

Liability Caps After Deepwater Horizon

Catherine Phillips

On April 20, 2010, about 48 miles from the shore of the southern United States, an oil well exploded in the Gulf of Mexico, killing 11 people and injuring 17.¹ Over the next several months, the world watched as an estimated 49 million barrels of crude oil spewed from the Deepwater Horizon well.² Debate immediately began about the extent of the short- and long-term damage to marine and coastal wildlife, as well as to the people working in the fishing and tourism industries along the southern Gulf Coast.³ Whatever the total damages would be, no one doubted that the \$75 million liability cap in the Oil Pollution Act of 1990⁴ (OPA) for damages arising from an oil spill would be woefully inadequate.⁵ What was less clear, however, was whether this inadequacy meant the end of liability caps for energy production as such or whether it just signaled the need to raise the cap.

The liability cap for damages arising out of an oil spill was enacted in 1990 following the *Exxon Valdez* oil spill.⁶ The purpose of the OPA, in theory, was to ensure that “each responsible party . . . is liable for the removal costs and damages . . . that result from”⁷ any oil spill. This legislation was intended to be an improvement to the patchwork of relevant laws applicable at

¹ Andrew Clark, *BP Contingency plan for dealing with oil spill was riddled with errors*, THE GUARDIAN (London), June 9, 2010, at 7, available at <http://www.guardian.co.uk/environment/2010/jun/09/bp-oil-spill-contingency-plan>.

² Maureen Houch, *New Estimate Puts Gulf Oil Leak at 205 Million Gallons*, PBS NEWSHOUR, (August 2, 2010, 10:07 PM), <http://www.pbs.org/newshour/rundown/2010/08/new-estimate-puts-oil-leak-at-49-million-barrels.html>.

³ See, e.g., Scott Neuman, *Extent of BP's Liability Still Murky*, NPR (June 9, 2010), <http://www.npr.org/templates/story/story.php?storyId=127561028>.

⁴ Oil Pollution Act of 1990, 33 U.S.C. § 2716 (2006) (amended by Pub. L. No. 111, § 281, 124 Stat. 2905 (2010)) (establishing liability in the event of an oil spill).

⁵ See, e.g., Neuman, *supra* note 3 (noting oil liability estimates vary widely up to as much as \$40 billion).

⁶ Keith J. Jones, *Drill Baby . . . Spill Baby: How the Oil Pollution Act's Economic-Damage Liability Cap Contributed to the Deepwater Horizon Disaster*, 40 ENVTL. L. REP. NEWS & ANALYSIS 11132, 11132, (2010).

⁷ Oil Pollution Act of 1990, 33 U.S.C. § 2702(a) (2006).

the time of the *Exxon Valdez* spill.⁸ The OPA established strict liability for corporate entities, like BP, responsible for an oil spill.⁹ But the heavy blow of strict liability was softened by a benefit: a \$75 million liability cap for damages suffered by public or private entities,¹⁰ including all damages to “natural resources, real property, personal property, subsistence . . . , revenues, profits, earning capacity, and public services.”¹¹ The liability cap is waived if the responsible party engages in grossly negligent behavior, “willful misconduct,”¹² or “the violation of an applicable federal safety, construction, or operating regulation.”¹³

Notwithstanding the cap, injured parties would still be potentially eligible for damages beyond the \$75 million cap.¹⁴ However, these additional damages would not be paid directly by the responsible party.¹⁵ Rather, the money would come from an Oil Spill Liability Trust Fund (Trust Fund), set up by the OPA and managed by the U.S. Coast Guard.¹⁶ Parties involved in the oil industry pay into the Trust Fund through a variety of taxes, penalties, and other mechanisms.¹⁷ Any responsible party may be further responsible for reimbursing the fund for any money expended on its behalf.¹⁸ When a covered incident, like an oil spill, occurs, the Coast

⁸ Jones, *supra* note 6, at 11133.

⁹ *Id.* at 11132.

¹⁰ *Id.* The responsible party would be still responsible for the cost of cleaning up the disaster in full. *Id.* Moreover, the amount expended in clean-up is not considered part of the damage liability cap. *Id.*

¹¹ Andrew F. Popper, *Capping Incentives, Capping Innovation, Courting Disaster: The Gulf Oil Spill and Arbitrary Limits on Civil Liability*, 60 DEPAUL L. REV. 975, 989 (2011).

¹² 33 U.S.C. § 2704(c)(1)(A)(2006).

¹³ Patrick H. Martin, *The BP Spill and the Meaning of “Gross-Negligence or Willful Misconduct,”* 71 LA. L. REV. 957, 961 (2011).

¹⁴ *Id.*

¹⁵ *Id.*

¹⁶ *Id.* As of March, 2011, the Trust Fund had expended approximately \$625.9 million for the Deepwater Horizon incident. See Nick Snow, *GAO: Macondo spill claims pass 60% of OPA liability cap*, OIL & GAS J., May 2011, at 42. The Trust Fund has a \$1 billion-per incident limit on expenditures. *Id.* Note that this is distinct from, and in addition to, the \$75 million cap on liability paid directly by a responsible party.

¹⁷ *The Oil Spill Liability Trust Fund*, UNITED STATES COAST GUARD (Nov. 09, 2010), http://www.uscg.mil/npfc/About_NPFC/osltf.asp. Arguably, the total damages from the Deepwater Horizon spill will surpass both the \$75 million liability cap and the \$1 billion-per incident fund limit, which would leave substantial unpaid damages, were that all the money available.

¹⁸ *Id.*

Guard utilizes the Trust Fund to respond.¹⁹ Thus, in theory, injured parties may be fully compensated even if damages exceed the liability cap. Nonetheless, even were such full compensation to occur, the liability cap would still raise policy issues relating to how allocating damages impacts corporate behavior.²⁰

Some scholars, while acknowledging that the liability caps may need to be increased with more regularity,²¹ have nonetheless argued that the caps are necessary for industry to do business in many energy fields, including oil production.²² First, the liability scheme created by the OPA, and other similar legislation, creates stability in the energy sector, particularly in terms of the companies' ability to purchase insurance for future possible disasters.²³ This stability is essential for the continuation of global trade and oil exploration, particularly for smaller oil operations.²⁴ Any change in OPA's liability scheme would require significant study to determine the best way to balance all the different interests at work.²⁵ Any hasty, politically-driven action on the part of Congress in the wake of the Deepwater Horizon oil spill could have devastating effects on our long-term energy stability.²⁶

Second, the liability scheme set-up by OPA reflects our nation's public policy that "certain liabilities against certain parties should be limited for the better of our overall society or as a trade-off for some other compelling need."²⁷ OPA's liability cap is similar to Workers'

Compensation Laws, medical malpractice caps, no-fault automobile liability, the National

¹⁹ Snow, *supra* note 16.

²⁰ See Popper, *supra* note 11; Jones, *supra* note 6.

²¹ Patrick J. Bonner, *Limitation of Liability: Should it be Jettisoned After the Deepwater Horizon?*, 85 TUL. L. REV. 1183, 1197(2011); *but see*, Vincent J. Foley, *Post Deepwater Horizon: The Changing Landscape of Liability for Oil Pollution in the United States*, 74 ALB. L. REV. 515, 526 (2010) (noting that the OPA limits compare favorably with legal limits worldwide).

²² See *id.*

²³ Foley, *supra* note 21, at 515–16.

²⁴ *Id.*

²⁵ *Id.*

²⁶ *Id.*

²⁷ Bonner, *supra* note 21, at 1185.

Childhood Vaccine Injury Act, and liability limitations for nuclear plants.²⁸ In these instances, legislators have chosen fixed liability as the best means to balance the needs of business with those of the injured; likewise, such a scheme makes sense in the context of the oil industry business.²⁹

Finally, these scholars argue that OPA's liability scheme has worked without complaint for twenty years, and any change could put many small oil operations out of business.³⁰ Until the enormity of the Deepwater Horizon oil spill, the liability cap had been adequate, when supplemented with small payments from the Trust Fund, to pay for all damages arising out of oil spills.³¹ Congress should be hesitant to alter a long-standing, functioning liability scheme in reaction to just one incident.³²

Conversely, others argue that liability caps encourage risky behavior on the part of energy companies by causing companies to undervalue potential costs in the face of disproportionately large benefits.³³ Faced with the relatively solid potential of billions in profits, the chance of paying \$75 million in damages for a seemingly improbable accident naturally leads companies to undervalue the long-term fiscal importance of costly safety measures.³⁴

For this reason, liability caps are ultimately bad for businesses.³⁵ BP will likely be on the hook for much more than \$75 million, as may other responsible corporate entities.³⁶ However, it

²⁸ See generally *id.* at 1185–1194.

²⁹ *Id.* at 1194–1205.

³⁰ *Id.*

³¹ *Id.*; see also Matthew L. Wald, *Tax on Oil May Help Pay for Cleanup*, N.Y. TIMES, May 2, 2010, at A31, available at <http://www.nytimes.com/2010/05/02/us/02liability.html>.

³² Bonner, *supra* note 21.

³³ Jones, *supra* note 6.

³⁴ *Id.*

³⁵ *Id.*

³⁶ See *infra* notes 52–58 and accompanying text. Indeed, BP estimates its total liability will be around \$20 billion, not including any civil fines (Clean Water Act fines, for example) or clean-up costs. See Rowena Mason, *BP's Gulf of Mexico Oil Spill Bill Could Hit \$60bn, Moody's warns*, THE TELEGRAPH (London) (Apr. 20, 2011, 5:30 AM), <http://www.telegraph.co.uk/finance/newsbysector/energy/oilandgas/8462057/BPs-Gulf-of-Mexico-oil-spill-bill-could-hit-60bn-Moodys-warns.html>. Many independent commentators estimate BP's liability will likely be more

is possible this catastrophe could have been averted with a simple \$500,000 blow-out prevention device.³⁷ Thus, the liability cap created the illusion of relative immunity from damage liability that caused the company to make poor risk decisions about the cost-effectiveness of installing additional safety technology.³⁸ The cost of this illusion will likely be substantial to all corporate parties insofar as they failed to prepare for or insure themselves against more than \$75 million in damages.³⁹

Moreover, liability caps are socially unjust because they ultimately punish the most severely harmed parties and leave the public on the hook for corporate misdeeds. Caps on liability, of any kind, deny “just and reasonable compensation for victims,”⁴⁰ and the injustice grows as the harm grows.⁴¹ While a \$75 million cap is sufficient to compensate victims of a minor incident, it is ill suited to larger catastrophes.⁴² When major incidents cause significant damage to wildlife and people, injustice in terms of damage compensation becomes an unavoidable outcome.⁴³ In such instances, liability caps simply shift the cost of “privately caused harms” to the public.⁴⁴

For now, the argument about the continued viability of liability caps remains largely academic in the face of Congressional stalemate. In the weeks following the Deepwater Horizon explosion, Congress appeared poised to act swiftly in lifting the liability cap.⁴⁵ Initial legislation

than this amount. *Id.* Additionally, the Federal District judge ruled recently that punitive damages would be allowed for some claims, opening the door to the potential for substantially increased damages. *Punitive Damages Rules Possible in Gulf Oil Spill*, ASSOCIATED PRESS, Aug. 26, 2011.

³⁷ Popper, *supra* note 11, at 989.

³⁸ Jones, *supra* note 6.

³⁹ *Id.*; see *infra* notes 52–58 and accompanying text (discussing the waiver of the liability cap by BP).

⁴⁰ Popper, *supra* note 11, at 975.

⁴¹ *Id.*; *Cf.* Wald, *supra* note 31 (discussing how liability cap has worked for small incidents, but not for the large Deepwater Horizon disaster).

⁴² See Popper, *supra* note 11, at 997-1001.

⁴³ *Id.*

⁴⁴ *Id.* at 991.

⁴⁵ Jones, *supra* note 6.

even made the changes retroactive to remove any doubt that BP and other responsible corporate parties would be wholly responsible for clean-up and damages.⁴⁶ The House passed legislation lifting the liability cap; however, despite numerous hearings on the issue, the Senate failed to act.⁴⁷ The primary issue in contention is what to do with the liability cap – whether to raise it slightly or abolish it altogether.⁴⁸

Regardless, the issue may be largely irrelevant insofar as it relates to the Deepwater Horizon incident. BP has voluntarily waived the liability cap, first through press release,⁴⁹ and then ultimately through an official filing with the court handling the litigation arising from the disaster.⁵⁰ Other potentially responsible corporate entities, including Transocean Holdings LLC (the rig owner), Anadarko Petroleum Corp, and MOEX Offshore 2007 LLC, have not waived the cap as yet.⁵¹

Moreover, BP has set up a \$20 billion fund to pay claims, an amount clearly in excess of the cap.⁵² Injured people file claims with the fund administrator and, if eligible, receive some amount of money in exchange for waiving their rights to sue for further damages.⁵³ Additional damages beyond the designated fund are also likely to arise from the consolidated lawsuits

⁴⁶ *Id.*; see, e.g., S. 3305: Big Oil Bailout Prevention Liability Act of 2010, 111th Cong. (2010).

⁴⁷ Gerard Shields, *Gulf Oil Disaster: One Year Later*, BATON ROUGE ADVOCATE, April 20, 2011, at A1. The House bill has now expired and given the political shifts in the House is unlikely to pass again. *Cf. id.*

⁴⁸ Jennifer A. Dlouhy, *Lawmakers struggle with spill liability*, HOUSTON CHRONICLE, April 18, 2011, at B1.

⁴⁹ Laurel Brubaker Calkins & Margaret Cronin Fisk, *BP Waiver of \$75 Million Spill Damage Cap May Recognize Liability Reality*, BLOOMBERG NEWS, (May 21, 2010, 11:50 AM), <http://www.bloomberg.com/news/2010-05-21/bp-waiver-of-75-million-spill-damage-cap-may-recognize-liability-reality.html>.

⁵⁰ Tom Hals, *BP tells court it waives cap on spill liability*, (Oct. 19, 2010, 10:28 AM), <http://www.reuters.com/article/2010/10/19/us-oil-spill-bp-liability-idUSTRE69I3C420101019>. Some commentators noted that the liability cap would have been waived anyway, regardless of BP's intention. See Calkins and Fisk, *supra* note 49. The OPA waives the liability cap if the incident was caused by "gross negligence" or was the result of a violation of any regulation. See 33 U.S.C. § 2704(c)(1)(A)(2006). Perhaps invariably, some regulation was violated and thus the "voluntary" waiver is good public relations, but it practically changes nothing about the ultimate outcome.

⁵¹ *Id.*

⁵² Amy Harder, *BP Chief Skirts Oil Liability Issue at CERA Conference*, NAT'L J. DAILY (March 9, 2011).

⁵³ The fund has generated its own controversy over the slow pace with which the money has been paid. See, e.g., John Schwartz, *Judge is Asked to Provide New Oversight for BP Fund*, N.Y. TIMES, July 26, 2011, at A12, available at http://www.nytimes.com/2011/07/26/us/26brfs-JUDGEISASKED_BRF.html?_r=1&ref=gulfomexico2010.

currently pending before Judge Carl J. Barbier of the United States District Court for the Eastern District of Louisiana.⁵⁴

The debate as to the justice and economic utility of liability caps will likely continue in other jurisdictions as well, including North Carolina. After vetoing earlier legislation to support offshore drilling off the North Carolina coast, North Carolina Governor Beverly Perdue recently signaled her possible support for offshore drilling if certain safety measures are in place to protect people and the environment.⁵⁵ Safety measures notwithstanding, unless Congress acts to increase or remove the liability cap in OPA, any entity responsible for an oil spill off the coast of North Carolina in the coming decades, should offshore drilling move forward, would only be responsible for damages in the amount of \$75 million.⁵⁶ Were such a catastrophe to happen, we may well discover, as others have before, that such a limit is woefully inadequate to compensate for any damages inflicted upon our citizens and environment.

⁵⁴ In RE: Oil Spill by the Oil Rig “Deepwater Horizon” in the Gulf of Mexico, on April 20, 2010, MDL No. 2179, U.S. Dist. Court Eastern Dist. of LA, (transferred and consolidated 8/12/2010).

⁵⁵ Rob Christensen, *Perdue leans toward offshore drilling*, NEWS & OBSERVER (Raleigh) (Sep. 24, 2011), <http://www.newsobserver.com/2011/09/24/1512927/perdue-leans-toward-offshore-drilling.html>.

⁵⁶ It is important also to note that the issue of liability caps has resonance with North Carolina, regardless of the status of offshore oil drilling. Liability caps also apply to nuclear plants, like the Shearon Harris Plant in Wake County. Additionally, given the current debate over fracking, it is likely that liability caps in relation to natural gas exploration may become a significant issue for North Carolina in the near future.