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EX POST REGULATION:
JUDGEMENT PROOF,
FINANCIAL RESPONSIBILITY,
AND THE BP CASE

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LIUC COURSE:
CORPORATE CITIZENSHIP FOR GLOBAL FIRM

JUDGEMENT PROOF

- ☛ The experience made with the implementation of legal provisions in the US shows that cases may occur where liability is escaped by transferring dangerous activities to firms that have minimum capital resources.
- ☛ This is the issue of the judgement proof that, in the light of the relative comparison between the firm's financial resources and the extent of the damage, does not only concern "catastrophic" events, but also minor environmental accidents, including those causing limited damage, which is however not internalized due to the polluting firm going bankrupt.

EXTENDING LIABILITY TO LENDERS

- ☛ The lender's liability solution as a remedy to the judgement proof provides for extending liability to other parties related to the firm and, in particular, to its lenders, that are considered at least partially liable for the consequence of the activity carried out by the firms financed by them.
- ☛ With respect to specific cases, the term lender's liability was introduced, and then used to describe all those cases where the firm that is directly liable for the environmental damage may not refund such damage and therefore the judges involve the lenders of the firm if these have carried out some sort of supervision or have exerted some influence on the production activity and on the adoption of preventive measures.

THE LENDERS' LIABILITY: U.S. CASES

- ☛ This solution was occasionally adopted in the United States where, within the system of strict liability of the polluting firms established by the CERCLA, we find an application in some cases expanding the notion of owner and operator used by the wording of the law to include lenders.
- ☛ In one case, a bank was judged liable for the damage because the Court claimed it had been significantly involved in the supervision of the firm's operations; the Court stated that, in this case, the firm's lenders could be considered either as the owners or as the operators and, as such, liable for the damage (the famous case United States vs. Fleet Factors Corp.)
- ☛ DEBATE IN U.S. DIFFICULT IMPLEMENTATION IN EU

FINANCIAL RESPONSIBILITY

- ☛ The term financial responsibility refers to the whole set of instruments that provide for the potential polluters to demonstrate ex ante that their financial resources are adequate to the restoration of potential environmental damage they may cause.
- ☛ In one of its practical application, financial responsibility provides for production activities in risky sectors to be only authorized if the companies concerned may demonstrate their ability to provide an appropriate financial or insurance coverage for future obligations resulting from the assignment of environmental liability.

FINANCIAL RESPONSIBILITY PRODUCTS

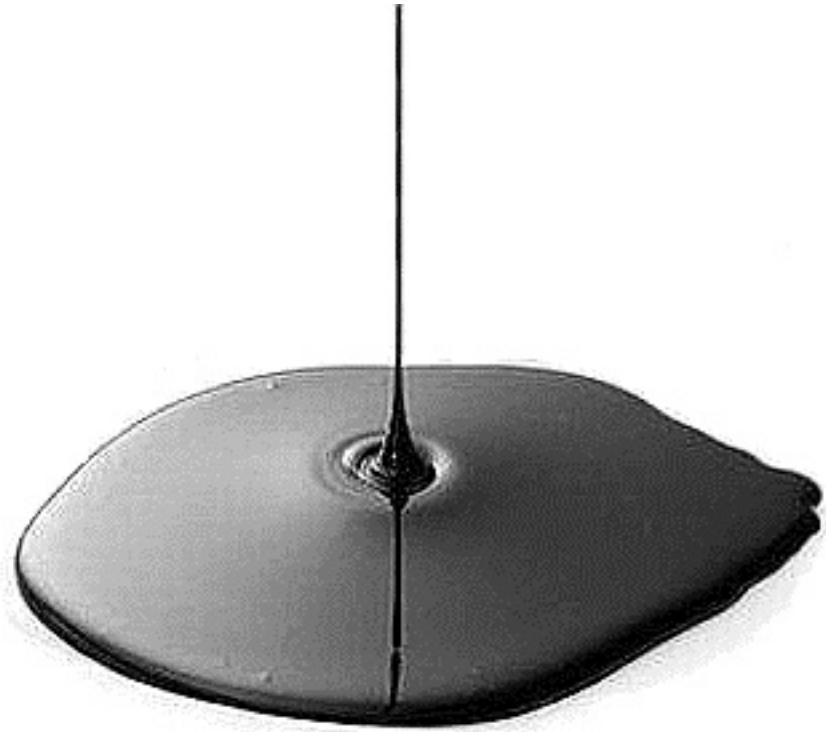
- ☛ Financial responsibility includes various kinds of instruments: letters of credit and surety bonds; cash accounts and certificates of deposit; selfinsurance and corporate guarantee.
- ☛ In this broad definition is included also a kind of instrument such as e-bond that can be defined as “compulsory deposit which must be paid by anyone who wants to utilise certain natural resources the disposal of which may damage the environment”.

ADVANTAGE OF FINANCIAL RESPONSIBILITY

- ☛ Financial responsibility ensures that the expected costs related to environmental risks are recorded in the firm's balance sheet and accounts.
- ☛ Other benefits result from the fact that, since financial guarantees are purchased by banks or insurance companies, a contract relation is established by which the latter are keen on protecting their investments through the monitoring of the production activity of their corporate customers.
- ☛ “Financial guarantors” force the firm to take into account the whole extent of the damage ex ante and to pay a premium adjusted to the granted financial guarantees: in this case a internalization of the damage resulting from environmental accidents can be achieved.

Look at US experience:

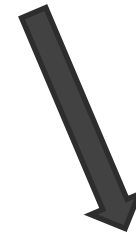
<http://www.epa.gov/oust/ustsystem/finresp.htm>



BP OIL SPILL

THE ACTORS

Deepwater Horizon



Builder:
Hyundai-
2001



Owner:
Transocean



Leasee:
British Petroleum



LOCATION

🌿 GULF OF MEXICO



80Km from Louisiana

🌿 One of the biggest drill:
around 9000 barrels of oil
per day



THE FACTS

☘ 20 April, 2010 - EXPLOSION

- 11 **Casualties**
- 17 **injured**



- 22 April, 2010 -
deposited on the seabed



OIL SPILL

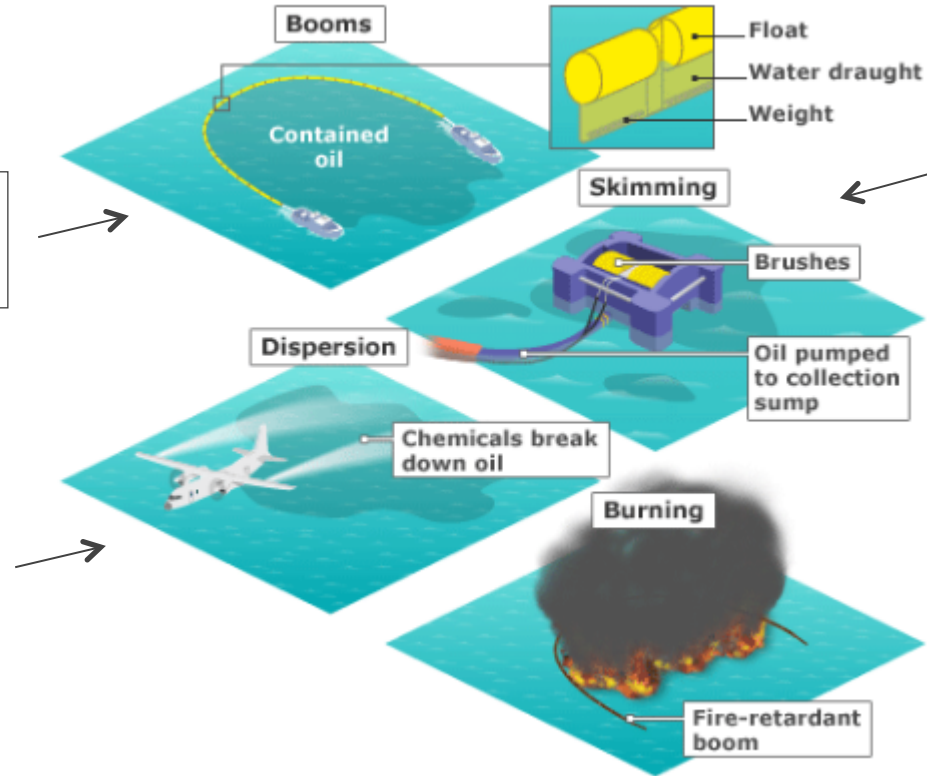
CLEAN-UP ATTEMPTS

Over
30,000
people

Floati
ng
booms

Dispersa
nt to
break up
the oil

Surface measures used to contain oil spillages



Skim
mer
ships

Controll
ed burns

STEM ATTEMPTS

- ☛ Remote controlled machines
- ☛ Containment “Dome” (a capping device)
- ☛ “Top Kill” approach (pumping heavy fluids in the blowout preventer)
- ☛ 15 July – temporary cap
- ☛ 3rd August – “Static Kill” operation (mud and cement injected)
- ☛ 19 September, 2010 – well officially “dead”

OIL SPILLED

☛ 106 days long leak

☛ More than 4.9 million barrels

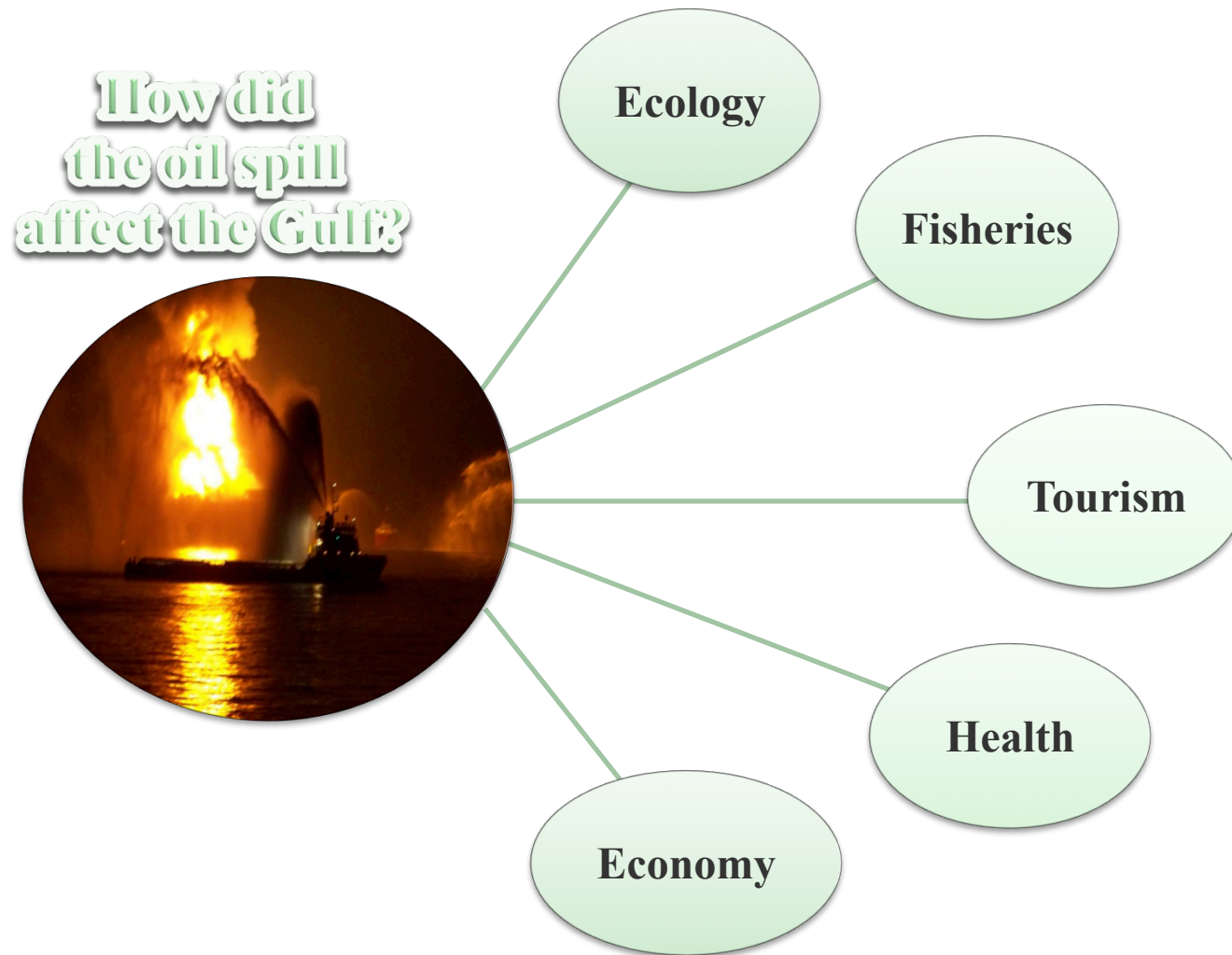
☛ 11,300 miles – distance covered

by milk jugs lined up side by side - farther than New York to Buenos Aires and back

- 102: school gymnasiums filled floor-to-ceiling



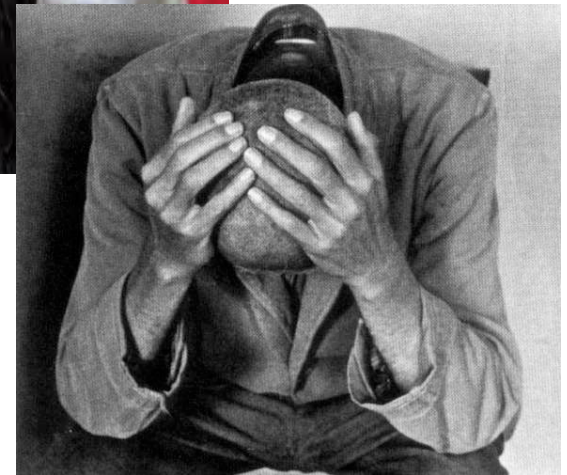
DAMAGE EVALUATION



DAMAGE EVALUATION



DAMAGE EVALUATION



AN UPDATE OF THE SITUATION

Assessing Progress: Three Years later



Administration



Offshore drilling industry



US Congress

Administration:

- fast to reorganize the criticized Minerals Management Service; two agencies established, BOEMRE and BSEE
- asked for more funds to help the authorities to carry out their job

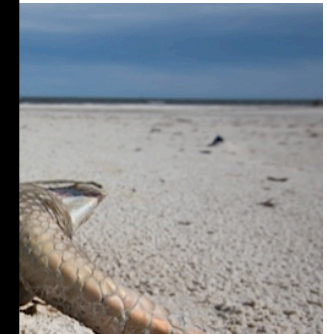
Offshore drilling industry:

- introduced tools to contain a high-pressure blowout in deep water
- negligent in the creation of an independent safety institute that will focus on safety

US Congress:

- Inefficient; it has introduced just the RESTORE Act (80 percent of the fines used for environmental and economic restoration projects)
- should increase the financial responsibility and the liability cap requirements for offshore facilities; raise the Oil Spill Liability Trust Fund's limitation

AN UPDATE OF THE SITUATION



EX-ANTE REGULATION

“...a two-step process: first, standards or targets for environmental quality are set, and, second, a regulatory system is designed and put in place to achieve these standards.” (Cropper e Oates)



EX-POST REGULATION

Scope: internalize environmental damages associated to an accident occurred and caused by third parties.

It is a liability system.

EX POST REGULATION SCHEME

- 1. FIRM, INJURER, POLLUTER: BP***
- 2. CAUSALITY: environmental pollution, oil spread in waters and on lands***
- 3. EVENT: oil spill, an accident***
- 4. DAMAGE EVALUATION***
- 5. DAMAGE EVALUATION EFFECTS AND TIMING***
- 6. VICTIMS: individuals, society, animals, environment***

EX-POST REGULATION

The **Oil Pollution Act** of 1990 (OPA 90) should be considered.

3 different principles at the heart of the law :

1. **Strict liability:** parties responsible for oil spills are considered strictly liable for damages caused even if they have not acted in a negligent way
→ BP
2. **Channels liability:** companies should exactly specify who is to be considered as the responsible party for the liability purposes → the holder of the drilling permit, meaning Bp, is the sole responsible party
3. **Liability limits:** there is the imposition of some caps on the liability of parties responsible for spills → damages are capped at \$ 75 million (luckily, BP is a *deep pocket firm*, it ignored the cap and beared the full costs of responding to the spill)



EX-POST REGULATION

CERCLA charges the reimbursement of the clean-up costs to the liable parties.



Who should pay for the damages?

Three major firms involved: BP, Halliburton, and Transocean.

US report of September 2011: BP can be considered ultimately the responsible of the spill, but the other two companies have to share some of the blame.

Class actions after BP publicly took its responsibility:

- individuals and businesses that considered themselves victims of the oil spill
- typical plaintiff represented by the fisherman



TRIAL



- **Start:** February 25
- **Where:** federal court in New Orleans
- **Parties involved:** a team of private plaintiffs' attorneys, the federal government, the British company BP, the rig owner Transocean Ltd., the cement contractor Halliburton, dozens of company executives, rig workers and expert witnesses.
- **US District Judge appointed:** Carl Barbier, expert of maritime law
- **Main focus:** did BP's actions constitute gross negligence or wilful misconduct?
- **First phase:** identify the causes that lead to the blowout of BP's Macondo well and allocate faults to the companies involved.
- **Second phase:** (scheduled to begin in September) quantify how much crude spilled into the Gulf, explore BP's tentative to stop the flow of oil.

TRIAL

BP:

- **guilty of the death of 11 workers** and other criminal charges
- **paid \$ 4 billion in criminal penalties**
- reached an agreement for a **fine of \$ 1.3 billion**
- new claims: the damages to natural resources
- reached more than \$ 24 billion utilized for the spill-related expenses (compensation for both individuals and businesses and cleanup costs)

Costs may rise → **Clean Water Act**: a polluter has to pay an amount that goes from a minimum of \$1,100 per barrel of spilled oil to a maximum of \$ 4,300 if it is found grossly negligent [\$ 18 billion for BP]

TRIAL

Has BP acted in a grossly negligent way?

- Plaintiffs' attorneys: to complete the drilling project in the fastest way possible, BP gave up safety
- BP: strongly rejects the idea that it acted in a negligent way; Halliburton and Transocean liable
- Patrick O'Bryan, BP's vice president of completions and drilling: BP never decided to decrease the level of safety

BP has sued Transocean for damages, requesting a refund of \$ 20 billion.

U.S. government has sued Transocean (on 3 January 2013, declared guilty of the violation of the Clean Water Act; it paid \$ 1.4 billion in criminal and civil fines and penalties) **and the Halliburton Group** (it reported that the contract relieved them of any responsibility).

TRIAL

Disputes still open between BP and:

- the various countries of the Gulf of Mexico affected by the oil spill
- the rescuers who later accused sickness
- the US government.

EPA has banned the British oil group to:

- compete for the award of exploration licenses in Texas;
- participate in the selection of public contracts in the United States until it has clarified what kind of conduct it will take to prevent another oil spill.

EX-ANTE IMPROVEMENTS

☞ In order to increase the effectiveness of **ex-ante** regulation in the oil industry, we propose the introduction of some new regulations:



- BUILDING PROCEDURES
- DRILLING OPERATIONS
- SAFETY REVISIONS



EX-POST IMPROVEMENTS

How to state who is liable for an oil spill?

1. Identifiable responsible party
2. Strict liability
3. Tax on no compensable risk inflicted
4. Financial capacity's demonstration
5. Damages assessment and restoration
6. Moratorium imposed on all new deepwater drilling

CONCLUSIONS

☞ SANCTIONS

☞ INSURANCE

☞ INFORMATION GAP

☞ POLITICAL COMPROMISES

☞ We are confident that these innovations/implementations will result in a better functioning of the EPA and in less environmental damages.

