James Rose

Professor Wertheimer

November 16, 2023

American Legal History

The Reach of Oil

In 1859, Edwin Drake struck oil in Titusville, Pennsylvania, creating the United States' first oil well. Drake's discovery lit the match for one of the United States' largest industries. In the years that followed, many small oil firms were founded and began to supply the nation's growing demand for petroleum products. John D. Rockefeller created Standard Oil in 1864 and, through innovative business practices, grew the company into one of the most powerful and successful firms in America's history. Although Rockefeller's company was split up after an antitrust suit in 1911, the fragments of Standard Oil are still the major players in the oil industry. As the United States' demand for gasoline increased throughout the 20th century, a lack of supply began to threaten the country's national security. In order to meet the demand for oil, the Federal Government weakened antitrust enforcement in the oil industry. This policy decision led to large amounts of consolidation of oil companies, which culminated in the 1999 merger between two ex-Standard Oil companies, Exxon and Mobil, into ExxonMobil. The United States' dependence on gasoline has created a complex relationship between oil suppliers and the government, which can be interpreted through the law. Wars have been fought, treaties signed, and billions in profit have been made, all due to the petroleum industry. Social pressures, when widely supported, tend to force the government to regulate the oil industry. However, the oil supply, as it relates to national security, causes the government to weaken its regulation of large oil companies. Through an examination of the legal history of ExxonMobil, it is clear that the relationship between the law and ExxonMobil is intrinsically linked to global politics, the state of the nation, and the public's opinions on the industry.

John D. Rockefeller used innovative business practices to rise above [and crush!] competition and stretch Standard Oil's reach nationwide. In the early days of the oil industry, many small firms competed on all production levels. This caused volatile prices in refining, transporting, and selling as each firm attempted to undercut the other. Rockefeller, eager to bring stability to market prices, expanded Standard Oil's control to encompass the whole production process. This allowed his company to undercut its competitors' prices. By the 1880s, Standard Oil "sold nearly 90 percent of all the oil produced in America." The oil industry, as one of America's first national industries of the Gilded Age, faced very little government regulation, which left no barriers for Standard Oil to build its monopoly. During the 19^{th} century, most state and federal judges, as well as politicians, agreed with laissez-faire economic principles, so they did little to regulate industry. As the Industrial Revolution fueled the growth of big business, the negative effects of monopolies like Standard Oil's began to challenge the benefits of laissez-faire economics.

State officials, rather than federal, were the first to attempt antitrust challenges against Standard Oil. However, such as in the case of Ohio's attempts, state courts often fell short of breaking Standard's market control. Standard Oil was founded in 1870 in Cleveland, Ohio; however, by the late 19^{th} century, the company's headquarters had moved to New York to better control its operations. This presented a challenge to Standard executives because if they continued to control Standard Ohio's operations from New York, they would violate the company's Ohio charter. In order to subvert the charter, the company created a complicated trust agreement that gave Standard Oil Board of Trustees in New York full control over Standard Oil of Ohio.

Realizing this arrangement violated Ohio regulations, the Ohio Attorney General, David Watson, filed for *quo warranto* (repeal of the company's charter) in Ohio court. This decision, although not politically popular, was supported by the working class of Ohio as they believed that Standard's control had grown too large and were well aware of Standard Oil's history of predatory and malicious business practices. Ultimately the State Supreme Court ruled that Standard had violated their charter, but the decision did not adequately force them to cease operation in Ohio. This decision was in line with previous state court antitrust decisions in which courts ruled against monopolies, however, did not properly dissolve them. After slightly restructuring the corporation, Standard continued to operate in Ohio, continuing their monopoly.

Texas's enforcement of its antitrust laws better protected the state's oil fields from the Standard Oil monopolies during the early 20th century than previous state attempts. In 1883, the Texas state government passed into law one of the first antitrust acts of the nation. Farmers broadly supported this act due to predatory pricing at the hands of railroad operators. Still, the act applied to the growing petroleum industry in Texas. In 1901, the Spindletop oil fields were discovered, and Standard Oil, along with its affiliate companies, began to invest there. However, the 1883 Act outlawed vertically integrated companies, like Standard, from operating in Texas. By the early 20th century, public opinion had broadly shifted against oil monopiles, especially Standard Oil. Journalists such as Ida Tarbell and others successfully turned Texans' opinions against Standard Oil. The State responded to anti-oil sentiment by prosecuting one of Standard Oil's affiliate companies for breaching the 1883 Antitrust Act. In *Water-Pierce Oil Company v. State of Texas*, 1909, on appeal, the Supreme Court of the United States upheld the constitutionality of Texas's antitrust laws. The court protected Texas' right to regulate intrastate commerce—which, in this case, was regulating monopolies in the state—and allowed Texas to fine and revoke Water-Pierce Co.'s charter. Public opposition to Standard Oil provided the state government with political capital to attack Standard Oil's monopoly in the state.

In 1890, due to growing anti-industry sentiment, Congress passed the Sherman Antitrust Act, which made it illegal to run a trust or monopoly in "restraint of trade or commerce." During the first two decades of the Sherman Act's life, there was much public support against oil monopolies. However, business-aligned presidents Cleveland and McKinley did not instruct their Justice Departments to prosecute Standard Oil. During this time, antitrust suits against Standard Oil were carried out on a state-by-state basis, but the complexity and political power of the company made it nearly impossible for states to rid their markets of Standard control. Due to Standard's large control over the entire nation, antitrust prosecutions would only be successful if they were brought by the Federal Government.

The dissolution of Standard Oil due to the Supreme Court's 1911 decision, while significant, did not effectively allow for free market competition to replace Standard's monopoly. In 1907, Theodore Roosevelt's Attorney General brought a suit against Standard Oil of New Jersey for breaching the Sherman Antitrust Act. In *Standard Oil Co. of New Jersey v. United States*, the government argued that S.O. of New Jersey should no longer be able to have a controlling interest in other oil companies. Therefore, the court would be taking away Standard Oil's ability to control its nationwide monopoly. Instead, Standard would be divided into small regional companies. Evidence of how Standard Oil had worked around previous state courts' decisions by using "subterfuge and shams," encouraged the court to break up the trust once and for all. However, the system the government used to divide the Standard Oil companies maintained the restrictive market operations and, in effect, its monopoly. The court divided the companies along "corporate rather than functional lines." The thirty-four new companies the court ordered were not designed to compete against each other; instead, they were highly reliant on each other's goods and services. This incentivized consolidation between the new companies, which would take place throughout the following century of the industry, creating an oligopoly in the petroleum industry. Additionally, the justices failed to successfully address the issues of stock ownership in a way that would limit monopolistic control of the new oil companies. The dissolution decree divided the stock in the new oil companies proportionally among S.O. of N.J. stockholders. This allowed the majority stockholders of Standard New Jersey to legally continue their monopolistic practices as majority stockholders in the new companies. The antitrust suit against Standard Oil was hugely popular amongst the public. The seemingly pro-competition decision won praise and made the public believe the federal government was finally standing up to the widely loathed trusts. However, through the shield of complex financial and legal language, the 1911 decision continued to allow the oil industry to be dominated by a few firms at the expense of the public.

The Federal Government also supported Standard Oil’s industry dominance internationally through law. In the late 19th and into the 20th centuries, Standard Oil affiliates controlled vast amounts of Mexican oil. During the early 20th century, the Mexican revolution against the previous Porfirio Diaz government threatened Standard Oil's ownership of Mexican subsoil rights. The Diaz administration welcomed foreign investment and control of Mexican resources; however, the new government was in favor of nationalizing the oil fields. This threatened Standard Oil's control, so they called on the Federal government to protect their interests. In response, the Coolidge administration and President Obregón of Mexico signed the Bucarelí Treaty of 1923, which protected US-owned oil fields from Mexican nationalization attempts (in exchange for U.S. diplomatic recognition of Obregón's government).

Although previously, the US Government had supported the protection of US enterprises in Mexico, their policy incentives shifted due to World War II. During the lead-up to WWII, under the Roosevelt administration, US foreign policy shifted in an attempt to create better relations among foreign nations. If the United States were to enter into the world war, it would depend heavily on Latin American nations for raw materials and support. In 1937, the Mexican government nationalized American-owned oil fields. However, due to changes in diplomacy goals, the

Roosevelt administration did not attempt to sign a treaty with the Mexican government protecting American oil interests, as the United States had previously done during the 1920s. This change in United States policy shows how the US government uses laws regarding the oil industry to strengthen national security.

After emerging from WWII as one of two dominant world powers, the United States quickly became embroiled in the Cold War, an ideological battle between capitalism and communism. During the Cold War, the importance of the oil industry on national security was clear to lawmakers. In 1947, Congress passed the National Security Act, which, among other things, created the National Security Resources Board. The board would report on and manage the nation's oil supply and suggest energy ventures the US should support.

During the Cold War, the United States government supported Exxon and other oil producers in the Middle East because of national security concerns over the supply of oil. In 1954, after a pro-western government took power in Iran, seven of the largest Western oil companies formed a consortium to begin producing Iranian oil. The agreement divided stock equally amongst S.O. of New Jersey (Exxon), S.O. of California, S.O. of New York (Mobil), Gulf Oil, and Royal Dutch Shell. The Truman administration supported this plan because it secured the United States as a consumer of Iranian oil and kept the Soviet Union from investing in increasing ties with Iran. However, the Iranian oil project violated Federal laws regulating international trade monopolies, which had previously been stringently enforced by the courts. President Truman found the national security benefits of having American oil companies in the Middle East outweighed the constraint on free trade that the oil cartel created. Therefore, the Truman and later Eisenhower administrations repeatedly delayed and weakened antitrust suits against American producers of Iranian oil. During the Cold War, the executive branch influenced the enforcement of the law in order to strengthen the supply of oil to the United States and expand its control of the developing world.

During the 1970s and 60s, public demands for stricter environmental regulations forced the Federal government to act. In 1959, Rachel Carlson published *Silent Spring,* which alerted the public to the harm industrialization had done to the environment. In the following two decades, the government passed stricter environmental regulations in response to voters' demands. During the 70s, Congress created the Environmental Protection Agency (EPA) and the Occupational Safety and Health Administration (OSHA). Contrary to the antitrust disputes at the beginning of the century, Congress and the Judicial Branch were now positioned to strictly enforce their statutes and precedents due to the growth of the Federal Government. After the 1989 Exxon Valdez oil spill in Alaska, Congress passed the 1990 Oil Pollution Act. This act created stricter tanker and oil transportation standards that would lessen the possibility of future oil spills. Criminal and civil suits were also brought against Exxon (S.O. of N.J. rebranded as Exxon in 1972) after the Valdez spill. In *Eyak Native Village v. Exxon Corp* 1994, the Federal Courts levied heavy fines against Exxon after finding the corporation liable for environmental damages due to the spill. To date, Exxon has paid millions in fines in cooperation with court orders and settlements due to increased environmental regulations during the late 20th century. Increased federal prosecution and regulation have caused Exxon to reconsider and adjust the environmental impact of its business practices. Public support and the rise of the regulatory state allowed the government to prosecute Exxon for environmental damages the company has committed.

The United States' loss of control over the global oil supply caused the government to weaken antitrust enforcement during the ExxonMobil merger. In the late 1960s and early 70s, Middle Eastern oil-producing countries renegotiated contracts with major US oil companies, including Exxon, Mobil, and others. The new agreements nationalized oil, which drastically limited the United States' control over the oil market. The United States relied on Middle Eastern oil because of large domestic demand. In 1973, Middle Eastern countries and Venezuela, organized through OPEC, began an oil embargo against the US. The embargo led to fuel shortages, which drastically hurt the US economy. In hopes of recapturing control over the global supply of oil, the US government allowed for major consolidation among American oil corporations, including the ExxonMobil merger. The Federal Trade Commission required Exxon and Mobil to divest some of their assets upon merging. However, the divestitures did not allow for proper competition in the oil industry to continue. In testimony to Congress, the head of the FTC's Board of Competition stated that " 'moderate concentration' in any industry can have substantial adverse effects on competition." The ExxonMobil merger allowed the five largest American oil companies to control fifty-five percent of the market for United States oil sales but was still allowed by the FTC. The government hoped that, through consolidation, ExxonMobil would be able to fund research and extraction of oil that would otherwise not be achievable as two competing firms. This would alleviate the

United States' dependence on foreign oil and recontinue the country's dominance in the global oil market. Due to fears of oil supply shortages, the United States government allowed the ExxonMobil merger to be carried out with limited antitrust protections.

In its early stages, Standard Oil's growth was fueled by the lack of antitrust regulations. Standard Oil was also able to take advantage of the difficulties the government and law had adjusting to the new industrial economy. Both State and Federal antitrust decisions were not strong enough to successfully create balanced competition in the oil market. As oil companies became multinational endeavors, the government began to use them as tools for their foreign and domestic policy. Often, this resulted in fewer restraints on oil companies' control of the market and antitrust enforcement. As the largest American oil company, ExxonMobil has overall benefited greatly from these policy decisions. Social calls for stricter regulation in the oil industry have, at times, led to change. In the 1800s, reformers passed antitrust acts at both the state and federal levels. During the later decades of the 20th century, increased environmental restrictions forced the industry to adjust to the new standards. However, many climate activists claim that more regulations will need to be passed in order to effectively reign in the industry. ExxonMobil has continued to lead the charge in consolidation in the oil industry. In October of 2023, the company announced its plan to buy Pioneer Energy for 60 billion dollars. Much like its predecessor, Standard Oil, ExxonMobil has used the government and law to continue its market dominance in the oil industry.