

THE 2010 GULF OIL SPILL: THE LEGAL PICTURE

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I.

INTRODUCTION

Like everything else about the 2010 Gulf oil spill, the legal picture is complicated, and at this point, eight weeks into the disaster, there are very few clear-cut answers. As a starting point, this paper contextualizes the spill, identifies the key players, and briefly summarizes the applicable law. Matters are in a state of flux, however, and are subject to rapid change.

II.

LEGAL CONTEXT OF THE 2010 GULF OIL SPILL

On April 20, 2010, an explosion on the oil rig Deepwater Horizon killed 11 workers and injured 17 others. At the time, the rig was located 41 miles off the coast of Louisiana in an area known as the “Macondo Prospect.” Two days later, the rig sank. Since the explosion, oil has been escaping from the exploratory well that the rig was drilling. Preliminary indications are that proper safety procedures were not followed to save time and money.

Although the exact amount remains in dispute, the daily flow of oil may be as high as 60,000 barrels (2.5 million gallons). In comparison, the supertanker Exxon Valdez, which ran aground in Prince William Sound, Alaska, in March 1989, released a total of 262,000 barrels (11 million gallons). Litigation arising from that incident is still ongoing, although most of the claims have been resolved. It is thought that the spill cost Exxon (now ExxonMobil) \$5 billion and that oil from the ship traveled as far as 1,300 miles.

According to present estimates, oil will continue leaking in the Gulf until August 2010, when two relief wells are completed (some experts, however, think December 2010 is a more realistic date). Even with improved containment efforts, the total amount of released oil could reach five million barrels (210 million gallons). This would make the Gulf spill 19 times larger than the Exxon Valdez spill. President Barack Obama has called the spill “the worst environmental disaster America has ever faced.” If the Gulf is hit with a hurricane before the well is capped, the situation could become even graver.

Comparisons are also being made to the “Ixtoc I” disaster. In June 1979, the Sedco 135-F oil rig, operating 62 miles off the coast of Campeche, Mexico, suffered a catastrophic blowout while drilling an exploratory well. The well was not capped until March 1980, by which time three million barrels (126 million gallons) had escaped. Although Pemex (Mexico’s national oil

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company) spent \$100 million cleaning up the spill, it avoided paying any of the victims by claiming “sovereign immunity.” From a technical standpoint, the blowouts on the two rigs appear to have been nearly identical. But while the Sedco 135-F rig was drilling in 160 feet of water, Deepwater Horizon sank in 5,000 feet of water. This has made the current effort to stem the flow of oil much more challenging.

III.

KEY LEGAL PLAYERS IN THE 2010 GULF OIL SPILL

1. Corporate Defendants (this list will expand as more claims are filed)

(a) WELL OWNERS: BP PLC (65%) (UK); Anadarko Petroleum Corporation (25%) (US); Mitsui Oil Exploration Corporation (“Moex”) (10%) (Japan).

(b) RIG OWNER: Transocean Ltd. (Switzerland).

Notes: 1) Deepwater Horizon, valued at \$560 million, took nearly three years to build. In 2008, it was leased to BP at a cost of \$496,800 a day.

2) Until recently, Transocean was a US company. It re-incorporated in Switzerland in 2008 for tax reasons.

(c) SUB-CONTRACTORS: Halliburton Energy Services Group (US); M-I Swaco LLC (US); Weatherford International, Ltd. (Switzerland).

(d) RIG MANUFACTURER: Hyundai Heavy Industries Co., Ltd. (South Korea).

Note: At this point, Hyundai’s liability is purely speculative.

(e) “BLOWOUT PREVENTER” BUILDER: Cameron International Corporation (US).

Note: The blowout preventer (“BOP”) was the key part that failed.

(f) INSURANCE COMPANIES: Hannover Re A.G. (Germany); Jupiter Insurance Ltd. (Guernsey); Munich Reinsurance Company (Germany); Partner Re Ltd. (Bermuda); Swiss Reinsurance Company (Switzerland).

Note: Jupiter is BP’s “captive insurance” company. In other words, BP is self-insured.

2. National Governments

(a) UNITED STATES (multiple interests).

Notes: 1) In May 2010, Liz Birnbaum, director of the Minerals Management Service (“MMS”) (the federal agency responsible for overseeing drilling on the outer continental shelf), resigned amid suggestions that lax governmental supervision contributed to the spill (her replacement—Michael Bromwich, a former assistant U.S. attorney—has been told to make sweeping changes). In June 2010, Attorney General Eric Holder announced that the Justice Department had begun civil and criminal investigations into the spill.

2) Since May 2010, a grass roots movement known as “Seize BP” (www.seizebp.org) has been calling on the federal government to nationalize BP’s American-based assets to ensure that all spill-related claims are paid. Based on *Youngstown Sheet & Tube Co. v. Sawyer*, 343 U.S. 579 (1952) (“The Steel Seizure Case”), President Obama cannot legally issue such an order.

3) In June 2010, 54 senators (nearly the entire Democratic caucus) called on BP to voluntarily establish an independently-administered \$20 billion victims’ escrow fund. A short time later, President Obama issued a similar demand. It is not yet clear how BP intends to respond, although preliminary indications are that it will agree to do so after certain operational details are worked out.

4) If BP fails to act, Congress may try to force it to create the fund. The legality of any such effort, and the extent to which it would displace existing laws, is unclear. Senator Mark Begich (D-Alaska) is currently drafting a bill that would require BP to set up the fund but would not preclude private lawsuits. Senator Lisa Murkowski (R-Alaska) has called for capping attorneys’ fees at 5%.

(b) GREAT BRITAIN (because BP is a British company).

Notes: 1) In June 2010, Prime Minister David Cameron asked President Obama to tone down his increasingly harsh criticism of BP. Although saying he was not trying to put the company out of business, President Obama subsequently likened the spill to 9/11 (a comparison deemed unfair by much of the British media).

2) Since the spill, the company’s stock has dropped 49% (wiping out \$92 billion in market value), raising questions about its future survival. (Some

analysts believe the company's stock will continue to fall until it is worth 25% of its pre-spill value.) Under pressure from US officials, BP is expected to suspend its second-quarter dividend (\$2.5 billion), a development that has roiled the British public (BP accounts for 14.2% of the country's dividends and its stock is held by virtually every British insurance and pension fund).

3) Given BP's importance to the British economy (at \$9 billion a year, it is the country's largest taxpayer), it is possible that Prime Minister Cameron might retaliate if Congress takes "unfair" action against BP. The nature of any such response is uncertain.

(c) MARSHALL ISLANDS (as the rig's "home" country).

Note: The decision to register Deepwater Horizon in the Marshall Islands was made to take advantage of favorable health, safety, and tax laws. Although using a "flag of convenience" is a common practice in the shipping industry, the laws of the Marshall Islands are unlikely to be looked to in any spill-related court proceeding.

(d) JAPAN (due to its 20% ownership of Moex).

Note: Japan's stake is held by its Ministry of Economy, Trade and Industry. Because most of Moex is owned by private interests, the company's assets are not shielded by the Foreign Sovereign Immunities Act of 1976 (28 U.S.C. §§ 1602 et seq.).

(e) OTHER COUNTRIES (as ecological or economic victims).

Note: Since May 2010, the United States has been discussing contingency plans with numerous countries, including The Bahamas, Cuba, and Mexico.

3. State and Local Governments

(a) ALABAMA, FLORIDA, LOUISIANA, AND MISSISSIPPI (already affected—depending on how far the spill spreads, more states might need to be added to this list).

Note: In June 2010, Florida Attorney General Bill McCollum asked BP to place \$2.5 billion in an escrow account to cover potential losses. Likewise, Alabama Superintendent of Education Joe Morton has said he intends to hold BP liable for an estimated \$1.5 billion in lost school tax revenues. While BP has not commented on these matters, it has given various "block grants" (worth a total of \$200 million) to the affected states and

pledged additional funds for specific recovery projects (including \$300 million to build sand berms in Louisiana).

- (b) TEXAS (although not yet directly affected by the spill, BP's American headquarters are in Houston—other Texas-based corporate defendants include Anadarko, Cameron, Halliburton, and Swaco).

Note: *In July 2010, the Judicial Panel on Multidistrict Litigation is expected to transfer all of the spill's federal lawsuits to a single judge. While most plaintiffs want the cases to be heard in New Orleans, the corporate defendants are pushing for Houston. In the meantime, nearly a dozen federal judges have recused themselves from hearing any spill-related suits, primarily because they own oil stocks.*

- (c) LOCAL GOVERNMENTS (particularly counties and cities along the shoreline).

Note: *In June 2010, the United States Conference of Mayors, meeting in Oklahoma City, called on the federal government to help local communities mitigate the spill's economic effects.*

4. Private Claimants

- (a) THIRD PARTIES: Dock owners, fishermen, hotels, marinas, oil workers, restaurants, seamen, travel agents, tour operators, and other businesses and individuals who suffer injuries as a result of the spill.

Notes: *1) Law firms are aggressively recruiting potential plaintiffs through the use of billboards, newspapers, television and radio ads, and the internet. Sample pitches can be viewed at www.BP-OilSpillLawyers.com, www.GulfCoastOilDisaster.com, and www.GulfOilClaim.com. To date, 225 lawsuits have been filed in 11 states.*

2) In May 2010, BP began making voluntary payments to victims. So far, it has received 51,000 claims and issued checks worth \$63 million, although it has been widely criticized for paying too little and too slowly. In addition, its insistence on documentation (such as tax returns) has angered many people. In June 2010, it agreed to adopt a faster and more transparent claims procedure.

3) In May 2010, President Obama imposed a six-month moratorium on deepwater drilling in the Gulf, putting 10,000 people out of work and costing the economy \$4 billion. Considerable debate has taken place over whether BP is liable for these losses, and the issue illustrates how difficult it will be to fairly apportion liability.

(b) INVESTORS: Stockholders in the corporate defendants.

Notes: 1) In May 2010, a shareholder's derivative suit was filed against BP in federal court in New Orleans, accusing Tony Hayward, the company's chief executive officer, of cutting costs at the expense of safety and lobbying government officials to reduce their inspection efforts. A short time later, a class action was instituted in the same court alleging that the company made false and misleading statements regarding the safety of its offshore oil facilities, in violation of the Securities Exchange Act of 1934 (15 U.S.C. §§ 78a et seq.). A similar complaint has been filed against Transocean.

2) For the moment, BP's board of directors is standing behind Hayward (despite his numerous spill-related publicity gaffes), but some observers believe he will lose his job by the end of the year. Also on the hot seat is Carl-Henric Svanberg, BP's chairman. Both men are in Washington this week—Hayward to appear before the House Energy and Commerce Committee and Svanberg to meet with President Obama.

(c) CLEAN-UP WORKERS: Both professionals and volunteers.

Note: Many responders became ill after 9/11 and Hurricane Katrina. So far, 100 Gulf oil spill clean-up workers have suffered "heat incidents" and a dozen others have required medical attention for more serious conditions. (It is estimated that 27,000 people are currently engaged in direct spill-related activities. Many observers have complained that, due to a lack of coordination by the federal government, the clean-up effort is in chaos.)

(d) CONCERNED CITIZENS.

Note: In June 2010, the Gulf Restoration Network and the Sierra Club sued the Interior Department in federal court in New Orleans, claiming that it should not have approved BP's oil spill response plan. Other citizen suits against the government are likely, although a lack of "standing" (i.e., actual injury) will cause many of them to be quickly dismissed.

**IV.
LAWS LIKELY TO PLAY A ROLE IN THE 2010 GULF OIL SPILL
(SUBJECT TO POSSIBLE DISPLACEMENT BY THE
PROPOSED VICTIMS' COMPENSATION FUND)**

1. Federal Environmental Laws (partial list—US waters are subject to more than 140 laws)

(a) Rivers and Harbors Act of 1899 (“Refuse Act”) (33 U.S.C. § 407)

Note: The Refuse Act imposes “strict liability” (i.e., without fault). Accordingly, experts consider BP’s culpability to be clear.

(b) Migratory Bird Treaty Act of 1918 (16 U.S.C. §§ 703 et seq.)

Note: As of June 2010, some 1,300 birds have been killed by the spill.

(c) Clean Water Act of 1972 (“CWA”) (33 U.S.C. §§ 1251 et seq.)

Notes: 1) The CWA authorizes fines of \$2,500-\$25,000 a day plus up to one year in prison for “negligent” violations and fines of \$5,000-\$50,000 a day plus up to three years in prison for “knowing” violations. In addition, a fine of up to \$250,000 and a prison term of up to 15 years can be imposed for the “knowing endangerment” of any person. Civil penalties under the CWA begin at \$1,100 per barrel and increase to \$4,300 per barrel if gross negligence is proved (making BP’s potential exposure as high as \$21 billion). In 1991, Exxon paid \$1 billion in CWA-related fines and penalties for causing the Exxon Valdez spill.

2) Although the CWA includes the possibility of jail sentences, only a few experts think that anyone will go to prison for the Gulf oil spill. No one was sent to jail after the Three Mile Island nuclear reactor meltdown in Pennsylvania (1979); the United States refused repeated requests to extradite Warren Anderson, the chairman of Union Carbide, to India following the Bhopal gas leak disaster (1984); and the only person prosecuted for the Exxon Valdez spill was Joseph Hazelwood, the ship’s captain (he ended up paying a \$50,000 fine and performing 1,000 hours of community service).

3) Still, the possibility of jail time appears to be on the minds of at least some BP officials. In May 2010, Robert Kaluza, a BP well-site leader on Deepwater Horizon, invoked his Fifth Amendment right not to incriminate himself and refused to testify before a joint investigatory panel consisting of officials from the MMS and the United States Coast Guard.

(d) Marine Mammal Protection Act of 1972 (16 U.S.C. §§ 1361 *et seq.*)

Note: *As of June 2010, at least 38 marine mammals (primarily dolphins) have been killed by the spill.*

(e) Endangered Species Act of 1973 (16 U.S.C. §§ 1531 *et seq.*)

Note: *As of June 2010, more than 300 turtles have been killed by the spill.*

(f) Comprehensive Environmental Response, Compensation, and Liability Act of 1980 (“CERCLA” or “Superfund”) (42 U.S.C. §§ 9601 *et seq.*)

Note: *In using chemical dispersants (one million gallons, consisting mainly of Corexit, a highly toxic solvent) to fight the spill, BP has almost certainly triggered the statute.*

(g) Oil Pollution Act of 1990 (“OPA”) (33 U.S.C. §§ 2701 *et seq.*)

Notes: *1) OPA, enacted after the Exxon Valdez disaster, is the country’s primary law dealing with marine oil spills. It requires the “responsible party” (BP) to pay all “removal expenses” and up to \$75 million in economic damages (this cap is lost if the spill resulted from gross negligence or the violation of a federal safety rule). It also jump started the Oil Spill Liability Trust Fund (“OSLTF”) (26 U.S.C. § 9509), which is funded by petroleum taxes and is authorized to pay up to \$1 billion per incident.*

*2) In May 2010, Senator Robert Menendez (D-NJ) introduced the Big Oil Bailout Prevention Liability Act (S. 3305). If passed, the Act would raise the economic damages cap to \$10 billion and eliminate the OSLTF’s “per incident” limit. Some members of Congress would prefer to keep the existing limits (to protect small oil companies) but make them unavailable to BP. Doing so, however, might constitute an unconstitutional “bill of attainder.” (In *SeaRiver Maritime Financial Holdings, Inc. v. Mineta*, 309 F.3d 662 (9th Cir. 2002), Exxon failed to convince the courts that a provision in OPA banning the Exxon Valdez from Alaskan waters was a bill of attainder.)*

2. Other Federal Laws

(a) Shipowners’ Limitation of Liability Act (“LOLA”) (46 U.S.C. § 30505)

Note: *LOLA, on the books since 1851, permits shipowners to limit their liability to the post-accident value of their vessels (subject to various exceptions).*

In May 2010, Transocean petitioned a federal court in Houston to limit its liability to \$26.7 million.

(b) Federal Criminal Code (18 U.S.C. §§ 2 et seq.)

Notes: 1) *The False Statements Act (18 U.S.C. § 1001) makes it a crime to “knowingly” mislead a federal official. Some observers believe that BP repeatedly violated this provision both before (“operational capabilities”) and after (“flow rate”) the spill.*

2) *Federal prosecutors are said to be considering filing charges under the Manslaughter Act (18 U.S.C. § 1112) for the deaths of the 11 rig workers.*

3) *In 2007, BP pled guilty to a felony (for causing an explosion at a Texas City oil refinery that killed 15 people and injured 180 others) and a misdemeanor (for an oil spill on Alaska’s North Slope). Given its past conduct, some commentators believe BP should be deemed a “criminal enterprise” under the Racketeer-Influenced and Corrupt Organizations Act (“RICO”) (18 U.S.C. §§ 1961 et seq.).*

4) *In June 2010, the chief executives of Chevron, ConocoPhillips, ExxonMobil, and Shell told the House Energy and Commerce Committee that the spill occurred because BP failed to follow standard industry practices. (It is estimated that BP saved \$10 million by taking shortcuts.)*

(c) Federal Bankruptcy Code (11 U.S.C. §§ 101 et seq.)

Notes: 1) *In 2009, BP earned \$16.8 billion in profits. According to most experts, it will end up paying \$35 billion in spill-related costs (it has so far spent \$1.6 billion). Although the company insists it has sufficient financial resources to meet all of its obligations (before the spill, the company had cash reserves of \$5 billion), investors are worried that the federal government will make good on its threat to “debar” BP from the Gulf (and possibly the rest of the US), thereby diminishing its future profitability. Legendary oilman T. Boone Pickens has said he would not buy BP stock if he was currently looking to invest in the market.*

2) *In June 2010, Fitch cut BP’s credit rating from AA to BBB (two levels above “junk” status). Other rating agencies are expected to follow, making it much more expensive for BP to borrow money (and possibly forcing institutional investors to dump their holdings). In the meantime, the cost of insuring \$10 million of BP debt for one year has soared from \$29,000 to \$695,000.*

3) *Some observers believe that the spill's tab will be much higher than \$35 billion. Goldman Sachs, for example, has warned that the final figure could be \$70 billion, and made this calculation when the daily flow rate was 50% lower than present estimates. It is therefore possible that BP will eventually be forced into bankruptcy (in 1987, Texaco filed for bankruptcy after being ordered to pay Pennzoil \$10.53 billion for upending its planned merger with Getty). If this occurs, BP might seek to transfer its oil spill liabilities to a separate entity, which could end up being under-capitalized. (In 1982, the Johns-Manville Corporation used this procedure to free itself from 12,500 asbestos-related lawsuits.) In the meantime, it has been claimed that the company is transferring assets off BP North America's books in an effort to thwart US creditors.*

4) *As an alternative to bankruptcy, BP could be taken over by one of its rivals. Although ExxonMobil (US) and Royal Dutch Shell (UK-Netherlands) are said to be interested, anti-trust officials in the US and the European Union are likely to block any deal. This is expected to open the door for such suitors as Petrobras (Brazil's national oil company) and PetroChina. Undoubtedly, if a deal is consummated, it will be structured so as to protect the buyer. When the Dow Chemical Company purchased Union Carbide in 2001, it successfully disclaimed any responsibility for the Bhopal gas leak disaster.*

5) *In June 2010, a Gallup/USA Today poll found that 59% of Americans believe BP should pay all costs associated with the spill, even if doing so bankrupts the company.*

3. State Laws

Despite its comprehensive nature, OPA is not exclusive (see 33 U.S.C. § 2718), and states may therefore also rely on their own oil pollution liability laws (see, e.g., Florida's Pollutant Discharge Prevention and Control Act, codified at Fla. Stat. §§ 376.011 *et seq.*). In addition, state criminal and tort laws have not been displaced.

Following the grounding of the Exxon Valdez, state prosecutors successfully pursued charges against Captain Hazelwood under the Alaska criminal code. In the Gulf oil spill, the principal use of state law is expected to be in tort actions brought by litigants with remote (i.e., difficult to prove) economic injuries. Since *Robins Dry Dock & Repair Co. v. Flint*, 275 U.S. 303 (1927), federal maritime law has used a much stricter standard ("direct injury").

In the past, tort victims were sometimes awarded large punitive (i.e., exemplary) damages even though their compensatory (i.e., actual) damages were small. As a result of *Exxon Shipping Co. v. Baker*, 128 S. Ct. 2605 (2008), a case growing out of the Exxon Valdez disaster, the propriety of such awards has been called into question. In *Baker*, the Supreme

Court reduced an award of punitive damages in favor of a group of commercial fisherman from \$2.5 billion to \$507.5 million.

4. Contractual Agreements

Contractual agreements (also known as “private law” arrangements) will be important when the corporate defendants work out how much they owe each other. Both Anadarko and Halliburton have already said that BP is contractually obligated to indemnify them (i.e., reimburse them for any costs they incur as a result of the spill). Moex has declined to say whether it has a similar deal in place.

Likewise, the liability of any insurance company for spill-related losses will depend on the wording of its policies.