Drill Baby . . . Spill Baby: How the Oil Pollution Act's Economic-Damage Liability Cap Contributed to the Deepwater Horizon Disaster

by Keith J. Jones

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On April 20, 2010, the Deepwater Horizon oil rig exploded off the coast of Louisiana. The explosion and subsequent fire killed 11 workers and injured several others, and started the release of millions of gallons of oil into the Gulf of Mexico from more than one mile beneath the surface of the water. It is still too early to tell, but it may very well be the biggest environmental disaster in the history of the United States. Was it foreseeable? Was it preventable? Did a federal law enacted two decades earlier in response to a prior environmental catastrophe set the stage for international oil company executives to pursue dangerous deepwater drilling practices with little fear of economic liability? It will take years and probably many lawyers, judges, and juries to answer these questions, but it is not too early to start asking them.

I. The Oil Pollution Act

On August 18, 1990, after years of stalling, the U.S. Congress eventually passed comprehensive oil spill legislation in the form of the Oil Pollution Act (OPA) of 1990.[1] Congress was finally motivated to take this step because of growing public outrage resulting from another environmental tragedy that had occurred the year before. On March 24, 1989, the *Exxon Valdez* oil tanker struck the Bligh Reef and spilled millions of gallons of oil into the Prince William Sound, resulting in irreparable damage to formerly pristine sections of the Alaskan coastline. The *Exxon Valdez* incident resulted in years of litigation. It also raised for the first time numerous issues regarding economic-damage liability related to environmental harm arising from a major offshore oil spill. With the enactment of the OPA, Congress was attempting to address many of the liability issues raised in the innumerable legal actions that were part of the calamitous legacy of the *Exxon Valdez* spill.

Presumably, Congress started off with the best of intentions, having been mobilized to act in response to genuine public concern over the environmental threats presented by possible future oil spills. At the time, the U.S. Senate stated: "What the Nation needs is a package of complementary international, national, and State laws that will adequately compensate victims of oil spills, provide quick, efficient cleanup, minimize damage to fisheries, wildlife and other natural resources and internalize those costs within the oil industry and transportation sector."[2] However, as is often the case, as the legislation progressed, it became watered down through compromise. During conference between the Senate and the U.S. House of Representatives, amendments were added, including one to "establish limitations on liability for damages resulting from oil pollution."[3] Nevertheless, the OPA was ultimately enacted, and its general purpose is to make sure that:

> [E]ach responsible party for a vessel or a facility from which oil is discharged, or which poses the substantial threat of a discharge of oil, into or upon the navigable waters or adjoining shorelines or the exclusive economic zone is liable for the removal costs and damages . . . that result from such incident.[4]

The OPA goes on to define damages to include injury or loss of use of natural resources; destruction of real or personal property; loss of subsistence use of natural resources; net loss of taxes, royalties, rents, fees, or net profit shares that shall be recoverable by federal, state, or local government; profits or impairment of earning capacity that shall be recoverable by any claimant; and net costs of providing increased or additional public services during or after removal activities,

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1. 33 U.S.C. §§2701-2761, ELR Stat. OPA §§1001-7001.
2. S. Rep. No. 101-94, at 2 (1989).
3. H.R. Conf. Rep. 101-653, at 1 (1989).
4. 33 U.S.C.A. §2702(a).

caused by a discharge of oil, that shall be recoverable by state or local governments.[5]

The OPA also provides four possible and complete defenses to liability for an oil spill. An otherwise responsible party is not liable for the removal costs or damages resulting from a discharge of oil, if they are able to establish, by a preponderance of the evidence, that the oil spill was caused solely by: (1) an act of God; (2) an act of war; (3) an act or omission of a third party, other than employee or agent of the otherwise responsible party; or (4) any combination of the previously enumerated defenses.[6]

II. The Cap

Prior to the enactment of the OPA, oil spills were prohibited and regulated in the United States through a patchwork of state and federal laws including often-incomprehensible maritime laws. The hodgepodge of applicable statutes also included the oil and hazardous substance liability provision of the federal Clean Water Act (CWA).[7] By way of the 1977 CWA Amendments, Congress had previously established a $50 million liability cap per facility for all removal costs, including restoration of natural resources damaged by an oil spill.[8] The OPA was intended, at least in theory, to better compensate those injured as a result of an oil spill.[9]

Nevertheless, Congress, likely thanks to the influence of lobbyists representing the oil industry, still intended to have the OPA establish ultimate limits on liability for both removal costs and compensation for damages.[10] Consequently, the OPA states: "[T]he total of the liability of a responsible party . . . and any removal costs incurred by, or on behalf of, the responsible party, with respect to each incident shall not exceed . . . for an offshore facility . . . the total of all removal cost plus $75 million."[11] In other words, after paying for all the removal costs of a major oil spill, which could be substantial, the responsible party would only be liable for an additional $75 million, regardless of what the final calculation of the resulting damages might be. Obviously, such a cap on liability would have to have an impact on behavior.

III. Deepwater Horizon

The Deepwater Horizon was one of the biggest and most sophisticated deepwater, offshore drilling rigs in the world.[12] It was built by Hyundai Heavy Industries in South Korea in 2001 and measured 396 feet long by 256 feet wide.[13] The colossal drilling rig was stationed in the Gulf of Mexico about 50 miles southeast of the state of Louisiana in waters with a depth of almost 5,000 feet.[14] Apparently, the drilling rig was designed to operate in water as deep as 8,000 feet.[15] The U.S. Department of the Interior's bureau of Minerals Management Service (MMS) had inspected the rig three times within the last year, including one inspection in March 2010, but the MMS did not identify any safety or operational concerns with the drilling facility.[16]

At the time of the explosion, the Deepwater Horizon rig had already drilled into the sea floor and was completing a cement casing that is necessary for operation of a deepsea oil well.[17] This can be dangerous work, because of the potential for the release of uncontrolled gas known as a "blowout."[18] According to the *Wall Street Journal*:

> The process is supposed to prevent oil and natural gas from escaping by filling gaps between the outside of the well pipe and the inside of the hole bored into the ocean floor. Cement, pumped down the well from the drilling rig, is also used to plug wells after they have been abandoned or when drilling has finished but production hasn't begun.[19]

The cementing process is known to be a major cause of blowouts.[20] If the cement does not properly set or develops cracks, natural gas and oil can escape and result in an explosion or blowout.[21] Concerns over blowouts have raised issues regarding whether deepwater oil drilling can ever be properly regulated or truly safe.[22]

The Deepwater Horizon drilling rig was an international operation from start to finish. Despite being constructed in Asia, the rig is owned by the Transocean Company, which is based in Switzerland.[23] The cementing work was being conducted by the Halliburton Company, which is based in Houston, Texas.[24] Notably, in 2009, cement work accounted for approximately 11% of Halliburton's annual business, or roughly $1.7 billion, making it the world's largest cementing company.[25] Nevertheless, since September 2007, the Deepwater Horizon rig was actually being leased by BP as part of its international oil-production activities.[26] Consequently,

5. 33 U.S.C.A. §2702(b)(2)(A)-(F).
6. 33 U.S.C.A. §2703(a)(1)-(4).
7. 33 U.S.C. §§1251-1387, ELR Stat. FWPCA §§101-607.
8. S. Rep. No. 1010-94, at 5 (1989).
9. Michael J. Uda, *The Oil Pollution Act of 1990: Is There a Bright Future Beyond* Valdez*?*, 10 Va. Envtl. L.J. 403 (1991).
10. S. Rep. No. 1010-94, at 5 (1989).
11. 33 U.S.C.A. §2704(a)(3).
12. Campbell Robertson, *Search Continues After Oil Rig Blast*, N.Y. Times, Apr. 22, 2010, at A3, *available at* http://www.nytimes.com/2010/04/22/us/22rig.html.
13. *Id.*
14. *Id.*
15. *Id.*
16. *Id.*
17. *Id.*
18. *Id.*
19. Russell Gold & Ben Casselman, *Drilling Process Attracts Scrutiny in Rig Explosion*, Wall St. J., Apr. 30, 2010, *available at* http://online.wsj.com/article/SB10001424052748703572504575214593564769072.html.
20. *Id.*
21. *Id.*
22. *Id.*
23. Campbell Robertson, *Search Continues After Oil Rig Blast*, N.Y. Times, Apr. 22, 2010, at A3, *available at* http://www.nytimes.com/2010/04/22/us/22rig.html.
24. Gold & Casselman, *supra* note 19.
25. *Id.*
26. *Id.*

BP has been the company most associated with the ensuing environmental calamity.

IV. BP

BP was founded, not surprisingly, in England and Wales in 1909.[27] Since that time, it has grown into one of the planet's largest international corporations with operations all over the world. According to MarketWatch.com, BP "provides fuel for transportation, energy for heat and light, retail services, and petrochemicals products . . . ."[28] The company's statistics are truly staggering. BP conducts oil and gas exploration in 30 different countries.[29] BP has wholesale and retail operations in over 80 countries.[30] BP operates over 22,000 service stations[31] and employs over 80,000 people worldwide.[32] BP had, as of December 2009, net assets of over $136 billion.[33] BP's sales and other operating revenues for the year 2009 totaled $239 billion.[34] In theory, because of the length of its reach, BP is "subject to international, national, state and local environmental regulations concerning its products, operations, and activities."[35] However, in reality, can a behemoth like BP really have its global operations and activities regulated in any meaningful way? Moreover, can an environmental statue that caps liability to less than one four-hundredth of 1% of a company's annual revenue really be efficacious?

V. Risk Versus Reward

It is now very easy to point an indignant finger at BP and ask: "Didn't you know the risks you were taking with this type of deepwater oil drilling?" Everyone from the president of the United States to the environmental activist community is now asking such pointed questions. Unfortunately, the answer to such a question probably is: "Yes, we did know what the risks were." This response, of course, begs the question: "If you knew the risk, then why did you go ahead?" This is a much more complicated question to try to answer. Regardless of what the complete answer is, the OPA's liability cap for damages resulting from an oil spill is almost certainly part of it.

Even an enormous international company like BP is still run by people, and people often make bad decisions. Despite their recent vilification in the press, no one has seriously suggested that the people running BP are stupid or uninformed about the possible risk inherent in their deepwater oil-extraction activities. In fact, the people who have risen so high in their business careers so as to be the ones making decisions for a gigantic global company like BP are most likely fairly intelligent and pretty good at making certain types of business decisions. Those business decisions almost certainly result from some kind of risk-versus-reward analysis. It is inconceivable to seriously think that the OPA's cap on liability did not play a role in their analysis when they were balancing the potential risk versus the potential rewards associated with the operation of the Deepwater Horizon oil rig. In a recent *New York Times* article, economist, Michael Greenstone explained:

> [T]he law fundamentally distorts a company's decision making. Without the cap, executives would have to weigh the possible revenue from a well against the cost of drilling there and the risk of damage. With the cap, they can largely ignore the potential damage beyond cleanup costs. So they end up drilling wells even in places where the damage can be horrific, like close to a shoreline.[36]

The OPA economic-damage liability cap allowed BP to take some serious risks in its operations at the Deepwater Horizon facility, focus on the potentially enormous financial rewards of accessing millions of gallons of oil, all the while knowing that its potential liability would be limited to a dollar amount that it could easily pay with little impact to the company's bottom line. According to Craig Thomas, Vice President and Senior Economist for PNC Financial Services Group:

> All individuals and businesses alike consider both potential risk and expected reward in formulating actions by calculating, at least mentally, a risk-adjusted return. If that risk-adjusted return is higher than the next best option, the individual or business will push ahead. If there is a belief that one is shielded from potential risks such as financial liability, as was assumed to be the case with the Oil Pollution Act liability cap, risky actions can be justified by the lack of a compelling downside. In concept and practice, limiting liabilities encourages greater risk-taking. In the end, the liability cap, in BP's case, proved to be an illusion, as the firm is facing the full costs of the disaster that they have caused. In this case, the false promise of the liability cap harmed all parties—victims and perpetrator—as it both encouraged the risk-taking that threatens the gulf and its inhabitants while also punishing the risk-taker with potential insolvency. Theoretically, had there been no liability cap, there may not have been a disaster.[37]

Even before the Deepwater Horizon blowout, BP had developed a reputation as a "company that took risks to save money."[38] After the tragic events of April 20, 2010, the House Energy and Commerce Committee launched an investigation that has already uncovered several internal BP documents that reveal a series of bad decisions by BP employees with a common theme of trading safety for the sake of

27. BP Company Profile, http://www.marketwatch.com/investing/stock/BP/profile (last visited Sept. 14, 2010).
28. *Id.*
29. Key Facts and Figures, http://www.bp.com/extendedsectiongenericarticle.do?categoryId=9021229&contentId=7039276 (last visited Sept. 14, 2010).
30. *Id.*
31. *Id.*
32. *Id.*
33. *Id.*
34. *Id.*
35. BP Company Profile, *supra* note 27.
36. David Leonhardt, *Spillonomics: Underestimating Risk*, N.Y. Times Mag., June 6, 2010, at MM13, *available at* http://www.nytimes.com/2010/06/06/magazine/06fob-wwln-t.html.
37. Craig Thomas, Vice President and Senior Economist for PNC Financial Services Group, E-mail interview, June 25, 2010 (on file with author).
38. Leonhardt, *supra* note 36.

saving time or money.[39] In June of 2010, the *Washington Post* reported that Reps. Henry Waxman (D-Cal.) and Bart Stupak (D-Mich.) had stated: "Time after time it appears that BP made decisions that increased the risk of a blowout to save the company time or expense."[40] It is difficult to believe that the same decisions would have been made or that BP would have engaged in such pennywise but pound foolish behavior if it did not have some confidence that, should there be a problem, it would ultimately be shielded from liability for its actions thanks to the protections granted to it by the OPA. However, when performing their risk-versus-reward analysis, the decisionmakers at BP may not have ever contemplated the consequences of such an unprecedented oil leak that appears, at least at the moment, to be unstoppable, despite the best technological efforts of the oil industry and the U.S. government. It would require an acutely pessimistic person to fathom such a truly worst-case scenario.

VI. Efforts to Raise the Cap

Congress is nothing if not reactive. Within weeks of the explosion on the Deepwater Horizon, various bills were introduced in both the Senate and the House that would seek to raise the OPA's cap on economic-damage liability. Once again, Congress was being driven to act by public outrage at yet another national environmental disaster perpetrated by the oil industry.

On May 4, 2010, the Big Oil Bailout Prevention Liability Act of 2010 was introduced in the Senate by Sens. Robert Menendez (D-N.J.), Bill Nelson (D-Fla.), Frank Lautenberg (D-N.J.), Ben Cardin (D-Md.), Charles Schumer (D-N.Y.), Sheldon Whitehouse (D-R.I.), and Bernie Sanders (I-Vt.).[41] This Act is intended to "amend the Oil Pollution Act of 1990 to require oil polluters to pay the full cost of oil spills . . . ."[42] The Act would accomplish this specifically by amending 33 U.S.C. §2704(a)(3) to change the dollar amount of the liability cap from $75 million to $10 billion.[43] Notably, the Act is to have an effective date of April 15, 2010.[44] This effective date would be a full five days before the horrific events of April 20, 2010. Obviously, the senators are intending to create retroactive liability for BP.

Not to be outdone by the Senate, on May 5, 2010, Reps. Rush Holt (D-N.J.), Frank Pallone (D-N.J.), Suzanne Kosmas (D-Fla.), Allen Boyd (D-Fla.), Kendrick Meek (D-Fla.), Paul Hodes (D-N.H.), Artur Davis (D-Ala.), Jay Inslee (D-Wash.), Lois Capps (D-Cal.), and Bruce Braley (D-Iowa) introduced the Big Oil Bailout Prevention Act of 2010 in the House and had it referred to the Committee on Transportation and Infrastructure.[45] The House's version of the bill would also amend the OPA to raise the cap from $75 million to $10 billion and impose liability retroactively on those parties eventually found to be responsible for the Deepwater Horizon disaster.[46] These bills immediately raise numerous questions. While $10 billion is a dramatic increase from $75 million, it is still a cap. Is it even the right number? For a company like BP with annual revenues well above $100 billion a year, is such a number enough to make it behave differently? What about much smaller oil companies? With a liability cap of that level, will they be able to obtain insurance necessary to operate? Moreover, is it ever fair to impose retroactive liability?

It initially looked like the legislation to raise the OPA's economic-damage liability cap was going to be on a fast track. However, on May 13, 2010, Sen. Lisa Murkowski (R-Alaska) essentially ended any expedited effort with her objection.[47] Senator Murkowski, a Republican from a major oil-producing state, indicated that she had concerns that a higher cap could potentially put smaller refiners out of business.[48] In contrast, New Jersey Democrat Senator Lautenberg stated: "If an independent creates that kind of damage and it costs them their business, so be it."[49] The legislation is now scheduled to move through the traditional and more time-consuming committee processes in both the Senate and the House.

VII. Conclusion

Two days before the 40th anniversary of Earth Day, a purely man-made environmental disaster of still unknown proportions started. It seems more than a little ironic that the Deepwater Horizon rig, the source of the catastrophe, finally sank, thanks to the water being used in the firefighting efforts, on Earth Day. After four decades of "environmentalism," have any lessons been learned? Some thought that the *Exxon Valdez* tragedy in the late 1980s had taught the country something about the potential environmental dangers being created by the nation's addiction to oil. Allegedly, part of that lesson was codified in 1990, when Congress passed the OPA to make responsible parties liable for the damages resulting from any future oil spills. However, the OPA includes a $75 million cap on economic-damage liability.

Did the OPA's cap influence the behavior and decisions made by enormous international companies like Transocean, Halliburton, and BP? Many people, including Congress, seem to think the cap played some role. Consequently, there has been a rush to raise the cap and to make the revised cap retroactive. This legislation is far from enacted and could change in many ways before passing or may never even become law. BP almost immediately stated that it would essentially waive the cap and pay all "legitimate" claims resulting from the spill. As a result of pressure from President Barack Obama, BP has also agreed to create a $20 billion

39. Mathew Daly & Ray Henry, *Documents: BP Cut Corners in Days Before Blowout*, Wash. Post, June 14, 2010, *available at* http://www.washingtonpost.com/wp-dyn/content/article/2010/06/14/AR2010061404375.html.
40. *Id.*
41. S. 3305, 111th Cong. (2010).
42. *Id.*
43. *Id.* §2.
44. *Id.* §3.
45. H.R. 5214, 111th Cong. (2010).
46. *Id.*
47. Lisa Lerer, *Effort to Raise Oil-Spill Liability Fails in Senate*, Bloomberg, May 14, 2010, *available at* http://www.bloomberg.com/apps/news?pid=20601072&sid=asE4RNMDTGqY.
48. *Id.*
49. *Id.*

fund to satisfy claims. Beyond these public announcements, which may just be prudent public relations, only time will tell what, if any, legal defenses BP asserts under the OPA or other applicable laws as it attempts to define what a "legitimate" claim is. Regardless, it certainly will be interesting, on the 50th anniversary of Earth Day, to look back 10 years and to see if the BP Gulf of Mexico disaster resulted in modification of the OPA, changed the way Americans think about energy, or taught the world anything about the environmental impact of the search for oil.