

DEEPWATER HORIZON LITIGATION: WHERE THINGS STAND AND WHAT'S NEXT

Environmental Law Institute, Webinar

January 14, 2015

WEBINAR SUMMARY

The third phase of the BP oil spill trial began in New Orleans on January 20. This phase followed two other phases, which were focused on which parties were at fault for the spill and how much oil spilled into the Gulf of Mexico. Phase III (the “Penalty Phase”) was focused on the eight penalty factors set out in the Clean Water Act (CWA), which the court must take into account in determining civil liability under the CWA. This has important implications for the 80% of CWA penalties that will be channeled through the RESTORE Act for economic and ecological recovery activities in the Gulf.

The webinar brought together leading experts on the oil spill litigation to discuss the first two phases of the trial, including the court’s ruling that the oil spill was the result of BP’s gross negligence and willful misconduct, and previewed some of the major issues that will be addressed in Phase III.

MODERATOR:

- **Teresa Chan**, Senior Attorney, Environmental Law Institute

PANELISTS:

- **Jennifer Larino**, Business Reporter, The Times-Picayune
- **Blaine G. LeCesne**, Donna and John Fraiche Distinguished Professor of Law, College of Law, Loyola University
- **Edward F. Sherman**, W.R. Irby Chair in Law, Tulane University Law School

Ms. Chan provided introductory remarks, focusing on how civil penalties are decided and why they are important. Ms. Chan began by noting that the Clean Water Act (CWA) prohibits the discharge of oil into U.S. waters in amounts that may be harmful to the public or natural resources. Several factors are considered in determining a penalty amount. One of those factors is the violator’s conduct (Phase I of the trial). If a violator acted with gross negligence or willful misconduct, for example, the maximum penalty is enhanced. Another important factor is the number of barrels of oil discharged (Phase II of the trial). However, it is not only conduct and amount of oil that determine civil penalties—there are eight factors under the CWA that must also be considered. Those eight factors will be the subject of Phase III of the trial.

Ms. Chan then discussed the RESTORE Act. After oil spills, CWA civil penalties usually go into the Oil Spill Liability Trust Fund. In this case, however, a law passed in 2012 called the RESTORE Act channels 80% of civil and administrative penalties to economic and ecological restoration in the Gulf. Thus far, \$800 million is obligated to RESTORE via Transocean's settlement of its CWA civil penalties. Ms. Chan noted that it is expected that significantly more money will flow through the RESTORE Act once CWA civil penalties against BP and Anadarko are determined.

Ms. Chan concluded by highlighting what is not being covered by the coming trial. Buckets not covered include economic claims (including those by individuals, businesses, and governments) and natural resource damages.

Following Ms. Chan's introduction, Ms. Jennifer Larino provided an overview of the litigation. After the *Deepwater Horizon* blow-out on April 20, 2010, oil flowed into the Gulf of Mexico for 87 days. The CWA civil penalties trial concerns conduct before, during, and after the blow-out, along with how much oil was discharged into the Gulf of Mexico. Some of the key actors are BP Exploration and Production (subsidiary of BP responsible for offshore drilling), Anadarko (held minority interest in the well), Transocean (owner of the drilling rig), Halliburton (cement contractor), Cameron Intl. Corp. (blowout preventer producer), and MI, LLC (drilling fluid producer).

Ms. Larino next discussed the first two phases of the civil trial. After the *Deepwater Horizon* oil spill, the U.S. filed civil charges against BP and its partners for violations of the CWA. The U.S. argued that the spill was the result of BP's "gross negligence or willful misconduct." Phase I covered many technical aspects of the spill and actions taken by the companies and their employees before the spill. Phase II had two central elements—"Source Control" and "Quantification." "Source Control" examined what was done to stop the oil from flowing; "Quantification" examined how many barrels of oil were discharged into the Gulf of Mexico. In the Quantification segment, the U.S. argued that 4.2 million barrels were discharged, while BP argued that 2.45 million barrels were discharged.

Ms. Larino next provided an introduction to Phase III. She noted that Phase III is likely to be shorter than either of the previous two phases. A primary reason is that Judge Barbier indicated that new evidence presented will be limited. The central question will be how much BP owes in CWA civil penalties. The U.S. is arguing for the maximum penalty—greater than \$18 billion at the time of the webinar.¹ BP is arguing for a lower civil penalty, capped at \$3000 per barrel rather than \$4300 per barrel. The variation in maximum penalty per barrel relates to inflation (whether and how it is taken into account). In addition, Ms. Larino noted that, from her conversations with BP, BP will likely argue that it has incurred \$42 billion of expenses associated with the spill, and that those expenditures should be taken into account in determining civil penalties. The U.S., meanwhile, will argue that those expenses were required by law and should not be taken into account.

Ms. Larino then discussed past rulings of the court. The Phase I ruling was released on September 4, 2014, finding that BP acted with "gross negligence or willful misconduct." The ruling on BP's conduct means that it will be exposed to the maximum penalty under the CWA (the exact per-barrel total is being litigated), rather than the maximum penalty of \$1100 that would have applied in the absence of

¹ The court issued its "Findings of Fact and Conclusions of Law" for the Phase II Trial on January 15, 2015, the day after the webinar. In the ruling, the court held that "BP was not grossly negligent, reckless, willful, or wanton in its source control planning and preparation" and that "nothing from the Source Control segment alters" Phase I findings. For the purposes of calculating maximum civil penalties, the court found that "3.19 million barrels of oil discharged into the Gulf of Mexico."

gross negligence. In addition, the court made a separate ruling under maritime law that BP was 67% liable, Transocean 30%, and Halliburton 3%.

Ms. Larino concluded by emphasizing what the trial is not. The trial is not criminal penalties—BP reached a \$4 billion settlement on CWA criminal penalties in 2013. The trial is also not associated with the \$9.8 billion settlement with private litigants for economic losses associated with the spill. Other post-spill processes not at issue are the Natural Resources Damage Assessment (NRDA) process or maritime law claims by states, local governments, and businesses. While these processes are not directly a part of the civil trial or Phase III, they may be discussed by BP in its arguments for lower CWA civil penalties.

Following Ms. Larino's remarks, Mr. Blaine LeCesne gave an overview of the Phase I ruling that found BP's actions associated with the spill amounted to "gross negligence" and "willful misconduct." Mr. LeCesne noted that it was a crucial decision because it was one of the largest components of BP's liability exposure. In September 2014, Judge Barbier found that, in addition to gross negligence or willful misconduct, BP acted with recklessness, potentially exposing it to \$18 billion in CWA civil penalties as of the time of the webinar.²

Mr. LeCesne next discussed the ruling in detail. The determination of the proper legal standard is a question of law, which is important for appellate review by the Fifth Circuit. The CWA does not define gross negligence. Judge Barbier therefore interpreted caselaw. Much of the confusion in the caselaw has resulted from courts conflating "gross negligence" with "reckless" misconduct. Usually, recklessness requires a culpable state of mind, at least amounting to conscious indifference. Many courts have construed the terms to be synonymous, which could be an issue on appeal. BP argued gross negligence should require willful or intentional conduct, meaning that gross negligence would have an objective (extreme departure from standard of care) and subjective (awareness of risk and conscious disregard) element. The U.S., meanwhile, urged for an objective formula—arguing that gross negligence differs from ordinary negligence only in degree, not in kind. According to this reasoning, ordinary negligence is purely objective, thus gross negligence would be the same, just more extreme.

Mr. LeCesne noted that there is ample caselaw to support both arguments. Mr. LeCesne theorized that Judge Barbier accepted the U.S. argument partially because BP cited mostly Texas state law cases, while the U.S. cited cases stemming from the CWA and from the Oil Pollution Act. The definition adopted by the court was that gross negligence was "an extreme departure of care or the failure to exercise even slight care." The court also agreed with the U.S. that gross negligence "differs from ordinary negligence only in degree, not in kind."

Mr. LeCesne next analyzed another important issue in the ruling, namely the finding that multiple acts of ordinary negligence could amount to "gross negligence or willful misconduct." Mr. LeCesne wrote about this issue at the outset of the case, the argument being that in a high-risk environment, multiple acts of ordinary negligence exponentially increase the potential of harm. There is little caselaw to support the finding, with few courts squarely applying the aggregate gross negligence theory. Mr. LeCesne noted that it is a somewhat uncharted area, and it will likely be a major issue on appeal. In its motion for reconsideration, the aggregate gross negligence theory was BP's primary challenge.

Mr. LeCesne summarized that there were thus two main bases for finding that BP's conduct amounted to "gross negligence or willful misconduct": (1) a single act of gross negligence (BP's misinterpretation of

² After the Phase II ruling issued after the webinar, the maximum penalty is \$13.7 billion

the negative pressure test) and (2) multiple acts of ordinary negligence being the functional equivalent of gross negligence. The standard of review for legal findings is whether the standard used was correct. Meanwhile, the standard of review for fact-finding is more onerous, usually that the finding is clearly erroneous. In this case, the Fifth Circuit could find that the factual findings were made under an erroneous legal standard, which could result in the factual findings being overturned as well. Mr. LeCesne emphasized that everything hinges on whether Judge Barbier applied the correct theory of gross negligence.

Mr. LeCesne next discussed allocation of fault. BP had ultimate decision-making authority and Judge Barbier found that Transocean and Halliburton's actions were not grossly negligent, thus BP was apportioned 67% of the fault for purposes of maritime law. In regards to punitive damages under maritime law, Mr. LeCesne stated that punitive damages are not available under current Fifth Circuit precedent because a policy making corporate official must have participated in the egregious misconduct. Other Circuits abide by the rule that the decision-maker must only be functioning in a "managerial" capacity, which is a lower standard that would likely be met here. There is therefore a possibility that plaintiffs outside of the Fifth Circuit (e.g., Florida and Alabama) may be able to recover punitive damages.

After Mr. LeCesne's presentation, Mr. Edward Sherman discussed what we can expect in Phase III of the trial. Phase III will have three weeks for testimony. There may be later phases on issues not related to CWA civil penalties.

After reviewing the findings and arguments made in Phases I and II, Mr. Sherman analyzed the details of Phase III, the "Penalty Phase." Mr. Sherman noted that Judge Barbier has a wide range of discretion when determining CWA civil penalties. Both parties had submitted briefs at the time of the webinar related to eight CWA factors that are considered when determining penalties. The factors are: (1) the "seriousness of the violation or violations;" (2) the "economic benefit to the violator, if any, resulting from the violation;" (3) the "degree of culpability;" (4) "any other penalty for the same incident;" (5) the "history of prior violations;" (6) the "nature, extent, and degree of success of any efforts of the violator to minimize or mitigate the effects of the discharge;" (7) the "economic impact of the penalty on the violator;" and (8) "other matters as justice may require."

A threshold question is how the CWA penalties should be calculated. The U.S. argues for a top-down approach, with the court starting at the maximum penalty and decreasing it only if it finds mitigating factors. BP disagrees, arguing that the court should consider all eight factors and build up.

Mr. Sherman next discussed specific factors that may be important in Phase III. BP emphasizes that it has undertaken numerous efforts that have supported the recovery and revitalization of the economy in the Gulf of Mexico region. The U.S. argues that BP merely did what was required by law. Another important issue is the relevance of other liabilities incurred by BP associated with the spill. BP argues that it has spent \$42 billion in the Gulf region since the spill, with significant other liabilities pending. It argues that both purposes served by civil penalties—deterrence and remedying harm—would not be advanced by CWA civil penalties near the maximum. In addition, BP argues that in conjunction with the liabilities associated with the spill, the plummeting price of oil could bankrupt BP Exploration and Production. The U.S. contests each claim made by BP. Among other things, it argues that BP will not go bankrupt. One important disagreement is whether the court considers the economic impact on subsidiary BP Exploration and Production only, or also on the parent company BP.

Mr. Sherman stated that BP also argued that there has been a full recovery due to its massive efforts to clean-up and restore the region. The U.S. contests those claims, arguing that there was great harm caused by the spill and continued uncertainty regarding its impacts. As to the history of prior violations, Mr. Sherman stated that this factor weighs heavily in favor of the U.S.

A final issue is penalties to be levied against Anadarko. Judge Barbier has found that Anadarko does not have blame for the blow-out and oil spill. The question presented is whether an investor in an exploration well should be held liable. The U.S. argues that it should, and that Anadarko exposed itself to liability by profiting from deepwater drilling activities.

QUESTIONS AND ANSWERS

What is a key takeaway point regarding Phase III of the trial?

Ms. Larino discussed the question of aggregate gross negligence, and whether multiple acts of ordinary negligence can amount to gross negligence. She stated that it is an interesting concept that could have effects beyond the CWA civil penalties trial. Mr. LeCesne stated that only two factors of the eight considered in Phase III favor BP—specifically other penalties levied against BP for the same incident and that the economic impact on BP could be severe. He stated that most of the other six factors favor a higher end fine, and that it will be interesting to see how BP argues for a lower fine. Mr. LeCesne also stated that Judge Barbier could consider equitable factors to discount whatever civil penalty is levied against BP by the percent Transocean and Halliburton were at fault (33%). Mr. Sherman stated that the case will set precedent for similar cases and that it will be very important for future jurisprudence.

Will Transocean's settlement of CWA fines for \$1 billion effect the amount BP will have to pay?

Mr. Sherman stated that it could be argued that the fine should be subtracted or set off in some way, though it is unlikely to impact the fines levied against BP. Mr. LeCesne stated that the deterrent effect of the sanction will be an ultimate determinant, which could be affected by other CWA fines.

BP's argument that the Gulf has recovered is more about natural resource damages than civil penalties. How might the Phase III decision affect NRDA?

Mr. Sherman stated that not much is known publicly about the substantive status of the ongoing NRDA. He said that the NRDA liability may be considerable, possibly as much as the CWA civil penalties. While it may be the next largest component of BP's liability exposure, it is unlikely to impact CWA civil penalties because information is not public. BP would like to offset NRDA liability; however, it is difficult strategically to make that argument because it is still being determined and Judge Barbier has been clear that the court does not want the parties to discuss NRDA-related topics in Phase III.

Which part of BP did the court find liable and how does that impact the fines?

The panelists stated that the court is considering the actions of BP Exploration of Production, but the parties are arguing about whether the financial status of the parent company (BP) should be considered when making the final determination of liability under the CWA. This determination could be significant because the parent company has greater assets and would be unlikely to argue that penalties would impact its financial viability. Mr. LeCesne stated that the court must determine how the legal artifice of the parent-subsidiary financial relationship will be considered.

What concluding thoughts do the panelists have about Phase III of the trial?

Ms. Larino stated that once Phase III ends, in some ways it seems like just the beginning. There could be a long run of appeals and litigation concerning other processes ahead. Mr. LeCesne built from that statement, saying that there is so much at stake for deepwater drilling generally and the Gulf specifically. He stated that the standards will be set that will govern future drilling practices, in the Gulf and beyond. Many issues depend on what occurs on appeal, which could be influenced by the ideology of the appeals panel. Mr. Sherman noted that it was interesting that there was no settlement prior to trial. He stated that the U.S. government hung tough and there is unlikely to be a settlement at this point. Phase III will thus have massive implications for the future of the Gulf of Mexico region.

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