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FEDERAL TRADE COMMISSION ANNOUNCES RECORD US$5.68 MILLION FINE FOR GUN-JUMPING VIOLATIONS IN ACQUISITION OF OIL COMPANY

On January 7, 2025, the U.S. Department of Justice ("**DOJ**") and U.S. Federal Trade Commission ("**FTC**") announced that three U.S. crude oil producers had agreed to settle allegations of "gun-jumping" by paying US$5.68 million in penalties, the largest gun-jumping fine in U.S. history. According to the agencies' allegations,[1] XCL Resources and Verdun Oil Company, upon reaching an agreement to purchase EP Energy, took over EP's "key ordinary-course functions" almost immediately after signing, thereby unlawfully assuming beneficial ownership of the business before the expiration of the waiting period under Section 7A of the Clayton Act, 15 U.S.C. §18A, commonly known as the Hart-Scott-Rodino Act or "HSR" Act. Importantly, the complaint states that "[t]his was no mere technical violation; the Defendants' conduct effectively allowed one competitor to acquire beneficial ownership . . . before the transaction closed."

This enforcement action is the U.S. antitrust agencies' second in five months against gun-jumping violations and follows a settlement announced in August 2024 pursuant to which entertainment venue services company Legends Hospitality agreed with the DOJ to pay a US$3.5 million penalty for gun-jumping conduct related to its proposed acquisition of ASM Global. Prior to that case, the next most recent gun-jumping penalty in the U.S. was issued during the last week of the Obama administration in January 2017.

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1 The FTC referred the matter to the U.S. Department of Justice ("DOJ"), who filed the complaint and proposed settlement.

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KEY TAKEAWAYS

- Although gun-jumping enforcement actions have been relatively infrequent in the U.S. in recent years, compliance with prohibitions against gun-jumping remains an important consideration for transactions that are subject to review under the HSR Act. Parties should remember that the acquirer(s) and target(s) must continue to remain separate, independent companies and continue to compete (if applicable) until the closing of the transaction, including by establishing adequate safeguards to prevent any inappropriate exchanges of competitively sensitive information.
- Failure to comply with gun-jumping laws can be costly, both in the U.S. and globally. The maximum fine in the U.S. is currently set at US$51,744 per day in violation, an amount that is adjusted annually, while the maximum fine in the European Union is based on the offending party's revenue (up to 10% of global group turnover), potentially leading to enormous penalties.
- Merging parties should note that inappropriate pre-closing activities can not only trigger a gun-jumping violation but can also violate the Sherman Act, which is enforced both civilly and criminally and applies even where a transaction does not require notification under the HSR Act. While the complaint in this case did not include a claim under the Sherman Act, the type of conduct it alleged, including coordination on pricing, agreements to restrict production, and exchanges of competitively sensitive information, are hallmarks of a Sherman Act violation.
- The bipartisan support for the settlement among the FTC Commissioners suggests that U.S. agencies' appetite for enforcement against gun-jumping violations should not necessarily be expected to wane during the incoming Trump administration. The FTC vote to accept the settlement was 4-0-1 in favor, with Chair-designate Andrew Ferguson and the Democratic Commissioners voting in favor and Commissioner Melissa Holyoak recused.

LEGAL BACKGROUND

The HSR Act requires parties to certain transactions to notify the antitrust agencies by filing pre-merger notification report forms (often referred to as "**HSR filings**") and to observe a designated waiting period before completing their transaction to allow the DOJ and FTC time to consider whether the transaction may raise substantive antitrust concerns. Under the HSR Act, before the period of antitrust review has expired or otherwise been terminated, the parties may neither formally close their transaction nor engage in "gun-jumping," which occurs through a transfer of beneficial ownership or control of the target to the acquirer(s) before the parties have obtained regulatory clearance. Conduct that can constitute gun-jumping under the HSR Act includes premature integration of operations and impermissible exchanges of information.

GUN-JUMPING CONDUCT

On July 26, 2021, XCL and Verdun (the "**Buyers**") signed an agreement to acquire EP for approximately US$1.4 billion, a transaction subject to the HSR Act. The parties thereafter notified the DOJ and FTC of their transaction by submitting the necessary HSR filings. Because the FTC had questions as to potential substantive antitrust concerns with the transaction, the FTC issued the parties requests for additional information and documentary material ("**Second Reques**t"). The HSR Act's waiting period was thereby extended until the parties substantially complied with the Second Requests or the FTC otherwise terminated the waiting period. From the day of signing, however, according to the complaint, the parties engaged in various categories of unlawful conduct. The complaint describes the case as "a straightforward example of unlawful gun jumping where two companies agree to coordinate their activities before a transaction is permitted to close under the HSR Act." The alleged unlawful conduct included:

1. *The Buyers required EP to change its business plans and day-to-day operations prior to the expiration of the waiting period.*

   The complaint alleges that on the same day that the purchase agreement was signed, XCL required EP to immediately suspend its oil well drilling and planning activities in Utah, where XCL was also active, so that XCL "could take over the management of EP's development plans and designs moving forward." This suspension allegedly led to "production shortfalls" for EP in the following months. The complaint also alleges that, one week after signing, XCL began taking over EP's site design plans and vendor selection process and did not allow EP to resume its prior activities until August 17, 2021, "after the Defendants realized that the FTC would investigate the transaction." The complaint alleges that an indemnification provision in the purchase agreement, under which the Buyers assumed the financial risk and liabilities for the seller's business activity, was motivated by the Buyers' anticipation that the restrictions on EP's activities "would result in crude supply shortages for EP and its customers in the ensuing months and could cause EP to breach [its] existing obligations." The complaint characterized this provision as "further evidence of gun-jumping."

2. *The Buyers required that EP receive buyer approval for certain ordinary-course expenditures and activities.*

   Under the parties' agreement, according to the complaint, buyer approval was required for any expenditure above US$250,000 (which the complaint describes as "a relatively low threshold in the crude development and production business") without any exception for ordinary-course transactions. The complaint also alleges that EP submitted approval requests to the Buyers for expenditures "well below" that threshold. In addition, as alleged, the agreement required EP to obtain approval before hiring field-level employees or purchasing supplies for its drilling operations.

3. *The Parties coordinated their ordinary-course activities with respect to EP's customers.*

   The complaint alleges that XCL "held itself out" as the coordinator for EP's customer-facing operations in Utah, resulting in EP's customers contacting

XCL directly regarding EP's contractual obligations, volume projections, and delivery schedules.

In Texas, where both Verdun and EP operate, Verdun allegedly noted that some of EP's customer contracts included "below-market prices" and responded by directing EP to raise them. Verdun also allegedly used information gleaned from the Virtual Data Room ("VDR") created for the deal to "suggest changes to EP's customer pricing." EP "responded and continued to consult with" Verdun throughout customer negotiations taking place during the HSR waiting period.

4. *The Parties exchanged competitively sensitive information without appropriate safeguards.*

As alleged, the Buyers asked for and received "virtually real-time information about EP's operations, output, and sales" in addition to "seemingly any other aspect of EP's business or operations of interest" upon the Buyers' request. The complaint alleges that this information was actively used for anticompetitive purposes, given that Verdun had used information gathered from the VDR to inform pricing and contractual terms with EP's customers, at a time when Verdun and EP were still active competitors.

The complaint also chided EP for taking "no meaningful steps to resist" the Buyers' requests and making "no effort . . . to limit the access to, or use of, EP's competitively sensitive information." The VDR allegedly "lacked appropriate safeguards on access and use" despite being used "ostensibly for the legitimate purpose of conducting due diligence on the proposed transaction," and the information provided by EP was allegedly accessed by "XCL and Verdun businesspeople responsible for sales, marketing, and operations."

Although the HSR Act provides for fines up to approximately US$4.86 million per party given the length of the violation, the DOJ agreed to a lower penalty in part given that the parties agreed to resolve the matter through a consent decree in lieu of litigation. Under the settlement, the Buyers, jointly and severally, and EP each are required to pay approximately US$2.84 million.

CONCLUSION

The agencies' action serves as a strong reminder to merging parties to carefully negotiate the terms of their merger agreement, including interim operating covenants, to ensure that the target is permitted to continue to operate independently in its ordinary course of business. During the diligence period and thereafter, merging parties, particularly competitors, must follow safeguards regarding the sharing of competitively sensitive information. Finally and critically, for transactions subject to the HSR Act, acquirers must be careful not to engage in conduct that could be viewed as taking beneficial ownership or control of the target.

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