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TRENDS IN ENVIRONMENTAL LIABILITY FOR THE OIL & GAS INDUSTRY

Charles C. Steincamp

Environmental Liability Developments for Oil and Gas Operators

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Introduction

Although there are a myriad of environmental laws that may affect oil and gas operations, by far the most significant are those enacted at the federal level. The Resource Conservation and Recovery Act and the Comprehensive Environmental Response Compensation and Liability Act are the most sweeping. While the Clean Water Act and the Oil Pollution Act impose liability for spills of petroleum both require a connection to waters of the United States and are therefore more limited in application. This paper will focus on the liability provisions of these acts as it relates to pollution issues affecting the oil and gas industry and discuss some of the recent trends which may affect the industry. In addition, the recent ruling of the 11th Circuit requiring a permit under the Safe Drinking Water Act for hydraulic fracturing of producing formations will be discussed.

Resource Conservation and Recovery Act (RCRA)

The Resource Conservation and Recovery Act was first enacted in 1976 as part of the Solid Waste Disposal Act. 42 U.S.C. § 6901 et seq. It's focus was originally to regulate waste disposal. It was significantly amended in 1984 in the Hazardous and Solid Waste Amendments which added a number of requirements regarding the management of hazardous waste. The Act's guiding impetus is to avoid prospective problems associated with the disposal of hazardous waste.

When approaching a situation involving RCRA, the first question is what is a hazardous waste. Because RCRA was enacted as part of the Solid Waste Disposal Act, to be a hazardous waste a substance must first fit the definition of a solid waste. However, that requirement usually gives little comfort. First of all, “solid” waste does not have to be solid. In fact, RCRA defines “solid waste” to be “[A]ny garbage, refuse, sludge from a waste treatment plant, water supply treatment plant, or air pollution control facility and other discarded material, including solid, liquid, semisolid, or contained gaseous material resulting from industrial, commercial, mining, and agricultural operations, and from community activities...” The U.S.E.P.A. defines “discarded material to be any material which is “abandoned,” “recycled,” or which is considered “inherently wastelike.” 40 CFR § 261.2(a)(2). Abandoned is further defined to include materials that are “disposed of,” “burned or incinerated” or “accumulated, stored, or treated (but not recycled) before or in lieu of being abandoned by doing disposed of, burned or incinerated.” 40 CFR § 261.2(b). Finally, RCRA defines disposal to include both active and passive releases of waste by “The discharge, deposit, injection, dumping, spilling, leaking, or placing of any solid or hazardous waste into or on any land or water so that such solid waste or hazardous waste or any constituent thereof may enter the environment or be emitted into the air or discharged into any waters, including ground waters.” 42 U.S.C. § 6903(3).

Once a material has been determined to be a solid waste a determination is made whether or not it is hazardous. RCRA defines hazardous waste to include those substances which because of its “quantity, concentration, or physical, chemical, or infectious characteristics *may* cause, or significantly contribute to an increase in mortality or an increase of serious irreversible, or incapacitating reversible illness or pose a substantial present or potential hazard to human health

or the environment when improperly treated, stored, transported, or disposed of, or otherwise managed. EPA is charged with identifying **characteristics** of hazardous waste and **listing** hazardous waste. Therefore there are two methods for determining whether a material is a hazardous waste: test the waste to see if it exhibits the characteristics of hazardous waste; or determine if it or one of its constituents appears on an EPA list of hazardous waste.

Fortunately for the domestic oil industry, Congress has decided that it is better to tax it to death rather than regulate it out of existence. Congress has exempted many of the wastes created during the exploration process from treatment as a hazardous waste. “Drilling fluids, produced waters, and other wastes associated with the exploration, development, or production of crude oil or natural gas or geothermal energy shall be subject only to existing State or Federal regulatory programs in lieu of this subchapter...” 42 U.S.C. § 6921(b)(2)(A).

Therefore, the domestic oil and gas industry has been spared enormous costs associated with disposal of hazardous wastes. The author recently was given a bid of **\$.63 per pound** for disposal of hazardous waste at an E.P.A. approved disposal site. However, as documented in the recent CBS editorial piece by Ed Bradley “Town Under Siege”, even that exemption is under attack by both the EPA and private groups. Even assuming that the exemption survives, that is not the end of the story. The Act also contains a “citizen suit” provision at 42 U.S.C. § 6972(a)(1)(B) and a corresponding section providing a similar right of action for the EPA. This provision allows “any person” to bring a civil action against “any person” including “the past or present generator, past or present transporter, or past or present owner or operator of a treatment, storage or disposal facility, who has contributed or is contributing to the past or

present handling, storage, treatment, transportation or disposal of any solid or hazardous waste which may present an imminent and substantial endangerment to human health or the environment.”

Oil and Gas operations are protected from liability for hazardous waste disposal only to the extent that the waste is related to drilling fluids and produced waters that come within the terms of the exemption in the statute. Clearly, crude oil does not qualify for such an exemption, nor does any of the refined products created from crude oil production. All of these substances contain listed hazardous wastes such as benzene¹, ethyl benzene, xylene among others. See *United States v. Conservation Chemical Co.*, 619 F. Supp. 162 (W.D.Mo. 1985). In addition, many of the normal oilfield chemicals are either listed or characteristic hazardous wastes which would likewise not fit the exploration wastes exemption. Normally, both crude oil and refined products are not within the purview of RCRA, however, when they are released, they are at a minimum solid waste that RCRA requires be cleaned up. There is not an exception for petroleum in 42 U.S.C. § 6972(a)(1)(B). *Zands v. Nelson*, 34 E.R.C. 1561 (S.D. Cal. 1991).

The U.S. District Courts have the authority to order any person liable under the Act to take any action that might be necessary, or to restrain any person from taking action to the extent necessary to address the imminent and substantial endangerment. 42 U.S.C. § 6972 (a)(1)(B)(2). This can include an order to cease and desist from activities or an order to undertake a cleanup of a spill or release. In order to further create an incentive for private citizens to act as “private attorney’s general” the statute further provides for an award of the costs of litigation including

¹ Benzene is a class A human carcinogen.

attorney's fees and expert witness fees to a prevailing party. 42 U.S.C. § 6972(e). A further unnerving aspect of RCRA citizen suit is that there is no statute of limitations, an action may be brought as long as there is an imminent and substantial endangerment to health or the environment. *Meghrig v. KFC Western, Inc.*, 116 S.Ct. 1251 (1996). The citizen suit provision has been relatively little used to address oilfield contamination in the past however, it appears that day is coming. There appears to be a dramatic upswing in reported decisions applying the RCRA citizen suit to either oilfield waste or petroleum products. The American Bar Association has noted that citizen suits have exploded in the 1990's. *National Resources and Environment*, Vol. II, Number 4, Spring 1997.

There are a host of cases filed in federal court seeking an order requiring the cleanup of hazardous wastes resulting from the spill or release of petroleum products. See *Meghrig v. KFC Western, Inc*, supra; *Morris v. Primetime Stores of Kansas, Inc.*, 43 E.R.C. 1762 (D. Kan. 1996); *Zands v. Nelson*, 34 E.R.C. 1561 (S.D. Cal. 1991); *Buggsi Inc. v. Chevron U.S.A. Inc.*, 39 E.R.C. 1526 (D. Or. 1994); *Furrer v. Brown*, 62 F.3d 1092 (8th Cir. 1995); *Williams Pipe Line Co. v. Bayer Corp.*, 694 F. Supp. 1300 (S.D. Iowa 1997); *U.S. v. Valentine*, 38 E.R.C. 2086 (D. Wy. 1994). Several cases have been decided to date concerning whether crude oil is a hazardous substance requiring remediation. Highlights from only a few of the cases are instructive. In the case of *Nixon-Egli Equipment Co. v. John A. Alexander Co.*, 949 F. Supp. 1435 (C.D. Cal. 1996) an action was brought under both RCRA and CERCLA (discussed below) for cleanup of hazardous substances on a former oil field in the City of Santa Fe Springs, California. The field was produced from the 1920's to the 1960's and after the wells had been plugged it was acquired for commercial development by the defendants. Plaintiff leased the property for over 25 years and

finally purchased it outright. Expert opinion in the case established that at least one source of the hazardous substances at the site was crude oil. Because there is no shield from liability under RCRA for crude oil contamination there were few defenses available to the defendant under that act. The defendant argued that the last possible date of pollution was in the 1960's and that the statute of limitations had long run. The court gave short shrift to that argument holding that there was no statute of limitations under RCRA, as long as contamination was present, an action could be maintained. The court denied the defendants motions for summary judgment and allowed the case to proceed on both the RCRA and CERCLA claims.

Likewise in the case of *U.S. v. Valentine*, 38 E.R.C. 2090 (D. Wy. 1994), the U.S. E.P.A. brought an action against Conoco Pipeline Company, Eighty-Eight Oil Company, Phillips Petroleum Company and Texaco Refining and Marketing Inc. among others for cleanup, under the corresponding federal provision of the RCRA citizen suit provision, of a site which was used for processing below grade crude oil. The facility received crude that was below the pipeline standards and processed it into high quality crude. The facility was operated during the 1970's and 1980's. In 1993, the E.P.A. issued an order to a number of defendants requiring cleanup of the spilled oil waste, leaking tanks and saturated soils. The soils and oil waste contained benzene, toluene, ethyl benzene and xylene, which are all hazardous substances indigenous to crude oil. Conoco, Texaco, Phillips, Eighty-Eight and True settled with E.P.A., agreeing to joint and severally conduct a cleanup estimated to cost between \$4.4 and \$8.9 million. In addition, the settling defendants agreed to pay \$300,000 in civil penalties. The non-settling defendants were held liable for contribution and additional civil penalties and injunctive relief as well as fines under the Endangered Species Act and the Migratory Bird Treaty Act.

The *Nixon-Egli* case illustrates the point, crude oil contains hazardous substances and as urban sprawl takes in more and more areas that have formerly been operated as oilfields there will be increasing numbers of actions filed seeking cleanups of oilfield contamination. The focus will tend to be less in areas that are developed as residential real estate, simply because there is a smaller focus on the environmental condition of the property prior to development. However, that creates a further problem. Because these problems are not likely to be discovered until later, the risk maybe even greater. By the time anyone realizes the situation, there will be playgrounds built in contaminated areas, basements set down in contaminated soil, wells for watering lawns spraying contaminated groundwater. Therefore, instead of mere claims for cleanup, there may be additional toxic tort claims raised against the former operator of the wells that caused the contamination.

Comprehensive Environmental Response Compensation and Liability Act (CERCLA)

CERCLA was first enacted in 1980 as part of Congress' knee-jerk response to three well known hazardous waste sites: The Valley of the Drums, Love Canal, and Times Beach. The Act is also known as the "Superfund" due to the fund created from taxes on oil and chemicals that can be used by EPA to cleanup contaminated sites which have become known as "Superfund sites." The Act has become associated with extreme levels of waste and inefficiency. In fact, cleanups now average above \$30 million per site with a substantial percentage of those costs going to administrative costs and litigation.

Liability under CERCLA is based upon a party's connection to either the waste or the real property on which it is located. Liable parties include current "owners or operators of the vessel

or facility” as well as “owners or operators at the time of disposal”; any person who generated the hazardous substance; any person who arranged for disposal, treatment or transportation of a hazardous substance and any person who accepts or accepted any hazardous substances for disposal and selected the site of disposal. These parties are known as Potentially Responsible Parties (PRP’s).

While RCRA is a prospective statute, CERCLA is retrospective. It is designed to provide for cleanup of sites which are no longer active and have essentially been abandoned, however, because of the extremely broad language of the act, its applicability has few limits. CERCLA also requires the reporting of a release of any hazardous substance with fines of up to \$250,000 and imprisonment of up to 3 years for a first offense. 42 U.S.C. § 9603(b),(c). EPA is granted the authority to order that either a removal or a remedial action be taken by a PRP. 42 U.S.C. § 9606. Should a PRP fail to implement the ordered remedy, punitive damages of up to three times the amount of costs actually incurred may be assessed against the noncompliant party. *United States v. Parsons*, 738 F. Supp. 1436 (N.D. Ga. 1990), *aff’d* 936 F.2d 526 (11th Cir. 1991)(PRP held liable for three times the actual cleanup costs of \$753,391.24 for failure to provide ordered response). “Hazardous substances” are defined to include all hazardous substances designated pursuant to RCRA, the Clean Water Act, the Clean Air Act and an extensive list designated pursuant to CERCLA itself.

However, once again the Oil and Gas industry has been spared the economic carnage that was created by CERCLA. The act contains a “petroleum exclusion.” This specifically excludes from the definition of hazardous substance “petroleum, including crude oil or any fraction thereof

which is not otherwise specifically listed or designated as a hazardous substance... and the term does not include natural gas, natural gas liquids, liquefied natural gas, or synthetic gas useable for fuel (or mixtures of natural gas and such synthetic gas).” As can be imagined this has been an incredibly fortuitous provision for oil and gas operators. However, because the oil industry is seen as a deep pocket, there has been continuing attempts to erode the protections provided by the petroleum exclusion. These efforts have been successful in limiting the exclusion severely, and in some jurisdictions the exclusion has been largely circumvented. The decisions are legion which hold that the petroleum exclusion does not apply to hazardous substances that are added to or mixed with the petroleum product during or after use. See *Bunger v. Hartman*, 797 F. SUPP. 968 (S.D. Fla. 1992); *Niecko v. Emro Marketing Company*, 769 F. SUPP. 973 (E.D. Mich. 1991); *Wilshire Westwood Associates v. Atlantic Richfield Corporation*, 881 F.2d 801, 805 (9th Cir. 1989); *United States v. Western Processing Co., Inc.*, 761 F. SUPP. 713 (W.D. Wa. 1991); *United States v. Alcan Aluminum Corporation*, 755 F. SUPP. 531, 539 (N.D. N.Y. 1991); *New York v. Exxon Corporation*, 744 F. SUPP. 474, 489-90 (S.D. N.Y. 1990); *Washington v. Time Oil Company*, 687 F. SUPP. 529, 531-32 (W.D. Wa. 1988).

There are two cases that are of particular note to the Oil and Gas Industry. The first is the case of *Cose v. Getty Oil Co.*, 37 E.R.C. 1153 (9th Cir. 1993). In that case Getty Oil had disposed of tank bottoms from crude oil into what was known as the “Gravel Pit” near its pumping station in Tracy, California. After the Tracy facility was closed in 1968, Getty eventually leveled the gravel pit with topsoil and sold the 40 acre tract on which the “Gravel Pit” was located to Don Cose in 1974. Mr. Cose began to develop the property for residential housing in 1987 and in the process discovered a “subsurface asphalt or tar-like material” on the property. A

consultant confirmed that the tar-like substance contained 10.5 parts per million of Chrysene, a known carcinogen. The crude oil in the region was found to contain chrysene at 28.0 ppm. Based on the results of the consultants study, Cose filed suit under CERCLA to recover response costs for cleaning up the Gravel Pit property.

Getty filed a motion for summary judgment contending that Cose could not prove that they had disposed of a “hazardous substance” within the meaning of CERCLA. The district court granted the motion and Cose appealed to the 9th Circuit. After an exhaustive review of existing case law, legislative history, and EPA guidance, the 9th Circuit concluded that the petroleum exclusion did not apply. The Court reasoned that the crude oil tank bottoms are clearly “waste materials.” Getty disposed of the tank bottoms with no intention of recycling them. Further, the court found that the tank bottoms are not “petroleum or any fraction thereof” because they are not petroleum at all. Crude oil tank bottoms are merely comprised of water and suspended solids that settle out of crude oil and collect at the bottom of crude oil storage tanks en route to refineries. Therefore, the court found that since the presence of Chrysene at the site was undisputed, Getty was liable for the cleanup costs at the site as a matter of law.

The next case which focuses on liability for oil production that deserves mention is the *Nixon-Egli* case discussed above with regard to RCRA liability. In that case contamination was found on the site of an old oilfield. The plaintiffs brought an action under both RCRA and CERCLA as well as various State law causes of action. The plaintiffs consultant had concluded that the main source of contamination was crude oil. But the lead, the main hazardous substance at the site, was not solely from the crude oil. Following the reasoning in *Cose* the court found

that drilling by-products such as the drilling cuttings and the drilling mud would not fall within the petroleum exclusion. Therefore, if the lead at the site came from the crude oil, it would fall within the petroleum exclusion and would not be a hazardous substance under CERCLA. However if the lead was not from a petroleum source, it was a hazardous substance and could form the basis for CERCLA liability.

It is clear from an examination of the case law that oil and gas operators are on the horns of a dilemma. The combination of RCRA and CERCLA essentially avoids any protection afforded to oil and gas operators by the terms of either statute. While drilling fluids and production wastes may not be a hazardous waste under RCRA, they can form the basis for CERCLA liability. At the same time while petroleum may be excluded from CERCLA liability, it contains hazardous substances that require remediation under RCRA. Obviously, when these laws are used in concert, there is no safe harbor. Since the enactment of these laws environmental groups and courts have focused on non-petroleum type wastes, however, the case law seems to indicate that the honeymoon is coming to an end.

The question remains what can be done to avoid the massive liability from these two acts? The best answer is two fold: first, a concerted effort should be made to use legal structures that insulate the principals in any oil and gas venture from personal liability. The oil industry has long operated on oral agreements and general partnerships, even on multi-million dollar prospects. That day is coming to an end. Second, the industry must become proactive. Look before you leap. Whether buying existing production or taking a new lease it is important to pay careful attention to the environmental condition of the property. It is also important to respond quickly

in the event a spill or leak occurs. Clean up the mess when it happens rather than ignoring it and waiting until the problem is far worse. The cost savings can be enormous over waiting until a governmental agency forces a clean up or a letter arrives from an attorney representing parties affected by the pollution.

Safe Drinking Water Act

Another alarming development for the oil and gas industry is the recent case of *Legal Environmental Assistance Foundation v. E.P.A.*, 45 E.R.C. 1033 (11th Cir. 1997). LEAF filed an action for review of a ruling by E.P.A. denying their request to withdraw approval of the Alabama UIC (Underground Injection Control) program. UIC programs in the States are required by Part C of the Safe Drinking Water Act. The Act requires that E.P.A. promulgate regulations establishing minimum standards for State UIC programs. States must then submit to E.P.A. their proposed regulatory program to receive approval to regulate underground injection activities within the State. Among the minimum requirements is that the State must prohibit any “underground injection unless authorized by permit or rule.” 45 C.F.R. § 145.11(a)(5). Underground injection is defined to be “the subsurface emplacement of fluids by well injection.” 42 U.S.C. § 300h(d)(1).

Alabama has extensive reserves of coal-bed methane. However, to produce the methane at an economic rate it is necessary to hydraulically fracture the reservoir to increase permeability. Guar gel, nitrogen or carbon dioxide gases, gelled oil, diesel oil, sodium hydroxide, sulfuric acid and fumaric acids are used as fracture fluids. After the wells are fractured the fluids are pumped out to start the flow of the methane gas. However, the Court found that 20-30% of the fluid remains in the formation. Hydraulic fracturing is not regulated under the Alabama UIC program.

EPA argued that their interpretation of the statute was that it only required regulation of wells whose “principal function is the injection of fluids into the ground.” The Court held that the statute was clear that all underground injection is regulated under the statute. The only issue was whether the activity falls within the definition of underground injection. Using the statutory language the Court found that hydraulic fracturing precisely fit the definition. Clearly, fracturing involves injection of fluids into the subsurface. Therefore the Court granted LEAF’s petition for withdrawal of the Alabama UIC program approval.

The effect of this decision cannot be overstated. Hydraulic fracturing is an extremely common well stimulation technique. The prospect of obtaining a UIC permit each time a well is hydraulically fractured is daunting. Anyone familiar with the process will realize that it is extremely time consuming to obtain such a permit. A new permit requirement will no doubt paralyze the industry. EPA realizing that fact has asked for reconsideration of the Courts decision, and vows to appeal. However, the prospects are not good. The most realistic chance of relief will have to come from Congress.

The future appears ominous for oil and gas operations within the continental United States. The Oil industry has largely escaped the environmental slaughterhouse so far, however, recent judicial decisions and the Ed Bradley Special Report that aired recently indicate that the environmental movement is beginning to focus on the industry. The time is now to be proactive both in avoiding or eliminating environmental problems and also in convincing legislators that further liability and regulation will destroy the domestic oil and gas industry. To quote a recent citizen suit plaintiff, if you violate any requirement of an environmental permit “you are toast.”