon and Mobil need to be merged? They are among the largest privately owned oil companies in the world."—or at least Exxon is. But then when you look at all the charts, and you get all the information, you are not competing against Arco and some of the retail providers like Phillips 66. You are competing against state-owned oil companies, including the Iraqi oil company.

Mr. RAYMOND. You are right, Mr. Chairman, and that is particularly true in the upstream part of the business, which the average consumer in this country isn't aware of and I am not being critical, I am just saying they aren't aware of what goes on in the exploration and production side of the business.

Now in the downstream, you are right, in terms of Petroleos de Venezuela and Saudi Aramco. But I guess I would point out that in the downstream business in the country, 45 percent of the gasoline that is sold at the retail level—gas at what you and I would call "service stations"—are not owned by major oil companies. They are owned by independent retailers, independent marketers. And even Exxon and Mobil, when it is put together, will only have 12 percent of the U.S. retail gasoline market. Now that is a lot of gasoline; I'm not saying that is not true. But when you look at it, in terms of concentration, there are very few industries in this country as broadly based, that touch as many people every day as our industry does, but at the same time, has as many players in it as our industry does. The contrary is the case—the automobile industry, for example. You can just name almost any other industry, and they are very few players. Ours is unusual in that it has very many big companies as well as independent retailers.

Mr. BARTON. My time has expired.

The Chair recognizes the distinguished ranking member, Mr. Hall, for 5 minutes.

Mr. HALL. Mr. Chairman, I thank you.

I guess my first question would be directed to Mr. Noto whether or not—what would have happened to Mobil if this merger hadn't come around, and whether or not you could have gone it alone and still be the company that we know today and we respect today? Just what are the facts surrounding that?

Mr. NOTO. Sir, I am reasonably satisfied that we could have existed—continue to exist on our own. I think we could have survived. I think we have the skill base, the history, the reach. But my issue is, is that the best alternative for my shareholders, and

really also for my customers? Because, ultimately, if it is not a good deal for my customers, it is not a good deal for anybody.

We looked at a lot of alternatives. There have been a lot of changes in this industry. Lee touched on the arrival of new foreign competitors, these combinations in the U.S. downstream—Texaco and Shell, very formidable combination, probably has 14 to 15 percent of the U.S. gasoline market—the biggest of any marketer, and certainly would still be bigger than the combination of Mobil-Exxon. They have taken a lot of costs out of their business. For me to be competitive, I had to do something. Status quo just didn't work.

We looked at a lot of alternatives, both inside the company and with outside help. We looked at buying some; we looked at making some acquisitions. We looked at merger of equals, if you will—two similarly sized companies. At the end of the day, we concluded, based on everything we knew, the combination of Exxon and Mobil could create the kind of company that could be top quartile.

Our business is a great business. As long as you are either No. 1 or No. 2 in everything you do, you can make a living. If you are not, you are in trouble. There are a lot of companies in our business not making it and won't be able to satisfy their shareholders' aspirations.

Mr. BARTON. Second place in election, you don't make it a living. So——

Mr. NOTO. So, we concluded that this was, even though we could survive on our own, we concluded that this was a better alternative, notwithstanding the fact that it meant quite a bit of change. It meant a change for me personally, and it meant a change for a company that had survived for 130 years as a independent entity.

Mr. HALL. What regulatory body will give you the most scrutiny? And what is the, I guess, the program for that? And, time-wise, what kind of time are we talking about?

Mr. NOTO. Sir, we have a number of things happening simultaneously. We have filed a preliminary proxy statement with the SEC, and we have gotten some comments back, and we are working with the Commission. And we hope to be able to issue a final proxy to our shareholders in time for a shareholders' action at the end of May.

We are working with the FTC, who has jurisdiction over this proposed merger. They have made certain requests for information, and our people are meeting with them. We are trying to cooperate with them.

And outside the United States, the principal area of activity will be in Europe with the Director General of Competition, the so-called "DG IV," in the Economic Union in Brussels, and we have also started that process.

Mr. HALL. I yield back my time, Mr. Chairman.

Mr. BARTON. It is rare for a Member of Congress to yield back anything, so we appreciate that.

Mr. HALL. I don't have any problem with the merger. I don't want to ask too many, and I don't know how to lobby him an easy one to knock out of the park, so——

Mr. BARTON. The Chair would recognize the vice chairman of the subcommittee, Congressman Stearns of Florida, for 5 minutes.

Mr. STEARNS. I thank my chairman.

It is not often that you get an opportunity to ask questions of two high-ranking CEO's like this, so I am going to take a little bit a different approach here.

The question is, is big always better? And in this case, you think it is. But when you look at the landscape in your competition, particularly dealing with Texaco and Chevron, our staff points out that both Chevron and Texaco outperform Exxon in both production costs and net income as a percentage of revenue, and yet, Exxon still dwarfs Chevron and Texaco if you combine them.

So the question, "is big always better?"—it would appear from these facts that both of these companies outperform Exxon in these areas, so why do we need to merge?

Mr. RAYMOND. Well, I don't know the data you are looking at, but just let me comment that the standard which is universal in the industry is not percent of revenues, because percent of revenues in our business isn't a particularly useful piece of information. The standard that is used universally to judge the performance of companies is return on capital employed. And Exxon, for the last I will say 30 years that I know of, has always led the industry in return on capital employed. That is, we have made the most effective use of our capital as we have deployed it around the world and in our various businesses. And I, without fear of contradiction, I can tell you that in 1998, Exxon clearly led the industry in return on capital employed.

Mr. STEARNS. You don't dispute, then, that perhaps the facts that there are production costs and net income as a percentage of revenue?

Mr. RAYMOND. I would be amazed because our production costs are interesting, but the relevant issue is production profits. And the per barrel production profits that Exxon has had, have always led the industry. And I would dare say, without even looking at it, I would be amazed if our profit per barrel did not exceed that of Chevron and Texaco by at least $1 a barrel.

Mr. STEARNS. Okay.

Let me move to a real local level. You have a gas station on the corner. It is a Mobil station, and then you have a gas station right next to it that is an Exxon station. Now what is going to happen when you merge? You are going to have to divest yourself of some of these probably. And can you assure the gas owners, the people that are your franchisees that they are going to be protected as this moves—because you own the properties perhaps in many cases, in some cases? Explain to us, and what kind of assurances service station owners will have, that if they have a Mobil and an Exxon right next to each other, what you are going to do.

Mr. RAYMOND. Well—and Lou, you might add to this. First of all, the question of what happens where there is—I will call it both Exxon and Mobil service stations—is the issue that is really before the FTC. And in that sense, I can't answer that question.

They are looking at the data; they are looking at the information, and they will draw some conclusions, one way or another, of what needs to be done—if anything—for them to approve the merger.

Mr. STEARNS. Mr. Raymond, if we take a record, the FTC, with the BP-Amoco, required the company to divest of 134 gas stations and to allow branded resellers supplying over 1,600 gas stations to cancel existing supply contracts without penalty.

So we have a history here that this has occurred before. So we know that the FTC is probably going to force you to do the same. And so, again, going back to the service station people, you know——

Mr. RAYMOND. Not to be argumentative, but I am not going to conclude that, because it turned out in the BP-Amoco, that was the first time that the FTC had ever taken a position like that with regard to retail service stations. So I think it is an issue to be discussed with the FTC, and I am not going to prejudge——

Mr. STEARNS. Oh, I know.

Mr. RAYMOND. [continuing] a conclusion one way or another.

Mr. STEARNS. I understand. But wouldn't you agree that FTC is probably going to rule something similar to that, which would affect not only the gas stations, but the refineries also?

Mr. RAYMOND. I would hope not.

Mr. STEARNS. Okay.

Okay, thank you, Mr. Chairman.

Mr. RAYMOND. But they are protected by PMPA, the Petroleum Marketing Practices Act.

Mr. NOTO. Could I just add two things?

Mr. RAYMOND. Could you add to that one?

Mr. NOTO. First of all, on the second question—you need to remember that the dealers are an integral part of our business. We operate only about 8 or 9 percent of our service stations; the rest are dealer-operated stations. Sometimes they are dealer-owned, and sometimes they are dealer-leased from the company. They are an integral part of our business. We spend a lot of time and effort working together to try to get the best outcome for both of us.

So, start with the principle that we are going to behave in a responsible manner, because if we don't behave in a responsible manner, it is going to cost us.

Let me go back to your first question, "Is big, better?" We never put this together because we wanted to be the biggest in anything. We want to be the most efficient. Sometimes that means you are going to be the biggest. We are going to be more efficient in the U.S. downstream, but we are not going to be the biggest in the U.S. downstream. We are not concerned about that.

But we want the opportunity to get the efficiencies, both short-term cost efficiencies because we have overlapping operations, and long-term capital efficiencies because we can run our business better.

One day in—I think it was in October or November—the New York Times ran two stories on the front page—one about problems in Nigeria and one about problems in Indonesia. Those are two important core assets for me. I am a big company; those two represent a big piece of my business. My shareholders lost something in the order of $8 billion in capitalization that week because I do not have the kind of spread among different kinds of projects that I think is going to be necessary to manage the business successfully for the shareholder in the future and also to satisfy the re-

quirements that the market is going to want. They want more energy.

I can't do everything I want. I would like to be able to be there. I would like to be able to be here. I would like to be able to be here and be big everyplace, because those are big projects. I can't do it. This price problem that we have today is exacerbating my issues. I just don't have the cash-flow to allow me to support a budget which gives the U.S. public confidence that we can have a wide variety of diverse energy sources like this, even though we import 50 or 60 percent of our energy, it is relatively secure, and at the same time, give my shareholders the kind of return they need.

So, bigness is not bad. It gives you spread; it lets you manage risk. But we didn't do this just to be No. 1 on some Fortune chart. We did this because we think it would be a more profitable company than anybody else.

Mr. BARTON. We are going to have a second round for this witness panel, so we want to resume regular order.

Mr. Sawyer, of Ohio, is recognized for 5 minutes.

Mr. SAWYER. Thank you, Mr. Chairman.

Thank you, gentlemen, for your presence here today.

I mentioned in opening statement yesterday that I live in Akron, Ohio, and represent that community, a community that has been known for a signature tire industry for most of this century. It is an industry where, from the time that I was a kid, there were between 30 and 40 tire companies in Akron, alone. They rapidly began to coalesce into smaller numbers of companies and to the point where, today, we have some four global giants in that industry. The mergers and acquisitions and alliances that were put together were viewed as needed to survive changing times and the competition for capital and rapidly changing product and production technologies.

To what degree is that kind of analogy similar to the kinds of forces that you have been facing in your businesses and are likely to confront other large businesses that play on a transnational and global scale?

Mr. RAYMOND. Well, I think my reaction to that would be that while every business or every industry probably has its own unique characteristics, I think there are a few that are relatively similar.

I have often said that our industry is the largest high-tech commodity business in the world. For example, in exploration and production, some of the activities that we undertake, in terms of seismic technology—the offshore platforms we build are space-age type technologies—the facts are most people never see them because they are hundreds of miles offshore and there is no way to get there, and we, obviously, aren't in the tourism business and we are not about to take people out there.

But the facts are, in order to have that kind of technology, you have to have a very large enterprise to support it. To have leading-edge technology, it costs you a lot of money. You have to a have a large base over which to allocate the costs. The more and more we see the pressures on technology which are critical to our industry and the development of that industry, the more and more pressure you are going to see for companies to have to have the scale

to support it. And the people who don't have the technology, almost by definition as time goes on, get farther and farther behind.

I suspect there are many industries like that. The tire industry was one. We know that because we supply a lot butyl to the tire industry.

Mr. SAWYER. You are a feedstock supplier to——

Mr. RAYMOND. We are feedstock suppliers; we watch that very carefully. But the point is, that big isn't necessarily bad in the sense to be able to do the kinds of things you need to do on a world-scale basis and have the technology, you need to have that scale. You need to have the kind of financial resources that come from putting companies like ours together.

And, ultimately, everybody benefits from that because there, then, is available a broader array of supply sources to the United States—for example, to import crude oil or whatever else you want to do.

The facts are this country is a major importer of crude oil, and it is going to continue to become a larger and larger importer of crude oil. And the only real way you have of being able to protect that is have a wide array of sources. What you can't stand to be is an importer and have only a single source. And we found that out in the early 1970's.

Mr. SAWYER. Yes.

Mr. RAYMOND. And it is the ability of companies like ours to have that portfolio that really builds the kind of resources that you need to have so you do have some security of supply.

Lou, do you want to add to that?

Mr. NOTO. Yes. It would probably be nice to be able to go back to a world where you could support 40 family tire companies. And if you had not allowed those 40 to become 4, you might have 0 today, because Bridgestone, because Pirelli, because Michelin are as competitive with your Akron companies as they are with one another. So you may not like it, but at the end of the day, you have more competition because you have 4, and the consumer has more choice because you have 4 than conceivably he could have had if you had blocked those 40 from becoming 4.

Mr. SAWYER. Well, I am not suggesting that at all. I am suggesting that the decisions that we are seeing here today are not unique to your business——

Mr. NOTO. I don't disagree.

Mr. SAWYER. [continuing] and that they are driven by similar global forces over which you have little control but to which you can respond in the interest of survival—and not just survival, but thriving—in a rapidly changing environment.

Mr. NOTO. What is interesting about our business is that while we are facing that kind of international competition, we are also facing a brand-new innovative type of marketer—Costco's hypermarkets, perhaps Wal-Marts, in the future—that sell our main product at rock-bottom prices in order to attract customers to go inside their markets where they can buy higher margin products from them.

So this is a diverse, very competitive, very, very interesting marketplace that this business operates in.

Mr. SAWYER. Mr. Chairman, I appreciate your flexibility, and thank you for your insights.

Mr. BARTON. The gentleman's time is expired.

I would just make the point, before I recognize Mr. Bryant, there is a grocery store chain in Texas called HEB, H.E. Butt, and it is Tyler, Texas. I can buy gasoline at their pump for 75.9. I guess a gallon of gasoline is 64 fluid ounces, I am not sure. But then I go in the store, I can buy Coke for 79 cents.

Mr. RAYMOND. You have got it.

Mr. BARTON. So I am paying—if I had to pay the same for the Coke that I paid for the gasoline, I would be paying about $5 for the Coke, or visa versa.

Mr. RAYMOND. Mr. Chairman, there is no liquid in a grocery store that is as cheap as gasoline.

Mr. BARTON. So, the point about your competitive situation is well taken.

Mr. SAWYER. Mr. Chairman, my guess is the same thing applies to spring water that you can get in there. I just urge you not to carbonate your gasoline—the prices of——

Mr. BARTON. The gentleman from Tennessee, Mr. Bryant, is recognized for 5 minutes.

Mr. BRYANT. Thank you, Mr. Chairman.

And let me just follow my colleague's question with, I guess, a direct question—and probably you have answered it generally, but you can comment further if you would like to.

Some observations have been made—not in here, but outside here—that, as with other industries high fixed costs and low marginal costs, 5 to 10 giant, vertically integrated oil companies will emerge globally which will serve most markets, with many niche players filling gaps or providing the unique services. Do you share that observation?

Mr. RAYMOND. In general, I would share that observation; yes. I think the pressure of competition all around the world—I don't think the points that we are seeing that we judge to be important for Exxon and Mobil are any different than anybody else. We are a very highly capital-intensive industry, very long-term capital investment. We make 20- and 30-year decisions which means that, in order to assure that over time you have the kind of economic performance that you need to have for your shareholders, that you are going to be forced into assuring that you are among the most efficient in everything you do. A certain element of that is capital; a certain element is technology, and a certain element is size.

Mr. NOTO. I do think though, Congressman, that the "vertical" integration is a buzzword. I think people worry that that means reduced competition. It means some dominance. And very frankly, our business—you could divide our business into three separate businesses: the upstream, the refining, and the marketing. We have different competitors at each level. There is a very clear, transparent price interface between each of those functions. People are in the upstream business but are not in the refining business; people are in the marketing business but not in the other two segments.

But I think vertical integration has really been changed dramatically. We make an investment in the upstream because we think

it makes money. We don't build a refinery just because we found an oil field. And so the old concern—I would say bugaboo—about the control of molecules from well head to customers' tanks, I think really is an issue that has passed us.

Mr. BRYANT. Okay. Let me ask you another question along that line. Exxon has power generation assets overseas, and Exxon-Mobil will become the second-largest gas producer in the world, behind Russia's Gasprom. Moreover, the combined company will have the largest natural gas reserves in the United States and become the largest producer among the majors. Do these facts spell out a recipe for a future with Exxon-Mobil operating as an integrated energy company, and not just as an oil and gas company?

Mr. RAYMOND. Well, in that sense, Exxon has been an "integrated"—I use that word carefully—an "integrated" oil and gas company for 100 years. We have been a producer of crude oil in this country and around the world. We have had refining and marketing assets in 120 countries around the world. If you mean "integration" in the sense that the management is involved in all phases of the business, the answer to that is, "yes." If you mean or imply that because we produce crude oil, for example, in Malaysia, that that would impact our decision as to how large our marketing activity should be in Japan, those are totally one unrelated to the other. They are separate decisions.

It probably would surprise people to know, for example, that we sell today about 5.5 million barrels a day of petroleum products, but we only produce 1.5 barrels a day of crude oil. The rest we buy—and we generally buy from Saudi Aramco; we buy from the National Iranian Oil Company; we buy from Petroleos de Venezuela. So in that sense, we are not integrated today, but we are integrated in the sense that the management is involved in all activities of the business.

And I would expect that we would continue to be involved in all aspects of the business. But I would emphasize that each decision is made on its own bottom. It has to be economic on its own. And we don't take credits from some other place and say that means we should do something else.

Mr. BRYANT. Thank you, Mr. Chairman.

Mr. BARTON. Okay.

The gentleman from Massachusetts, Mr. Markey, is recognized for 5 minutes.

Mr. MARKEY. Thank you, Mr. Chairman, very much.

Welcome, gentlemen.

Twenty years ago, companies like Exxon and Mobil represented big oil before this committee. They were the big fish in the small pond of global oil companies. Today, Exxon and Mobil are small fish in a big pond of giant, state-owned oil companies across the planet, but they remain very big fish in the small pond of regional or local oil and gas markets in cities and towns across the United States.

So, as a liberal Democrat from Massachusetts, I do not oppose the merger of Exxon and Mobil. But, I believe the FTC has a responsibility to make sure that in individual markets and cities and towns across the United States—where state-owned foreign oil companies do not dominate, but Exxon and Mobil do dominate—

that your companies, as they merge, are not put in a position in individual cities and towns to artificially increase the price of oil and gas to consumers in those communities.

And I think that is the basis for this entire discussion and debate here today. So I have a couple of questions which I would like to pose.

In a December 4, 1998, article in the Wall Street Journal, there was a report that Mobil has 511 branded stations in Massachusetts, while Exxon has a much smaller presence in Massachusetts. According to that article, this is in part because Exxon is known to charge dealers much higher rents. The article reports that a Mobil station, for instance, might carry a $4,000 to $5,000 a month rent, while an Exxon station pumping the same amount of fuel might pay monthly rent of $10,000 to $12,000.

Mr. Reidy's testimony—that is the Service Station Dealers of America that are in the second panel—raises similar concerns about the prospect for the merger to result in higher rents for many independent dealers. What assurances can you provide us here today that, if the transaction is approved, that you will not increase the rents charged to your independent dealers, and as a result, the price of gasoline for our consumers in those communities?

Do you want to comment?

Mr. NOTO. It is difficult for me to be able to make a sensible comparison between those numbers. I am not doubting them, but there is a whole package of issues involved—the size of the facility, when the facility was built, the cost associated with it, whether there is a market in it that generates additional revenue for the dealers. It is very hard for me, and I apologize; I can't really comment directly on your point, and I don't really know what Exxon's policies are, frankly. I mean we are still competitors in Massachusetts, until we can merge.

So I would suggest to you that it may be a more complex issue than it appears on the surface, and that I will ask my people to try to educate me on this and——

Mr. BRYANT. But if it is not more complex? If all it is, is twice the rent——

Mr. RAYMOND. But it is not.

Mr. BRYANT [continuing] what do we do then?

Mr. NOTO. Frankly, I think the market is so competitive that it would be very difficult for it to be simply that, because I think Exxon, at the end of the day, wouldn't have any dealer stations in Massachusetts.

Mr. RAYMOND. If I could make a couple of comments. First of all, as you properly point out, the forum for this issue is the FTC, and that is exactly what they are doing, and that is what they should do. And as I have said to them and to the head of the FTC—and I will say here today—I don't doubt their role. We are going to work with them, in terms of how they implement what they judge to be the right things that should take place in order for this merger to be approved. How that will affect a specific market in Massachusetts, at this point, I don't know.

Mr. MARKEY. Okay. Well, let me ask another question.

Mr. RAYMOND. I don't have any idea. But the next point I would make, with regard to rents, is you can't look at rents in isolation. You have to look at all kinds of others things for the economics of the total unit. The rent—if you take out the rent, then I have to ask you, "Well, what other goods and services do you apply? How many tanks are at the service station?"

Mr. MARKEY. Again, I appreciate——

Mr. RAYMOND. All of them.

Mr. MARKEY. [continuing] all of what you are saying, but the disparity is so great that I just want to make sure that we don't wind up with everything going up to the higher number——

Mr. RAYMOND. Sure.

Mr. MARKEY. [continuing] even for the old stations that presently have this very low rent. That is all I am saying. So whatever economies of scale exists in the old stations today, it seems to me, should still hold——

Mr. BARTON. The gentleman's time has expired.

Mr. MARKEY. [continuing] in the future.

Mr. BARTON. But I think you had one more question.

Mr. MARKEY. I do, and if you don't mind.

Mr. BARTON. And if you could ask that one and then——

Mr. MARKEY. Another concern which Mr. Reidy raises—I thank you, Mr. Chairman—in his testimony is what he refers to as the refiner policy of "zone" or "pad" pricing.

He warns that the merger of your two companies will only exacerbate the oligopolistic tendency toward zone pricing throughout many geographical markets which could result in higher prices for consumers, particularly in urban markets.

How do you respond to that criticism? Does zone or pad pricing really amount to price fixing, in your opinion?

Mr. RAYMOND. The answer to that is, "No." And to the extent that you would have what I would call an "extreme concentration." Let's take a case where Mobil and Exxon, together, had half of the service stations. Then, that is where the FTC shows up. If, in fact, we are much smaller and have 10 percent of the service stations and there are many competitors, then this will not be an issue.

So I think it really comes back to the same point we were on before, and that is the FTC looking at the concentrations and the competitive landscaping each one of these locations.

Mr. MARKEY. Mr. Chairman, I thank you.

Mr. BARTON. Thank you, and I, with you, will work on the pronunciation of "oligopoly." It is hard.

Mr. MARKEY. "Oligopolistic" is definitely——

Mr. BARTON. You did well.

Mr. MARKEY. Well, let's hope it is word we don't have to know in the future.

Mr. BARTON. That's true. We don't want monopoly, and we don't like oligopoly.

Mr. MARKEY. Maybe the times have changed so much in the last 28 years, it has become chaotic in its usage.

Mr. BARTON. Mr. Pickering is recognized for 5 minutes.

Mr. PICKERING. Thank you, Mr. Chairman. It is always good to follow a liberal Democrat from Massachusetts, as a conservative

Republican from Mississippi. But who shares in agreement of support of this merger.

And also I would have to admit that the two questions you focused on were the two questions that I wanted to focus on as well.

And, Mr. Chairman, I commend you for focusing on the merger and the effect on competition, as well our competitiveness. And I wanted to follow up on some of the questions that have been asked as to how this really relates back to the service station dealers. Some are concerned that if Exxon and Mobil are ordered to divest themselves of service stations, they will choose to assign leases as a block to a third-party distributor.

Do you anticipate such an outcome? And will you offer station owners the right to buy their stations prior to offering to assign it to a third party?

Mr. RAYMOND. Well, in a sense, we are getting ahead of ourselves because I think this, again, is an area where the FTC gets involved, in the sense that, if we are required to divest of some service stations, they also get involved, not only in that you have to sell them, but who you sell them to and how you sell them.

And while I might have some views on if you had to do it, what would be the best way to do it, I think we are probably getting a little bit ahead of the, you know, the cart ahead of the horse here. But let me just make the comment; it would not be our intention—and I think I can speak for Lou from Mobil—it would not be our intention to ever use anything that the FTC required us to do to put a dealer at a disadvantage, that we would take the step to put him at a disadvantage. If the FTC requires something be done in a way that the dealer interprets it as a disadvantage, I can't deal with that. But we would not use it as a basis to try and put somebody at a disadvantage.

Mr. PICKERING. Do you have anything to add? And I understand the sensitivity as you go through with the FTC process. I do hope that we can address that concern adequately at the appropriate time.

My second question is more of a macro question as far as—and Mobil and Exxon both have had tremendous expertise and capability in projecting supply and demand and production. If one of the outcomes of this is that you have a more efficient production-exploration capacity in the capital that you can bring to bear on that, how does that play into supply and demand and price? And what are your projections for the next year to 2 years in relation to supply and price?

Mr. RAYMOND. Yes.

The only thing I can tell you about the price for the next 2 years is we don't have a clue—which, of course, is one of the reasons we are here, because we have to work on the things that we can control, which is our costs. But when I say, "we don't have a clue," I don't mean that to try and be humorous.

The facts are that if you look at the fundamentals of supply and demand, left totally unfettered—and, clearly, we are in an environment where the supply is in excess—but as you can tell by just reading the newspapers in the last couple of days, there are a lot of other issues that get involved in the balance of what supplies are actually available to the market. And I wouldn't begin to be able

to think that I could forecast how various governments and various state oil companies will respond, given the kind of price environment that we have just been in.

Mr. PICKERING. Let me ask just a quick followup question, Mr. Chairman. I hope my time has not extended too far.

Mr. BARTON. You still got a green light.

Mr. PICKERING. Well, how do you forecast—or can you forecast—how the merger may affect domestic production? Are your plans for domestic production exploration any relation to what we are seeing in the oil and gas industry right now, as far as independent production?

Mr. RAYMOND. Well, I think it would be fair to say that at least Exxon—and I think Lou should answer for Mobil, because this is kind of a competitive issue at this point—that the recent low prices will not have a significant, immediate impact on how much Exxon produces in this country. There is some volume at the margin, but it is not large. But if these prices were to persist for a significant length of time, then you would begin to revise your investment programs, and that could have a significant impact as we go down the road.

I would not expect that it will have a major impact once we put the two companies together, in the sense that—my sense is that the projects that both of us have under consideration are probably reasonably robust to most price environments.

Mr. NOTO. I would add two quick points, if I could, Mr. Chairman.

No. 1, we have seen a reduction in our U.S. production as a result of this price environment. We have cut back some discretionary spending which has resulted in lower than anticipated production levels. There is no question but that this price environment has hurt us.

No. 2, I don't think that independent producers in the United States should fear that the proposed combination of Exxon and Mobil, somehow, is going to adversely affect their price deck as we go forward in the future. I mean if you look at the two of us, we account for roughly 4 percent of the world's hydrocarbon production—in the United States, probably around 7-8 percent.

Anything we would do to bring to bear the efficiency that we anticipate would not have a significant impact on the world's balances. Remember, every day, 75 million barrels of oil is traded, more or less, around the world. So, I would not expect any kind of a negative impact on independent producers as a result of what we are talking about today.

Mr. PICKERING. Thank you very much.

Mr. BARTON. Thank you, Mr. Pickering.

The Chair recognizes the gentlelady from Missouri, Ms. McCarthy, for 5 minutes.

Ms. MCCARTHY. Thank you very much, Mr. Chairman.

Gentlemen, I am glad we are having this continued hearing to talk about the future and, particularly for your industry, I have some concerns—as I know other members of this subcommittee do—with regard to the kind of future your industry and your companies will be unfolding for us.

Sub-large oil companies are responding to calls for voluntary action to reduce emissions of greenhouse gases. British Petroleum comes to mind immediately to me because they are investing in solar energy and participating in efforts to provide credit for early action to reduce carbon emissions.

We are in competition with other countries on developing the technologies—the new cars of the future, as Japan has already done and is marketing—that will help us toward this goal of a cleaner and better air quality.

I wonder if you would share with us some of the actions that you are taking, with regard to diversifying us out of our dependence on fossil fuels and helping us, as a Nation, to compete globally with the technologies and the new autos that we will deal with in our own country and abroad, so that what we are turning this opportunity into is a win-win for the country, that we can be on the cutting-edge of those new developments. And I would like to know what you are doing toward that goal.

Mr. NOTO. Want me to start?

Mr. RAYMOND. Yes, go ahead.

Mr. NOTO. Ms. McCarthy, let me start with that.

No. 1, I think you have to live with the proposition that the world will depend on fossil fuels for the immediate future to fuel the kind of economic growth that we are going to see.

Ms. MCCARTHY. That is not in question here today——

Mr. NOTO. Good.

Ms. MCCARTHY. [continuing] or in doubt.

Mr. NOTO. Good.

Ms. MCCARTHY. My question is——

Mr. NOTO. But the real issue is, how do we use——

Ms. MCCARTHY. My question is——

Mr. NOTO. [continuing] the fossil fuel more efficiently?

Ms. MCCARTHY. Yes?

Mr. NOTO. Okay. And that, I can assure you, the industry is working on very, very diligently. I can talk about Mobil's activities in this area, and I will let Lee comment on Exxon's activities.

Ms. MCCARTHY. Well, and would you talk about your commitment to that in the future after your merger?

Mr. NOTO. Well, as vice chairman of the proposed company, I have no reason to believe that both of us will have a different view, with respect to our commitment to this issue.

We do not dismiss the risk of global warming. That doesn't mean we support the Kyoto Agreement, but we do not dismiss the risk. Each of the companies—and many companies in the industry—are taking steps to reduce emissions from their own facilities, but the bulk of the emissions associated with our business comes from our customers' use of our products and, therefore, we are committed to making sure our customers use our products more efficiently.

In Mobil's case, we have a number of research activities going on right now. One I would mention is with Ford, where we are working on a hydrocarbon feed to a fuel cell which should be able to increase well to wheel efficiency dramatically.

We are working with Ford on an advanced diesel engine program, which also has promise of being able to increase the well to wheel—when I say "well to wheel," I think if you just look at any

part of this chain, you could fool yourself into saying, “Gee, electric cars look great.” But somebody has got to generate the electricity to charge the batteries, and somebody has got to make the batteries, and somebody has got to get rid of the batteries when they are no good anymore. So, you have got to look at the whole process.

I am convinced that hydrocarbons will continue to play an important and vital role in the future. If you look at a new car in the United States running on new fuel and compare it to a 10-year-old car running 10-year-old fuel, the new car is more than 90 percent more efficient and cleaner. I think that is a great step in the right direction.

If you look at where the emissions in the United States are coming from, the bulk of the emissions come from 25 to 30 percent of the cars on the road which are old, which are pre-catalytic cars. There is a lot of social issues around that question. A lot of people have thought about buying back old cars; a lot of people have thought about a lot of things, but the fact is that new cars and new fuel are doing the job they are intended to.

And I am very optimistic that over the next 10 years, we will continue to see significant efficiency gains. We will use hydrocarbons; solar and electric cars will not supplant the use of fundamental hydrocarbons for transportation. And our job is to satisfy the customer, that we are doing it as efficiently as we can, and they can get more “bang for the buck” when they buy our stuff.

Mr. RAYMOND. I think, if I could—and perhaps I am misreading where you are coming from, and if I am, please, correct me—but the old canard that oil companies are against the efficient use of energy is wrong. I have always been for the efficient use of energy, whether it is in how our refineries operate, how our chemical plants operate, how our customers use the fuel. This notion that somehow people have that all we are interested in doing is selling more volume, if that was ever true, that is an historical perspective. That is not the perspective of today.

For those who talk about solar, I would have to remind you that back in the late 1970’s and the early 1980’s, Exxon, in today’s dollars, probably spent $300 million in the solar business. We were the first major oil company to spend money in solar energy and in fundamental research in solar—the same in batteries. So we have been there.

When I say that, how it fits into the future and whether it is economic in the future, is another set of issues. Because, fundamentally, what we want to make sure is that there is available to the economies of the world, the most efficient, lowest cost sources of energy there can be, because, after all, that is what really fuels the economic growth and economic activity in the world. And if you don’t have economic growth—well, if we have economic growth, we may be able to deal with some of our social issues. If we don’t, we are going to have a set of issues that are going to overwhelm all of us.

Mr. BARTON. The gentlelady’s time, unfortunately, has expired.

The witnesses, at the beginning, were a little tense, and they were responding quickly, but they are comfortable now, and they are responding like Senators at some length. So——

Ms. MCCARTHY. Mr. Chairman might I just have a brief extension in order to comment on their answers?

Mr. BARTON. Yes, we will give the gentlelady a brief extension and a comment.

Ms. MCCARTHY. I thank you.

Gentlemen, I did not mean in my questioning to put you on the defensive which, obviously, I did. What I was listening for, I did not hear. I did hear what I expected. But I am looking for a new way of thinking, and I am looking for a large, merged company like yours in the future to lead the way for this Nation.

And I thank you, Mr. Chairman, for the extension.

Mr. BARTON. Thank you.

I must say that, as an observer to the Kyoto Agreement and, also, to Buenos Aires, the Chair is not a supporter of the Agreement as it was initialed in Buenos Aires. But I think the gentlelady from Missouri is onto something. We need to work to find a way to seriously see if there is something that can be done about the emissions issue. And we do expect Exxon-Mobil to participate in that in a meaningful way.

The Chair would recognize the gentleman from New York, Mr. Fossella, for 5 minutes.

Mr. FOSSELLA. Thank you, Mr. Chairman. I compliment you for holding this hearing.

And just at the outset, gentlemen, I believe, fundamentally, that you are moving in the right direction. That anywhere we can control costs, become more efficient, enhance productivity, I think we are better off. I think the more that we have a stronger Exxon-Mobil, we have a stronger American economy, whether it is for your workers or your shareholders, so I applaud the decision.

However, if you answer my question the wrong way, I am going to have a different response, and that is that we have a Mobil terminal on Staten Island and integral to, I guess, your distribution center in the Northeast. And I am curious as to what, if any, change you envision with respect to that facility.

Mr. NOTO. Congressman, are you talking about Port Mobil?

Mr. FOSSELLA. That is correct.

Mr. NOTO. Formerly Port Socony—it has been an important part of the Mobil distribution system. We move a lot of volumes through there. I can't make the final comment on it, because we don't have the two companies together, but I see no reason to think that it is not going to continue to be an important location for us and an important point in the combined company's distribution up the coast.

Mr. FOSSELLA. Congratulations.

As I say, I think what you are doing is moving in the right direction. Overall, what we need to do as a country is, if we are concerned about economic growth—not just in this Nation, but beyond—become the most efficient company you can become. Create wealth for your shareholders, and, in the end, we will all be better off.

So, that is all, Mr. Chairman, thank you.

Mr. BARTON. I thank the gentleman, and would recognize the gentleman from Tennessee, Mr. Bart Gordon, for 5 minutes.

Mr. GORDON. Thank you, Mr. Chairman.

Let me add my welcome to Mr. Raymond——

Mr. RAYMOND. Thank you.

Mr. GORDON. [continuing] and Mr. Noto.

I am sure that you want to get on with business, and you don't really have much interest in being here so we appreciate your time. This is an important issue——

Mr. RAYMOND. Yes.

Mr. GORDON. [continuing] that faces all of us.

Mr. Raymond, in your testimony and in many other releases and justification that has been put forth for this merger, the discussion about how it is important for the United States to have a major player in the international energy market, I would like to get your thoughts, please, if you could better help me understand. Do you see, as chairman of this new company, do you think it would ever be appropriate for you to put the well-being of the United States above your shareholders?

Mr. RAYMOND. Well, that is a hard question to answer in the sense that it is a hypothetical. There is no question that we are, and will be, an American company. And, as such, we obviously have to be very, very sensitive to U.S. interests. And we will continue to be sensitive to U.S. interests. That isn't surprising because I would suspect that way over 90 percent of our shareholders are also American shareholders.

Mr. GORDON. But part of the justification for the merger is that it would be good for this country, and that, you know, that we need to have a major player. And so I am just trying to understand how that would be, you know, how this country is going to be better off, and if that would somehow mean you choosing between your shareholders and our country?

Mr. RAYMOND. Well, I don't think the issue is going to be one of choosing between our shareholders and our country.

And the point I would make, I guess—and perhaps you are reading it somewhat differently than I thought we wrote it—we did not put these companies together because they were both American companies and, therefore, there is a larger American company.

We put these two companies together because, in our judgment, it was the best we could do to create the most efficient international oil company. At the same time, it turned out it will be the largest American company. And by being the largest American company, I think it maintains what has been historically the U.S. position that in the world, the technology in this industry has been led by American companies.

It will enable us to continue to be the leader in technology in this industry, and that technology will be based in this country. And that, I think, is of value to this country.

Mr. GORDON. And if there was two different companies, you wouldn't be competing with each other to have better technology?

Mr. RAYMOND. What do you mean two different companies?

Mr. GORDON. I mean if Mobil and Exxon stayed as separate companies, rather than a merger.

Mr. RAYMOND. Oh, I think we would compete. But the ability to be able to develop technology is a function also of scale and your economic capability to develop that technology. You have to have a broad enough base of investment to justify the kind of research and development you need to have in order to be able to afford that

technology. The scale that we have will give us more ability to develop and deploy that technology than if either of us had remained alone.

Mr. GORDON. Well, let's say that a country or a company based in another country had better technology than we did. How would our country be disadvantaged?

Mr. RAYMOND. Well, the way it is going to be disadvantaged is that that other company will have better access, more effective access to resources—for example, crude production—than the company with the lesser technology.

Mr. GORDON. So, how was our country going to be disadvantaged? If other countries and other companies have the ability to produce more oil, then it will be likely to have a more stable price. How is our country going to be——

Mr. RAYMOND. It is not—it is more oil cheaper; it is not just volume.

Mr. GORDON. Yes.

Mr. RAYMOND. It is the competitive landscape. And to the extent that they are able to do that, then the profitability of our company will be less because, obviously, they will be able to have acceptable profitability at lower prices than we can have and, therefore, ultimately, our shareholders—largely Americans—are at a disadvantage.

Mr. GORDON. But they could own stock in British Petroleum or some other company——

Mr. RAYMOND. Oh, sure they could.

Mr. GORDON. Yes. I am just trying to better understand——

Mr. RAYMOND. I would prefer they owned it in us.

Mr. GORDON. Sure, sure; I understand. I am just trying to—I think there are lots of valid reasons for the merger. One that has been given is that, as a country, it helps us, and I am trying to better understand what that help is. Is it—and I am not sure I have gotten that quite yet——

Mr. RAYMOND. Well, I——

Mr. GORDON. [continuing] but your shareholders could invest in another company. I mean your shareholders are probably investing because they should; they want to get a good return.

Mr. RAYMOND. That is right.

Mr. GORDON. They have no particular affection for the company, other than they want to get, you know, a good return. So, they could be investing elsewhere.

Mr. RAYMOND. And they always have that capability. But the point being is that our job, as a company, is to provide the return by how we manage our business, how we select our assets, how we deploy those assets around the world so that people see it attractive to own our shares, as opposed to some other people's shares.

Mr. GORDON. Well I totally agree.

Mr. RAYMOND. Correct.

Mr. GORDON. I think that is your job. I am just trying to—but if part of the reason for the merger is to make America better, how does that make America better?

Mr. RAYMOND. Because it seems to me that America always comes out better if the most efficient companies in the industry are

American companies, whether that is aircraft industry, the petroleum industry, the tire industry—you name it.

Mr. GORDON. So can you be more specific on how we are going to be better off?

Mr. RAYMOND. Because you are going to have—if it is an American company that it is the leader, there are going to be more Americans, in this sense, in our company working on things that are of value to us in terms of technology, goods and services that flow from us being in this country, than if we were not.

Mr. BARTON. We are going to have to——

Mr. RAYMOND. And that flows all the through the economy in everything we do.

Mr. BARTON. The Chair is going to have to ask the gentleman from Tennessee to hold that thought if we wants to ask another round of questions.

But I have got some——

Mr. GORDON. I think I was going to say to say how many layoffs would be on it, too?

If we are going to be better off, do the layoffs make us the better, or the country better?

Mr. RAYMOND. Well the question is, what would the layoffs be if we do this versus if we hadn't done it now?

Mr. GORDON. Yes. That is——

Mr. RAYMOND. That is a relative judgment.

Mr. GORDON. Yes.

Mr. NOTO. I would have to reduce——

Mr. GORDON. The answer is know what that would be.

Mr. NOTO. I would have to reduce my staffing. Even if I did not do this merger, I would lose jobs. I mean you have to face that. And there are many companies is our industry—Shell just announced 6,000 people; Arco, 1,500 people. They are not involved in mergers. It is just the competitive nature of the markets that we are dealing with.

Mr. GORDON. Which is——

Mr. BARTON. There have been a half a million jobs lost in the oil industry in the United States in the last 10 years. We have lost a half million barrels of production in the United States in the last year. The pure fact of the matter is that it is more and more an international marketplace, and it is more and more difficult to find the oil and gas in this country. And for environmental reasons, it is more and more difficult to refine it in this country. And that is a subject that is larger than whether Exxon and Mobil should merge.

The Chair is going to recognize himself for 5 minutes. And then if Mr. Gordon wishes to stay, we will give you an opportunity for another 5 minutes also.

But then we are going to have to let this panel go because we have got another panel, and we have got a series of votes on House floor.

So, the Chair recognizes himself for 5 minutes.

These are kind of followup, more or less, nuts and bolts questions. My assumption is that once the SEC and the FTC have reviewed the merger that it will be presented to your shareholders for approval. Is that not correct?

Mr. RAYMOND. Actually, it will be presented to the shareholders probably before those reviews are——

Mr. BARTON. The shareholders have to agree to it before it is signed of on.

Mr. RAYMOND. Yes, I think the shareholders' meetings are scheduled for May 27.

Mr. BARTON. Okay; well that was my next question' what is the time table? So that the Exxon shareholder meeting is May 27? What about——

Mr. NOTO. And the Mobil shareholder meeting is exactly the same day.

Mr. BARTON. Okay. Are they in the same location or are they different?

Mr. NOTO. They both happen to be in Dallas, but that was purely fortuitous in terms of——

Mr. BARTON. Purely—well, it is fortuitous for me since if I wanted—I don't own any stock in either of your companies which is unfortuitous for me, I must say.

Going back to the situation about the globalization—when Mobil or an Exxon are out exploring for new oil fields, what is the minimum size field that you ask your explorationists to try to find? What is the magnitude? How many millions or hundreds of millions of barrels?

Mr. NOTO. Do you want to start?

Mr. RAYMOND. Well, that is a function, Mr. Chairman, of a number of things. Most fundamentally, it is a function of—for example, if we are in deep water, how deep is the water? And it is also a function of the fiscal regime that you have in the country where you are operating. For example, just in ballpark numbers, for a field to be economic in deep water Nigeria, it is 300 million barrels, more or less.

Mr. BARTON. Well the reason I asked, I have been told and it is just—I have not verified this—that, at your level, your size companies don't look for fields of less than 100 million barrels?

Mr. RAYMOND. That is not true.

Mr. BARTON. So, there are——

Mr. RAYMOND. That is not true.

Mr. BARTON. [continuing] occasions, if it is near the surface and——

Mr. RAYMOND. Yes, and, for example, in the North Sea these days, where there is a large infrastructure that has been put in place because of large projects we have had there. Then, what you do is you—there are many smaller opportunities that are directly available that can be hooked into the infrastructure at relatively low cost. In that case, a find of perhaps 20 million barrels could be economic.

Mr. BARTON. Well let me ask it this way; what is the last elephant field—so-called, however you define an "elephant field"—found in the United States or in the offshore waters that are controlled by the United States?

Mr. RAYMOND. The last elephant field is Prudhoe Bay, Alaska.

Mr. BARTON. And when was that?

Mr. RAYMOND. In 1973.

Mr. BARTON. In 1973. What is the likelihood of there being another find of that kind again in the United States or in the offshore waters controlled by the United States?

Mr. RAYMOND. I think the geologists would say it is remote.

Mr. BARTON. Okay. So isn't it a given that if an United States' company that is registered as a United States' corporation is going to maintain any type of a presence in the international oil markets, you are going to have to go overseas?

Mr. RAYMOND. Oh, absolutely.

Mr. NOTO. There is no question.

Mr. RAYMOND. Absolutely.

Mr. BARTON. And isn't it also a given that if you are going to do that, you are going to automatically be competing against these state-owned oil companies?

Mr. RAYMOND. Absolutely.

Mr. BARTON. And if that is the case, isn't it an automatic for the U.S. national security purposes, that companies of your sort are going to have to be big enough to have the capital resources to do that?

Mr. RAYMOND. Well, yes; I think that is the point. And, ultimately, security, as applied in this country, is going to come down to assuring, as best we can, that there are multiple sources of supply.

Mr. BARTON. Okay. Now, in the last fiscal year that each of you are CEO's of your company—I don't know if that is this year or last year—what was Exxon's exploration budget worldwide?

Mr. RAYMOND. Well, it was about the same in both years—about $1.1 billion.

Mr. BARTON. $1.1 billion, and what was it for Mobil?

Mr. NOTO. About $700 million I would say.

Mr. BARTON. So the combined was about $1.8 billion. What do you expect—and, again, you have not merged, but if the merger is approved—what do you expect the exploration budget for the combined company to be next year? Would it be that same order of magnitude?

Mr. NOTO. If they are not merged?

Mr. BARTON. No, if they are merged?

Mr. NOTO. Well, I think we could keep on the same level of activity and be able to save money, because we both have some duplicative functions.

Mr. RAYMOND. Right.

Mr. BARTON. Well, my time has expired. I am the only one here, but my time has expired.

Here is the point that I am trying to get at. You are playing in a world marketplace. You spent $1.8 billion last year separately trying to find oil. Your fact sheet shows that if the merger is approved, you are going to save about $2 billion a year. Does not some of that $2 billion savings go into exploration to try to find another elephant field?

Mr. NOTO. It goes into more efficient exploration.

Mr. RAYMOND. It goes into more efficient exploration.

Mr. NOTO. I think that is the key for us.

Mr. BARTON. I am trying to help you.

Mr. RAYMOND. Yes, I know but——

Mr. BARTON. Okay?

I am trying to give a reason that it is in the national interest of the United States of America to approve this merger.

Mr. NOTO. Sir, I appreciate the help.

Mr. BARTON. Okay.

Mr. NOTO. And the facts support your position. I think what we are trying to say is that it would be premature for me to judge what the exploration budget will be next year because it is also a function of opportunity. I mean you need to have the potential.

Mr. BARTON. I understand that. But if you save money——

Mr. NOTO. It was not our objective to reduce the exploration effort of the combined companies, but it was our objective to upgrade the exploration effort and to make it more likely that we will actually discover hydrocarbons by spending this money.

Mr. BARTON. And it is a good thing for the average motorist in this country if an American-owned, private company has more money to spend to find oil fields overseas so that oil can be transported and refined and made available for sale in the United States of America. That is a good thing.

Mr. NOTO. I would say it was a good thing.

Mr. BARTON. Okay. My time has expired. We are going to have other questions.

We have two votes on the floor. We are going to recess the committee for 30 minutes. We are going to let this panel go. And then when we come back at 1:30, we will hear from our second panel. I want to thank you, gentlemen, for your——

Mr. NOTO. Mr. Chairman, thank you.

Mr. RAYMOND. Thank you, Mr. Chairman.

Mr. BARTON. [continuing] cooperation today.

Mr. NOTO. It was a pleasure to be with you.

Mr. BARTON. Thank you.

[Brief recess.]

Mr. BARTON. The subcommittee will come to order. A quorum being present, we are going to reconvene the continuation of our hearing on the Exxon-Mobil merger.

On our second panel of witnesses, we have Mr. John Lichtblau who is the chairman of the Petroleum Industry Research Foundation, and we have Mr. Tom Reidy, who is with the Service Station Dealers of America. And, hopefully, at some point in time, we will be joined by Mr. Charles Shotmeyer—who is here—who is president of Shotmeyer Brothers Petroleum Corporation.

Each of you gentleman's statements is in the record in its entirety. I am going to recognize Mr. Lichtblau, and then we will just go right down the line. And I am going to set the clock on 7 minutes, and if you need a little bit more time, we will give you that opportunity.

Mr. Lichtblau, welcome to the committee.

STATEMENTS OF JOHN H. LICHTBLAU, CHAIRMAN, PETROLEUM INDUSTRY RESEARCH FOUNDATION; TOM REIDY, SERVICE STATION DEALERS OF AMERICA; AND CHARLES SHOTMEYER, PRESIDENT, SHOTMEYER BROTHERS PETROLEUM CORPORATION

Mr. LICHTBLAU. Thank you very much, Mr. Chairman.

In addition to my presentation here, I would like to submit for the record a paper we did about a month ago entitled, "How Big are the Oil Majors Now and After They Make a Merger?" Mr. BARTON. Without objection.

Mr. LICHTBLAU. Thank you very much.

Mr. BARTON. Has our staff seen that?

Mr. LICHTBLAU. I think they have; yes.

Mr. BARTON. Has the minority staff seen it, also?

Let's make sure than the minority doesn't have an objection to it, but if not, we will put it in the record at this point in time.

Mr. LICHTBLAU. Okay.

Mr. BARTON. But we need to get a copy——

Mr. LICHTBLAU. All right; fine.

Mr. BARTON. [continuing] so that they can look at it.

Mr. LICHTBLAU. We have copies here.

Mr. BARTON. Okay.

All right; continue, please, sir.

Mr. LICHTBLAU. The Exxon-Mobil proposed merger is another step in a long period of consolidation that has been taking place in the domestic oil industry. Ever since the end of price allocation controls in 1981, the industry has been adapting to an increasingly competitive environment. With no letup in competitive pressures, and diminishing returns from internal cost-cutting, attention has shifted toward strategic alliances and mergers, which are now taking place.

To a large extent, these pressures and the industry response reflect which is happening also in other industries exposed to growing competition. But there are also some important differences. The oil industry is much less concentrated than many others. For instance, the top three car makers in the United States account for over 75 percent of the domestic car market, the top three soft drink producers, about 85 percent of the market. It would take more than the 25 largest private oil companies to match the lower of these concentration ratios in the United States. Moreover, among the larger U.S. companies, retrenchment and rationalization has gone even further than for the industry as a whole.

Another big difference are the drastic declines in the price of the industry's major product, namely, crude oil.

So overall, the retrenchment is inevitable for an industry facing low growth, depressed prices, and intense competition. A process of consolidation offers the best opportunity for preserving the core strengths of what remains a critical industry for the United States.

In my testimony, I would focus partly on a group of major companies which are surveyed regularly by the Department of Energy and then the seven largest private U.S. oil companies.

As part of the long-term consolidation process, there has been a slowdown in the pace of the investment of these major oil companies, especially in the United States.

The worldwide value of petroleum-related property, plant and equipment reported by these companies remained more or less constant in 1997, but that was because the value of foreign fixed investments kept growing, while the domestic value declined.

The sharp decline in the U.S. oil industry's earnings in 1998—and apparently also in the first quarter of 1999—is a clear sign of

the industry's competitiveness. The beneficiaries are, of course, consumers who now pay the lowest price for oil products, ex tax, since 1987 in nominal dollars and the lowest since the 1940's in real dollars, which has caused a decline in the consumer price index.

Now I would like to turn briefly to some of the specific domestic developments in production, refining, and marketing among the major companies. The trends is, in all of these, toward rationalization and a declining role in the market.

The major companies' shares of total oil and gas production is significantly lower now than in the early 1980's, a sign that the consolidation process so far has not added to industry concentration in the producing sector.

In refining, the early 1980's left majors with substantial spare refining capacity which has been eliminated during the last decade. This process included outright withdrawals of the majors from this segment. In 1997, the major companies accounted for 60 percent of U.S. refinery output, down from 74 percent in 1990 and 83 percent in 1980. Incidentally, Exxon and Mobil have both been part of this withdrawal process. Both sold refineries that are continuing in full operation by their independent owners.

The process of share reduction has also occurred in gasoline marketing. In 1997, the reporting companies' gasoline sales through their associated automotive outlets amounted to 33 percent of national consumption, down from 42 percent in 1990.

We now look at the seven largest private oil companies in the United States which show the same trend. The role of these seven majors in U.S. and global crude production is now declining, both in share and in volume. Their low share of 9 percent in world oil production outside the United States reflects the large share of world oil production concentrated in OPEC and other producing countries where state oil companies predominate. The world's largest oil-producing companies currently are the state-owned companies of Saudi Arabia, Iran, Mexico, China, and Venezuela.

An important factor in analyzing the competitiveness of the refining sector of the U.S. oil industry is the composition of this sector. Between 1985 and 1999, the U.S. majors' share of refining capacity dropped from 65 percent to 36 percent as both independents and new foreign players came into the market and gained share.

My conclusion is that the U.S. oil market is highly competitive at all levels. It is an international market; 50 percent of all crude oil is imported; 10 to 12 percent of all oil products are imported, and there is an open market so that the price is an international price at all times. There is no company that has a dominate share of any segment of the market currently, and this would still be true after the Exxon-Mobil merger.

Equally important is the U.S. markets'—I just mentioned it—open access to the global oil market. Even in the most concentrated oil region, the Gulf Coast, Texas and Louisiana, the Exxon-Mobil combined share of refinery capacity is only 20 percent of the area's total refining capacity.

So we expect the U.S. oil industry to continue to be a competitive part of the world oil market. It is always part of that market. Since companies can't control the price of crude oil or the price of the products they sell, they can only respond to difficult market condi-

tions by acting on what they do control, namely, costs. Last year simply intensified the presence, the pressures, on the industry to move faster. Even the largest companies can no longer consider themselves exempt from this pressure.

Thank you very much, Mr. Chairman.

[The prepared statement of John H. Lichtblau follows:]

Trends Among the Major US Oil Companies

By
John H. Lichtblau, Chairman
Petroleum Industry Research Foundation, Inc.

Testimony before
US House of Representatives
Committee on Commerce

Washington, DC

March 11, 1999

Trends Among the Major US Oil Companies

Overview

The Exxon Mobil proposed merger is only another step in a long period of consolidation that has been taking place in the domestic oil industry. Ever since the end of price and allocation controls in 1981, the industry has been adapting to an increasingly competitive environment. The dramatic decline in oil prices in 1986 intensified pressures on the industry while the renewed price declines of 1998 means the process will go on. At first, the emphasis was on control of operating costs and elimination of internal redundant capacity. By the beginning of the 1990s, emphasis shifted toward reductions in working capital, most notably inventories. With no letup in competitive pressures, and diminishing returns from internal cost-cutting, attention has shifted toward strategic alliances and mergers, which allow the combined ventures to revisit all aspects of operations.

To a large extent, these pressures and the industry response reflect what is happening in other industries exposed to growing competition. But there are also important differences. The oil industry is less concentrated than many others. The top three car makers in the US account for over 75% of the domestic market, the top three soft-drink producers about 85%. It would take more than the 25 largest private oil companies to match the lower of these concentration ratios, yet no one doubts both industries are very competitive. Moreover, among the larger US companies, retrenchment and rationalization has gone even further than for the industry as a whole. The shares of the larger companies, here defined as those companies subject to the FRS reporting system, in the country's oil and gas production, refinery output, and gasoline sales are all lower today than in the early 80s.

Another big difference between oil and other industries are the drastic declines in the price of its major product, crude oil, that occurred first in 1986, and again, in 1998. While the industry was able to adapt with difficulty to the first, which was followed by a period of rough stability, the second is causing enormous difficulties. In 1998, employment in oil and gas extraction was nearly 400 thousand below its 1982 peak of about 710 thousand. In the past 12 months alone, employment in this sector has fallen by about 50 thousand and losses are continuing to mount.

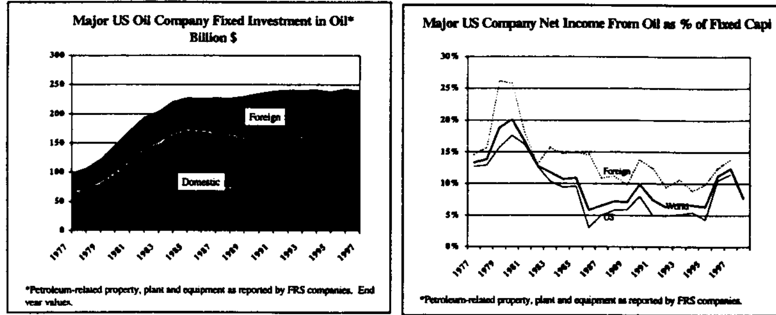
In a competitive environment, the gains from efficiency improvements by and large flow through to consumers rather than add to company profits. This indeed appears to be the case. Major oil company returns to their petroleum-related assets remain well below their levels of the early 1980s. While there was a modest recovery in 1996-97, they fell back dramatically in 1998.

Overall, retrenchment is inevitable for an industry facing low growth, depressed prices, and intense competition. A process of consolidation offers the best opportunity for preserving the core strengths of what remains a critical industry for the country.

In my testimony, I focus first on trends within the broader group of major companies defined as those who are subject to the FRS requirements of the Department of Energy and then turn to the world's seven largest privately owned oil companies.

Major Company Investment Trends

As part of the long-term consolidation process, there has been a slowdown in the pace of investment by the major oil companies, especially in the US.



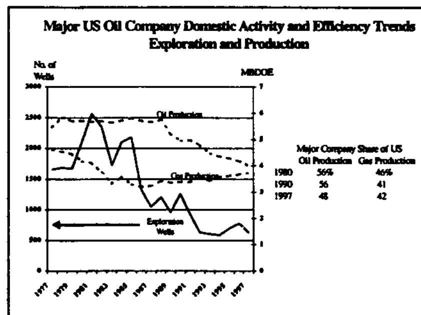
The decline in oil prices in 1986 brought an end to the strong buildup in oil investment. Since that year, as shown in the chart in the upper left, the world-wide value of petroleum-related property, plant and equipment reported by the major companies remained more or less constant through 1997, as growth in the value of foreign fixed investments offset ongoing declines in the US. Presumably, both figures are likely to show declines in 1998 and this year as companies adjust to the current depression in oil prices. The chart above on the right shows trends in major company net income from oil as a percent of their fixed capital invested. Returns as measured on this basis fell back drastically from their early 80s levels, especially returns in the US, and all the rationalization steps to date have only kept returns in about the 5 to 10% range. There was a brief improvement in 1996-97 but preliminary indications suggest 1998 returns will, on a worldwide basis, fall back to pre-1996 levels.

The sharp decline in the US oil industry's earnings in 1998 and, apparently, also the first quarter of 1999 is a clear, sign of the industry's competitiveness. The beneficiaries are the consumers who now pay the lowest price for oil products (ex tax) since 1986 in nominal and the lowest since the 1940s in real dollars. US oil ~~companies~~ consumers saved $40 billion last year as a result of lower prices and this led to a reduction in the CPI of nearly 0.7% all by itself.

Major Company Domestic Activity and Efficiency Trends

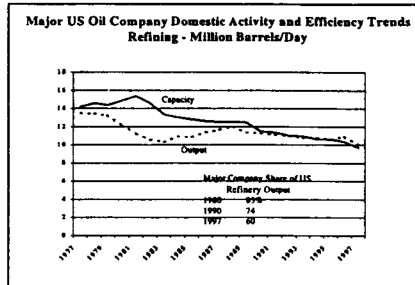
So far, the discussion has focused on financial indicators. I would like to turn now to specific, domestic, operational developments in production, refining, and marketing among the major companies. The trends are all toward rationalization, efficiency improvement, and a declining role in the overall US industry.

Exploration and Production



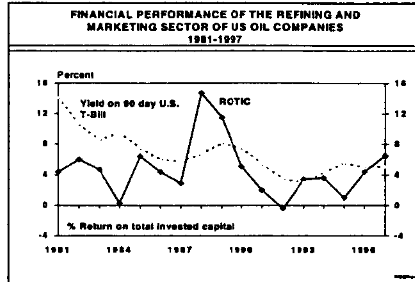
The chart on the right shows trends in exploratory wells drilled by the major companies and oil and gas production. The number of wells drilled annually in the 1990s was down by about 75% from the early '80s peak of about 2,500. Industry data suggest 1998 will show a significant decline from1990-97 levels for these companies as well as for the industry as a whole. Oil production by the reporting companies has shown a gentle decline over the 1990s while gas production has been making modest advances. In neither case has oil or gas production fallen back by

anything like the decline in exploration activity, perhaps an indicator of the technological advances and efficiency gains associated with finding and producing reserves. As the table shows, the major companies' shares of total US oil and gas production is significantly lower now than in the early 1980s, a sign that the consolidation process to date has not added to industry concentration in the producing sector.



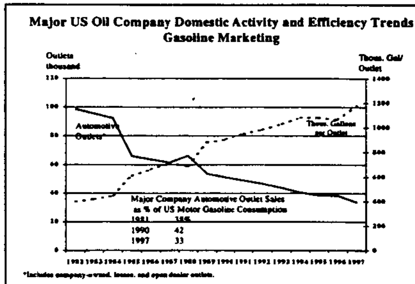
Refining

The end of controls set the stage for a major rationalization of the downstream segments of the industry. For the major companies, the early 80s left them with substantial spare refining capacity that, as shown in the chart above, was only eliminated by the end of the decade. Since then, refinery output of these companies has moved about in line with reported capacity (as measured at the beginning of each year). This process included outright withdrawals from this segment of the business. In 1997, these companies accounted for 60% of US refinery output, down from 74% in 1990 and 83% in 1980. (Exxon and Mobil have both been part of the withdrawal process. Both sold refineries in New Jersey that are continuing in full operation by their new independent owners.)



Gasoline Marketing

The process of share reduction has also occurred in gasoline marketing. As shown in the chart on the right, the number of automotive outlets reported by the FRS companies (company-owned, lessee, and open dealerships) declined from nearly 100 thousand in 1982 to less than 40 thousand in 1997. Over the same period, the average volume of gasoline sold at each outlet tripled, rising from 400 thousand gallons to about 1.2 million. As in refining, this rationalization and efficiency improvement was accompanied by a decline in overall market share, especially in the 1990s. In 1997, the reporting companies' gasoline sales through their associated automotive outlets amounted to 33% of national gasoline consumption, down from 42% in 1990 and 38% in 1981.



Shares of the World's 7 Largest (Pre-Merger) Majors in US & World Crude Production

We now focus on the world's seven largest (pre-merger) private oil companies. The sharp decline in the US oil industry's upstream earnings, in 1998 and, apparently, also the first quarter of 1999 is a clear sign of the industry's competitiveness. The beneficiaries are the consumers who now pay the lowest price for oil products (ex tax) since 1986 in nominal and the lowest since the 1950s in real dollars. An indication of the industry's competitiveness is that the reduced crude oil prices were fully passed through to refined

products prices. This confirms the findings of a recent study by the National Petroleum Council which states that "significant price excursions of major light petroleum products in the United States will continue to be driven primarily by movements in the global price of crude oil".[1]

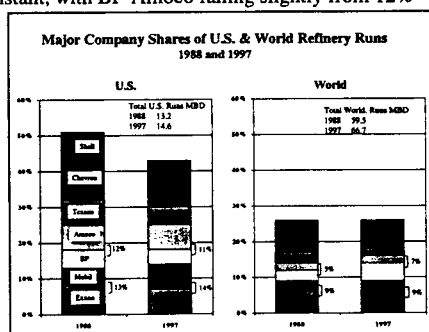
MAJOR COMPANIES SHARE OF OIL PRODUCTION (PIRA)

	U.S		World excl. U.S
	1997	1988	1997
	%	%	%
Exxon	6.8	7.8	1.5
BP	6.7	8.8	1.1
Shell	5.9	5.4	2.8
Texaco	4.8	5.4	0.8
Chevron	4.1	5.0	1.1
Mobil	2.9	3.0	1.1
Amoco	2.8	4.2	0.5
Total	34.0	40.0	8.9
Total Production MMB/D	8.27	9.76	65.0

Crude oil prices are determined internationally and, in turn, determine domestic crude prices since nearly 60% of US crude is imported. The role of the US majors in US and global crude production is declining, both in share and volume, as the chart on this page shows. The low shares of the 7 majors in world oil production outside the US reflects the large share of world oil production concentrated in OPEC and other producing countries where state oil companies predominate. Thus, the 7 majors' current share of world oil production is much too small to affect world oil prices. The world's largest companies in terms of oil production are, in descending order, the state-owned companies of Saudi Arabia, Iran, Mexico, China and Venezuela.

Shares of the World's 7 Largest (Pre-Merger) Majors in U.S. & World Refinery Runs

The chart below shows shares of US and world refinery runs of the seven companies in 1988 and 1997. The panel on the left shows the company shares of total US runs. The seven collectively in 1988 accounted for just over 50% of US refinery runs. In 1997, their share was significantly lower, 43%. The combined shares of BP and Amoco as well as Exxon and Mobil were relatively constant, with BP-Amoco falling slightly from 12% to 11%, and Exxon-Mobil rising slightly from 13% to 14%.[2]



As shown on the right, the seven companies together account for just over 25% of world refinery runs, well below their US shares. Neither the BP-Amoco pairing, nor Exxon-Mobil reach a 10% share on a world basis.

The chart suggests that certainly on a global basis, refining is highly competitive, a condition that would not change if Exxon and Mobil kept their refineries after a merger.[3] The US figures are higher. However, it should be kept in mind that oil products are traded in a world market. In 1998, the US imported about 2 MMB/D of products (including imports from the US Virgin Islands), over 10% of total consumption. There are also other very large international players besides the seven discussed here. These include Saudi Aramco and Petroleos de Venezuela, both of whom have global refining capacities larger than BP's, including US ventures.

[1] US Petroleum Product Supply, Dec. 1998, p. 9

[2] In 1998, Mobil sold its 155,000 barrel/day refinery in Paulsboro, New Jersey to Valero Energy Corporation. The sale reduces the combined Exxon-Mobil share of US refining by about 1.5 percentage points below the 14% figure for 1997.

[3] Exxon/Mobil's share of refining capacity is nearly 13% in both the US and Europe, 9% in Asia Pacific and less than 3% elsewhere.

Texas and Louisiana

Within the US, the Gulf Coast has the greatest concentration of refining capacity. The table on the right shows shares of crude refining capacity for the seven majors in Texas and Louisiana as of January 1, 1999. The two states' total refining capacity is 7.0 MMB/D.

In Texas & Louisiana – 1/1/99

	%
Exxon	13
Mobil	7
BP	4
Amoco	6
Motiva*	10
Shell**	5
Chevron	1
Others	54

* Joint venture between Texaco, Shell, and Saudi Aramco
** includes all of Deer Park Shell-Pemex interest.

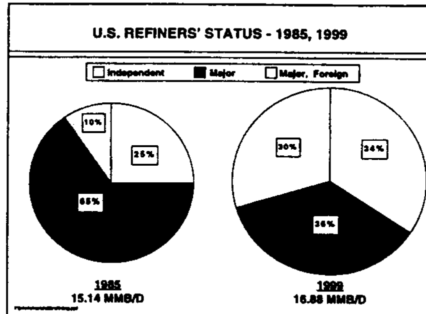
Source: *Oil & Gas Journal 1998 Worldwide Refining Survey*

Exxon and Mobil have shares of nearly 13% and 8% respectively. BP and Amoco have a combined share of 10%, Motiva, the joint venture between Texaco, Saudi Aramco and Shell also has a share of 10%. The seven companies altogether account for somewhat less than half of total crude refining capacity in the two states. A number of the companies in the "Others" category have refining capacities in the region comparable to most of the 7 majors. These include companies such as Citgo, Conoco, Crown, Clark, Koch, Marathon, etc.[4]

Share of Crude Refining Capacity

An important factor in analyzing the competitiveness of the refining sector of the US oil industry is the composition of this sector among the different groups of companies and the movements of these groups. The chart at the right shows the sharp decline of the US majors in both share and volume of total US refining capacity since 1985 and the substantial growth of independent refiners during this period, obviously an indication of the domestic refining industry's dynamic competitiveness. Between 1985 and 1999, the US majors' share of refining capacity dropped from 65% to 36% as both independents and new foreign players gained.

U.S. REFINERS' STATUS - 1985, 1999



Conclusion

The US oil market is highly competitive at all levels. No company has a dominant share of any segment of the market. This would still be true after the Exxon/Mobil merger. Equally important is the US market's open access to the global oil market. Currently over 50% of our crude oil requirements and over 10% of our refined products requirements are imported and these shares move continuously with supply/demand changes. Even in the most concentrated oil industry region, Texas and Louisiana, the Exxon/Mobil's combined share of refining capacity is only 20% of the area's total. Thus, we expect the US oil industry to continue to be a competitive part of the world oil market.

Since companies can't control the price of crude or the prices of products they sell, they can only respond to difficult market conditions by acting on what they do control, their costs. Last year simply intensified pressures on the industry to move faster. Even the largest companies could no longer consider themselves exempt.

[4] It should be kept in mind that a substantial amount of products refined at the US Gulf Coast is consumed elsewhere. For example, the Gulf Coast is the single largest supply source of products to the very competitively priced US East Coast.

Mr. BARTON. Thank you, sir.

We would now like to hear from Mr. Reidy, who represents the Service Station Dealers of America, and we'll note that there are a number of your members in the audience, and they have been very well-behaved so far in the hearing. So——

STATEMENT OF TOM REIDY

Mr. REIDY. So far, Mr. Chairman.

Mr. BARTON. Yes.

Mr. REIDY. Mr. Chairman, and members of the subcommittee, my name is Tom Reidy, and I appreciate the opportunity to appear before you today to present the dealer community's views and concerns about the proposed Exxon-Mobil merger and the need for the provisions contained in H.R. 811.

I am a second-generation service station dealer who operates two Exxon stations—Reidy's Exxon in Greenbelt, Maryland, and Milestone Exxon in Germantown, Maryland. I am the past president of Washington/Maryland/Delaware Service Station and Automotive Repair Association, and I am here today representing the Service Station Dealers of America and Allied Trades; that is SSDA-AT. It is a 53-year-old national association representing 22 State and regional associations with a total membership in excess of 20,000 small businesses in 38 States and individual members in all 50 States, the District of Columbia, Puerto Rico, and Guam.

It is overwhelming for an independent small business service station dealer to comment before the U.S. House of Representatives on a proposed merger which would result in the world's largest oil company, valued at some $82 billion.

The dealer community recognizes that overlaps exist between Mobil and Exxon in the areas of refining, marketing, and production. One would think that the new Exxon-Mobil company will eliminate excess refining capacity, thus limiting product and consumer choices and would close stations that are now competing against each other. This merger could result in a "squeeze out" of many independent dealers. For example, many Mobil dealers are very concerned that they will face higher rents that Exxon has historically imposed on its dealers.

Assuming that the merger is approved, conditioned on the divestiture of some service stations in certain markets, lessee dealers should be given a fair opportunity to acquire their businesses before they are sold off. This, we believe, is in accord with Congress' intent as set forth in the Petroleum Marketing Practices Act, PMPA.

Sales of stations to individual dealers will likely introduce more competition into the marketplace than would the sale in bulk of a large number of stations to another supplier. Once the dealer owns his or her station, he or she will have more freedom to acquire product on a competitive basis. As long as the stations are not deed restricted, which is prohibiting motor fuel sales, first right of refusal will make the market more competitive and will result in lower prices to consumers.

Another concern with the proposed merger is that it will only strengthen the refiner pricing policy of zone pricing or pad pricing. Exxon and Mobil utilizes zone prices, and eliminating another com-

petitor in the market will only exacerbate the oligopolistic tendency toward zone pricing through many geographical markets. This could result in higher prices for consumers, particularly in urban areas.

Not only is the proposed Exxon-Mobil merger huge in and of itself, it is part of a continuing trend that has made the market more and more oligopolistic. This trend not only includes other mergers but also the sale and exchange of service stations in different markets.

On February 23, 1999, Congressman Albert Wynn, from Maryland, introduced legislature, H.R. 811, to amend PMPA to address two issues of great concern.

The first amendment would remedy the effect of the Supreme Court's opinion in the State Oil v. Khan on dealer pricing independence by establishing a motor fuel dealer's unequivocal right to control his or her own retail prices. The impact of the Supreme Court's ruling could challenge the independence of service dealers. Independent dealers have invested significant capital into their businesses with the expectation that they would remain free to make their own pricing decisions and not be subject to prices set by distant suppliers having limited knowledge of the local market conditions.

Gasoline suppliers enjoy enormous leverage over dealers because they are typically the dealers' landlords, licensers, and exclusive suppliers, as ascertained in the reports accompanying the passage of the PMPA in 1978. Many jurisdictions, including Delaware, the District of Columbia, Florida, Hawaii, Maine, Maryland, Minnesota, Oregon, and Washington already prohibit suppliers from fixing retail prices charged for motor fuel by independent dealers. Such statutes could serve well as a model for congressional protection.

The second amendment would provide motor fuel dealers a first right of refusal to purchase their service stations prior to any assignment of the franchise agreement to a distributor or any other assignee. This addresses a loophole that presently exists in PMPA.

The last few years have witnessed a growing number of lease assignments to the harm of independent dealer service stations. Typically, the supplier who is a service station dealer's landlord, supplier, and franchisor will sell the service station to a third-party distributor to whom the supplier will also assign the dealer's franchise agreement. Such a circumstance requires the dealer to purchase through a middleman who is very likely to increase the dealer's price in order to generate profits for himself. Further, the dealer's continued right to use the supplier's name and mark is in danger. Finally, the dealer is likely to face increased rental demands when his or her lease comes up for renewal.

SSDA-AT urges this subcommittee and this Congress to pass H.R. 811 in a timely manner. At a minimum, we would hope that the Federal Trade Commission would include first right offers, similar to the provisions of H.R. 811 in any possible decree ordering the divestiture of service stations if the Exxon-Mobil merger is approved.

True, consumers are now enjoying low motor fuel prices because there is a glut of petroleum products. But as you know—and as you

have seen in the last few days with the price of gasoline going anywhere from one to three cents increase—gluts have come and gone in the past. The long-term effect of the proposed merger should be considered, mainly in view of the oligopolistic trend in the industry. That long-term view is not comforting.

Thank you.

[The prepared statement of Tom Reidy follows:]

PREPARED STATEMENT OF TOM REIDY ON BEHALF OF THE SERVICE STATION DEALERS OF AMERICA AND ALLIED TRADES

Mr. Chairman and Members of the Subcommittee on Energy and Power, my name is Tom Reidy and I appreciate the opportunity to appear before you today to present the dealer community's views and concerns about the proposed Exxon/Mobil merger and the need for the provisions contained in H.R. 811.

I am a second-generation service station dealer who operates two Exxon stations—Reidy's Exxon in Greenbelt, Maryland and Milestone Exxon in Germantown, Maryland. I am past president of the Washington/Maryland/Delaware Service Station and Automotive Repair Association and I am here today representing the Service Station Dealers of America and Allied Trades (SSDA-AT). SSDA-AT is a 53 year-old national association representing 22 state and regional associations with a total membership in excess of 20,000 small businesses in 38 states; and individual members in all 50 states, the District of Columbia, Puerto Rico, and Guam.

It is overwhelming for an independent small business service station dealers to comment before the U.S. House of Representatives on a proposed merger which would result in the world's largest oil company, valued at some $82 billion. The dealer community recognizes that overlaps exist between Mobil and Exxon in the areas of refining, marketing, and production. One would think that the new Exxon/Mobil company will eliminate excess refining capacity thus limiting product and consumer choice and would close stations that will be competing against each other. This merger could result in a "squeeze out" of many independent dealers. For example, many Mobil dealers are very concerned that they will face higher rent terms that Exxon has historically imposed on its dealers.

Assuming that the merger is approved conditioned on the divestiture of some stations in certain markets, lessee dealers should be given a fair opportunity to acquire their businesses before they are sold off. This, we believe, is in accord with Congress' intent as set forth in the Petroleum Marketing Practices Act (PMPA).

Sales of stations to individual dealers will likely introduce more competition into the marketplace than would the sale in bulk of a large number of stations to another supplier. Once the dealer owns his or her station, he or she will have more freedom to acquire product on a competitive basis. As long as the stations are not deed restricted prohibiting motor fuel sales, first right of refusal will make the market more competitive and will result in lower prices to consumers.

Another concern with the proposed merger is that it will only strengthen the refiner pricing policy of zone or pad pricing. Exxon and Mobil utilize zone pricing, and eliminating another competitor in the market will only exacerbate the oligopolistic tendency toward zone pricing throughout many geographical markets. This could result in higher prices for consumers, particularly in urban markets.

Not only is the proposed Exxon/Mobil merger huge in and of itself, it is part of a continuing trend that has made the market more and more oligopolistic. This trend not only includes other mergers but also the sale and exchange of service stations in different markets.

On February 23, 1999 Congressman Albert Wynn (D-MD) introduced legislation, H.R. 811, to amend PMPA to address two issues of great concern.

The first amendment would remedy the effect of the Supreme Court's opinion in *State Oil v Khan* on dealer pricing independence by establishing a motor fuel dealer's unequivocal right to control his or her own retail prices. The impact of the Supreme Court's ruling could challenge the independence of service station dealers. Independent dealers have invested significant capital into their businesses with the expectation that they would remain free to make their own pricing decisions, and not be subject to prices set by distant suppliers having limited knowledge of local market conditions. Gasoline suppliers enjoy enormous leverage over dealers because they are typically the dealers' landlords, licensers, and exclusive suppliers, as ascertained in the Reports accompanying passage of the PMPA in 1978. Many jurisdictions—including Delaware, the District of Columbia, Florida, Hawaii, Maine, Maryland, Minnesota, Oregon, and Washington—already prohibit suppliers from fix-

ing retail prices charged for motor fuel by independent dealers. Such statutes could well serve as a model for congressional protection.

The second amendment would provide motor fuel dealers a first right of refusal to purchase their service stations prior to any assignment of their franchise agreements to a distributor or any other assignee. This addresses a loophole that presently exists in the PMPA. The last few years have witnessed a growing number of lease assignments to the harm of independent service station dealers. Typically, the supplier who is the service station dealer's landlord, supplier, and franchisor will sell the dealer's station to a third-party distributor to whom the supplier will also assign the dealer's franchise agreement. Such a circumstance requires the dealer to purchase through a middleman who is very likely to increase the dealer's price in order to generate profits for itself. Further, the dealer's continued right to use the supplier's name and mark is in danger. Finally, the dealer is likely to face increased rental demands when his or her lease comes up for renewal.

SSDA-AT urges this Subcommittee and this Congress to pass H.R. 811 in a timely manner. At a minimum, we would hope that the Federal Trade Commission would include rights of first offer similar to the provisions of H.R. 811 in any possible decree ordering the divestiture of stations if the Exxon/Mobil merger is approved.

True, consumers are now enjoying low motor fuel prices because there is a glut of petroleum products. But as you know, gluts have come and gone in the past. The long-term effect of the proposed merger should be considered. Particularly in view of the oligopolistic trend in the industry, that long-term view is not comforting.

Thank you.

Mr. BARTON. Thank you, Mr. Reidy.

We now would like to hear from Mr. Shotmeyer. Again, your statement is in the record, so we will give you 7 minutes to elaborate on it.

STATEMENT OF CHARLES SHOTMEYER

Mr. SHOTMEYER. Thank you, Mr. Chairman, for allowing me to be here.

My name is Charles Shotmeyer, president of Shotmeyer Brothers Petroleum Corporation, of Hawthorne, New Jersey, a 70-year-old family business distributing Mobil products.

The first station to sell Mobil gas—then Socony-Vacuum—in New Jersey after the Standard Oil breakup was owned by my dad and uncle when the market was dominated by Exxon—then Standard, of New Jersey. Our business was built station by station to become a significant factor in the eight counties of northern New Jersey. Today, the Mobil gas sold by stations we own and operate is 20 percent of the Mobil gas sold in northern New Jersey.

Today, I speak on behalf of the Fuel Merchants Associations of New Jersey, FMA, whose over 300 independent marketers sell 90 percent of the fuel oil sold in New Jersey and 20 percent of the gasoline. While I am speaking on behalf of FMA's full membership, I am particularly addressing issues of FMA's seven Mobil distributors impacted by the proposed Exxon-Mobil merger. The number of years, number of stations, vary, but we have common concerns regarding the Exxon-Mobil merger, not only for ourselves, but for our dealers and the consumers as well. These seven family owned businesses distribute Mobil gas to roughly 25 percent of the total Mobil stations in New Jersey in each of the 21 counties.

The proposed Exxon-Mobil merger is disconcerting to Mobil distributors who could literally see generations of families' efforts go for naught in a single ruling by the FTC. If this merger is not properly consummated, the impact in New Jersey on both consumers and small businesses could be devastating.

Many in the public—and possibly even some at the FTC—do not realize that when they are filling up at a service station, such as a Mobil station, they may be filling up at a location where the land, buildings, labor, underground storage tanks, property taxes, insurance, canopies, and signs are owned by a Mobil distributor who has a contract with Mobil to "fly their flag." Mobil's current corporate policy is to allow distributors to compete directly against Mobil where they are both competing in the same market.

Exxon, by contrast, does not allow distributors to compete against it in the areas where it markets directly. Since Exxon is the former Standard Oil Company of New Jersey, and the State's market so urban, Exxon supplies almost every one of their branded stations directly.

The branded wholesale distributor performs a vital service to the consumer by offering intrabrand competition which exerts a corresponding downward pressure on prices. This service is all the more valuable with a brand that the public perceives at having a tremendous value such as Mobil.

New Jersey's concentration of Exxon-and Mobil-branded outlets—probably 35 percent combined marketshare—including the outlets owned by Mobil distributors where they proudly fly a Mobil flag, makes it highly likely that the FTC could order a divestiture of service stations.

It is imperative that the FTC not force our members to divest service stations they own that are branded Mobil. Hundreds of thousands of dollars have been invested in each of these locations, and the only way the investment will be recouped is to preserve the Mobil brand.

To fully appreciate the concerns of FMA's members, regarding the proposed Exxon-Mobil merger, it helps to understand the recently announced joint marketing venture between Shell and Texaco. While not an actual merger, the joining of the downstream marketing operations has the same real world effect in the marketplace.

The facts of Shell-Texaco alliance are striking in their similarity to the Exxon-Mobil merger. Shell—Exxon—the larger of the two companies is merging/buying Texaco—Mobil—the smaller of the two companies. Shell—Exxon—has a corporate philosophy of not allowing competition against it by its distributors in the same market. Texaco—Mobil—has a corporate philosophy which does allow competition with their distributors in the same market.

It has been widely rumored in the industry and published in the trade press that Texaco was preventing jobbers from opening new stations and branding them Texaco. This is the result of the Shell philosophy taking precedence in the arrangement in the joint venture.

I shudder to think that the fate of the Texaco distributors has been sealed. If a branded wholesale gasoline distributor cannot have the opportunity to expand its business, it will die. If the Exxon philosophy prevails in the same manner, FMA's Mobil distributors will eventually no longer exist.

In closing, it is imperative that the FTC understand that, in New Jersey, consumers and Mobil distributors must be protected by somehow allowing the Mobil brand to remain a strong factor in the

marketplace, providing competition and growth, even after it is purchased by Exxon. This type of arrangement has been previously sanctioned by the FTC when it allowed for the continued use of the Getty and Gulf brands after the companies had been purchased in the mid 1980's when Chevron purchased Gulf and Texaco purchased Getty.

Being a pragmatist, I understand that the FTC will allow the merger to be completed, and we are not opposed to that. However, FMA urges you to please help educate the FTC on how the Exxon-Mobil merger in New Jersey will impact not only the small family businesses your represent, but consumers as well—for it is the branded gasoline wholesale distributor who ensures that competitive pressures are exerted against the major oil companies.

Thank you.

[The prepared statement of Charles Shotmeyer follows:]

PREPARED STATEMENT OF CHARLES SHOTMEYER, PRESIDENT, SHOTMEYER BROTHERS PETROLEUM CORPORATION ON BEHALF OF THE FUEL MERCHANTS ASSOCIATION OF NEW JERSEY

The Implications of the Exxon-Mobil Merger

My name is Charles Shotmeyer, President of Shotmeyer Bros. Petroleum Corp. of Hawthorne, NJ, a 70 year old family owned business distributing Mobil products.

The first station to sell Mobil gas, then Socony-Vacuum, in New Jersey after the Standard Oil breakup, was owned by my dad and uncle when the market was dominated by Exxon, then Standard of New Jersey. Our business was built station by station to become a significant factor in the eight counties of Northern NJ. Today the Mobil gas sold by stations we own and operate is 20% of the Mobil gas sold in Northern NJ.

Today, I speak on behalf of the Fuel Merchants Association of NJ (FMA), whose over 300 independent marketers sell 90% of the fuel oil sold in NJ and 20% of the gasoline. While I am speaking on behalf of FMA's full membership I am particularly addressing issues of FMA's seven Mobil distributors impacted by the proposed Exxon-Mobil merger. The number of years /number of stations vary but we have common concerns regarding the Exxon-Mobil merger not only for ourselves, but for our dealers, and the consumers as well. These seven family owned businesses distribute Mobil gas to roughly 25% of the total Mobil stations in NJ in each of the 21 counties.

The proposed Exxon/Mobil merger is disconcerting to Mobil distributors who could literally see generations of their families' efforts go for naught in a single ruling by the Federal Trade Commission (FTC). If this merger is not properly consummated, the impact in New Jersey on both consumers and small businesses could be devastating.

Many in the public, and possibly even some at the FTC, do not realize that when they fill-up at a service station, such as a Mobil station, they may be filling at a location where the land, buildings, labor, underground storage tanks, property taxes, insurance, canopies, and signs, are owned by a Mobil distributor who has a contract with Mobil to "fly their flag". Mobil's current corporate policy is to allow distributors to compete directly against Mobil where they both compete in the same market. Exxon by contrast does not allow distributors to compete against it in areas where it markets directly. Since Exxon is the former Standard Oil Company of New Jersey and the state's market so urban, Exxon supplies almost every one of their branded stations directly.

The branded wholesale distributor performs a vital service to the consumer by offering intrabrand competition which exerts a corresponding downward pressure on prices. This service is all the more valuable with a brand that the public perceives at having a tremendous value, such as Mobil.

New Jersey's concentration of Exxon and Mobil branded outlets, (probably 35% combined marketshare), including the outlets owned by Mobil distributors where they proudly fly a Mobil flag, makes it highly likely that the FTC could order a divestiture of service stations. It is imperative that the FTC not force our members to divest stations they own that are branded Mobil. Hundreds of thousands of dollars have been invested in each of these locations and the only way the investment will be recouped is to preserve the Mobil brand.

To fully appreciate the concerns of FMA's members regarding the proposed Exxon/Mobil merger it helps to understand the recently announced joint marketing venture between Shell and Texaco, (while not an actual merger, the joining of the downstream marketing operations has the same real world effect in the marketplace).

The facts of Shell/Texaco alliance are striking in their similarity to the Exxon/Mobil merger. Shell (Exxon), the larger of the two companies, is merging with (buying) Texaco (Mobil), the smaller of the two companies. Shell (Exxon) has a corporate philosophy not allowing competition against it by its distributors in the same market. Texaco (Mobil) has a corporate philosophy which does allow competition with their distributors in the same market.

It has been widely rumored in the industry and published in the trade press, (*US Express, 2/8/99*) that Texaco is preventing jobbers from opening new stations and branding them Texaco. This is the result of the Shell philosophy taking precedence in the arrangement in the joint venture. I shudder to think that the fate of the Texaco distributors has been sealed. If a branded wholesale gasoline distributor cannot have the opportunity to expand its business, it will die.

If the Exxon philosophy prevails in the same manner, FMA's Mobil distributors will eventually no longer exist.

In closing, it is imperative that the FTC understand that, in New Jersey, consumers and Mobil distributors must be protected by somehow allowing the Mobil brand to remain a strong factor in the marketplace, providing competition and growth, even after it is purchased by Exxon. This type of arrangement has been previously sanctioned by the FTC, when it allowed for the continued use of the Getty and Gulf brands after the companies had been purchased in the mid-1980's, when Chevron purchased Gulf and Texaco purchased Getty).

Being a pragmatist, I understand that the FTC will allow the merger to be completed. However, FMA urges you to please help educate the FTC on how the Exxon/Mobil merger in New Jersey will impact not only the small family businesses you represent, but consumers as well. For it is the branded gasoline wholesale distributor who ensures that competitive pressures are exerted against the major oil companies.

Mr. BARTON. Thank you, sir.

The Chair is going to recognize himself for 5 minutes and recognize Mr. Shimkus. We notice that Mr. Shimkus' legislative assistant seemed to be barely above the child labor wage rate.

So we assume those are visitors from his district and being educated on the Congress at work.

The Chair recognizes himself for 5 minutes for the first question period.

Just so we have a complete record of the three witnesses before us in this panel, do any of you, individually or representing your associations collectively, formally oppose the Exxon-Mobil merger? Is there anybody here that—I know you have got some concerns about it, but does anybody here express total opposition to it?

Mr. LICHTBLAU. No.

Mr. REIDY. No.

Mr. SHOTMEYER. No.

Mr. BARTON. Okay.

Mr. Lichtblau, you have got the broader perspective in your testimony. What is your opinion of the OPEC cartel right now, as an effective cartel in the sense that they are able to control supply of the world's oil?

Mr. LICHTBLAU. Well, sir, everything is different since yesterday. As you know, prices just jumped because OPEC started to discuss the possibility of reclusing their supplies in order to strengthen the world price market. Whether they will succeed or not, we don't know.

OPEC has been generally and relatively an ineffective organization in terms of what they want to achieve, but if they want to, they control 40 percent or so of the world's oil exports. So, they are

definitely in a position to strengthen—up—prices by cutting their production. If they cut by something like 2 or 3 percent, it will be enough to raise prices maybe 3 or 4 times that much. And this is what the market is looking for.

But if you look at OPEC over the last 15-20 years, the only time prices really rose, was when there were external extraneous events of which OPEC had no—like a war or something like over which OPEC had no control. But it is an organization of the world's most important oil exporters. It has the largest oil producing companies, so that it is in a position to affect the world oil supply. But it has no plan to do this beyond the present situation in which prices are so low that their governments are politically in trouble because of it.

Mr. BARTON. Do any of the OPEC state-owned oil companies explore for oil outside of their national boundaries?

Mr. LICHTBLAU. OPEC oil companies?

Mr. BARTON. Of the member states in OPEC——

Mr. LICHTBLAU. Yes.

Mr. BARTON. [continuing] that they are state-owned companies, do any of them explore for oil outside of their national——

Mr. LICHTBLAU. Yes; on a small scale, they do.

Mr. BARTON. They do?

Mr. LICHTBLAU. Some of them have but——

Mr. BARTON. But, basically, they manage their oil——

Mr. LICHTBLAU. Mostly they develop their own resources; yes.

Mr. BARTON. Okay.

Mr. LICHTBLAU. The state oil company does, but they have gone abroad, but not on a large scale.

Mr. BARTON. Okay. How does——

Mr. LICHTBLAU. Because they—and also their basic interest is to develop their own resources.

Mr. BARTON. Right. How does an Exxon-Merger, if it takes place, from a national perspective, does that give the United States a larger player to compete against these state-owned companies, or does it matter?

Mr. LICHTBLAU. Not really; not really, because these state companies are so much bigger—Saudi Aramco and Petrogal-Petroleos de Portugal—that a Mobil-Exxon merger would still keep a share of this company of total world production—very small, maybe a few percent of the total world—so they don't compare anywhere near with any of these major OPEC national companies.

It would strengthen them somewhat, but marginally. It would still be—the prices would still be determined internationally, and OPEC would still have, whenever it can, an influence on it. And right now it does, but as I said, it was driven to it by an incredible price drop which affected or threatened their economy.

Mr. BARTON. Okay.

Mr. Reidy, the Service Station Dealers Association—obviously, your membership—and the—I know there is another association, also, of service station dealers—your concern is that the dealers that own their stations or the dealers that lease their stations will not be given an opportunity to maintain their lease or their contract with a merged Exxon-Mobil? Is that correct?

Mr. REIDY. Our concern is that the station which a majority of us are lease dealers from the oil company, we would like to be able to get the opportunity, if they decide to divest or if they have to divest so many of the stations, we would like the opportunity, first, to be able to go and purchase the property and everything involved with it.

Mr. BARTON. So you would like, as a part of the merger agreement, that the FTC put in there a stipulation that your membership be given a right to maintain the lease or to purchase outright?

Mr. REIDY. We would like the first option to purchase the property and everything involved with it.

Mr. BARTON. The property?

Mr. REIDY. Now, we might——

Mr. BARTON. The actual tangible land——

Mr. REIDY. Exactly.

Mr. BARTON. [continuing] and pumps and building.

Mr. REIDY. What now belongs to the oil company—rather than them give it to the distributor, a handful of stations at one time—we would like to be, on each individual case, we would like to be able to at least have the opportunity to purchase a station and equipment and everything we need.

Mr. BARTON. Now would that mean, in addition to purchasing the tangible property, you would maintain the right to use that brand of gasoline?

Mr. REIDY. Well at that particular point, what you would more than likely have to do is get a contract with a supplier—and it might be stay with Exxon; I've dealt with them for years.

Mr. BARTON. So your concern is a physical location and a property, as opposed to maintaining the brand?

Mr. REIDY. Right. I am concerned because—as we have seen in the past, and the history will show you that—a lot of times when these distributors and groups like this take over a group of stations, the dealers will maintain their stations, quite a few will maintain. But there is also a problem or a chance that a lot of these dealers will be forced out by higher rents if they have a very nice location, and the company, themselves, will operate that. And these people that are with us will no longer be in business.

Mr. BARTON. Okay. Now, Mr.—my time has expired but I am going to ask unanimous consent to extend a little bit.

Mr. SHIMKUS. I object, Mr. Chairman—no.

Mr. BARTON. The Chair has the power of recognition.

Mr. Shotmeyer, now your concern is different. Your concern is—if I understand it—that your distributors and the dealers in New Jersey that have been using the Mobil name, the brand, may not have the opportunity to continue to sell or use that brand. Is that correct?

Mr. SHOTMEYER. That, sir, is correct. In New Jersey, because of the highly concentrated market—and I don't think there is another market in this country, with the combined Exxon-Mobil merger, that will have as high a concentration as the whole State of New Jersey will have.

It is so important that the dealers and us, as distributors, have the Mobil brand to continue on and build on, because we have invested large sums of money, gone into long-range planning, based

on Mobil's encouragement to do such, to put forth their image, buy locations and to develop locations and spend a lot of money, time, and energy to develop the market so that the consumer has a choice.

Mr. BARTON. Now are you concerned that the Mobil brand will disappear, and it will just be an Exxon brand? Or are you concerned that Mobil will still have the brand, but they will have it owned by the company, as opposed to an independent distributor?

Mr. SHOTMEYER. All of the above, sir.

Mr. BARTON. All of the above?

Mr. SHOTMEYER. We are—if I could elaborate just for a short——

Mr. BARTON. Yes, and then I am going to recognize Mr. Shimkus.

Mr. SHOTMEYER. The possibly that the FTC would say that the Mobil brand has to be sold off to a large supplier, another supplier, not dealers or distributors, is something that has happened in the past. And we need to have some protections against that.

Mr. BARTON. Okay.

Mr. Shimkus, we will recognize you for such time as you may consume.

Mr. SHIMKUS. Thank you, Mr. Chairman.

I want to focus on the dealer issue in a minute, but I—one of the reasons why I love this subcommittee is I am continually concerned about our national energy policy and energy security, and I think it is in the national interest that we have a readily reliable, readily accessible supply of fuel.

So, Mr. Lichtblau, if I may start with you.

Mr. LICHTBLAU. Yes.

Mr. SHIMKUS. How vulnerable is the United States to interruptions in imported petroleum supplies today?

Mr. LICHTBLAU. The interruption—well, it could happen any time.

Mr. SHIMKUS. So we are very vulnerable?

Mr. LICHTBLAU. Pardon me?

Mr. SHIMKUS. So we are very vulnerable?

Mr. LICHTBLAU. Well, in theory, we are very vulnerable. But, of course, we have a diversification of supply sources. We now have a strategic petroleum reserve, which I think it is a very good idea; it is being increased, if only slightly. It is up nearly 600 million barrels, so that it could, for awhile, if we lost 2-3 million barrels a day for quite some time, it could offset that loss.

But we are no more, no less vulnerable than any other country, in fact, somewhat less because most European countries and Japan import 100 percent of their oil requirements, while in our case, it is only about 50 percent so that—and, of course, any of these disruptions also hurt the disrupting country more than the receiving country because they stop their oil exports. And for them, it could be a 100 percent loss.

But we are vulnerable, and we have to live with this vulnerability; we have for the last 50 years. So do most all other countries which are oil importers including, as I say, Europe and Japan.

And between a growing strategic petroleum reserve—I think it should be built up some more—and the policy of diversification of supply sources and, of course, any kind of benefit, any kind of stim-

ulant that we can give to developing additional domestic sources, particularly in the Gulf Mexico, would be very desirable.

Mr. SHIMKUS. What percentage of the world oil production is controlled by OPEC today?

Mr. LICHTBLAU. Oh, I would think about 40 percent roughly. They produce nearly 30 million barrels, 28 million barrels, out of a world production of 74-75 million barrels. So it is in that range altogether.

Mr. SHIMKUS. Okay.

Mr. LICHTBLAU. Not everything, of course, is exported, but their total production is, as I say——

Mr. SHIMKUS. And that percentage, how does that compare to the percentage in the 1970's?

Mr. LICHTBLAU. Well, at one time it was much higher when OPEC was producing in the 32-33 million barrels, then it dropped and the prices went to $25-$30. World oil demand dropped substantially, and all of the reduction came from OPEC countries, while countries like the United States actually increased their production because of the very high prices, and 60 percent came from OPEC, of the decline. And then it moved in the other direction.

But when you look at OPEC production today, it is not much bigger than it was a few years ago. Now, of course, you have one OPEC member, Iraq, which is really not a member of OPEC, but it is under the jurisdiction of the United Nations. The Iraqi oil exports are determined by the U.N. Security Council.

And one of the reasons why you had this price decline in 1998, is because the U.N. Security Council permitted Iraq—for very good reasons—to substantially increase its exports by almost a million barrels a day from the beginning of 1998 to the beginning of 1999 in order to pay for food and medical supplies. But it did enter the world market, of course, and it was a major factor—almost offsetting the attempt of the other OPEC nations to reduce their production in order to stay in the price structure.

Mr. SHIMKUS. Okay. And following this line of questioning, would the Exxon-Mobile merger, specifically—and consolidation, in general—have an effect on the U.S. dependance on imported oil, in particular, a Middle Eastern oil?

Mr. LICHTBLAU. No, it wouldn't; not really. It may make that company stronger. The merged company might be stronger; therefore, it might be in a better position to bargain with foreign governments then because, instead of two major companies competing with each other for access to a specific area, you have one company which is much stronger, and it is in the better bargaining position. So it could possibly, when it comes to getting access to Saudi Arabia to Venezuela, be in a stronger position. So it might possible help, but, basically, it wouldn't make any—basically, any changes.

Mr. SHIMKUS. Thank you.

Mr. Reidy—and I am trying to find the exact words, but you talked about the pricing aspects, and you mentioned padding.

Mr. REIDY. Padding and zone pricing.

Mr. SHIMKUS. Yes. Can you explain that in layman's terms?

Mr. REIDY. Well, what padding and what zone pricing is, if you would take like a State, and we will say it has 10 counties in it. You might think that each county has a different price for one rea-

son or another—and you have that now with the taxes, the metro taxes, and things like that. What is happening in the marketplace now, is that 1 company might have 230-240 locations within their—we will say their sales' territory—the territory of Maryland, and D.C., and Virginia, because I am familiar with this area. They will have like 240 locations. In that particular 240 locations, there might even be 240 different prices to the dealer. You can go out right now, in just about every area, every street in this area, and you can go a mile and a mile and a half, and the price that these dealers are paying will vary anywhere between 1 and 4 and 5 cents. And that is just in a mile and a half.

So, it is not like it is a general location—like I said in the counties—it is just all over the place. And the situation with that is when all of you are out there buying gasoline today, you might think that the gentleman with the lowest prices is a hero, and the guy with the highest price is just squeezing everybody or just overcharging, when it is just the opposite. He might be making less money than the gentleman or the lady at the five cents below. So that is what it is.

And when I first heard about this Exxon-Mobil merger, I figured this is tremendous. I have a Citgo by me and a Cosco. I was hoping that this would really work, that they would be able to get pricing so cheap that I can face these dealers every day because they are selling the gasoline at prices lower than I am even paying for it at this particular time. But as we found out from some of these other mergers, it just doesn't seem to be working that way. And that is one of our great concerns, that with the less competition there, the chance of this zone pricing and padding will just get even higher.

Mr. SHIMKUS. And then in your statement, you mentioned that this merger will eliminate excess refining capacity, thus, limiting product and consumer choice.

Considering that Exxon-Mobil will control 12-13 percent of the refining capacity in the United States, is that a large enough of that refining sector to do what you think it will?

Mr. REIDY. I am not sure. I don't have any handle on how that part of the business works. All I know is when they send me their price increase everyday.

Mr. SHIMKUS. All right.

Mr. REIDY. That is where I get in there.

Mr. SHIMKUS. And the last question I will have, Mr. Chairman—in this round of questions.

Oh, this is "the" round; Okay.

Mr. Shotmeyer, could you explain to me who bears the cost of brand naming a product? Is it the dealers, the distributors, the major oil company, or a combination of these?

Mr. SHOTMEYER. All——

Mr. SHIMKUS. If dealers or distributors have spent resources building up a brand name, what is the impact if they are no longer allowed to market under the brand name?

So there are two questions there.

Mr. SHOTMEYER. They are well put questions, and it is really one question. The value of the brand name is built by the dealers, the distributors, and the major supplier. And the consumer gets to appreciate that brand name for quality products and associates that

brand name in his mind with something that he wants. And that is why it is valuable to us to be able to continue to have that brand name.

Mr. SHIMKUS. And, Mr. Chairman, if I may. The last question I wanted to ask kind of goes back to my first series.

During the oil crisis of the 1970's, under the dealers—and this is really initially for Mr. Reidy—under the dealers, how did that shift out through the dealers? And am I wrong to assume that the independent dealers bore a major brunt of the effect of the embargo?

Mr. REIDY. Oh, sure. At that particular time, we were limited as to the number of gallons of gasoline that we could purchase per month. But you were told, based on some formula, how much gasoline you would get each day. Now granted, it looked like everything was nice because we were closed Saturdays, and Sundays, and evenings. We didn't have any product, but we still had all the expenses, all the rents that you heard about today; all those were still there.

And, yes, it was a very tough time.

Mr. SHIMKUS. So, in essence, the industry acts as a commodity so you have to—your profit is based upon volume?

Mr. REIDY. Yes.

Mr. SHIMKUS. For the most part?

Mr. REIDY. Very little margin and, hopefully, a lot of volume.

Mr. SHIMKUS. Thank you, Mr. Chairman.

Mr. BARTON. Thank you, Congressman Shimkus.

I just have a few wrap-up questions.

Now I thought I understood pad pricing and zone pricing, until I heard Mr. Reidy's explanation, and now I am confused so——

Mr. REIDY. So are we, Mr. Chairman.

Mr. BARTON. Beg your pardon?

Mr. REIDY. So we are very confused on how it works, too.

Mr. BARTON. Oh, okay. Well——

Mr. REIDY. You might not want to ask the question.

Mr. BARTON. Let me ask Mr. Shotmeyer. Let's do it one step at a time. Define, in your term—understand what a "pad price" is, or "pad pricing."

Mr. SHOTMEYER. Sir, we buy at a rack price.

We don't get involved—we don't get involved in the kind of——

Mr. BARTON. I know, but you ought to know. I am trying to get somebody who knows it but is not involved in it.

I know what a rack is; I think I know what a rack price is.

Mr. SHOTMEYER. We buy as the distributor at a rack price at the terminal, which is the price the company sets for us at the terminal. And much the same, as I understand, the pad pricing, even though I am not involved directly in the pad pricing, those can vary from terminal to terminal by reasons of which I have no clue of why.

Mr. BARTON. Well who sets the pad price? Who is the——

Mr. SHOTMEYER. The major oil company.

Mr. BARTON. But at what level? Do they have a marketing director at the refinery, or is it done at a higher level than that?

Mr. SHOTMEYER. Traditionally, in the past, pricing used to be done either in a regional division office or corporate headquarters.

More recently, from what I understand, the pad pricing is done more in the field, and they have relegated the responsibility to field personnel to respond to competitive situations in the marketplace.

Mr. BARTON. Now the zone price, as I thought I understood zone pricing, was the dealers needed to compete against independent operators, and they set a zone price that they could vary so that you would be able to compete against the independent across the street who had been underselling you. Was that the theory, or not the——

Mr. REIDY. Yes. I guess it depends on who you are asking if that is the theory. Yes, it——

Mr. BARTON. Well, I am—well, I don't know.

Mr. REIDY. We look at it differently, as the dealers. In theory, right. You are supposed to be able to lower the price to the guys that need the help because they are going up against the Coscos and the——

Mr. BARTON. But would a zone price theoretically be available to anybody within that zone? Any dealer within that zone should get that zone price?

Mr. REIDY. Well, the problem with that is there really isn't a zone. A zone is established by one dealer having a different price than the other.

And to continue what I was saying, a lot of times—and we found when this zone pricing in our area first came out, it wasn't established to help the dealers with the lower prices, the lower market. It seemed like it was starting with the dealers with the higher prices, and it is almost as though that the dealer can charge a little bit more because, once again, he is in a nicer neighborhood. He has got higher expenses; his rent could be anywhere from $17,000 to $20,000, so he might need—as opposed to making 6 cents a gallons, he might need 7. And so they were the guys—and ladies, I am sorry—that seem to have gotten the higher prices at one time. Then it started going all over the place. So, really it is tough question.

Mr. BARTON. So whatever the pricing mechanism is—and we can find that out. We can do followup, written questions. How does the merger affect those kinds of—the zone and pad pricing? Why would the pricing mechanism be a concern in a merger?

Mr. REIDY. Because we found, like in the last Texaco and Shell merger, where they had very few zones at one time—and I think when it first came around in my particular area, it was like county by county, like I spoke. But now since this merger, for one reason or another, the problem has gotten a lot worse. And I call it a problem, especially if I am the guy with the higher price.

So we are just saying because of the last—historically, on that last merger we just saw—or buyout or whatever you want to call it—we found that the problem has gotten even worse.

Mr. BARTON. Okay. Do either of you two gentlemen expect, if the merger goes through, that there will be fewer Exxon-Mobil stations than there are today? That stations will close because of the merger?

Mr. REIDY. Well, I would—speaking for my particular self and my location in Germantown, Maryland. It is right out here, not too far from here. If you go down within 1.5 miles on the straight line on Route 355, there are three Mobil stations, two Exxons, and one

Chevron. So you would have to think, out of those five stations, somebody is going to go.

Mr. BARTON. Okay.

Mr. Shotmeyer?

Mr. SHOTMEYER. In New Jersey, as having the highest concentration of both Mobil and Exxon, there are several Mobils directly across the street from an Exxon. And for economies of scale, if one company is allowed to totally dominate that market. They are going to say, "Yeah, we can have an economy of scale by getting rid of the one location."

Mr. BARTON. If I understood you correctly, your family has been in the Mobil distribution business since there was a Mobil. You said your father was the first Mobil distributor in New Jersey, I think?

Mr. SHOTMEYER. That is right.

Mr. BARTON. Okay.

Mr. SHOTMEYER. That was correct, sir.

Mr. BARTON. So, let's don't go back to, I guess, 1906 or whenever it was. Let's go back, say, 20 years ago. What would an average station's volume expected to be then as opposed to today?

Mr. SHOTMEYER. Twenty years ago, an ideal volume for a station would be a half a million gallons a year.

Mr. BARTON. Half a million a year. What would that be today?

Mr. SHOTMEYER. Today, the minimum is a million three, for Mobil to take a look at.

Mr. BARTON. So it is almost tripled.

Mr. SHOTMEYER. That is right.

Mr. BARTON. So regardless of whether we have this merger, this economy of scale issue is going to be there. And not only are you going to bigger and bigger station volumes, in terms of gasoline, but my understanding is, now, that you have also got to have a little supermarket and something there because you almost can't make it just on gasoline and—what we would call them—"traditional service station operations." Is that correct?

Mr. SHOTMEYER. You have a very good working knowledge of the business, sir.

Mr. BARTON. Well, I shouldn't admit this, I worked as a gasoline station attendant when gasoline was 25 cents a gallon. And they got their car filled up, you washed the window, you checked the oil, you swept it out. And if you didn't do those things with a smile on your face, they went in and told the owner, who was my uncle—what a rude young man there was out on the pump.

And he chewed my rear out pretty good. So, I learned your business from ground up. I also changed flats and would even go out and change the flat on the side of the road for no extra charge if it was a friend of my uncle. And he had lots of friends. So I have been around the business a little bit.

But I mean the point is that some of what—you all are both in a business that is changing the way——

Mr. SHOTMEYER. Yes, it is.

Mr. BARTON. [continuing] the way oil and gasoline is marketed. In my hometown now, in Ennis, I can only think of one what we would call full-service station. Everything else is self serve. So it is very, very competitive.

My assumption is that the FTC is going to allow both Mr. Reidy's association and Mr. Shotmeyer's association to submit your concerns for the record. I would be stunned if that is not correct. But if you have any problems, work with the committee staff, because we will certainly make sure that your issues are something that they seriously look at.

Mr. SHOTMEYER. Thank you.

Mr. REIDY. Thank you, sir, very much.

Mr. BARTON. While I support the merger, because I think it is in the best interest of the country, and I think most—if Mr. Markey supports it—it is pretty safe to say that, as a panel, we are not going to oppose it. But that doesn't mean we don't have serious concerns about the independent dealers and distributors and market concentration that you all have highlighted.

We will have written questions for each of you gentlemen. Seeing no other members present, we are going to adjourn the hearing. We thank you for your attendance. We apologize for the delay in doing the hearing today because of some of the votes.

[Whereupon, at 2:28 p.m., the subcommittee adjourned.]