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Purchase Agreement Drafting and Interim Compliance Considerations Following the FTC's Record-Breaking HSR Penalty for Gun-Jumping

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In connection with a recent civil antitrust action pursued by the United States of America against XCL Resources Holdings, LLC (XCL), XCL's subsidiary, Verdun Oil Company II, LLC (Verdun) and EP Energy LLC ("EP" and together with XCL and Verdun, the "Defendants,"), the Defendants have agreed to a record-breaking \$5.6 million settlement stemming from allegations that they violated the Hart-Scott-Rodino Antitrust Improvements Act of 1976 (the HSR Act) by engaging in "gun-jumping" with respect to actions taken during the interim period between the signing of their Membership Interest Purchase Agreement on July 26, 2021 (the Purchase Agreement), and the closing of the transaction. Gun-jumping refers to activities by the parties to a proposed transaction that violate the waiting period obligations of the HSR Act by integrating the parties' businesses or otherwise coordinating their commercial behavior in a way that effectively transfers "beneficial ownership" of the target company before the end of the waiting period. This case highlights the dangers of "gun-jumping" under the HSR Act and, notably, involved the oil and gas industry – an industry that historically has not drawn much attention from the Federal Trade Commission (the FTC) and the Department of Justice (the DOJ), which are jointly responsible for enforcing U.S. antitrust laws.

The acquisition contemplated by the Purchase Agreement, under which Verdun agreed to acquire EP and its crude oil production operations in the Uinta Basin area of Utah and the Eagle Ford area of Texas for approximately \$1.4 billion, triggered the HSR Act's notification and waiting period requirements, and ultimately resulted in an investigation by the FTC into the expected competitive consequences of the acquisition on development and production in the Uinta Basin. In the course of its investigation, the FTC became aware of actions by the Defendants that constituted "gun-jumping" under the HSR Act. Ultimately, the DOJ filed a complaint on January 7, 2025 (the Complaint), alleging that from the execution of the Purchase Agreement, the Defendants improperly engaged in operational and decision-making control over significant aspects of EP's day-to-day business operations. The Complaint sets forth several specific examples of conduct that the DOJ alleges violated the HSR Act and offers valuable guidance to parties contemplating a transaction subject to the HSR Act.

Alleged HSR Act Violations

The Complaint alleges that Verdun and XCL effectively gained "beneficial ownership" of EP's business in the following manner:

- Approval of Operations and Expenditures: The Purchase Agreement provided Verdun and XCL approval rights in connection with EP's ongoing and planned crude oil development and production activities, ranging from approval for well-drilling activities to the purchasing of supplies and hiring of field-level contractors. While the Purchase

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Agreement did provide an exception to such approval for operations that were otherwise expressly permitted pursuant to the terms of the Purchase Agreement, the interim covenants did not contain an exception for ordinary course activities. In addition, EP was restricted from proposing, agreeing to or commencing any individual operations anticipated to result in expenditures in excess of \$250,000. Further, the Complaint alleges that in practice, EP submitted ordinary-course expenditures to Verdun and XCL for approval that were below the \$250,000 threshold. Verdun and XCL agreed under the Purchase Agreement to accept all liability resulting from their failure to approve any operational acts, which the Complaint alleges indicates Verdun's and XCL's anticipation of restricting EP's operational activities.

- Changes to Operations; Temporary Shutdown: Upon execution of the Purchase Agreement, XCL immediately halted EP's planned well-drilling activities so that, as the Complaint alleges, XCL could assume control over EP's developmental plans and designs. In connection with this control over operational planning, the Complaint alleges that Verdun and XCL made changes to EP's drilling and site design plans and that EP employees were reporting to XCL team members as they led the development projects. Importantly, the Complaint notes that the temporary shutdown of EP's operations caused EP to experience crude oil shortages (an outcome anticipated by the Purchase Agreement, which provided that XCL and Verdun would cover all costs associated with such supply deficits), during a period when the U.S. was already experiencing substantial shortages and rising crude oil prices.
- Directing Customer Commitments and Relationships: During EP's supply shortage resulting from the shutdown, XCL coordinated with EP regarding the ongoing fulfillment of EP's customer contracts, an effort which involved XCL covering EP's customer commitments either from XCL's own supplies or through third-party purchases by XCL. XCL also directed EP with respect to terms under future EP contracts by suggesting and approving customer pricing during ongoing negotiations between EP and its customers. Specifically, Verdun and EP worked together in negotiations with certain EP customers, and EP complied with Verdun's directive to raise prices for those customers for the upcoming contracting period. The Complaint further alleges that XCL engaged directly with EP's customers to discuss supply and delivery commitments and that during these communications, XCL held itself out to EP's customers as being responsible for coordinating EP's obligations in the Uinta Basin. In some cases, EP's customers began contacting XCL directly regarding volumes and deliveries under the EP contracts.
- Receipt of Confidential Information: Verdun and XCL requested, and received, competitively sensitive information regarding EP's operations in Utah and Texas that the Complaint alleges went beyond that required for transactional due diligence and had no legitimate business purpose. In connection with the receipt of this confidential information, neither EP nor Verdun or XCL took steps to limit access to the information to specific employees and the information was disseminated outside of the due diligence data room that the Defendants had in place. The Complaint alleges that EP delivered

daily and weekly updates to Verdun and XCL, such that they essentially had real-time information with respect to EP's operations.

The HSR waiting period for the transaction ran from July 26, 2021, through March 25, 2022. The alleged conduct occurred during this time, until the Purchase Agreement was amended on October 27, 2021 to allow EP to operate independently and resume ordinary-course development activities.

Future Drafting and Interim Compliance Considerations

The action pursued by the FTC and DOJ and the resulting settlement agreed to by the Defendants provides parties in the energy space with a stark reminder to refrain from actions that could constitute gun-jumping. In addition, purchase agreements should include the necessary safeguards to allow the parties to conduct business operations during the waiting period without a transfer of the indicia of beneficial ownership. The key is that the target entity should be able to continue operating in the ordinary course without obtaining a consent from the buyer for such activities. To that end, below are key takeaways to consider in drafting purchase agreements where the parties are required to observe the HSR Act waiting period:

- Approval Rights for On-Going, Planned and Ordinary-Course Operations: Interim operating covenants in purchase agreements should make clear that purchaser approval is not needed for certain on-going and planned development and production activities, including operations that are in the ordinary course of the seller's business. While the Defendants' Purchase Agreement did provide an exception to approval for operations that were expressly permitted pursuant to the terms of the Purchase Agreement, the Complaint does not indicate that any meaningful interim operations were carved out from the restrictions or otherwise allowed. It is not uncommon for interim operating covenants to provide an exception to approval rights for certain scheduled on-going or planned activities, which the parties typically agree are allowed to continue during the interim period (subject to certain other restrictions). The inclusion of such a schedule is likely the best way to make clear which operations are permitted and which are subject to purchaser restrictions. In addition to these on-going or planned operations, carveouts should be made for those activities considered to be in the ordinary course of the seller's business (e.g., entering into certain ordinary contracts, the replacement of various pieces of equipment and the hiring of field-level contractors). While what is considered "ordinary course" will vary from seller to seller, the Complaint makes clear that the existence of approval rights on ordinary-course conduct (or lack of an exception for such conduct) will weigh in favor of the FTC finding that a purchaser has gained "beneficial ownership" by controlling the minutia of the target company's activities.
- Approval Rights for Certain Expenditures: Approval rights in the interim operational covenants for expenditures over a certain dollar threshold are common in purchase agreements and should not be avoided as a result of this action. That being said, any thresholds included in the interim covenants should be set at an appropriate amount based on the target company's business to ensure that the purchaser is not effectively

controlling the day-to-day activities of the target company by having the ability to reject expenditures incurred in the ordinary course. From the perspective of complying with such interim covenants during the period from signing to closing, sellers should ensure that any expenditures that they ultimately submit for purchaser approval can reasonably be expected to meet the thresholds set forth in the Purchase Agreement, as the FTC noted in the Complaint that EP habitually submitted expenditures to Verdun and XCL for approval that were beneath its \$250,000 threshold.

- Integration into Customer Contracts and Activities: While the Complaint does not make clear whether the Purchase Agreement contained express language granting Verdun and XCL the ability to coordinate on customer contracts with EP (and such inclusion is doubtful), parties to purchase agreements moving forward should ensure that such rights are either not present or are limited so that the target company's operations can remain distinct from those of purchaser. Fulfillment of obligations under customer contracts should remain the sole responsibility of seller/the target company during the interim period, and parties should take care to ensure that any direct communication or coordination between customers and purchaser is done for legitimate interim business purposes, rather than as a means for purchaser to direct the company's business before the consummation of transaction. In addition, any customer contracts being negotiated or entered into during the interim period (if permitted by the interim covenants) should not be subject to overt purchaser influence.
- Limitations on the Receipt of Competitively Sensitive Information: The exchange of certain confidential information for due diligence purposes during the period between signing and closing is the norm in connection with purchase agreements in the energy space. Parties may share confidential information where there is a legitimate and objective business reason for the exchange, such as conducting the parties' due diligence review, confirming the accuracy of representations and warranties, preparing for post-closing integration, and ensuring that covenants and closing conditions are met. Permissible exchanges might include information regarding basic business issues, human resources capabilities and other necessary employee information, operational capabilities, IT systems, historical and aggregated price or cost data, and financial data necessary for evaluating the proposed transaction. However, the parties should take efforts to place appropriate safeguards on the dissemination of such information, particularly when it is of a competitively sensitive nature, and any such exchanges of sensitive information should be supported by a legitimate business purpose (as opposed to impermissible attempts to integrate the businesses or limit competition in violation of the HSR Act). Standard protections include limiting all such information to a virtual data room and/or creating a "clean team" (which would typically not include marketing or operations personnel of the purchaser) to ensure that the sensitive information reaches only those team members necessary for the due diligence process.