The Antitrust Aspects of Oil Company Ownership of Deepwater Ports*

CHRISTOPHER A. HART**

The projected United States consumption of petroleum is recognized by most authorities as exceeding by a substantial margin the projected United States production of petroleum for many years to come. In the continuing quest for more efficient methods of transporting foreign source petroleum to the United States, the economies of scale have resulted in the creation of larger and larger oil tankers. There are now in operation very large crude carriers (VLCC's) which are over 1,300 feet long and nearly 250 feet wide.

For the foreseeable future, VLCC's could potentially provide the most efficient means of transporting oil to the United States. However, oil from the Middle East, Africa and Venezuela, which would be delivered to the eastern and Gulf Coast United States[1] cannot be delivered in a VLCC because the draft (distance from waterline to keel bottom) of a fully loaded VLCC is about 90 feet, and no Eastern or Gulf Coast port now in existence is deep enough to accommodate such a vessel. Thus, the United States

* The opinions, analysis, and conclusions expressed in this article are solely those of the author and do not necessarily reflect the views of the Department of Transportation.

** Special Assistant to the General Counsel, Office of the Secretary of Transportation. B.S.E. Princeton University, 1969; M.S.E. Princeton University, 1971; J.D., Harvard Law School, 1973.

1. West Coast ports are not considered in this article because no interest has yet been shown in building a deepwater port on the west coast—perhaps in part because of lack of sufficient refineries and/or transportation facilities (pipelines) to refineries in that area.

cannot now fully enjoy the transportation economies of scale of VLCC's carrying foreign oil.

The inability of the existing U.S. ports to accept VLCC's requires either that the oil be carried the entire distance in smaller vessels, or that it be transferred at some point from a VLCC to smaller vessels. The latter method is presently more cost effective and is used whenever possible, with the transfer occurring either directly, from ship to ship ("lightering"), or indirectly, with an intervening onshore loading and unloading facility, typically in one of the Caribbean or Bahamian Islands ("transshipment"). Deepwater ports would eliminate the need for lightering or transshipment by allowing VLCC's to bring the oil directly to the United States.

A deepwater port is an offshore port facility placed in water deep enough to accommodate VLCC's. The port consists of one or more mooring buoys to which a vessel can secure for the purpose of pumping its oil into a buried submarine pipeline which extends from the buoy to the onshore storage and distribution facilities. In addition to permitting greater realization of the presently available marine transportation economies of VLCC's, deepwater ports offer the opportunity to reduce traffic in many of the congested harbors which now receive large quantities of oil shipments. Moreover, the environmental hazards of shipping petroleum can be reduced by deepwater ports because the number of vessels importing oil is reduced, the total number of transfer operations engaged in by those vessels is also reduced, and the need to navigate near the shores of the locations to which the oil is being shipped is alleviated, resulting in a decreased likelihood of running aground.

In much of the Eastern and Gulf Coast United States, the slope of the continental shelf is so shallow that a port which can accommodate a vessel of 90 foot draft must be many miles offshore. Consequently, the ports in those areas must be constructed beyond the three-mile limit within which the states may exercise jurisdiction. The federal response to the need for deepwater ports, in conjunction with the inability of the states, acting alone, to license or build a deepwater port, was the Deepwater Port Act of 1974 ("Act").[2] The Act provides for a "one window" licensing process, by which an applicant submits an application to the Department of Transportation ("Department") for a deepwater port license, whereupon the Secretary of Transportation ("Secretary") is required by the Act to obtain the advice and comment (and for some matters the consent) of other affected federal and state agencies and the public at large, as to the desirability and feasibility of a deepwater port, and is required to decide whether and under what conditions to issue a license.[3]

2. P.L. 93-627, 88 Stat. 2126 (codified at 33 U.S.C. §§ 1501-1524 (1976)).
3. 33 U.S.C. § 1503 (1976).

At the time of this writing, two companies have applied for and were offered deepwater port licenses—LOOP, Inc. and Seadock Inc.—both owned primarily by oil companies.[4] LOOP accepted its license to construct a deepwater port off the coast of Louisiana, but Seadock, which would have constructed a port off the coast of Texas, lost its major owners and did not accept a license due to inability to find enough new owners to finance the project. The State of Texas has begun the steps necessary to build a deepwater port at the same location and of comparable size as the port which Seadock would have constructed.[5]

The Act reflects the recognition by Congress that a deepwater port might be owned by oil companies which ship their own oil, and that such owners might operate the port in an anticompetitive manner. This article enumerates the possible anticompetitive effects of oil company ownership of deepwater ports and, in relation to those possible anticompetitive effects, discusses their treatment by the Act, sets forth the recommendations by the Attorney General and the Federal Trade Commission, and analyzes the safeguards incorporated by the Department into the deepwater port license. No attempt is made in this article to analyze the manner in which the antitrust laws could provide a remedy for abuses which may occur in the operation of deepwater ports.

I. Antitrust Problems With Oil Pipelines and Deepwater Ports

Federal economic regulation of transportation common carriers has been precipitated by different circumstances for different modes—it began for the railroads and oil pipelines, for example, because of widespread monopoly abuses, while it began for the airlines to help a fledgling industry develop. Whatever led to economic regulation of such carriers, it was generally implemented with the underlying belief that free competition might not, under the circumstances then existing, produce a system which best serves the public interest.

Most transportation common carriers provide service generally to any eligible member of the public who seeks service. Because this service often

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4. "LOOP" is an acronym for Louisiana Offshore Oil Port. It is presently owned by Ashland Oil, Inc. Marathon Oil Company, Murphy Oil Corporation, Shell Oil Company, and Texaco, Inc. Union Oil Company was an owner when the deepwater port license application was filed,but it withdrew before the license offer was accepted. When its application was filed, Seadock was owned by Cities Service Company; Continental Pipe Line Company (a subsidiary of Continental Oil Company); Crown-Seadock Pipeline Corporation (a subsidiary of Crown Central Petroleum Corporation; Dow Chemical Company; Exxon Pipe Line Company (a subsidiary of Exxon Corporation); Gulf Oil Corporation; Mobil Oil Corporation; Phillips Investment Company (a subsidiary of Phillips Petroleum Company); and Shell Oil Company.

5. In 1977, Governor Dolph Briscoe appointed the nine members of the Commission which will govern the Texas Deepwater Port Authority. *See* Tex. [Water] Code Ann. tit. 2, ch. 19 (Vernon Supp. 1977). The Commission has met with the Department to discuss its proposals.

involves cooperation among competing carriers, for example, in providing end-to-end joint through service between two points not served by any one carrier—most common carrier statutes permit the economic regulatory agency to exempt from the operation of the antitrust laws various types of agreements between those competitors which might otherwise be unlawful. To assure that each agreement has received scrutiny by the regulators before it goes into effect, the antitrust exemption normally extends only to those agreements which have specific prior approval. Generally the economic regulator can grant the exemption only if it finds that the public benefit which can result from the agreement more than justifies the potential harm to competition.[6]

For oil pipelines, end-to-end intercarrier agreements are not the major source of potential anticompetitive problems. Rather, the potential anticompetitive abuses from oil pipelines derive from a combination of distinct but highly interdependent circumstances unique to the oil industry.[7] Because deepwater ports are, from an economic and antitrust standpoint, quite similar to oil pipelines, these potential abuses can extend to the ports as well.

A. Owner-Shipper Competitive Advantages

Unlike most transportation common carriers, much of oil transported by oil pipelines is owned by a company which owns or is under common ownership with the company that owns the oil pipeline. Because few other common carriers are owned by industries which have large transportation needs, shippers which own the carriers ("owner-shippers") are rare. One major instance of owner-shipper abuses, that of railroads shipping their own coal, resulted in the addition of the "commodities clause" to the Interstate Commerce Act in 1906.[8]

Conceptually, the most obvious problem created by owner-shippers is that an owner-shipper has every incentive to favor the shipment of its own goods over the shipment of its competitors' goods. This problem has been addressed for oil pipelines by the legislative imposition of the common

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6. *See, e.g.*, 49 U.S.C. § 5b (1976) (Interstate Commerce Commission); *id.* § 1382 (Civil Aeronautics Board). Many of the agreements which have been approved by these agencies have come under considerable attack by the antitrust agencies, among others.

7. *See* F. Scherer, Industrial Market Structure and Economic Performance Chap. 22 (1970); M. de Chazeau & A. Kahn, Integration and Competition in the Petroleum Industry (1959); L. Cookenboo, Crude Oil Pipelines and Competition in the Oil Industry (1955); J. Bain, The Economics of the Pacific Coast Petroleum Industry: Part I (1944).

8. The "commodities clause" provides, in pertinent part:

> It shall be unlawful for any railroad company to transport . . . any commodity manufactured, mined, or produced by it, or under its authority, or which it may own in whole or in part, or in which it may have any interest direct or indirect, except such articles or commodities as may be necessary and intended for its use in the conduct of its business as a common carrier.

49 U.S.C. § 1(8) (1976).

carrier requirement to serve the public on a nondiscriminatory basis,[9] and has been addressed in other contexts by other means.[10]

Another undesirable effect of shipper ownership of the carrier is that such ownership eliminates the incentive of the otherwise most interested group, the affected shippers, to press for lower rates before the appropriate economic regulatory agencies. The owner-shippers will not seek lower rates for obvious reasons, and the nonowner-shippers may not seek lower rates for fear of retaliation, however subtle, from the owner-shippers.

The major unresolved problem created by owner-shippers is that both the owner-shipper and the nonowner-shipper pay the same tariff for the same service, as required by the Interstate Commerce Act,[11] but the owner-shipper receives a dividend on its ownership (assuming the pipeline is not a non-profit venture) which effectively offsets part of the rate for the shipment and creates for the owner-shipper a competitive advantage over other shippers. This problem is inherent in oil company ownership of oil pipelines generally, and the deepwater port in particular, without regard to whether the owners are seeking to avoid or to produce an anticompetitive result.

The U.S. government attempted to put an end to the oil pipeline owner-shipper's competitive advantage in the early 1940's when it brought suit against several oil companies and oil pipeline companies, alleging that the dividends of ownership constitute an illegal rebate to owner-shippers under the Interstate Commerce Act and the Elkins Act.[12] With the onset of World War II, the action was settled by Consent Decree.[13] This Consent Decree does not provide that owner-shipper dividends are illegal rebates, but provides that owner-shippers can lawfully receive a dividend which does not exceed 7% of the pipeline "valuation."

On the liability side of a balance sheet, the pipeline company's "valuation" for the purpose of the Consent Decree consists of debt plus equity. Using "throughput and deficiency agreements"[14] as security, many oil pipeline companies are able to obtain debt financing up to 90% of the total original capital input, and the owners must provide only 10% of the original

9. 49 U.S.C. § 1(4) (1976).

10. *See* United States v. Terminal R.R. Assn. of St. Louis, 224 U.S. 383 (1912), relating to railroad-owned corporation which owned both railroad bridges and the only railroad ferry service across the Mississippi River into St. Louis, in which the Court required reformation of various agreements to prohibit discrimination against nonowners.

11. 49 U.S.C. § 3 (1976).

12. 49 U.S.C. §§ 41, 43 (1976).

13. U.S. v. Atlantic Refining Co., Civ. No. 14060 (D.D.C., Dec. 23, 1941) (Complaint and Final Judgment).

14. A throughput and deficiency agreement is an agreement either to ship at least a certain amount of oil or to pay for the shipment of that amount of oil even if the oil is not tendered for shipment.

capital input from their own funds as equity. In addition, the ICC has normally allowed debt service to be treated as an expense, to be subtracted from gross income in determining the allowable cost of capital.[15] The combined effect of the use of throughput and deficiency agreements as security (which facilitates a high debt-to-equity ratio), and the accounting practices which have been allowed by the ICC (which encourage a high debt-to-equity ratio) is that an initial 90/10 debt/equity ratio is common for oil pipeline companies.[16] As a result, the 7% Consent Decree limit on "valuation" effectively allows a 70% return on equity, initially, and is not in any real sense a limit at all.[17] Thus, the Consent Decree, in combination with the failure of the ICC to require the inclusion of interest in determining the cost of capital, exacerbates the owner-shipper competitive advantage for oil pipelines.

The recent *Trans Alaska Pipeline System* case may signal a significant change in this situation.[18] For the first time in many years, the ICC suspended the rate tariffs filed by oil pipeline owners, notwithstanding their "compliance" with the Consent Decree, and indicated that the Consent Decree has served as a measure of lawfulness of dividends under the Elkins Act but has never been used by the ICC as a measure of reasonableness under the Interstate Commerce Act. Moreover, the ICC's calculations of a reasonable *interim* rate included interest within the cost of capital for determining allowable rate of return. If this interim rate standard were adopted as a standard for permanent rates, the allowable return on equity for owner-shippers could be reduced from the present 70% to a more realistic 12-15%, depending on the capital structure of the company. Whether the transfer of ICC regulatory duties to the Federal Energy Regulatory Commission ("FERC")[19] will alter this ICC trend in the direction of closer scrutiny of oil pipeline rates is not known at this time. However, in view of

15. Most regulatory agencies compute the total cost of capital as the cost of debt (debt service) plus the cost of equity (dividends to stockholders) and compute the allowable total cost of capital as gross income less expenses. In such a context, the company carefully limits its debt-to-equity ratio because an increase in the cost of debt reduces the amount that is available from the total allowable cost of capital for stockholder dividends. The allowance by the ICC of debt service as an expense has the opposite effect. As with any other expense, an increase in the cost of debt which results from an increase in the debt-to-equity ratio provides justification for an increase in the tariff rate to increase gross income, but it does not decrease the amount available for stockholder dividends.

16. *See* S. REP. No. 1217, 93d Cong., 2d Sess. 22, *reprinted in* [1974] U.S. CODE CONG. & AD. NEWS 7549.

17. This construction of the Consent Decree was affirmed in United States v. Atlantic Refining Co., 360 U.S. 19 (1959).

18. Trans Alaska Pipeline System, ICC Investigation and Suspension Docket No. 9164 (June 28, 1977). The ICC's authority to suspend these rate tariffs was recently upheld in Trans Alaska Pipeline Rate Cases, 46 U.S.L.W. 4587 (U.S. June 6, 1978).

19. The transfer of ICC functions to the FERC occurred under the Department of Energy Organization Act, P.L. 95-51, 91 Stat. 565, §§ 306, 402(b) (codified at 42 U.S.C. §§ 7155,

several recent legislative and administrative efforts to make regulatory agencies more responsive to the broad public interest and less protective of the industries they regulate, a continuation by FERC of this trend is likely, at least in the near future.

B. Vertical Integration

Another aspect of oil pipelines which makes them unique as a common carrier is the extensive vertical integration of the oil industry of which they are a part. Not only do the companies that own the oil also own the oil pipeline, but many also own the oil tankers, the tank farms, the refineries, the refined product distribution systems and in some instances, the retail outlets.[20]

If an oil pipeline or the port is part of a vertically integrated structure, the port owners will want the port capacity to be that needed by their vertically integrated operation, rather than that desired by all users of the port. Thus, there is no incentive for vertically integrated oil company port owners either to make the port large enough for nonowners originally or to expand the port to meet the needs of nonowners.

With respect to rates for use of the port, vertical integration facilitates the spreading of profits and losses across the total structure. In general, this permits individual segments of the structure to operate at lower prices with cross subsidy from the other segments, to the detriment of non-integrated competitors of the lower-priced segment. In particular, if one segment is regulated, as many oil pipelines are and deepwater ports will be, the profits which could otherwise be realized in the regulated segment can be realized in other segments, resulting in effective circumvention of the regulatory rate constraints. Moreover, if any link of a vertically integrated structure is a monopoly, the monopoly characteristics are extended to a degree throughout the structure. The effect would be that non-integrated competitors would be forced either to pay the higher prices charged in the monopolized segment of the industry or to use less cost-effective alternatives to that segment, both to the detriment of the non-integrated competitors. Oil pipelines and deepwater ports would fall into this category if not regulated because they are a monopoly, as discussed below. Thus, vertically integrated oil companies are more able to manipulate the total system to maximize the advantages of port ownership and to maximize the extent to which port ownership can be leveraged to produce advantages in the total system.

7172(b) (1976)). The transfer occurred without any changes in the statutory provisions relating to oil pipeline economic regulation.

20. *See, e.g.*, Report of the Senate Comm. on the Judiciary, Petroleum Industry Competition Act of 1976, pt. 1 (June 28, 1976); Vertical Integration in the Oil Industry (E. Mitchell ed., American Enterprise Institute for Public Policy Research, 1976).

This vertical integration of the oil industry has not escaped the attention of Congress, and bills have been introduced which would require various degrees of divestiture.[21]

C. MONOPOLY

Oil pipelines generally are a natural monopoly.[22] They are a *natural* monopoly because of their "geographically fixed facilities designed to serve customers in close proximity to such facilities and almost entirely useless for any other purpose."[23] They are a natural *monopoly* because it is generally more efficient, due to the economies of scale, for one pipeline to be utilized between the same two points. In practice, of course, many other factors could result in multiple pipelines, such as a need for phased growth which makes it desirable to add other pipelines when needed, rather than to commence with an oversized pipeline or to replace the original pipeline with a larger pipeline, the need to be able to carry more than one substance simultaneously, or limitations in the size of readily available pipeline.[24]

For the same physical reasons that an oil pipeline is a natural monopoly, a seaport is a natural monopoly. Thus, a deepwater port is a natural monopoly both in its role as an oil pipeline and in its role as a seaport.

In addition to the naturally monopolistic character inherent in oil pipelines and seaports, deepwater ports are also, in effect, a *statutory* monopoly because the Act precludes the construction of more than one port within an "application area."[25] This prohibition provides a port investment in-

21. *See, e.g.*, S. 795, 95th Cong., 1st Sess. (1977), and its identical predecessor, S. 2387, 94th Cong., 2nd Sess. (1976).

22. *See, e.g.*, NAT. BUREAU ECON. RESEARCH, PRICE RESEARCH IN THE STEEL AND PETROLEUM INDUSTRIES (1939).

23. W.K. JONES, CASES AND MATERIALS ON REGULATED INDUSTRIES 51 (2d ed. 1976).

24. *See* L. COOKENBOO, *supra* note 7.

25. Sections 5(d)(1) and (2) of the Act provide:

> (d)(1) At the time notice of an application is published pursuant to subsection (c) of this section, the Secretary shall publish a description in the Federal Register of an application area encompassing the deepwater port site proposed by such application and within which construction of the proposed deepwater port would eliminate at the time such application was submitted, the need for any other deepwater port within that application area.
> (2) As used in this section, "application area" means any reasonable geographical area within which a deepwater port may be constructed and operated. Such application area shall not exceed a circular zone, and center of which is the principal point of loading and unloading at the high water mark of the nearest adjacent coastal State.

33 U.S.C. §§ 1504(d)(1), (2) (1976).

Upon receiving application for a deepwater port, the Secretary is required by § 5(d)(3) of the Act to publish notice of the application in the Federal Register (after having determined pursuant to § 5(c)(1) that the application contains all information required by § 5(c)(2)), and to publish therewith pursuant to § 5(d)(1) a description of the application area. *Id.* § 1504(d)(3). Within 60 days after such Federal Register publication, any applicant intending to submit an application for a deepwater port within the application area is required by § 5(d)(3) to submit notice of intent to file an applicacentive by eliminating the possibility of a diminution in the value of the investment by a competing port.

The absence of competition in a monopoly leaves the monopoly holder free of the constraints which in a competitive market would help cause supply to be responsive to demand. In a competitive context, the supply-demand relationship helps to assure that the price of goods or services is a reflection of their real value to society and that the quantity of goods or services provided is the quantity desired by society. Due to the absence of the market constraints which result from the supply-demand relationship, possibilities for pricing and other market abuses are inherent in a monopoly.

There are both economic and legal constraints in relation to monopoly abuses. As an economic matter, the alternative means of importing oil would establish the limits beyond which additional monopoly abuses would provide no additional benefits to the monopolist because nonowner-shippers would turn to those alternatives. In decreasing order of present economic attractiveness, these alternatives are lightering, transshipment, and nonuse of VLCC's. However, because lightering is encountering increased environmental opposition, and many transshipment facilities are not available for public use, the only certain limiting alternative is nonuse of VLCC's. With nonuse of the VLCC's as the limiting alternative, it is apparent that monopoly abuses could eliminate almost entirely the economic advantages which deepwater ports can enjoy over existing methods of importing oil, for the nonowner-shipper.

As a legal matter, the license provides no antitrust immunity, and the issuance of a license is not admissible as a defense to any civil or criminal antitrust action.[26] Thus, aside from the prospective standards which the Department can incorporate in the deepwater port license, as discussed below; monopoly abuses generally would be subject to the antitrust laws. The analysis of the manner in which the antitrust laws could be relied upon to remedy abuses by deepwater port licensees, if they should occur, is not presented here—such analysis would in itself be sufficiently complex to justify an entire article, and would be more meaningful if undertaken after operational experience had been acquired with the ports. For purposes of this article, it is necessary only to note that Sections 1 and 2 of the Sherman Act[27] among other antitrust statutes such as Section 5 of the Federal Trade

tion, and is required to submit the application itself within 90 days after publication. Any application for the application area which fails to comply with these 60- and 90-day requirements cannot be considered until the Secretary has denied all pending applications for the application area which have satisfied the time requirements.

26. 33 U.S.C. § 1506 (1976).

27. Section 1 of the Sherman Act, 15 U.S.C. § 1 (1976) provides, in pertinent part: "Every contract, combination in the form of trust or otherwise, or conspiracy, in restraint of trade or commerce among the several States, or with foreign nations, is declared to be illegal . . . ." This could be applied in relation to agreements between the port and third parties, and could conceiva-

Commission Act,[28] would be applicable both in relation to the acts of the port itself and in relation to agreements between the port and third parties such as connecting downstream pipeline companies.

Natural monopolies and "statutory" monopolies result from situational and legal circumstances, respectively, which are beyond the control of the monopoly holder. To assure that such a monopoly holder does not unduly benefit therefrom, most natural transportation monopolies in this country are common carriers which are required to serve the public without discrimination and are regulated as to the rates they may charge for their natural monopoly service. Likewise, the natural monopoly advantages inherent in seaports normally inure to the public benefit ultimately, because they are public or quasi-public facilities which, by that fact, operate in the public interest.[29]

D. Oligopoly

The concept of oligopolistic behavior in a given market relates in its most common usage to a situation in which that market is dominated by a few large competitors.[30] Their status as competitors and their large size result in the likelihood of a commonality of interest. This commonality of interest, combined with the small number of participants which helps generally to facilitate similarity of action, can result in market behavior which resembles the behavior of one very large and dominant joint-venture competitor.

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bly also be applied in relation to agreements between the shareholder corporations themselves with respect to the acts of the port.

Section 2 of the Sherman Act, 15 U.S.C. § 2 (1976) provides, in pertinent part: "Every person who shall monopolize or attempt to monopolize, or combine or conspire with any other person or persons, to monopolize any part of the trade or commerce among the several States, or with foreign nations, shall be deemed guilty of misdemeanor . . . ."

Monopoly has been defined as "the power to control market prices or exclude competition." United States v. Grinnell Corp., 384 U.S. 563 (1966). It has been stated that § 2, in proscribing "monopolizing" without proscribing "monopolies," prohibits conduct rather than status. United States v. E.I. DuPont Nemours & Co., 118 F. Supp. 41, *aff'd* 351 U.S. 377 (1956). Thus, in determining whether unlawful "monopolizing" has occurred, the § 2 analysis looks to the manner in which a monopoly is (a) acquired and/or maintained, and (b) used after having been acquired. *See*; United States v. United Shoe Machinery Corp., 110 F. Supp. 295, *aff'd per curiam* 347 U.S. 521 (1954). In relation to a deepwater port, as to which the monopoly has been acquired and maintained by virtue of being both a natural and statutory monopoly, § 2 of the Sherman Act would therefore be applied primarily in relation to the manner in which the port monopoly is used, and any abuse of the lawfully acquired monopoly power would violate § 2. *See, e.g.*, United States v. Otter Tail Power Co., 410 U.S. 366 (1973); United States v. Griffith, 334 U.S. 100 (1948).

28. 15 U.S.C. § 45 (1976).

29. The economic regulation of seaports is a matter of local concern. Thus, the public interest is defined by a local authority. *See generally* S. Rep. No. 1217, 93d Cong., 2d Sess. 23 *reprinted in* [1974] U.S. Code Cong. & Ad. News 7550.

30. C. Kaysen & D. Turner, Antitrust Policy 27 (1959)

The ownership structure and operation of a deepwater port will determine whether there is potential for oligopolistic abuse, stemming from the marine transportation of oil, which might be felt throughout the petroleum industry. As a general matter, greater similarity of the interests of each participant to the interests of the other participants and the interests of the whole results in greater potential for oligopolistic behavior. There is nothing inherent in a deepwater port which favors either the number, type, or size of participants from which oligopolistic abuses might be expected. With respect to the number of participants, the magnitude of the necessary capital commitment to the port favors a large number of owners; on the other hand, the desire of each owner not to see its large financial commitment directed against its wishes favors a small number of owners. With respect to the nature of participants, the ability of oil companies to ship their oil through a common carrier deepwater port without incurring any ownership risk would seem to discourage oil company ownership; on the other hand, the owner-shipper competitive advantage, in conjunction with the relative inability of any investor other than an oil company to provide or obtain adequate capital, favors oil company ownership.[31] With respect to the size of the participants, the larger companies are more able to use the port to derive benefit over the entirety of a vertically integrated structure, and are financially probably more capable of acquiring an ownership interest; on the other hand, the smaller companies are less able than the larger companies to obtain or provide alternative means of transporting their oil.

Inasmuch as oil company owners of an oil pipeline are joint owners rather than competitors in that pipeline, a pipeline fits squarely within the classical oligopoly concept of a dominant joint venture. The oil company owners are often vertically integrated competitors in the oil industry at large, within which oil pipelines are obviously an important element. Therefore, in addition to the opportunities provided by this joint participation for competitors to share information they would not otherwise share and to act in accordance with their mutual interest, the potential for abuse lies in the joint participation by competitors in an important segment of the total industry, a type of joint participation that is not common in any unregulated portion of the American economy, and that generally occurs only with the oversight or prior approval of a regulatory agency in regulated enterprises.

Thus, the potential for oligopolistic abuse would be greatest in relation to oil pipelines, including deepwater ports, if the owners were large oil companies, few in number, of comparable nature in the oil industry at large, and in combination, a vertically integrated dominant portion of that industry. In

31. As noted above, few investors can command the 90 % debt financing which oil companies can obtain with throughput and deficiency agreements as security. *See* note 15 and text accompanying notes 15 & 16 *supra*.

such a situation, each owner's individual interest would be similar to the collective interest of the whole. The small number of owners would increase the likelihood of their pursuing similar courses of action in general by decreasing the likelihood of a diversity of interests. The large size and similar nature of owners would also increase the likelihood of a similarity of owner interest in the deepwater port because, for example, large oil companies have many similar needs in terms of market structure, corporate structure, financial structure, and equipment, to name a few, all of which may be different than those needs for medium or small oil companies. By the same token, vertically integrated oil companies would have many needs that are similar to the needs of other vertically integrated oil companies but dissimilar from the needs of companies that are not vertically integrated. The similarity of interests would narrow the scope of considerations which must be taken into account in relation to business decisions and would thereby decrease the likelihood that decisions of the port owners will affect positively the public interest. The combined vertically integrated dominance of the owners in the oil industry at large would increase their incentive and ability to manipulate the total system to increase the leverage which port ownership could provide over the total system. With diverse owners, on the other hand, the collective interest of the whole is an amalgamation of differing individual interests, such that the collective interest is less like the interest of any individual but more like the broader public interest.

In sum, the unique nature of oil pipelines as compared with other common carriers combines with the nature of the oil industry to result in a combination of potential abuses which is not susceptible to easy remedy. If any one of the problems were eliminated, the severity of the others would be mitigated. Some of the potential abuses would not be expected unless the port owners chose to operate the port in an anticompetitive manner, while other potential abuses are inherent in the nature of oil company ownership of deepwater ports irrespective of the manner in which the port owners choose to operate the port.

All of the potential problems are greatly exacerbated by the vertically integrated oil industry structure and the 1941 Consent Decree, discussed above, which effectively allows the port owners to establish rates that permit as much as 70% return on equity.

II. Treatment of Competitive Concerns by the Deepwater Port Act of 1974

The legislative history of the Act indicates that considerable attention was given to the possibility of competitive abuses from oil company owned deepwater ports.[32] Indeed, this concern resulted in recommendations by the Senate Commerce Committee and the Justice Department that the Act prohibit port ownership by oil companies.[33]

A. Ownership Priorities

These recommendations were not incorporated in the Act because of the countervailing concern that oil companies which use the port might be the only entities which would be willing and able to acquire or provide the estimated $600-900 million needed to construct a deepwater port.[34] However, as a compromise between the desire for deepwater ports and the concern that oil company owners might abuse their ownership privilege, the Act permits oil company ownership only if no other prospective owners apply, and it imposes certain mandatory and discretionary safeguards.

To encourage deepwater port ownership by non-oil companies, the Act establishes a priority of ownership. If more than one eligible application is submitted for an "application area,"[35] section 5(i)(2) of the Act provides:

> (2) In the event more than one application is submitted for an application area, the Secretary, unless one of the proposed deepwater ports clearly best serves the national interest, shall issue a license according to the following order of priorities:
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> (A) to an adjacent coastal State (or combination of States), any political subdivision thereof, or agency or instrumentality, including a wholly owned corporation of any such government;
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> (B) to a person who is neither (i) engaged in producing, refining, or marketing oil, nor (ii) an affiliate of any person who is engaged in producing, refining, or marketing oil or an affiliate of any such affiliate;
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> (C) to any other person.[36]

As forecast by many of the legislators involved in framing the Act, most of the serious initial interest shown in seeking a deepwater port license has

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32. S. Rep. No. 1217, 93d Cong., 2d Sess. 2, 13-15, 19-27 *reprinted in* [1974] U.S. Code Cong. & Ad. News 7530, 7540-42, 7547-7554.

33. *Id.* at 19, 27 (Senate Commerce Committee Recommendation), [1974] U.S. Code Cong. & Ad. News 7546, 7554; *Id.* at 21, [1974] U.S. Code Cong. & Ad. News 7548 (DOJ Testimony).

34. S. Rep. No. 1217, 93d Cong., 2d Sess. 14 *reprinted in* U.S. Code Cong. & Ad. News 7542.

35. *See* note 25 *supra*.

36. 33 U.S.C. § 1504(i)(2) (1976).

been from companies desiring to ship their own oil.[37] However, at the time of this writing, legislation had recently been introduced in Delaware which would permit it to apply for a deepwater port license, and,[38] as noted above,[39] the State of Texas had begun to show serious interest in applying for a license to build a port similar to that which Seadock had applied to build.

B. COMMON CARRIER STATUS

Another provision in the Act which helps reduce the likelihood of abuses is section 8, which provides that the deepwater port and affiliated storage facilities are subject to regulation as a common carrier under the Interstate Commerce Act, and requires a deepwater port licensee to convey without discrimination all oil tendered to the port.[40] This provision applies to all deepwater ports, but its benefit is most apparent in relation to ports owned by oil companies.

C. CONSULTATION WITH DOJ, FTC

Finally, the Act contains a provision which provides the licensing flexibility that the Secretary needs to respond to the wide variety of situations which could occur. The Secretary cannot issue, transfer, or renew any license without first obtaining the opinions of the Attorney General and the Federal Trade Commission as to whether the issuance, transfer, or renewal "would adversely affect competition, restrain trade, promote monopolization, or otherwise create a situation in contravention of the antitrust laws."[41] In contrast to the ownership priority and common carrier provisions, this consultation requirement facilitates examination by the antitrust agencies of each license issuance, transfer, or renewal situation that is presented, and allows the Secretary to tailor safeguards to the needs of each situation.

The extent to which each of these provisions is necessary or desirable can only be determined from experience with the actual operation of the deepwater ports.

III. RECOMMENDATIONS BY THE DEPARTMENT OF JUSTICE AND THE FEDERAL TRADE COMMISSION

After the LOOP and Seadock deepwater port license applications were submitted, the Secretary requested the views of the Justice Department

37. *See* S. REP. No. 1217, 93d Cong., 2d Sess. 13, *reprinted in* [1974] U.S. CODE CONG. & AD. NEWS 7540.

38. *See* Del. S.B. 449, 129th Gen. Assembly, 1st Sess. (1978).

39. *See* text accompanying note 5 *supra*.

40. 33 U.S.C. § 1507 (1976).

41. Sections 4(c)(7), 7, 33 U.S.C. §§ 1503(c)(7), 1506 (1976).

and the Federal Trade Commission pursuant to Sections 4(c)(7) and 7 of the Act.[42] The Justice Department and the Federal Trade Commission each submitted their report on these applications to the Secretary on November 5, 1976 ("DOJ Report" and "FTC Report," respectively). A brief summary of the views of both agencies is presented here.

As a general matter, because the Act does not prohibit oil company ownership of the ports and because no one else had then applied for a license, neither the DOJ Report nor the FTC Report recommends against issuance of the licenses to the oil company applicants.[43] However, both Reports express concern that the vertically integrated oil company port owners will earn excessive profit. They also express concern about the incentive for such port owners to discriminate against nonowners, both as to the port itself and as to pipelines owned by the port owners which connect the port to inland common carrier distribution pipelines, and about the lack of incentive for such port owners to expand the port when demand exceeds capacity.

More particularly, the DOJ Report notes the following:

> The major conclusion to be drawn from our antitrust analysis is that the integrated oil company owners of the proposed ports have attempted to maximize their profits through various overt and subtle requirements which will have the effect of restricting port throughput by limiting port capacity and access, thus enhancing the owners' profits in downstream product markets. Our economic analysis indicated that the port owners have the incentive to act in this manner, since port profitability is limited by rate regulation. We believe that the evidence demonstrates that the owners propose to operate the ports in a restrictive and anticompetitive manner, and that this will result in a misallocation of our nation's resources.[44]

In order to address these concerns, the DOJ Report lists four competitive rules which are recommended for adoption by the Secretary as conditions in any deepwater port license issued to the oil company applicants. The four competitive rules are:

1. Deepwater ports must provide open and nondiscriminatory access to all shippers, owner and nonowner alike.
2. Any deepwater port owner or shipper providing adequate throughput guarantees at the standard tariff can unilaterally request and obtain expansion of capacity.
3. Deepwater ports must provide open ownership to all shippers at a price equivalent to replacement cost less economic depreciation.
4. The ownership shares of the deepwater ports' owners must be revised frequently (annually) so that each owner's share equals his share of aver-

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42. *Id.*
43. Dept. of Transportation, The Secretary's Decision on the Deepwater Port License Application of LOOP Inc. (Dec. 17, 1976) app. B-22 (DOJ), C-2 (FTC) [hereinafter cited as Decision].
44. *Id.* app. B-7.

age throughput.[45]

With these competitive rules as a core, the DOJ Report enumerates 18 specific implementing recommendations, along with five additional recommendations relating to the port financing, tariffs, and other matters.[46]

The DOJ Report provides the following explanation concerning the competitive rules:

> The competitive rules have the potential to eliminate most of these excess port and downstream profits. The rules achieve this result by prohibiting integrated oil companies from unreasonably or discriminatorily restricting access to and the capacity of the port, so that the owners will not be able to restrict use of the port. Rule 3, by permitting any non-owner to become an owner, serves as an expansion incentive by making the excessive port profits available to all shippers. Rule 4 completes the process of giving a shipper the ability to ship at the true economic cost of shipping. As an owner he will receive dividends to offset the excessive tariffs which are charged.
>
> But rules, 1, 3 and 4 alone are insufficient, since the owners old and new could restrict port capacity and achieve the same result—excess downstream profits—although they are now shared by all shippers. To forestall this type of restriction, first, an owner or a shipper must be able to force port expansion unilaterally, as long as that shipper is willing to guarantee the expansion by executing a throughput agreement and is willing to pay the going tariff for the expanded shipments.
>
> It is likewise important to note that all four rules must be allowed to work together, for paradoxically, reliance on some of them and omission of the others may lead to a worse result than no rules at all. For example, if Rules 1, 3 and 4 were implemented and Rule 2 omitted, we would in effect be sanctioning a cartel with the power to veto the capacity decisions of each member firm in the industry.
>
> The rules are designed to achieve the most competition possible short of nonintegration.[47]

The FTC Report likewise enumerates several rules and recommendations which are intended, solely or in combination with other recommendations, to address competitive problems similar to those isolated in the DOJ Report.[48] In broad terms, the recommendations in the Reports can be classified into three major categories: port design/ownership, port operation and rate tariffs.

A. Port Design and Ownership

First, with respect to major port design and planning decisions, the primary concern relates to the lack of incentive for vertically integrated oil company port owners either to make the port large enough originally to

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45. *Id.* app. B-10.
46. *Id.* app. B-14 to B-21.
47. *Id.* app. B-11 to B-12.
48. *Id.* at C-1 to C-2 (rules), C-2 to C-6 (recommendations).

allow capacity in excess of expected owner demand for expected nonowner demand, or to expand the port when total demand exceeds capacity, especially when the "excess" demand is nonowner demand. The theory is that as a general matter, in addition to the lack of incentive for oil company port owners to expand when an expansion would help their competitors at least as much as it would help them, vertically integrated oil companies have incentive only to make the port large enough to support their vertically integrated structure without regard to the needs of nonowners, because the port can provide a bottleneck which can restrict supply and thus support higher prices at the end of the vertically integrated structure.

The most direct remedy proposed by the Reports is a license requirement to permit nonowners to buy ownership shares in the port at a price based upon replacement cost less economic depreciation of the port facilities.[49] This would create an incentive for the owners to consider the expansion requests of nonowners seriously because those nonowners would have the leverage of their right to become an owner if the existing port owners ignored their expansion requests. In broader terms, it would also help deter any anticompetitive abuses which enhance port profitability because the greater the profit from the port, the higher the incentive for outsiders to become owners. A second remedy is a requirement in the license that any shipper (owner or nonowner) which is willing to guarantee the throughput can unilaterally compel an expansion.[50] To be effective, this remedy would require the license to provide the means by which the debt of the port could be increased to finance the necessary expansion. Finally, the backstop remedy which the FTC Report recommends, if all else fails, is that the Secretary retain in the license the authority to compel an expansion as he deems necessary.[51]

As part of the total capacity problem, the Reports also address the throughput demands of the owners in relation to each other. As long as dividends are in the same proportion as owner throughput, each owner receives the same percentage offset on its shipping rates. If ownership percentages remain fixed while owner throughput varies, any owner shipping more than its initial ownership percentage would receive a lower percentage offset. To assure that ownership percentages are periodically adjusted to equal owner throughput percentages, and to eliminate the disincentive to expansion caused by dividends which are proportionately less than throughput, the Reports propose a license requirement for periodic readjustment of share percentages.[52]

49. *Id.* app. B-18 to B-19 (DOJ), C-3 (FTC).

50. *Id.* app. B-18 (DOJ), C-3 (FTC).

51. *Id.* app. C-3.

52. The DOJ Report recommends annual readjustments, *id.* app. B-20; the FTC Report recommends "periodic" readjustments, without specifying the period, *id.* app. C-3.

B. Port Operation

With respect to day-to-day physical operations of the port, the primary concern is the lack of incentives for the port owners to assure and facilitate access to the port by nonowners. The remedies proposed for this problem fall into two major categories. First, the Reports recommend license conditions either specifying or requiring prior approval by the Secretary of various port access conditions, for example, size of minimum tender, segregation capability, and other factors affecting the practical utility of the port to nonowners.[53] Second, the Reports recommend that the license contain various provisions to assure that nonowner-shippers can transport their oil from the port to the inland oil distribution pipeline system.[54] The intent is to avoid the frustration of protective measures at the port itself by more restrictive conditions in connecting downstream pipelines, especially as to downstream pipelines which are owned or controlled by owners of the port.

C. Rate Tariffs

Both Reports express concern with respect to the day-to-day financial operations of the port. The ability of the port owners to charge rates which provide up to 70% return on equity could discourage use of the port by nonowners, and would in any event frustrate a basic purpose of the Act —to pass the transportation economies of deepwater ports to the consumer. The Reports recommend that the Secretary not allow tariff rates which provide more than the "true costs of capital" (DOJ Report)[55] or "a reasonable rate of return on total investment in light of the risks involved and in light of the types of financial commitments made by the owners" (FTC Report).[56]

IV. Competitive Safeguards Incorporated in the Licenses

Section 4(c) of the Act provides that the Secretary may issue a deepwater port license if, among other things, "he determines that the construction and operation of the deepwater port will be in the national interest and consistent with national security and other national policy goals and objectives, including energy sufficiency and environmental quality."[57]

Likewise, Section 4(e)(1) of the Act gives the Secretary the authority to impose conditions in the license in order to help assure that a deepwater port will be in the national interest:

53. Decision, *supra* note 43, at app. B-16 (DOJ), C-4 (FTC).
54. *Id.* app. B-16 (DOJ), C-5 to C-6 (FTC).
55. *Id.* app. B-20.
56. *Id.* app. C-2.
57. 33 U.S.C. § 1503(c)(3) (1976).

In issuing a license for the ownership, construction, and operation of a deepwater port, the Secretary shall prescribe any conditions which he deems necessary to carry out the provisions of this [Act], or which are otherwise required by any Federal department or agency pursuant to the terms of this [Act].[58]

On December 17, 1976, then Secretary of Transportation William T. Coleman, Jr. issued "The Secretary's Decision on the Deepwater Port License Application of LOOP, Inc." and "The Secretary's Decision on the Deepwater Port License Application of Seadock, Inc." These documents announced his decision to offer nearly identical licenses to the two applicants.[59] Because LOOP has accepted its license, the LOOP Decision will be the reference document for this article.

A. Analytical Framework

In deciding which recommendations from the DOJ and FTC Reports to incorporate as conditions in the license, the Secretary was faced with a complex and unprecedented combination of factors, both with respect to the antitrust analysis itself and with respect to the role which that analysis should play in deciding whether and with what conditions to issue a license.

1. *Antitrust Factors*

The first step in the antitrust analysis is the selection of the appropriate analytical framework. A classical free market analysis of problems such as shipper-ownership and vertical integration cannot by itself yield realistic results in a regulated context because the economic regulation of the port results in various structural controls and constraints which destroy the validity of several fundamental assumptions of a free market analysis. On the other hand, a regulated industries antitrust analysis is not entirely appropriate because, although a deepwater port itself will be a regulated common carrier, the vertical integration of the oil company owners necessitates an analysis which goes beyond the port itself to the oil industry at large. As the analysis broadens to the oil industry at large, it is confronted with an industry which is regulated in some segments, narrowly "regulated" by price "controls" (ceilings) in other segments, and unregulated in still other segments. In addition, the vast diversity of end products which results from crude oil creates a flexible and dynamic industry the shape and mixture of which at any point in time is partly a reflection of the mixture of regulation, price controls, and nonregulation which forms the legal and economic environment in which the industry exists. Given this dynamic mixture of vertically linked regulated, semi-regulated, and unregulated segments of an

58. *Id.* § 1503(e)(1).

59. *See, e.g.*, Decision, *supra* note 43. Appendix A of each decision is the license itself. In order to clarify certain ambiguities in the two licenses, they were modified slightly and reissued on January 17, 1977.

industry, the threshold task of determining the appropriate antitrust analytical framework is in itself a difficult matter as to which knowledgeable analysts vary widely.[60]

An added complexity which must be factored into the analysis derives from the possibility that oil company owned and publicly owned ports may someday be operating contemporaneously. Although it is unlikely that there will ever be two or more geographically proximate "competing" ports, it is clear in the broader view of the oil industry at large that the extent to which a deepwater port could engage in anticompetitive activities would in a very real sense be limited by the existence, or even the possibility, of a publicly owned deepwater port somewhere else in the system. This potential for parallel operation of private and public "competing" facilities presents a situation which is rare to antitrust analysts. By the same token, as noted above,[61] the extent to which transshipment and lightering will provide viable alternative methods of transportation depends upon legal and environmental constraints which may change drastically in the future.

Finally, perhaps the most fundamental problem presented in the antitrust analysis is that deepwater ports are an unknown entity in this country. Thus, in addition to all of the other uncertainties which are inherently presented to an analysis of this kind, such as the impact of Alaskan oil, the reliability of Middle East supply, the nation's future energy consumption patterns, and the rate regulation of oil pipelines, all anticompetitive safeguards imposed in deepwater port licenses must be based upon an educated guess as to what owner-shippers and nonowner-shippers, as well as possible public owners and investors generally, *might* do in future years in relation to deepwater ports. Most of the competitive safeguards are preventive, rather than after-the-fact remedies. As with any prospective safeguard, and more so in relation to a situation such as the deepwater ports which has never existed before, these prospective safeguards must be very carefully constructed in order to provide complete coverage without overkill; they must retain the flexibility to respond to future situational changes; and they must avoid creating obstacles which merely redirect future behavior into less efficient mode without eliminating the abuses.

2. Transportation Factors

Added to these difficulties of developing a reliable antitrust analysis and solutions is the problem ultimately placed by the Act upon the Secretary in determining the extent to which the antitrust problems should be

60. *See, e.g.*, Lipsey & Lancaster, *The General Theory of Second Best*, 24 REV. OF ECON. STUDIES 11-32 (1956); M. DE CHAZEAU & A. KAHN, *supra* note 7; R. CASSIDY, PRICE AND PRICE BEHAVIOR IN THE PETROLEUM INDUSTRY(1954).

61. *See* introductory discussion at the beginning of this article *supra*.

incorporated in order to assure the development of a transportation project which is "in the national interest," as required by the Act.[62]

B. License Safeguards

Most of the safeguards recommended in the DOJ Report and the FTC Report were incorporated in the licenses. In determining which safeguards to apply, the Decision notes:

> In general, the findings of the Attorney General and the FTC are consistent, and both agencies express similar concerns . . . . Although I do not agree with every statement made in the analysis of either the Attorney General or the FTC, I have found their conceptual framework and specific recommendations generally reasonable, sound and constructive. I have accepted and incorporated into the license almost all their recommendations for conditions.
>
> Where I have not followed their specific advice, I have adopted an alternative course, explained below, that, in my judgment, will work more effectively. Where I have chosen an alternative, it has been primarily because another Federal agency has the statutory authority and operating responsibility, and the statute permits the regulatory agency to do exactly what the Attorney General and the FTC request. Thus, I am reluctant to assert my conditioning authority in a way that duplicates or conflicts with the proper exercise of another agency's authority.[63]

The Decision continues by indicating the basic policy guidelines which were applied in deciding which anticompetitive safeguards to incorporate:

> In my judgment (and the Attorney General apparently agrees), the proper construction and operation of a deepwater port offers certain environmental, economic and transportation benefits. We must ensure, therefore, that in furtherance of antitrust objectives, we do not defeat important transportation objectives by creating unnecessary impediments to construction of the port. Accordingly, I am applying the following policy guidelines in reconciling the antitrust recommendations with other important transportation objectives:
>
> (a) Consistent with our stated policy, we will encourage the action of competitive forces to the maximum extent feasible.
>
> (b) In the interest of rational delineation of Federal agency responsibility, we will avoid exercising jurisdiction that duplicates that of other agencies, instead seeking reform of ineffective agency practices through intervention in that agency's proceedings and, if necessary, by proposing legislation to amend its statutory charter.
>
> (c) We will exercise our authority in conditioning the license and regulating the port to the extent necessary to fill the gaps in the regulatory framework in order to prevent discrimination and anticompetitive practices in an effective manner.
>
> (d) In constructing or advocating any regulatory scheme, we will follow the advice of the Supreme Court in *American Trucking Association v. Atchi-*

62. 33 U.S.C. § 1503(c)(3) (1976).
63. Decision, *supra* note 43, at 45.

son, T. & S.F.R.R. "flexibility and adaptability of changing needs and patterns of transportation is an essential part of the office of a regulatory agency." We will attempt to avoid regulating ". . . the present and the future within the inflexible limits of yesterday," by devising a regulatory and enforcement mechanism, rather than fixing rigid conditions.

(e) We will seek to ensure that the applicant is both motivated and required to comply with the traditional obligations of a common carrier "clothed with public interest."[64]

Finally, the Decision reviews the four major areas of concern expressed in the DOJ and FTC Reports—discrimination to nonowners, capacity, rate regulation, and inland transportation—and indicates why the recommendations with respect to each area of concern were or were not accepted.

1. *Use by Nonowners*

The Decision expresses agreement that oil company owners of a deepwater port would have incentive to discourage the use of the port by nonowners by designing and operating the port in a fashion that favors owners. The Decision notes that despite this incentive, the shareholders of the port "must recognize that possession and control of the deepwater port brings with it certain obligations to furnish service to all shippers, even competitors of the shareholders."[65] To help assure that the port design and operation do not discriminate against nonowners, the Decision establishes the following license conditions, consistent with the recommendations in the DOJ and FTC Reports:

> In the license, we utilize the mechanism of review and approval of the Operations Manual to control the imposition of conditions of service by the licensee. DOT, and in particular, the Coast Guard, which will have primary responsibility for the Operations Manual, will consult and cooperate with the Department of Justice and the FTC on all matters of the Operations Manual which relate to conditions of service and limitations imposed on vessels calling and cargoes tendered.
>
> The proration policy of the port, applicable when cargoes tendered exceed capacity, shall be included in the Operations Manual and similarly reviewed. We also will conduct public hearings, as suggested by the FTC, if after examination of any proposed limitations, the FTC deems such hearings necessary to explore the reasonableness of such limitations.
>
> To provide guidance on the reasonableness of any conditions imposed by the licensee, and to be generally responsive to the particular recommendations of the Attorney General, we have included in the license specific requirements ensuring nondiscrimination in vessel handling, and acceptance of cargoes and storage segregations.

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64. *Id.* at 46 (footnotes omitted).
65. *Id.* at 47.

> We have made an explicit condition of the license a general prohibition against discrimination, prohibiting either a licensee or owner from discriminating against shippers or owners of oil in the facilities furnished, services rendered, or rates charged, so as to make available the remedies of the Deepwater Port Act for discriminatory behavior.[66]

Prior approval requirements such as these create tremendous uncertainty for potential owners because there have never been any deepwater ports. By the time the Operations Manual is ready for approval, the port owners will already have invested tens and perhaps hundreds of millions of dollars into the port. At that point in time, when the Department of Transportation can require that the Manual be modified in a certain fashion, the owners have little bargaining leverage, short of political pressure beyond the scope of the license process itself. On the other hand, if an offer of the license itself had to await approval of the operating details which will be in the Operating Manual, the cost of proceeding to the point where a license could be offered would be so high, given the risk that an offer might not be made, so as to discourage most or all potential investors. Thus, imposition of these prior approval requirements reflects the decision to require those approvals after, not before, the license is offered. As in many areas of government regulation, this decision is the result of a situation in which either the government must assume that private enterprise will act in the public interest (in which case there would be no prior approval requirements), or private enterprise must assume that the government officials will act responsibly (in which case prior approval would be denied only upon good cause)—and the government, with the "upper hand" (the licensing authority), elects to proceed along the latter course because responsible government is institutionally more likely in our society than publicly-minded private enterprise.

2. Capacity

The DOJ and FTC Reports indicate that the demand estimates presented by the applicants are conservative, and that oil company port owners have little incentive to expand, especially if the expansion is desired only by nonowners.[67] In response to these concerns, the Decision notes that three steps will be taken. The first step is simply that the port must be expanded at least as large as contemplated in the license application if shippers willing to make throughput commitments so desire. The second requirement is that "the Secretary can compel expansion of capacity an additional 25% in a situation where demand is evidenced by commitments of shippers for throughput, and he finds that expansion is technically practical, economically reasonable, financially feasible and environmentally

66. *Id.* at 48 (references to license articles omitted).
67. *Id.* app. B-18 (DOJ), C-3 (FTC).

sound."[68]

In conjunction with such a mandated expansion, the Decision notes that:

> In any action to compel expansion, the Secretary must observe the tenents of due process by affording opportunity for hearing, and will be bound by standards of reasonableness and consistency with regulatory principles. In view of the extra capacity which is possible in the design approach taken by LOOP, we do not forsee that this requirement will impose undue hardship.[69]

Finally, the Decision notes that the DOJ and FTC recommendations which are intended to induce expansion will be adopted as license conditions. The Decision indicates that:

> Proration policies will require review and approval of DOT, in like manner as the conditions of service. The FTC advises that effective proration policies can create incentives to expand (or at least reduce incentives to restrict the size of the Port).
>
> Any shareholder or group must be able to authorize the corporation to expand the facilities. As LOOP explains, additional shareholder action is not now required for expansion to the limit of the application, but without this provision in the license, shareholders holding, in the aggregate, more than 25% of the shares could block expansion.
>
> Preferential rights of shareholders to the shares of other owners, offered for sale, will be prohibited . . . .
>
> Shares must be made available at times of expansion, when new financing is required. The Attorney General has recommended that shares be available during the life of the project, on a continuous basis. We believe that such availability would diminish incentives for investment, in the early, higher risk stages of construction. Accordingly, we will require LOOP to hold ownership open until the closing of the initial financing, which will be for six months after the effective date of the license. We also will require . . . that ownership be reopened upon subsequent financing for expansion. This will give outside shippers an opportunity to join in the benefits (and risks) of new facilities, but minimize the potential dilution of profits arising out of the original investment risks.
>
> Shareholders must have the option to purchase additional shares to adjust ownership interests to conform to throughput percentages. The Attorney General recommends annual adjustments of ownership shares; the FTC does not specify a period (but prefers a short period) and LOOP has suggested five-year adjustments. We think that three-year intervals for adjustment of ownership shares, the interval selected by the LOOP shareholders for the initial share redistribution (after a two-year "start-up" period), should be the maximum interval, and we have so provided in [the license]. The concern of LOOP about the threat of future antitrust litigation on this point should be put to rest by the offer of a "Business Review Letter" by the Department of Justice.[70]

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68. *Id.* at 49.
69. *Id.* at 50 (footnotes omitted).
70. *Id.* at 50-51 (footnotes and references to license articles omitted).

As intended, these conditions have two advantages. They help reduce the incentive to owners to maintain their original throughput, as discussed above,[71] and they help to provide the authority and incentive for anyone who desires to obtain an expansion of the port. One disadvantage is that, unlike most other oil pipelines, the original owners have no control over who the subsequent owners may be. Perhaps a more fundamental disadvantage is that the imposition of conditions on the sale of shares requires federal oversight in relation to the internal corporate documents of the licensee, which is generally unprecedented except as to federally chartered entities such as banks.[72]

The extent to which these license conditions are necessary or desirable to achieve their intended purpose, and the effect of this detailed federal oversight, will be viewed with great interest by many. This type of federal "regulation" is a concept which may appear more frequently in years to come with respect to a variety of joint quasi-public projects that can benefit the nation but are too large to interest any significant number of non-federal public entities, or with respect to private projects that are too large for any private firm to undertake alone.

3. Rate Regulation

To keep the competitive advantage of the owner-shipper from being exacerbated by the potential 70% return on equity allowed by the Consent Decree,[73] both the DOJ and FTC Reports recommend that the Secretary exercise indirect control over port tariff rates by making determinations as to the reasonableness of the port rate of return.[74] In declining to accept this recommendation, the Decision notes:

> Since this problem is common to oil-company owned deepwater ports and oil-company pipelines, the solution should also be common. Any remedy imposed by DOT to control deepwater port rates ignores the larger problem of pipeline rates. The correct approach is broader, including pipelines as well as deepwater ports. As I read the Interstate Commerce Act, the ICC [now FERC] now has the authority to handle the rate issue in the manner that the Attorney General suggests that I do by imposing conditions. Thus, DOT will urge, by participation in regulatory proceedings, that the [FERC] reassess the methods used to compute the proper rate of return, and to give full consideration to the fact of ownership by principal customers in determining the reasonableness of the return itself. The Attorney General, no doubt, will join in such proceed-

In certain circumstances, the Antitrust Division of the Justice Department will "review proposed business conduct and state its enforcement intentions" in a business review letter in response to a written request describing the situation in question. 28 C.F.R. § 50.6 (1977).

71. *See* text accompanying *note* 52 *supra*.

72. For national banks, for example, *see* 12 U.S.C. §§ 21-42 (1976) (organization and other general matters); *id.* §§ 51-67 (capital, stock, and stockholders); and *id.* §§ 71-78 (directors).

73. *See* text accompanying notes 16-17 *supra*.

74. Decision, *supra* note 43, app. B-21 (DOJ), C-2 (FTC).

ings. If the [FERC] considers itself bound by statute or precedent, DOT will seek remedial legislation, and the Attorney General can join in such request. A solution developed for oil-company owned petroleum pipelines would also be applicable to the LOOP project.[75]

The argument that the Department will not interfere with the establishment of rates because it is within the domain of the FERC could, of course, be applied with equal vigor to the conditions of service, over which the Department has retained authority in the license to exercise control. Although there is sound basis for exercise of control by the Department over certain matters of port design because the FERC has no statutory authority to do so, nothing in the Deepwater Port Act or in the Interstate Commerce Act would support including conditions of service within the Department's control while excluding ratemaking. Apparently, the basis for the distinction is that the conditions of service are essential to assure that the ports are operated in the manner contemplated by Congress in creating the Act, especially in assuring that nonowners have access to the port. Thus, waiting to see if the FERC will impose such conditions after experience has shown a need for them, rather than imposing them in advance in the license, could jeopardize the viability of the entire deepwater port concept. With respect to rates, on the other hand, there is no reason to believe that nonowners would not at least have access to the ports, as contemplated by Congress, even if the ports operated under the existing rate regulation formula. In this sense, it is apparent that the decision to retain authority in the license was based in some instances on the need for safeguards where the ICC has no authority under the Interstate Commerce Act, and was based in other instances on the need for safeguards where the ICC has the authority but simply has not acted. This dichotomy illustrates that two policy guidelines enumerated in the Decision can be inconsistent to a certain extent, because in attempting to "fill the gaps in the regulatory framework in order to prevent discrimination and anticompetitive practices," it is not always possible to "avoid exercising jurisdiction that duplicates that of other agencies."[76]

4. *Inland Transportation*

In response to the concern noted in the DOJ and FTC Reports that the ability of nonowners to use the port would be meaningless unless they could be assured of receiving equally nondiscriminatory treatment in the connecting downstream pipelines, the Decision notes:

The Secretary has a special obligation to ensure that the oil imported through the deepwater port by a non-owner can be delivered to a common carrier pipeline for further transportation without discrimination. Consequently, DOT will exercise such regulatory responsibilities as are necessary to ensure that ship-

75. *Id.* at 53.
76. *Id.* at 46.

> pers through the port have access to common carrier pipelines and that the policies applicable to the port are not frustrated downstream.[77]

This obligation will be fulfilled in the following manner:

> The license . . . provides for review of joint arrangements by DOT, including proration policies, and [as] an additional incentive, we have included a requirement for storage until accepted by connecting carriers. [The license] also requires provision of facilities for delivery to connecting carriers, which are not now required by the Interstate Commerce Act, but are clearly part of the duties of a common carrier of this kind.[78]

The implementing provision in the license divides the connecting pipelines into three categories—existing pipelines owned or controlled by the port owners, new pipelines owned or controlled by the port owners, and pipelines not owned or controlled by the port owners—and specifies requirements which vary in accordance with the ability of the owners to implement them, which in turn varies with the degree of ownership of the port owners over such pipelines.[79]

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77. *Id.* at 55.

78. *Id.* at 56 (references to license articles omitted).

79. Article 16 of the LOOP license provides:

> The License shall establish with such common carrier pipelines as are owned or controlled by the Owners of the Licensee and their affiliates, or any of them, fair and adequate arrangements as may be reasonably required for the transportation of oil from the Port Complex to inland points served by such pipelines. Any requirements in such arrangements for minimum tender, shipment specification, or other conditions of shipment shall not be more restrictive than the conditions of shipment for the Port Complex, except such requirements that may be justified by pre-existing physical limitations of connecting facilities which cannot be readily corrected without substantial investment. The arrangements shall include a requirement that policies and practices concerning acceptance of cargoes when tenders exceed capacity shall be consistent with the policies and practices of the Port Complex. If any such common carrier pipeline fails or refuses to accept a shipment of any part thereof when properly tendered, the Licensee shall store such shipment or part without penalty until it shall have been accepted by such carrier.
>
> Any pipeline constructed or extended after the date of issuance hereof, owned or controlled by the Owners or affiliates, or any of them, which will or reasonably could provide a connection between the Port Complex and any common carrier pipeline, shall (a) be owned by a single entity which shall operate such pipeline as a common carrier under the Interstate Commerce Act; (b) provide for terminal tankage on a common warehouse basis; and (c) participate in joint arrangements and conduct operations in a manner consistent with the provisions of the preceding paragraph.
>
> The Licensee shall use its best efforts to establish similar arrangements with common carrier pipelines, not owned or controlled by Owners or affiliates, which will or reasonably could provide a connection with the Port Complex.
>
> As used in this Article, the term "ownership" shall include, but not be limited to, ownership of any corporation owning pipeline facilities and any joint interest in pipeline facilities. The term "control" shall mean actual or legal control, contractual control, control by ownership of the majority of the voting stock in a corporation owning pipeline facilities or ownership of the majority of joint interests in pipeline facilities. The term "affiliate" shall include any corporation or business entity, controlled by, controlling, or under common control with the Licensee or any Owner.

Id. app. A-10 to A-11.

Thus, the Decision notes that although the Interstate Commerce Act and the antitrust laws are the most suitable vehicles by which the basic abuses of shipper-ownership are to be cured, the Department will exercise oversight in relation to joint arrangements between the port and connecting downstream pipelines. The unavoidable difficulty in this approach, of course, is the impossibility of specifying in advance the connecting downstream pipelines to which this oversight could or should apply. In theory, this could extend the Department's reach to a large portion of the nation's total oil pipeline system. In practice, the Department's reach via this provision would probably remain within the immediate geographical area of the port, given the strong suggestions in the Decision of a desire to avoid the use of a deepwater port license to involve the Department in oil pipeline economic regulation generally.[80]

One recommendation not accepted in the Decision is that each shareholder, rather than only the licensee, be liable to fulfill the joint tariff conditions of the license.[81] The license does impose individual shareholder liability for certain matters,[82] and the rationale for rejecting the recommendation in relation to joint tariffs is not clear. On one hand, direct shareholder liability for nondiscriminatory license conditions such as nondiscriminatory joint tariffs may not be effective because each shareholder could plead that it did not individually have complete control over the port's end of a joint tariff. On the other hand, the absence of direct shareholder liability may eliminate the Department's ability to oversee joint tariffs because the port as an entity had no control over the other end of a joint tariff. Thus, both shareholder and licensee responsibility for joint tariffs would be necessary for effective enforcement.

C. Port Ownership by Non-Shippers

As noted above,[83] the Act establishes a priority of ownership for deepwater ports—first to adjacent coastal states, second to entities other than oil companies, and finally, to oil companies. Nonetheless, the Decision mentions only the possibility of port ownership partially or entirely by oil companies shipping their own oil. The Decision is probably silent about the ownership by non-shippers because no non-shippers joined in the license applications.[84] However, it is possible that the port could in time become an attractive investment to one of the relatively few independent oil pipeline companies or to other types of public and private investors. As a general matter, the presence of other investors would help to reduce the

80. *Id.* at 55.
81. *See* note 79 *supra*.
82. *See* Decision, *supra* note 43, app. A-7 to A-8 (Article II: Nondiscrimination).
83. *See* text accompanying note 36 *supra*.
84. *See* Decision, *supra* note 43, at 3.

possibility of anticompetitive behavior because a vertically integrated owner may have different motives for a port than an investor whose sole purpose is to reap the best return on the port investment itself. Without delving into the theoretical possibilities which may flow from partial or entire ownership by non-shippers, it is noted at this point that such ownership of the ports could fundamentally affect the basic assumptions underlying this analysis.

V. Conclusion

In the process of analyzing the two deepwater port applications submitted by the oil companies, the Department of Justice and the Federal Trade Commission have made clear their considerable suspicion as to the motives of the oil company applicants. Those agencies are, of course, acutely aware of the difficulty of relying solely upon the antitrust laws to remedy problems after they have developed; thus, they recommended the implementation of an ounce of prevention at the outset as being considerably more desirable than a pound of cure.

The Secretary of Transportation, on the other hand, while acknowledging the concerns of the antitrust experts, added the countervailing concern that an overabundance of prospective safeguards in relation to perceived potential abuses which have not yet ripened and may never ripen could discourage potential owners from constructing a port. Thus, the Secretary, who is required by the Act to have a broader view of the problem than merely attempting to curtail anticompetitive practices within the oil industry, noted that some of the preventive measures proposed by the DOJ and FTC Reports were aimed at problems which are far broader in scope than just the deepwater ports. To that end, the Secretary refused to jeopardize the deepwater ports by allowing them to be used by the antitrust agencies to cure a much broader problem, the responsibility for which rests with another agency. Moreover, there are inherent social and economic inefficiencies in attempting to solve broader problems with remedies which are aimed in a piecemeal or patchwork fashion at individual narrow aspects of the broader problems.

Most of the prospective safeguards recommended in the DOJ and FTC Reports were incorporated into the licenses. Only time will tell whether those safeguards will reduce the potential for harm, or merely shift an undiminished burden from enforcement after-the-fact to policing during-the-fact.

Many elements in the equation are as yet uncertain—oil demand, oil supply, oil pipeline rate regulations, and the number of deepwater ports, to name a few—and it remains to be seen how these elements will affect the ultimate outcome. As the situation progresses, the deepwater ports will be viewed with avid interest by many—the Department itself, the antitrust agencies, several other government agencies, the oil industry, antitrust lawyers everywhere, and the American consumer who, if all goes well, will be the ultimate beneficiary of the ports.