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of a private party), the RAC enjoys immunity from liability for damages unless the RAC's actions were intentional, reckless, or grossly negligent. This limitation is not subject to the same exceptions as exist in AS 46.03.825, such as not being contrary to orders of the persons in charge and not involving personal injury or death. It does apply to the efforts of governments themselves, acting as emergency responders.¹¹

The Good Samaritan statute raises some difficulties which the courts have not yet addressed. When a RAC contracts with a governmental agency to provide response services during a declared emergency, is it acting "at the request of a governmental agency" so that its liability is limited by the immunities granted by the Good Samaritan statute, rather than by the provisions of the contract? We believe that the contract terms (e.g., an agreement by the RAC to indemnify the State for the RAC's negligence) would probably be held to control, as an implied waiver by the RAC of its statutory immunities. But the result is far from certain and it is likely that a RAC in a potentially liable situation would make the claim to Good Samaritan immunities. Would the original spiller be immunized under the Good Samaritan statute if it took steps at the request of a government agency and those steps caused additional damages? It seems unlikely that the legislature intended to immunize the party causing the problem in the first place, when its response actions are arguably required by law, but the legislature did not state its intentions explicitly in the statute; whether this limitation should be read into the statute may need to be litigated before a clear answer emerges. Finally, the wording of the statute implies that a government which provides direct response services does not itself come within the immunities granted by the statute; but if the government's response is at the request of another governmental agency, it may well be covered by the statute. Clearly the Good Samaritan statute was not drafted with response action contractors and oil spills in mind, so it does not fit the situations likely to be encountered in the field very precisely. In any future overhaul of the main RAC immunity statutes, the Legislature would do well to harmonize the Good Samaritan statute at the same time.

In summary, state statutes place a heavy burden of strict liability on a variety of persons involved with storage or transportation of oil when the oil is spilled. There already is a Good Samaritan statute affording

¹¹ Bunting v. United States, 662 F. Supp. 971 (D. Alaska 1987), aff'd 884 F.2d 1143 (9th Cir. 1989).

immunity from strict liability and liability for negligence to persons who respond at the government's request in a declared emergency. The legislature has also provided a broad set of exemptions from liability for all but grossly negligent and intentional acts, applying to most oil spill damages. But these exemptions are set to expire on July 1, 1992, when somewhat less generous immunities applicable to hazardous substance spills are set to take their place. It is possible that the current limitation on liability may prevent recovery of damages by parties injured by RACs in some situations where there is no other financially solvent responsible party.

CONTRACTUAL MODIFICATIONS OF OIL SPILL LIABILITY

As noted above, the Legislature modified common law liability for oil spills by its enactment of key oil spill statutes. In particular, enactment of AS 46.03.823 and .825 were promoted by RACs and segments of the oil industry as a means to reallocate -- and in some cases lessen -- the overall liability burden. But a second, and possibly equally effective method of shifting the liability burden, is through contractual arrangements. This section of the report will examine the contract terms negotiated by RACs and their employers. In particular it will examine indemnification provisions and insurance provisions, which are the main devices used in RAC contracts to shift the ultimate burden of spill liability. It will also focus on the differences in typical contract terms negotiated by small and large RAC businesses, and in the contracts of RACs which are normal business corporations and those which are consortiums of major oil companies.

As a preliminary, it should be noted that parties cannot alter a statute with a contract. Hence a party liable under AS 46.03.822 cannot actually make itself not liable by a contractual arrangement with another party. But a potentially liable party can -- as the contracts discussed below show -- arrange to have another party bear the burden of its liability, i.e., require the second party to pay amounts required to be borne by the first party under the statute. Hence, as long as the party agreeing to carry the actual burden is able to pay it, the party liable under the statute effectively escapes the liability.

The Contracts: A Brief Summary

The Department of Environmental Conservation has identified most of the entities providing professional response action services and sent each of them a questionnaire on RAC issues. We have obtained all of the questionnaires returned by this time as well as a collation by DEC of representative RAC service contracts.¹² Copies of the contracts and questionnaires are attached as an appendix to this report. The following is a brief summary of the common

¹² As part of the contingency plan approval process, every contingency plan holder which relies on a RAC for all or part of its spill response is required to submit a copy of the RAC contract to ADEC with the contingency plan. Naturally this does not include contracts which are negotiated on a spot basis at the time of an actual spill, but standing contracts for services which are a formal part of a contingency plan.

provisions found in the contracts.

The most striking fact is the diversity of the contracts. Generally, the larger and more sophisticated the business, the more professional is its contract drafting and the more likely it is to have carefully crafted provisions protecting the RAC's interests. This is particularly the case with the contracts written by Alyeska Pipeline Service Company (which provides RAC services to marine transporters of TAPS oil of Valdez) and by CISPRI and Alaska Clean Seas, the cooperatives made up of major oil producers for spill response in Cook Inlet and off the Arctic and west coasts of Alaska, respectively. At the other end of the spectrum are small companies for whom spill response is just one of their activities. It is a fair assumption that many smaller companies hired at the time of the spill to perform general work, e.g., earthmovers or haulers, have even less sophisticated contracts which provide even less protection against liability.

Also noteworthy is that even among established companies which have obviously used legal counsel in drafting contracts, there is no real uniformity of contract terms. Also, a single RAC may have different provisions in contracts with different employers, reflecting, it appears, the relative negotiating acumen of each employer. An example is the two contracts of VRCA, an established spill response company, with Tesoro and with Mapco, two medium sized refiners. VRCA's contract with Tesoro reflects careful draftsmanship, and gives significant protections to VRCA against bearing liability for mishaps during its cleanup. But when VRCA negotiated a later contract with Mapco, Mapco was able to negotiate significantly better terms for itself than Tesoro had.¹³

Reviewing all the contracts and questionnaires together, we can reach the following general conclusions on types of contractual provisions of special importance to RACs:

¹³ For example, Mapco obtained agreement that VRCA could be liable to Mapco for VRCA's own negligence or gross negligence; Tesoro agreed to language that can be interpreted to be a complete indemnification of VRCA for indirect damages, i.e., damages to a third party. Mapco obtained an agreement that VRCA could not subcontract without consent; Tesoro agreed that VRCA could subcontract without consent. Mapco obtained language agreeing that VRCA's actions were not under Mapco's control, while Tesoro stated that it could control VRCA's actions, a significant difference because the ability to control an independent contractor is a prime test of whether a principal can be vicariously held liable for the misdeeds of its agent (see below, p.27).

Obligations of Parties

The contracts we examined were all non-specific as to duties to be performed by the contractors. Typical provisions read, "scope of work...to respond to any cleanup effort requested"... "shall commence as soon as possible"... "an indefinite quantity of work/services". Most refer generally to spill "response" or "cleanup" without greater specificity, and only a few explicitly relate performance to contingency plans.¹⁴ The contracts are, by definition, contingency contracts, i.e., general agreements that a certain type of service shall be available upon some future contingency and when the principal issues a work order or notice to proceed. They provide very little detail about specific services or products, and although the RAC in each case agrees to perform, the client must invoke the contract first by issuing a specific request for the services in the event of a spill. Alyeska's response contract is unique among those we reviewed in explicitly limiting response to the first 72 hours and requiring a hand-off of response duties to the client after that time. In none of the contracts is the client required to use the services of the RAC, i.e., the client chooses when and whether to invoke the contract. None of the contracts contain specific performance standards (e.g., x numbers of vessels and y personnel mobilized within z hours of call-out).

Most of the contracts do not have termination dates built in, while some have annual expirations. Some permit termination by either party upon a notice period, e.g., five days or thirty days. Alyeska's response contract requires six months notice for termination by either party, and also permits Alyeska to suspend work upon the insolvency of the client. Some contracts permit termination only upon default by the other party.

Most of the contracts we examined did not specify remuneration but indicated standard rates of the RAC at the time of use. Alyeska's contract simply calls for reimbursement of its expenses without setting out rates. In few cases the RACs declined to provide information on remuneration.

¹⁴ Alyeska's response contract does define its proposed services in terms of spill response services under contingency plans.

Concern regarding claims

The questionnaires we examined showed a near uniformity of responses regarding concern about adverse claims for damages caused during a spill response. Not a single RAC had experienced any claims arising from spill response.¹⁵ At the same time almost all of them considered the potential for claims to be a concern. We believe this dichotomy reflects the uncertainties that exist about spill damage claims and the great cost in both litigation expenses and liability when litigation actually occurs. Hence it is not surprising that RACs attempt to use means such as indemnification and insurance requirements to deflect potential exposure, even without a history of such claims.

Indemnification provisions

"Indemnification" generally means the obligation of one party to make good a loss suffered by another party.¹⁶ It is very common in contracts for one party or the other to attempt to shift to the other party the burden of bearing liability, either liability created by the first party's acts or by the second party's acts. The most common use of such provisions in RAC contracts is for RACs, as independent contractors, to require the other party to the contract (usually the responsible party for the oil spill) to indemnify the RAC for liability that results from the response action. A typical provision requires the responsible party to "defend, hold harmless, and indemnify" the RAC from claims arising out of the response action (essentially defend claims against the RAC and pay any judgments against the RAC). All of the contracts with indemnity provisions require at least that the responsible party is to indemnify the RAC for claims arising out of negligent acts by the responsible party and arising out of

¹⁵ There is one obvious exception which did not show up in the questionnaires. The response effort in the Exxon Valdez case resulted in numerous claims against Alyeska, the State, and the Federal Government for improper handling of the spill response. As defined in state law, all three of those entities were response action contractors. It is undeniable that in any sizeable spill the response itself will be examined critically and may be fertile grounds for legal claims, apart from the original spill. So far, however, there appears to be a distinction in whether RACs are targeted as defendants between actual field response companies and either governments or entities like Alyeska, which many plaintiffs may view as surrogates for the owners.

¹⁶ *Fairbanks North Star Borough v. Kandik Constr. Co.*, 795 P.2d 793 (Alaska 1990).

compliance with government requirements; some require indemnification also for all claims arising out of the RAC's own negligence, or even out of the RAC's own grossly negligent or intentional acts; and some (notably those of Alyeska and the industry coops) require indemnification for all claims including those arising out of the RAC's actions, no matter who was at fault.¹⁷

To the extent that these contracts require another party to bear the burden of the RAC's own gross negligence or intentional acts, they go beyond the relief given RACs by AS 46.03.825, which maintains RAC liability for grossly negligent and intentional acts. It should also be noted that most of the contracts with aggressive indemnity provisions also do not have the exception in .825 for claims for personal injury or death.

Some RACs agreed to hold their clients harmless (i.e., indemnify them) for the RAC's own negligence. In only one of the contracts we reviewed was there a basic two-sided indemnity agreement. The Chempro contract has Chempro indemnifying the client for negligent or wilful acts by Chempro employees, and the client indemnifying Chempro for negligent or wilful acts by the client's employees or subcontractor's employees. Also, when Chempro causes a loss but not through Chempro's own negligence (e.g., through application of strict liability to a Chempro action), the client indemnifies Chempro. Hence the RAC is relieved of strict liability but both sides bear the burden for their own negligent or wilful acts.

It is not certain that the contractual indemnity provisions will actually succeed in shifting the burden of liability to another party. The courts have defined areas in which indemnification provisions will not be upheld because the

¹⁷ The Alyeska contracts are the best example of a RAC with bargaining power crafting contract terms to protect itself to the maximum. Its contracts require the client to give complete indemnification, including for liability arising out of Alyeska's own negligence. It is arguable that the Alyeska/BP contract also provides for indemnification for liability arising out of Alyeska's own gross negligence or intentional acts. (Tesoro was able to negotiate language that excludes indemnification for grossly negligent or intentional acts.) One compelling fact is that Alyeska, when it contracts with others to serve as RACs for itself, requires its RACs to indemnify Alyeska; hence it protects itself from both directions. Finally, as will be noted later, Alyeska requires its clients to maintain financial responsibility far in excess of what any other RAC requires from a client.

are contrary to "public policy", and would tend to promote a breach of a duty owed to the public at large.¹⁸ The activities identified in this category tend to be those in which there needs to be a constant guarding against negligence. In a case involving operations of an airport, for example, the Alaska Supreme Court refused to enforce an indemnification provision in favor of the State as airport operator because of the importance of avoiding a reduction in the State's incentive to avoid negligence.¹⁹ In contrast it permitted enforcement of an indemnity provision in a highway maintenance contract, because the clause was only a minor disincentive to proper highway maintenance.²⁰ These cases are not limited to indemnification of governments or other public entities, but include public utilities and common carriers. Generally the activity in question must be one in whose safety the public at large has a significant interest. There is an open question whether indemnification of RACs for their activities during a spill would be considered in violation of the public duty exception.²¹

The basic theme of a review of all the contracts is that there is no uniformity, but that most RACs make some attempt to shift some portion of potential liability to the responsible party through indemnification provisions. The questionnaires indicated that except for Alyeska and the two industry cooperatives, none of the RACs required indemnification for their own actions in all circumstances. Generally, we believe the degree of aggressiveness in demanding indemnification in RAC contracts corresponds to the RAC's business sophistication and its negotiating leverage. In the most

¹⁸ See *State of Alaska v. Korean Airlines*, 776 P.2d 315 (Alaska 1989); *Burgess Construction Co. v. State of Alaska*, 614 P.2d 1380 (Alaska 1980); *Northwest Airlines v. Alaska Airlines*, 351 F.2d 253, 258 (Ninth Cir. 1965).

¹⁹ *State of Alaska v. Korean Airlines*, 776 P.2d 315 (Alaska 1989).

²⁰ *Burgess Constr. v. State*, 614 P.2d 1380 (Alaska 1980).

²¹ AS 45.45.900 explicitly bars indemnification provisions for a variety of injuries in construction contracts, on the grounds that they are against public policy. This statute is basically a codification of the common law principle discussed above. However, in 1986 the legislature amended the statute to state that it did not affect the validity of an indemnification agreement "respecting the handling, containment or cleanup of oil or other hazardous substances..." Note that this amendment did not validate such indemnification agreements, but merely stated that the statute did not invalidate them. Hence it is still an open question whether the courts, applying common law principles, would uphold RAC indemnification agreements.

aggressive contracts, the shifting of liability goes well beyond that available to RACs under existing statutes.

Insurance requirements

Some -- but not all -- of the RAC contracts we examined require that the client carry insurance which would cover some portion of the total liabilities arising from the RAC's activities. Whether insurance is required, in what amount, and whether the insurance must explicitly identify the RAC as a third party beneficiary of the insurance, varies widely. And again the variances appear to depend on the sophistication and bargaining power of the RAC.

Insurance requirements appear to run in both directions in these contracts, i.e., in some cases the client requires the RAC to have insurance, and in some cases the RAC requires the client to have insurance. The latter instances are generally those in which the RAC also requires indemnification by the client. An insurance requirement is a natural corollary to indemnification, since indemnification is meaningless unless there exists the financial means to bear the liability.

What is particularly interesting is that most of the contracts requiring insurance do not specify particular amounts. This may reflect in part the difficulty of predicting liability exposure of either the client or the RAC in any particular instance, or it may reflect the assumption by RACs that insurance held by a client who is a potentially responsible party, to protect against the party's own liability, will also be adequate to protect the RAC.

The only contracts we found in which specific amounts of insurance were required by RACs were those of CISPRI, the Cook Inlet industry cooperative, and Alyeska. CISPRI requires its clients to show at least \$10 million in insurance which includes CISPRI as a named additional insured. Alyeska, in what to our knowledge is an entirely unique requirement, has in the past required one billion dollars in financial responsibility.²² Alyeska required that any insurance used to show financial responsibility be directly actionable,

²² "Financial responsibility" means proof of ability to pay liabilities, and generally entails a showing of some combination of insurance, "self-insurance" (a showing of net assets available to satisfy legal judgments), bonds, guarantees, and letters of credit.

i.e., it would permit an injured party to bring its claim directly against the insurer instead of having to sue the insured party first. This requirement presented a major problem for Alyeska's clients since direct action insurance is currently not available in the maritime insurance market. Starting in October 1991 Alyeska requires that if a combination of insurance and other means of demonstrating financial responsibility is used, the total which the client must show is \$1.2 billion. That amount must be made up of a combination of general business liability coverage, P&I insurance²³, and excess pollution coverage. However, according to Tesoro Alaska, Alyeska has dropped the requirement that insurance be directly actionable.

Alyeska officials have told us that the amount it now requires, \$1.2 billion, was arrived at by calculating the maximum amounts for which Alyeska could be held liable in responding to a spill. The amount certainly exceeds any figure that anyone has proposed for the State to require as financial responsibility for the same activities, or which, to our knowledge, any other response organization has required of a potential client. The requirement has caused a considerable amount of difficulty for some of Alyeska's clients²⁴ and was the prime motivating factor behind passage of the bill which became AS 46.03.825, limiting RAC liability.²⁵ Currently, there is no legal limitation on the extent to which a RAC may require insurance or other concessions before it enters into a

²³ P&I insurance is coverage for losses by protection and indemnity clubs whose members are vessel owners. P&I clubs are a primary and established form of maritime insurance.

²⁴ The chief difficulty was for Tesoro Alaska, which charters vessels to take TAPS oil from Valdez to its refineries, and which is the only entity now transporting oil from the Valdez terminal which is not either an owner company of Alyeska or a major oil company. Unlike the major companies, Tesoro is unable to make its showing of financial responsibility through "self-insurance" (a showing of net worth) and already available insurance. Since Alyeska dropped the requirement of direct action insurance, Tesoro has been able to arrange coverage meeting Alyeska's requirements, but the cost of insurance in such an amount puts companies which must obtain this insurance at a disadvantage compared to the larger owner companies which have enough assets to self-insure.

²⁵ A number of legislators involved in the passage of the bill expressed the belief that providing relief to response action contractors was necessary to convince Alyeska to lessen its requirements for providing RAC services in Prince William Sound, and hence relieve Tesoro of its heavy insurance burden. However, as noted above, following passage of the bill Alyeska raised rather than lowered its financial responsibility requirements for Tesoro.

contract with a client.²⁶ It may be possible for the State to legislate such restrictions -- for example, prohibiting financial responsibility requirements in excess of what the State itself requires for entities in similar situations -- but such legislation would raise legal and practical problems. Legally, if the result were to bar a business from protecting its assets in a reasonable way, it could be held that the State had performed a "taking", i.e., had appropriated some part of the business's value and was therefore required to compensate the business. The obvious practical problem is that the more risky the State makes a potential business opportunity, the less likely it is that businesses will enter into it. The State may prohibit certain contract terms, but it cannot require a business to enter into a contract in the first place. In short, State restrictions on RAC contracts could simply result in fewer RACs willing to engage in response actions.

In summary, it is to be expected that RACs which require indemnification also require proof of insurance adequate to fulfill the indemnification requirement. However, we are unaware of any situation in which a response organization has required the amount of financial responsibility required by Alyeska.

Control of Cleanup and Independent Contractor Status

One final aspect of the contracts we examined shows lack of uniformity regarding control of cleanup operations. Some of the contracts include acknowledgement that the client will control and direct the cleanup operations. A few are directly the opposite and include recitations that the client is only interested in the result and will not attempt to control the cleanup operations.²⁷ These contrasting provisions reflect real but incompatible concerns of the clients.

²⁶ If a RAC were discriminatory between different clients, for example putting heavier burdens (or impossible burdens) on some potential clients which it did not place on other clients with which it has a corporate relationship, it is possible that an antitrust violation could be found. Antitrust violations depend on specific facts, however, so it would be unwise to speculate in general terms about the success of such actions.

²⁷ See the CISPRI contract as an example of a client disavowing any control of the cleanup. Interestingly, the two VRCA contracts take opposite tacks on this point: VRCA's contract with Tesoro permits the client to control the cleanup while VRCA's contract with Mapco bars Mapco from control.

On one hand, clients, as potentially responsible parties for the original spill, are concerned that the liability laws are so broad that all damages from a spill which are reasonably foreseeable may be imputed to them, so they have an incentive to oversee the cleanup and maximize its efficiency. Naturally the clients are also concerned about their ability to keep a cap on expenses by RACs. But on the other hand, the clients are concerned to avoid vicarious liability under the theory of respondeat superior. Respondeat superior requires that an employer or principal bear the liability for acts of an employee or agent committed during the course of the employment. There is a recognized exception to the respondeat superior doctrine for acts of an independent contractor, but only if the client does not actively control the actions of the contractor.²⁸ Hence there appears to be a tactical difference of opinion among the clients of RACs over whether maximizing control over RAC activities is preferable or whether distancing oneself from RAC activities is more advantageous.²⁹

²⁸ See Restatement (Second) of Torts, §414; Prosser and Keeton, Law of Torts, §71 (5th Edition 1984); *Everette v. Alyeska Pipeline Service Company*, 614 P.2d 1341 (Alaska 1980); *Hammond v. Bechtel*, 606 P.2d 1269 (Alaska 1980).

²⁹ Several cases indicate that the responsible party which engages a RAC but disavows control of RAC activities may be held responsible for damages caused by the RAC, despite the independent contractor exception to the respondeat superior doctrine. The courts have held that the duty of due care in certain activities -- mainly those with a high potential for injury to the public and where the work itself is inherently dangerous -- is non-delegable. In other words, a party responsible for such an activity may not insulate itself from liability for the harm that results by engaging an independent contractor to do the work. Examples of such activities are common carrier duty to transport passengers safely, the duty of a railroad to fence its tracks, and the duty to provide lateral support for land adjacent to others; the duty to operate airports safely; and the duty to provide safe hospital emergency rooms. See *Jackson v. Power*, 743 P.2d 1376 (Alaska 1987); *Alaska Airlines v. Sweat*, 568 P.2d 916, 925-26 (Alaska 1977).

THE STATE'S RELATIONSHIP TO RACS

The State and liability

The first point to realize regarding the state's relationship to RACs is that it is itself both a RAC and an employer of RACs. Every time the state sends personnel to respond to a spill, it is a RAC; every time it engages others to respond, whether for pay or as volunteers, it is employing a RAC. So the State encounters most of the same problems as other RACs and other RAC employers.

The State, as a sovereign, enjoys sovereign immunity, that is, immunity from liability because of its status as a sovereign government. Sovereign immunity, however, is more often than not a hollow protection because of the many exceptions to the doctrine. In a nutshell, although the state probably does not have a duty to others to respond to spills³⁰, when it does respond (as it inevitably will with large spills), it has a duty to do so with at least some degree of care. Its own actions in the field which cause injuries are likely to give rise to liability just as they would with a private RAC. But, as with private RACs, the state is not liable except for grossly negligent and intentional misconduct, as long as its actions are taken in response to an emergency. (This limited immunity, given at AS 46.03.822(h), is in addition to whatever immunity the state obtains with other RACs under AS 46.03.825.)

Likewise, a contractor acting as a RAC for the State can cause the state to incur liability, subject to the same rules as for private employers as to respondeat superior and non-delegable duties. The State may attempt to fend off liability from below by requiring RACs it employs to indemnify it for their misdeeds, and it could attempt to require indemnification for its own misdeeds, but it would face the same difficulties mentioned above regarding non-delegable duties of care and with the public policy concern over insulating itself from liability for damages it causes.

As to restricting its liability when it acts as a RAC for another responsible party, the state's quandary is that it becomes most active in field

³⁰ The exception is when the state itself causes a spill, in which case the state is obligated to contain and clean it up like anyone else under AS 46.04.020.

response when there is no clear responsible party and when it takes on a spill response on its own initiative. In such cases there is obviously no way to shift liability for response mishaps to another party.

One other aspect of state involvement deserves mention. When a responsible party engages a RAC, there is usually a provision requiring the client to indemnify the RAC from liability arising from carrying out the orders of an authorized state or federal official. But what of the liability of that official or that government? The likelihood is that the RAC or its client will attempt to shift the ultimate burden of liability onto the government by proving that the government action was itself the cause of the damage. There is no protection or meaningful limitation on such suits, unless the government can convince the court that as a RAC, within the broad meaning of that term in AS 46.03.825, the government comes within the protections of that statute. To our knowledge this possibility was never considered during any of the legislative debate on that statute. Further, it is an open question whether the terms of the statute would be interpreted to apply to the governmental oversight function as well as to actual fieldwork. But neither is there any clear exclusion of the government as RAC from the provisions of Section 825.

In summary, the State is not in any clear way different from any other RAC or employer of a RAC, and would likely share the same legal burdens. It is an open question whether the state can limit its own liability under the terms of AS 46.03.825.

The State and control of response activities

Since holders of contingency plans and other potentially liable spillers of oil have moved toward greater use of independent RACs to perform spill response, there is an obvious concern. Does the State have the same control over a RAC as it would over the RAC's client? In other words, how can the State ensure that a RAC which is an essential element of a cleanup actually takes the field and performs according to an approved plan and under the direction of government authorities? Under existing law most of the State's authority over RACs is indirect and exercise of the authority could be cumbersome if it were resisted. Reexamination of that authority is warranted.

As noted above, the current RAC contracts we have examined are

two-party documents with no participation by the State and few references to either the State or any other governmental authority. The only common reference to governmental oversight -- and it exists in only the more sophisticated contracts -- is a provision requiring the client to indemnify the RAC for liability incurred while carrying out the orders of a governmental authority. This provision may be an implicit recognition that in the field, during the heat of initial response, the RAC will effectively be under the control of whatever governmental official has jurisdiction. But we do not believe it can be taken as a legal concession of that authority, enforceable by the government agency. We perceive no intent in any RAC contract to place the State (or any other government) in the position of a third-party beneficiary, that is, to empower the State to require the parties to the contract to abide by it.³¹ In any case, even if the State were an implied third-party beneficiary, it would require litigation over that point to require a balking RAC to perform, so would not be of benefit in ensuring immediate field response.

Under existing law, the State's authority over a RAC comes from two sources, both problematic. First, the State has authority over the person causing the spill, who has a legal obligation to contain and remove it. AS 45.04.020. This legal requirement would support an injunctive action by the State, i.e., a request for a court order requiring that person to conduct a response. If the spill created an emergency situation there would also be legal authority to require the spiller to take immediate action to abate it. AS 46.03.865. It is arguable that the emergency order authority also permits the State to order a RAC to participate in the response, since AS 46.03.865 does not limit emergency orders to actual spillers, but such an extension of the statutory authority has never been tested and could be found to be lacking as to a person with no preexisting legal obligation regarding the spill. A stronger argument can be made for emergency orders directing RAC participation when the RAC has committed itself by contract to the spiller to perform a response, but the outcome of a legal challenge is far from certain. In any case both injunctive actions and administrative emergency orders have a significant drawback in that they are time-consuming, especially the injunctive action, when a crisis does not permit waste of time. Moreover, although they may be useful in getting a RAC into the field in the first place, they are far too cumbersome to use in directing the daily

³¹ In one of the contracts examined, CISPRI's contract with Chevron U.S.A., the contract explicitly disavows the existence of any third party beneficiaries, both private and governmental.

or hourly field tasks actually performed during a response.

The second existing avenue for State authority over RAC participation in a spill response comes from the contingency plan requirements of AS 46.04.030. That statute puts a clear burden on a potential spiller to have, and to demonstrate upon request of the State, minimum capabilities for responding to a spill. The regulations implementing the statute require, at 18 AAC 75.425(e)(3)(H), that the plan holder who uses the services of a RAC provide detailed information on the RAC, its equipment and services, and its contract. The regulations do not prescribe particular provisions which must be put in the RAC contract, but do state that reliance on a RAC does not relieve the plan holder of its responsibilities. This combination of requirements gives a plan holder a firm incentive to require, in its RAC contract, that the RAC provide the services required of the holder in the manner required of the holder. If the RAC fails to perform the plan holder assumes the significant liability that would attach if the plan holder itself failed to perform a response according to the contingency plan. (We note, however, that none of the RAC contracts we reviewed has any specific provision both tying RAC performance to the specific duties in the contingency plan and putting the RAC in jeopardy of bearing the plan holder's liability for not performing according to the plan, though, as a matter of contract law, the plan holder might be able to shift the liability to the RAC if the RAC failed to perform under the contract without legal justification.) In any case the State now has the authority to require the plan holder to demonstrate, on a regular basis, the ability and willingness of its RACs to perform their role under the contingency plan, and to revoke plan approval if the RAC is unwilling or unable to perform. If properly exercised, this authority places the burden -- and the penalty for failure -- on the plan holder to ensure RAC performance, and it should eliminate most problems regarding RAC ability to perform. However, it does leave a narrow but critical gap as to unforeseen inability or refusal of the RAC to perform after a spill actually occurs. The State's direct authority under the contingency plan laws is over the plan holder, not the RACs, so there is little legal basis for directly controlling RAC performance rather than plan holder performance.

There are several ways in which State authority over field actions by RACs could be strengthened. On the regulation level, the State could require that any contractual component of a contingency plan, such as a RAC, agree in writing that it will accept State authority over its field actions to the same degree

that such authority exists over the plan holder. The regulations could also require that RACs which are components of a contingency plan also agree in writing to be bound by the same requirements put on the plan holder to give immediate notification to the State of inability or unavailability to perform. This requirement could be supplemented by requiring a RAC wishing to terminate a contract to give prior notice, sufficient to permit substitute services to be secured, to both the plan holder and the State. It may also be possible to require that a RAC performing as part of a contingency plan agree in writing to accept joint liability with the plan holder for damages which result from failure to carry out its part of the contingency plan.

There is an obvious danger to imposing such requirements on RACS, namely that the contractors perceive them as so onerous that they simply choose not to enter into the contracts in the first place. While the plan holder would then be obligated to provide the mandated services in some other way, the absence of specialized response contractors could significantly decrease the efficacy of the response.

One other possibility for increasing State control over RACs would be to require RACs -- or at least those RACs which are component parts of contingency plans -- to have a direct contractual relationship with the State before its role in the contingency plan were approved. This option offers little advantage. Although couched in terms of a voluntary contract, such a requirement would in reality be a mandated burden, and to the extent that the burden exceeded the State's direct regulatory authority, would probably be seen as an illegal taking and would require compensation to the RAC itself. The more direct approach of requiring a contingency plan holder to obtain written agreement from the RAC that it accepts the same State authority as exists over the plan holder, would accomplish the same goal in a more direct and more clearly legal way.

IN THE ABSENCE OF A RESPONSIBLE PARTY

Attempts to shift the burden of liability away from RACs may cause public policy concerns, but the concerns are considerably alleviated in the majority of large spills because under AS 46.03.822 and .825, liabilities will merely be shifted to the original responsible party. There will still be a party from whom injured persons can secure redress. But what happens when there is no solvent responsible party? This situation can occur because the original spiller is unknown; because the original spiller is insolvent; because the original spiller has insufficient assets or has, through complex corporate ownership structures, successfully hidden its assets; because the original spiller has successfully limited the extent of its liability under federal admiralty law or other laws³²; or for other reasons. Can there be a situation in which a person is injured by a RAC's actions but finds himself unable to proceed against either the RAC (because it has statutory immunity) or the original responsible party (because it is missing or insolvent)?

At the present time the answer appears to be that such situations will occur, although hopefully not frequently. Just as RACs have the incentive to reduce their exposure, so do the corporations which are likely to be responsible parties, and their insurers. It is openly acknowledged in the field that each of these groups is actively searching for ways to deflect or minimize liability. It may also be, as several of the corporations have suggested, that the answer to the conundrum of injured parties with no one to sue is to rely on compensation funds, such as that created by the Oil Pollution Act of 1990. Such funds -- financed by the industry -- may or not be an adequate answer, since obtaining compensation may be too costly or complicated for the small injured party, and with large spills the total claims may exhaust the funds. Overreliance on compensation funds may also reduce incentives of individual operators to maximize their preventive and safety measures, particularly if combined with immunity provisions or corporate structures that reduce direct liability of responsible parties. The point is simply that anytime consideration is given to further immunities for segments of the oil

³² See the Limitation of Liability Act of 1851, 46 U.S.C. §§181 et seq. This Act, which puts a cap on the amount of liability which can be placed on owners and operators of vessels causing damages in most circumstances, was made inapplicable to vessels subject to the liability scheme of the Oil Pollution Act of 1990. It still applies to maritime traffic in general, however, and could conceivably apply to RAC-owned vessels which cause damage through means other than oil.

transportation or spill cleanup industries, one of the prime considerations must be whether there is an adequate substitute source of compensation for injured parties, and whether securing compensation from that source is so difficult or costly that legitimate claims will in fact go uncompensated. There is a potential, due to the combination of statutory immunities and contractual liability shifting, that some damage claims will not be compensated.

CONCLUSIONS AND RECOMMENDATIONS

Response action contractors are now a necessary part of oil spill response. With advances in technology and continued change in the oil production and transportation fields, specialized response action contractors will become even more important. It is natural and understandable for RACs to want to reduce the potential liability they face for their actions during a spill, just as it is to be expected that the responsible parties will attempt to minimize their own exposure. Compensation schemes for oil spill victims can be expected to evolve in the future, as various parties attempt to use legislation, contractual agreements, and internal restructuring to reallocate the burden of oil spill liabilities. Protection of the public interest requires careful observation and understanding of these adjustments and skillfully working with the segments of the industry to minimize the disadvantage to injured parties from such reallocations. The bottom line must involve balancing the need for fair and full compensation for all spill injuries with the need for a liability scheme that does not discourage response action contractors from acting to prevent spill damages. Achieving that balance will require constant monitoring of both the legalities and practicalities of oil spill liability and compensation.

Beyond those general recommendations, we believe that requiring RACs to exercise due care, i.e., to act without negligence in their response activities, does not place an undue burden on them. The negligence standard includes the recognition that reasonableness must be viewed in light of the circumstances, including whether a crisis atmosphere exists. If the Legislature retains a broader immunity (for all actions not grossly negligent or intentional), it should reconsider the 15 day period now prescribed for immunity. A more rational scheme would replace that arbitrary period with a system that reflects the fact that the initial crisis may last for far fewer days in some cases and far more in others.

Finally, we recommend that the Department of Environmental Conservation revise its contingency plan regulations to require that RAC contracts which are an integral part of an approved contingency plan include an agreement subjecting the contractor to the same degree of governmental authority as the plan holder. ADEC should also prohibit by regulation a RAC from terminating or refusing to carry out its duties under a contract and contingency plan, without substantial prior notice to both the plan holder and the State.

**INSURANCE ISSUES RELATED TO
RESPONSE ACTION
CONTRACTORS**

Prepared by Gene Burden
Tesoro Alaska Petroleum Company
October 30, 1991

The work plan established by the Citizen's Oversight Committee on Oil and Other Hazardous Substances (hereinafter the "COC") in response to the legislature's directives under H.B. 196 included a section on the status of insurance as it relates to the Response Action Contractor (hereinafter "RAC") as defined under AS 46.03.822. Tesoro Alaska agreed to provide input on this topic with the initial objective of determining to what extent insurance is available for RACs; the costs of such coverage; and the affects on coverage based on the existence of state responder immunity law.

INTRODUCTION

The availability and cost of insurance coverage for a RAC is subject to the same factors as other insurance applicants and can vary substantially between geographic areas based on the applicant's experience, local and state laws/regulations, and the perceived risks of a particular operation. The variability in these ratings makes concise cost comparisons between jurisdictions difficult; and based on our review, precludes offering definitive conclusions as to the specific effects of RACs liability immunity

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on actual expected premiums.

The RAC liability concerns arise from damages caused by their negligence in the clean-up operations and in the disposal of the contaminating substances. The availability of public liability insurance for emergency response contractors including oil spill response contractors is typically available in the London market and is rated based on the following factors:¹

- 1) Revenues and/or payroll size;
- 2) Historical loss experience;
- 3) Contractual indemnities and their value;
- 4) Statutory immunities; and
- 5) The general state of the insurance market.²

INSURANCE SCENARIO FOR A RAC

A recommended package of coverage for a RAC was developed by a Soriero & Seffens broker to include the following:³

1. Hull & Machinery: covering equipment, barges, service boats/tugs, and crew/miscellaneous boats;

The Hull & Machinery coverage would provide

¹Source: Mark R. Mozell, Commercial Broker, Soriero & Seffens, Inc., 1300 Post Oak Boulevard, Suite 1300, Houston, Texas 77056-3013 (713)993-9913 in letter dated August 20, 1991.

²Mr. Mozell reports that the London insurance market is currently suffering through its worst results in years which has prompted rises in rates and additional underwriting restrictions.

³Recommendations provided by Soriero & Seffens in letter dated September 20, 1991.

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physical damage coverage on an "all risks" basis subject to a rate of approximately 1.25% of value. Coverage would be the usual required for vessels subject to a deductible of \$25,000 each occurrence.

2. Protection and Indemnity Risks;

Protection and Indemnity covers liabilities over water arising out of the owned vessels. This can include injuries to the crew. The costs for coverage provided by Soriero and Seffens were as follows:

- Barges.....\$ 7,500 each
- Crewed Boats.....\$10,000 each
- Crew coverage.....\$ 7,500 - \$10,000 per crew member
- Pollution coverage...\$25,000

The above premiums would obtain \$1,000,000 coverage subject to a \$25,000 deductible.

3. Real and personal property;

This would cover the office and contents, miscellaneous property and inventory, materials and equipment. The expected premium would be based on a rate of 1.0% of coverage with a \$10,000

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deductible for each loss.

4. Comprehensive General Liability; and

The General Liability insurance provides the "land based" liability coverage. It is expected that the limits would be \$1,000,000 with this coverage placed as underlying to an Excess Liabilities section.

5. Excess Liabilities.

The Excess Liabilities coverage would augment the underlying placements described above. Limits for excess can presently be obtained at a pricing of approximately \$2,000 per million of coverage. A \$25 million limit would cost \$50,000. The coverage would include Pollution liabilities on a "sudden and accidental" basis.

Our inquiry into insurance rates for RACs focused on two different RAC scenarios:

1) **SPILL CO-OP:** The model spill co-op for insurance underwriter evaluation was described as located in Alaska with approximately \$10 Million in capital equipment; 15 employees; one 30,000 bbl barge; four response assist boats (24' - 40' each); 1 larger service boat (50'+); and most likely responding to small

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fuel spills of less than 100 barrels. The planning standard required for crude oil response by this co-op is to remove 50,000 barrels within 72 hours after a spill.

The above description illustrates that a co-op such as described above would expect to incur annual insurance costs in excess of \$245,000 as illustrated below:

> Hull and Machinery (rate 1.25% of value)...	\$ 12,500
> Protection & Indemnity.....	\$ 132,500
> Real & Personal Property.....	\$ 10,000
> Comprehensive general liability.....	\$ 40,000
> Excess Liability of \$25 Million.....	\$ 50,000

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ESTIMATED TOTAL FOR A CISPRI SIZED RAC \$ 245,000

2) **GENERAL ENVIRONMENTAL SERVICE COMPANIES:** This type of firm may offer a variety of services to a wide range of clients. This could include refineries, processing plants, etc. for operations and maintenance work and for land based environmental clean-ups. In addition this firm may maintain a cadre of trained response personnel and support equipment to assist in response to a spill that is managed by another party such as a Responsible Party, a Spill Response Co-op, or a governmental entity.

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Soriero & Seffens views this type of organization much differently than a pure spill response co-op. Such an organization would probably not have as much spill response equipment and as high a capital investment to insure. In addition these firms were expected to rely more heavily on limited indemnity provisions in their agreements.

A review of RAC indemnifications was attempted via a survey conducted by the Alaska Department of Environmental Conservation. The survey information solicited included questions about the level of general liability coverage maintained and its cost. In addition information regarding the RAC's requirements for indemnification was requested. The ADEC will report the results of their survey to the Citizens Oversight Council.

Tesoro Alaska has response agreements with five different response action contractors: Cook Inlet Spill Prevention & Response, Inc. (CISPRI); Alyeska Pipeline Service Company (Alyeska); VECO; Martech; and VRCRA. A summary of the relevant indemnity language in each of these contracts is provided on the following page.

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**SUMMARY OF TESORO ALASKA CONTRACTS WITH
SPILL RESPONSE CONTRACTORS AND
EXISTING INDEMNITY PROVISIONS**

R A C	DATE OF CONTRACT	GENERAL DESCRIPTION OF SERVICES	INDEMNIFICATION LANGUAGE
CISPRI	5/29/91	Spill response services in Cook Inlet, Alaska	Article 7 of the Agreement is enclosed as Attachment 1 to this report.
ALYESKA	10/1/91	Spill response services (minimum of 72 hours after a spill) in Prince William Sound	Article 5 of the Agreement is enclosed as Attachment 2 to this report.

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VECO	8/14/90	Back up manpower and clean up assistance in Cook Inlet	"Any damage or loss of equipment, tools or consumable, etc., utilized in the course of any response efforts will be considered part of the cost of the response effort and repair and/or replacement cost will be the responsibility of the Client. If, however, gross negligence on the part of VECO's employees is determined to be reason for said damage or loss, then VECO would stand responsible for said additional cost, but only to the extent of repair or replacement cost that were a direct result of VECO's negligence."
MARTEC	8/14/90	Back up manpower and clean up assistance in Cook Inlet and Prince William Sound	"In no event shall Contractor be liable to Client for any direct damages, other than failure of the Contractor to exercise reasonable care, nor indirect damages, such as loss of profits or loss of use of property."

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VRCA	8/15/90	Back up manpower and clean up assistance in Cook Inlet and Prince William Sound	"In no event shall Contractor be liable to Client for any direct damages, other than failure of the Contractor to exercise reasonable care, nor indirect damages, such as loss of profit or loss of use of property."
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CONCLUSION

There is insurance available to Response Action Contractors to cover potential damage claims arising from their activities in response to a spill. The cost of the insurance is dependent on numerous variables including the existence of indemnities and state provided immunities. The spill response co-ops such as CISPRI and Alyeska have broad indemnity provisions in their response action contracts while the contracts examined that have been executed by the General Environmental Service Companies are more limited.

ATTACHMENT I

CISPRI

RESPONSE ACTION CONTRACTOR

May 15, 1991

Article 7. Indemnification

4.2. any applicable remedial action plan approved by the Alaska Department of Environmental Conservation,

4.3. any applicable contingency plan held by CISPRI and approved by the Alaska Department of Environmental Conservation, and

4.4. any applicable order by a State or Federal agency asserting jurisdiction over the actual or threatened release.

5. Spill Notification. User shall provide, and confirm to CISPRI the receipt of, all notifications of any release or threatened release of liquid hydrocarbons to the Alaska Department of Environmental Conservation in the manner prescribed by law.

6. User Warranty. User warrants that all directions and mandates given by User to CISPRI in connection with any release or threatened release of liquid hydrocarbons will be consistent with the plans and orders described in Paragraph 4, above. In the event CISPRI believes that a direction or mandate given by User to CISPRI is not consistent with such plans and orders, CISPRI may suspend or discontinue all or any part of the services being provided, or to be provided, by CISPRI under this agreement.

7. Indemnification.

7.1. Special Recitals. User acknowledges that:

7.1.1. Neither this agreement nor any other instrument requires User to use the services of CISPRI or its contractor(s), or to use equipment or materials acquired by CISPRI in connection with any spill control or clean up activities;

7.1.2. User is solely responsible for all planning, preparation, equipment acquisition, contracting and operations in connection with spill control or clean up necessitated by a spill originating from User's equipment or facilities;

7.1.3. For the purposes of any dispute related to the enforceability of these indemnification provisions, User waives any claim that:

7.1.3.1. it did not have adequate opportunity to participate in decisions made by or on behalf of CISPRI with regard to planning, equipment and materials acquisition and maintenance, operations, and other functions;

7.1.3.2. it did not have adequate opportunity to inspect the equipment, materials and supplies that have been acquired by CISPRI and to evaluate their condition and usefulness to the member in the event of a spill;

7.1.3.3. it did not have adequate opportunity to evaluate the ability of contractor(s) engaged by CISPRI to be of assistance to User in the event of a spill;

7.1.4. Any and all equipment, supplies, materials, and services provided by CISPRI to User are provided "as is, where is," and neither CISPRI nor any member of CISPRI makes any representation as to the merchantability or fitness for any particular purpose of the same.

7.1.5. If these indemnification provisions were not included in this agreement, CISPRI would be unwilling to enter into this agreement.

7.2. Indemnification. It is the intent of the parties that User shall assume all indemnification responsibilities provided herein. User hereby agrees to indemnify, defend, and

hold harmless CISPRI, its members, directors, officers, managers, executive committee, contractors and employees, together with all officers, directors, employees and affiliates of each of the members of CISPRI, and each of them, from and against any and all claims, demands, causes of action, damages, costs, fees (including reasonable attorneys' fees), expenses, penalties, losses or liabilities, in law or in equity, of every kind and nature whatsoever, arising out of or in any way connected with:

7.2.1. Any and all actions, or failures to act, on the part of CISPRI, its members, staff and contractor(s), carried on under or in connection with materials, equipment, supplies or services (hereinafter, collectively, "assistance") requested or received by User, including, without limitation, the activities of members of CISPRI as participants in business entities providing vessels, equipment and material to CISPRI;

7.2.2. Any and all penalties, fines or other liability imposed on account of the violation of any law or regulation, compliance with which is left by these bylaws to User, if such penalties, fines or other liability arise out of or are in any way connected with assistance requested or received by User; and

7.2.3. Any and all liens, claims, assessments, levies and stop notices of labor, and any other liens or claims on account of overdue or other deficient handling of charges for labor or materials, if such liens, claims, assessments, levies, and stop notices of labor, or other liens or claims arise out of or are in any way connected with assistance requested or received by User.

7.3. Extent of Indemnification. The indemnification obligations of User are fully effective even if such claims, demands, causes of action, damages, costs, expenses, penalties, losses or liabilities were caused or contributed to, in whole or in part, by:

7.3.1. The active or passive negligence or other fault (including gross negligence) of CISPRI, its members, staff or contractor(s), or their agents, representatives or employees;

7.3.2. Any equipment or materials supplied to User by CISPRI, howsoever caused, whether by failure, malfunction or defect, latent or otherwise, in said equipment or materials, or by the maintenance thereof; or

7.3.3. The liability without fault of CISPRI, its members or contractor(s), or their agents, representatives or employees.

The obligations of indemnification are not limited, restricted, or in any way affected by the amount of insurance carried by User, or by any terms or conditions of any insurance policies. The obligations of indemnification shall survive the termination of this agreement, the dissolution of CISPRI and the withdrawal of any member from CISPRI.

7.4. Indemnification Duties. User assumes, without limitation, the following obligations:

7.4.1. At its own cost, expense and risk, to accept and conduct the defense of any and all suits, actions and other legal proceedings that may be brought or instituted against the indemnitees, or any of them, and prosecute any appeals;

7.4.2. To pay and satisfy any and all settlements, final judgments and decrees that may be paid by, or enforceable against, the indemnitees, or any of them;

7.4.3. To reimburse the indemnitees, and each of them, for any and all reasonable attorneys' fees, costs and expenses incurred by the indemnitees, or any of them, in order to enforce the indemnification provisions of these bylaws; and

7.4.4. To reimburse the indemnitees, and each of them, for any and all reasonable attorneys' fees, costs and expenses incurred by the indemnitees, or any of them, prior to the assumption of indemnification responsibilities by User in connection with any and all suits, actions and other legal proceedings described above.

7.4.5. After User has assumed such responsibility, any and all indemnitees are entitled to participate at its or their sole cost and expense in the defense of any suit, action, or other legal proceeding without affecting the indemnity obligations of this agreement.

7.5. Administration.

7.5.1. In requesting that CISPRI furnish assistance, and in utilizing and receiving the benefits of assistance, User reaffirms thereby its commitment to perform its indemnification obligations as provided herein.

7.5.2. CISPRI may, if it so elects, pay and discharge any liens or overdue charges for labor, equipment, or materials incurred by User as may be reasonably necessary to protect the interests of CISPRI. Any and all such payments shall be for the account of User.

7.5.3. The provision of assistance by CISPRI to User does not constitute or affect any construction contract under AS 45.45.900.

8. Insurance. At all times during the term of this agreement, User shall carry and maintain in force with carriers satisfactory to CISPRI, Workers' Compensation (including adjustments for marine service) and Employers' Liability Insurance in accordance with the law that may be applicable to its employees, and Comprehensive General Liability and Automobile Liability Insurance covering injury or death of persons and property damage in an amount not less than ten million dollars. User shall provide certificates of insurance for each of these policies at the request of CISPRI. No such insurance will be materially changed during the term of this agreement without at least thirty days' written notice to CISPRI. Nothing contained in this clause shall limit or waive User's legal or contractual responsibilities to CISPRI or others.

8.1. User agrees to have its insurers add CISPRI as an additional insured or loss payee under any policies of insurance applicable to this agreement, and to obtain a waiver of its insurers' rights of subrogation against CISPRI and CISPRI's members and their employees.

8.2. In the event User elects to self-insure, CISPRI reserves the right to approve such self-insurance and to request and receive such information as CISPRI deems necessary to evaluate the self-insurance provided by User. In any case, if User elects to self-insure, User shall treat CISPRI as an additional insured or loss payee and hereby waives any rights of subrogation against CISPRI and CISPRI's members and their employees.

9. Accounting and Audit.

9.1. CISPRI agrees that all financial settlements, billings, and reports rendered to User, as provided for in this agreement, and/or any amendments to it, will reflect properly the facts about all activities and transactions handled for the account of User, which data may be relied upon as being complete and accurate in any further recording and reporting made by User for any purpose.

ATTACHMENT II

ALYESKA

RESPONSE ACTION CONTRACTOR

October 1991

Article V. Indemnify

Alyeska shall use its best efforts to include in any contracts with its subcontractors a provision similar to the foregoing so that Contracting Vessel shall have access to pertinent records of such subcontractors for the purpose of verifying the accuracy of Alyeska's costs in performing services under this Agreement.

ARTICLE V

INDEMNITY

5.1 Alyeska and Contracting Vessel recognize that, in connection with the performance of this Agreement: (i) AS 46.03.826(15) defines a response action contractor as a person who is retained by a person potentially liable for a release or threatened release of a hazardous substance to provide response actions to such release; (ii) AS 46.03.825(a) provides that a person who is a response action contractor with respect to a release or threatened release of oil (defined to mean a derivative of a liquid hydrocarbon and includes crude oil, lubricating oil, sludge, oil refuse or another petroleum-related product or by-product) whose act or omission is not contrary to an order of the federal or state on-scene coordinator is not civilly liable for injuries, costs, damages, expenses, or other liability that results from the release or threatened release or from the response action contractor's act or omission in response to the release or threatened release, unless the person bringing a claim against the response action contractor proves by a preponderance of the evidence that the response action contractor (1) would have been liable for the initial release or threatened

release under AS 46.03.822, (2) acted with gross negligence or intentional misconduct, or (3) without the approval by the federal or state on-scene coordinator, substantially deviated from an oil spill contingency plan previously approved under AS 46.04.030, and the plan was either prepared by that contractor for a party responsible for the release under AS 46.03.822 or that contractor previously agreed to comply with the terms of that plan under a contract with parties responsible for the release under AS 46.03.822; provided, however, the above limitations of liability do not apply to (1) an action for personal injury or death, (2) an action for damages to tangible personal property not caused by oil, or (3) an act or omission that occurs more than 15 days after the release; (iii) the Services to be performed by Alyeska are in the public interest to protect the environment and are in the best interests of Contracting Vessel to attempt to minimize its exposure to liabilities; (iv) accidents and events may occur that result in the damage to or loss of property, in the injury to or death of persons, in spillage, or pollution, or environmental damage; (v) the extraordinary nature of the Services may require actions by Alyeska, its Owner Companies or their respective subcontractors that can give rise to fines, penalties, and claims, including but not limited to claims based on negligence; (vi) Alyeska has based the charges for its Services on the understanding that Contracting Vessel, or anyone asserting rights on its behalf, will not challenge Alyeska's right to be indemnified as provided in this Article V and that without such assurances Alyeska

considers its potential risks and liabilities to be too substantial to provide the Services for the charges set forth herein; and (vii) certain risks and liabilities may be covered by Financial Responsibility, Insurance, or other means not addressed in this Agreement. Notwithstanding any such Financial Responsibility, Insurance, or other means that Alyeska or Contracting Vessel may have or acquire to cover such risks and liabilities, and notwithstanding that certain legal authorities may have questioned the concept of one party contractually agreeing to indemnify another party for its sole negligence, Alyeska and Contracting Vessel fully understand and recognize that the nature of the Services to be provided under the terms set forth in this Agreement make it appropriate and equitable to allocate the risks and liabilities as set forth in this Article V. Therefore Alyeska and the Contracting Vessel agree that responsibility for risks and liabilities arising out of the performance of (or the failure to perform) the Services by Alyeska shall be allocated to Contracting Vessel in the manner set forth in Sections 5.2 and 5.3, regardless of who may be at fault or otherwise responsible under any statute, rule, or theory of law, even if the subject damage, loss, injury or death is wholly or partially attributable to the active or passive negligence of Alyeska or its Owner Companies or Alyeska's subcontractors or the unseaworthiness of any vessel.

5.2 The following risks and liabilities that may occur as a result of or in connection with the Services performed by Alyeska are allocated solely to the Contracting Vessel:

(a) Any damage to or loss of: barges, lighters, tugs and other vessels owned, chartered or used by Alyeska or third-parties, specifically including but not limited to all items set forth in Sections 4.1 (e), (f) and (g) of this Agreement; docks, berths, wharfs, shoreside facilities and installations; and navigation aids, and any other property that may be damaged or lost.

(b) Bodily injury including but not limited to physical injury, death, sickness, disease or any other type of injury to: employees of Alyeska, its Owner Companies or the Contracting Vessel; employees of subcontractors of Alyeska, its Owner Companies or Contracting Vessel; and all other persons.

(c) Any fines, penalties, or other charges or costs imposed by any federal, state or local authority.

(d) Any claims for environmental damage to, or loss of, natural resources, wildlife, or public and private property; any other claims concerning the environment; any claims by fishermen, boat owners, or any other party or interest asserting any claim.

5.3 For the risks and liabilities set forth in Section 5.2, Contracting Vessel shall indemnify, defend and hold harmless Alyeska, its Owner Companies, their affiliates (including any person or entity controlling, controlled by, or under common control with Alyeska or any of its Owner Companies), subcontractors of Alyeska who assert claims against Alyeska, and each of their respective directors, officers, employees, agents, successors, and assigns (collectively, the "Indemnified Parties")

against all claims, liabilities, obligations, demands, losses, deficiencies, or damages in personam and/or in rem (including but not limited to compensatory, incidental or consequential damages, to the fullest extent permitted by law) that may be asserted against the Indemnified Parties by any party. The obligations undertaken by Contracting Vessel in this Article V are in addition to the reimbursement of expenses provided in Article IV.

5.4 The Contracting Vessel shall, at its sole expense, investigate, respond to, and provide defense for, any claim, demand or suit for which it gives an indemnity herein. Nothing in this Article V is intended to, or shall be construed to, constitute an admission of liability on the part of either Alyeska, its Owner Companies or Contracting Vessel with respect to third parties, and Alyeska and Contracting Vessel expressly disclaim any intention that any third party (other than the Indemnified Parties and third parties providing evidence of Financial Responsibility) shall be a third party beneficiary of the provisions of this Article V.

5.5 Contracting Vessel shall reimburse the Indemnified Parties for all legal expenses (including but not limited to actual attorneys' fees, costs and allocated expenses for in-house legal services) related directly or indirectly to (i) the Spill Prevention Services that are in addition to the regular vessel escort services and Oil Spill Response Services provided by Alyeska, (ii) any claim against the Indemnified Parties for which liability is allocated to Contracting Vessel, or (iii) any action

or proceeding to enforce the rights provided the Indemnified Parties under this Article.

5.6 Notwithstanding any of the provisions of this Article V, Alyeska and Contracting Vessel agree that the Contracting Vessel's responsibility to Alyeska to indemnify, defend, and hold harmless does not include risks and liabilities arising out of Alyeska's gross negligence, willful misconduct and/or criminal misconduct.

ARTICLE VI

FINANCIAL RESPONSIBILITY

6.1 Contracting Vessel, prior to the effective date of this Agreement, shall provide written evidence to Alyeska of Financial Responsibility, Insurance or a combination thereof.

6.2 The minimum amount of Financial Responsibility that Contracting Vessel shall provide to cover Contracting Vessel's obligations under this Agreement shall be in an amount equal to one billion dollars (\$1,000,000,000); provided, however, if Contracting Vessel uses a combination of Financial Responsibility and Insurance, or solely Insurance, to underwrite its obligations under this Agreement, the amount shall be One Billion Two Hundred Million Dollars (\$1,200,000,000). In the event Alyeska agrees to a lesser amount of financial responsibility and/or insurance during the term of this Agreement, the lesser amount will also be available to Contracting Vessel by a mutually agreed to amendment to this Agreement.

GROSS & BURKE

A PROFESSIONAL CORPORATION
424 NORTH FRANKLIN STREET
JUNEAU, ALASKA 99801

1

AVRUM M. GROSS
SUSAN A. BURKE

907 586-2777

October 10, 1991

To: Sheila Gottehrer

From: Av Gross

Re: Legislative History of Immunity
for Response Action Contractors
under Oil Pollution Act of 1990

Section 4201(a) of OPA 90 amends 311(c) of the Federal Water Pollution Control Act to create a limited liability for certain persons who assist in the clean up of an oil spill. The relevant portion of Sec. 4201 reads as follows:

SEC. 4201. FEDERAL REMOVAL AUTHORITY.

(a) IN GENERAL. -- Subsection (c) of section 311 of the Federal Water Pollution Control Act (33 U.S.C. 1321(c)) is amended to read as follows:

"(c) FEDERAL REMOVAL AUTHORITY. --

* * * * *

(4) EXEMPTION FROM LIABILITY. -- (A) A person is not liable for removal costs or damages which result from actions taken or omitted to be taken in the course of rendering care, assistance, or advice consistent with the National Contingency Plan or as otherwise directed by the President.

(B) Subparagraph (A) does not apply --
(i) to a responsible party;
(ii) to a response under the Comprehensive Environmental Response, Compensation, and Liability Act of 1980 (42 U.S.C. 9601 et seq.);
(iii) with respect to personal injury or wrongful death; or

(iv) if the person is grossly negligent or engages in willful misconduct.

* * * * *

You have asked that we provide you with a brief history of how this limited exemption from liability became a part of OPA 90 and, in addition, an analysis of what was intended by the Congress that included the provision in the Act. Toward that end, we have reviewed the complete legislative history of OPA 90, including all committee reports and the floor debate. That review has produced a fairly clear picture of both the history of and intent behind the limited liability provision.

OPA 90 is the result of an amalgamation of two separate proposals; S.686, which was introduced in the Senate on April 4, 1989 and HR 1465, which was introduced in the House on March 16, 1989. Neither of the bills as initially introduced included any provision limiting the liability of parties who assisted in cleaning up an oil spill. The Senate bill went through limited committee hearings and passed the Senate on August 15, 1989 without any provisions relating to the liability of response action contractors.

The House of Representatives held extensive hearings on HR 1465 as well as on HR 3027, a similar measure. The early mark ups in the Public Works and Transportation Committee and the Science, Space and Technology Committee did not deal with the issues of liability for those who assist in spill

clean-up activities. The first committee to focus on that problem was the Committee on Merchant Marine and Fisheries. The committee added a new section to HR 1465 to deal with clean up activities directed by the President. The new section (Sec. 431 of HR 1465) amended section 311(c) of the Federal Water Pollution Control Act to read in part as follows:

Sec. 431. FEDERAL REMOVAL AUTHORITY

(a) REMOVAL. -- Paragraph (1) of section 311(c) of the Federal Water Pollution Control Act (33 U.S.C. 1321(c)(1)) is amended to read as follows"

(c)(1)(A) The President shall ensure an effective and immediate removal of a discharge of oil or hazardous substance --

- (i) into or on the navigable waters; or
- (ii) on the adjoining shoreline to these navigable waters; or
- (iii) on the waters of the exclusive economic zone or

- (iv) that may affect a natural resources belonging to, appertaining to, or under the exclusive management authority of the United States;

in accordance with the National Contingency Plan, any other contingency plans prepared under subsection (j) of this section, and applicable state law.

(B) The President may remove or arrange for the removal of a discharge, or the threat of a discharge, of oil or a hazardous substance at any time.

(C) The President may direct all Federal, state, responsible party and private actions to remove a discharge, or the threat of a discharge, of oil or a hazardous substance.

(D) When the President retains or directs a person (other than a responsible party) under the authority of subparagraph (B) or (C) of this paragraph, that person is not liable for removal costs or damages other than personal injury or wrongful death arising from his or her removal activities conducted in

accordance with the direction of the President, except in the case of gross negligence or willful misconduct.

(E) Each responsible party shall act in accordance with the National Contingency Plan, the applicable contingency plans required under subsection (j) of this section, and as otherwise directed by the President.

(F) Nothing in this paragraph affects the liability of a responsible party under the Oil Pollution Prevention, Removal, Liability and Compensation Act of 1989 (emphasis supplied).

The Committee explained the meaning of the limitation on liability at page 84 of its September 18, 1989 report in these terms:

Under section 311(a)(1)(D) the Committee allocated the primary risk of liability arising from removal and cleanup activities to the responsible party rather than to those persons responding to the spill under the direction of or retained by the Federal government. The Committee intends to ensure immediate response to oil and hazardous substance spills and believes this provision is necessary in light of the substantial financial risks and liability exposure which would otherwise deter vessel operators, spill cooperatives, and spill contractors from providing active assistance. To avoid paralysis of remedial action to spills, this paragraph provides that those persons -- other than responsible parties -- who are retained or directed by the President to participate in a cleanup action will not be liable for removal costs or damages as defined in this legislation, except in the case of gross negligence or willful misconduct. This limitation of liability does not affect liability for wrongful death or personal injury. Nor does it diminish the liability of those responsible for the spill nor the amount of compensation available to claimants. This limited protection will encourage individuals to assist in cleanup

operations without fear of collateral attacks from responsible parties. The Committee expects that all who take part in removal actions will act responsibly and believes that the elimination of the liability except for gross negligence or willful misconduct will serve as sufficient protection.

Section 311(c)(1)(E) requires the responsible party to act in accordance with the National Contingency Plan, other applicable contingency plans, and as otherwise directed by the President. This provision is also intended to underscore the fundamental obligation that the responsible party has to be prepared at all times and to take immediate and effective action in the event of a discharge. Report of the Committee on Merchant Marine and Fisheries on the Oil Pollution Prevention, Removal, Liability and Compensation Act of 1989, September 18, 1989 - Part 2.

The limitation on liability for simple negligence drafted by the Committee of Merchant Marine and Fisheries differs significantly from the language that eventually became part of OPA 90. The proposed limitation as only applicable to a person who was retained or directed by the President to clean up the spill. It had no application to volunteers or to contractors retained by responsible parties to clean up spills or to anyone else except those directed or retained by the Federal government.

The House debated and subsequently passed HR 1465 on November 9, 1989. The provision for limited liability drafted by the Merchant Marine and Fisheries Committee was included in the final bill without amendment.

Since different versions of the bill had passed the House and the Senate, the two measures were sent to a conference committee. Through the Washington D.C. office of Birch, Horton, Bittner and Cherot, I have obtained a copy of an undated memo that purports to set out the status of negotiations between the Senate and House conferees as of March 13, 1990. I have no way of independently verifying the accuracy of the contents of the memo. Assuming the memo is accurate, during the course of the negotiations the Senate conferees offered a new section to replace the section on limited liability, which had passed the House. The proposed section would have read as follows:

[A]mend proposed CWA Sec. 311(c)(1)(C)(1) as follows:

"No person shall be liable for removal costs or damages under this Act or the Oil Pollution Act of 1990 as a result of actions taken or omitted in the course of rendering care, assistance, or advice consistent with the National Contingency Plan or at the direction of an on-scene coordinator appointed under such plan, with respect to an incident creating a danger to public health or welfare or the environment as a result of any discharge of oil or the substantial threat thereof."

If the memo is accurate, the Senate proposal is the first instance in which a broader immunity was proposed for those who respond to a spill. The Senate proposal apparently sought to immunize those who responded to a spill so long as their activities were consistent with the National Contingency Plan or occurred at the direction of an

on scene coordinator. The language of the proposal is not crystal clear, was never explained in detail and did not appear in the final act; but it does represent the first effort to expand immunity beyond those working at Presidential direction.

The language that ultimately was adopted as a part of OPA 90 first appears in the tentative agreement of the conference committee contained in its report on HR 1465, issued on July 26, 1990. Section 4201 of the bill proposed by the conference committee contains the language that ultimately became section 4201 of OPA 90. Because the language was new, the conference committee included a specific explanation as to the meaning of the provision. That explanation is contained at page 146 of the conference report accompanying HR 1465 issued on August 1, 1990, to the House of Representatives. The report states:

The Conference substitute establishes a new paragraph (4) of FWPCA section 311(c) to provide limited immunity for persons involved in oil spill cleanup. The provision is similar to that contained in section 420(a) of the House bill except that the limited immunity is extended not only to those persons retained or directed by the Federal On-Scene Coordinator but also to those persons rendering care, assistance or advice consistent with the NCP. The substitute's provision also clarifies that it does not apply to a response under the Comprehensive Environmental Response, Compensation, and Liability Act of 1980.

This subsection provides immunity from liability established under the substitute for those taking action in response to an oil

spill or the threat of a spill whether that action is performed under the aegis of the National Contingency Plan or under the direction of the President. This takes into account the fact that the NCP and Presidential orders may not cover every detail or eventuality of a spill response and that actions that are in keeping with the overall objectives of the NCP or Presidential order are deemed to be within the scope of this provision. This section reflects the Conferees' intention that responses to oil spills be immediate and effective. Without such a provision the substantial financial risks and liability exposures associated with spill response could deter vessel operators, cleanup contractors, and cleanup cooperatives from prompt, aggressive response.

There was no specific debate on the section of the conference committee report limiting immunity for response action contractors. Therefore, we can assume that the conference committee report will be taken as the definitive source of legislative intent on response action liability, particularly since the report specifically discussed the section in question. Two points bear mention in reference to the final provision. First, what started as an idea to protect those who were retained by Federal authorities to clean up a spill grew into a Congressional effort to insure "that responses to oil spills be immediate and effective." Congress apparently was convinced that if the risk of exposure to liability was not limited to gross negligence or intentional conduct, it "could deter vessel operators, cleanup contractors, and cleanup cooperatives from prompt, aggressive response." Disputes over the meaning of the act,

then, will be resolved with this Congressional intent in mind -- a deliberate relaxation of liability to encourage more aggressive spill response efforts. However, even though Congress clearly intended to take some risks to encourage spill response actions, it did not extend immunity to all situations in which a party participated in cleaning up a spill. Even in the expanded version, Congressional immunity only applies to actions "consistent with the National Contingency Plan or as otherwise directed by the President." The Federal Act does not go as far as Alaska's present law, which specifically permits deviations from a contingency plan so long as they are not "material." While it is possible that a court would permit parties seeking immunity under Federal law to show that Congress meant to allow some deviation from the National Contingency Plans so long as that deviation was not material, the words of the act, at least, do not permit any deviation.

Hopefully, this analysis of the federal immunity provision will prove of some benefit in formulating an overall strategy concerning HB 196. Please make this memorandum available to all appropriate parties and advise them to contact us directly if they desire any further information.

MEMORANDUM

NOV 04 1991
State of Alaska
Department of Law

TO: Citizen's Oversight Council on
Oil and Other Hazardous
Substances

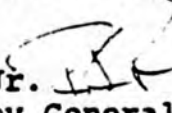
DATE: October 30, 1991

FILE NO: 663-92-0026(c)

TEL NO: 465-3600

THRU: Janice Adair, Special Asst.
Dep't Envtl. Conservation

SUBJECT: Litigation Threat to
Response Action
Contractors

FROM: Robert K. Reges Jr. 
Assistant Attorney General
Natural Resources Section - Juneau

Task Number 7 on the list of research projects sought a brief analysis of whether response action contractors have been sued or found liable in Alaska or in other states for damages for oil spills when there was no other cause for liability. I believe the focus of this issue statement was slightly too narrow. If good Samaritans were sued or found liable for damages arising from marine catastrophes then their cases are probably applicable to response action contractors sued or found liable for damages arising from oil spills. Accordingly, this memorandum briefly analyzes cases involving good Samaritans at sea, and the scope of their liability.

I also briefly review legislative histories of other provisions in law that protect response action contractors because these other histories provide insight into the rationale for such provisions.

Research did not reveal any case involving "contractors" and "oil spills." However, to report only that dearth would give

the false impression that contractors do not face potential liability. Courts often rely upon cases analogous to the one they have before the bench. Cases involving good Samaritans can be analogous to cases involving contractors. Cases involving hazardous substances can be analogous to cases involving oil. Consequently, this analysis looks at cases arguably analogous to one that might arise in Alaska involving response action contractors and oil spills.

GOOD SAMARITAN CASES

Introduction

The law of admiralty has always sought to "encourage and induce men of the sea to go to the aide of life and property in distress." 1/ Toward that end the concept of a "good Samaritan" has long been incorporated in maritime law. 2/ As a general rule, the concept is this:

A good Samaritan has no obligation to act. If he does act, however, he must exercise due care. If,

1/ *Berg v. Chevron, U.S.A., Inc.*, 759 F.2d 1425, 1429 (9th Cir. , Alaska, 1985) quoting 3A M. Norris, *Benedict on Admiralty* § 234 (7th ed. 1980).

2/ *Indian Towing Company v. United States*, 350 U.S. 61, 76 S. Ct. 122, 100 L. Ed. 48 (1955).

by his actions the Samaritan leaves the injured party in worse condition, then the Samaritan is liable for all damages suffered by the injured party. 3/

There are two significant differences between this doctrine and the doctrine underlying AS 46.03.825. First, the Samaritan is under no obligation to act while a response action contractor is contractually obliged to act. Second, the Samaritan is sometimes held liable for simple negligence (although this is exceptional) while AS 46.03.825 would only impose liability on those who act with gross negligence or intentional misconduct. Bearing those distinctions in mind, the caselaw is noteworthy.

Reported Cases

- I. *Burgess v. M/V TAMANO*, 373 F. Supp. 839 (S.D. Me. 1974) (Tamano I), vacated by *Burgess v. M/V TAMANO*, 564 F.2d 964 (1st Cir. 1977) (Tamano II).

These two opinions set-out a factual scenario that is close to the factual scenario of concern to the Oversight Council. The Tamano opinions involve an oil spill and negligent response actions. But, since Tamano turns on *Indian Towing Co., Inc. v. United States*, *supra*, that case must be briefly explained first.

3/ Compare 46 U.S.C. § 2303 (c) (USCA 1991 Partial Revision).

Indian Towing involved the tug NAVAJO. Towing a barge laden with fertilizer, NAVAJO ran aground on Chandeleur Island, Mississippi. Water entered the barge and the cargo was ruined. Indian Towing Company, owner of the NAVAJO, was forced to pay for the lost cargo. It sued the United States for reimbursement. The Company contended that the Coast Guard had established a lighthouse on Chandeleur Island but had failed to properly maintain the light, allowing it to extinguish. But for its reliance on the light, the NAVAJO would have used other navigational tools. Had it used those tools, it would not have run aground. These were the Company's contentions.

The Coast Guard responded that it never had to establish the light in the first place and, therefore, it had no obligation to keep the light burning and no responsibility for losses occasioned by extinguishment of the light. The Supreme Court rejected this argument. A good Samaritan service -- such as establishment of a lighthouse -- need not be undertaken, said the court, but once undertaken the effort must be completed or carried on with due care. If care is lacking, the Samaritan will be liable for damages arising from that lack of care. 4/

4/ Although Indian Towing turns on an interpretation of the Federal Tort Claims Act (FTCA), it has been widely cited for the proposition stated above. The FTCA merely waives sovereign immunity. Substantive legal duties applied in Indian Towing -- such as good Samaritan matters -- arose out of the maritime common law.

With this principle in mind, let me turn to the Tamano cases. In Tamano the Coast Guard had located a floating buoy, intending to mark "Soldier Ledge." Apparently it did so improperly, for the M/V TAMANO hit Soldier Ledge, spilling 100,000 gallons of Bunker C oil into Casco Bay. Various persons injured by the spill sued the Coast Guard alleging that the grounding resulted from misplacement of the buoy; that after the grounding the Coast Guard undertook responsibility for containing and cleaning oil; that this containment and clean-up failed, allowing oil to escape and spread; and, that such escapement occurred because the Coast Guard negligently performed its response actions.

In district court the Coast Guard was found to be liable. The district court's opinion, designated Tamano I, states:

. . . [I]f the Coast Guard undertook responsibility for stemming the flow of the oil from the TAMANO and for the cleanup operation, and the Coast Guard negligently discharged such assumed responsibilities, it is clear, as the United States concedes, that the United States may be found liable for any resulting damage on *Indian Towing* principles.

* * *

. . . [I]deed, those cases which have applied *Indian Towing* principles in an admiralty context make clear that the United States, in undertaking any "good Samaritan" task such as buoyage or pollution abatement, is liable in tort for the

consequences of its negligence to the same extent as a private person would be liable under similar circumstances.

The tort liability of a private person for the foreseeable consequences of his negligence is equally well established . . . [W]e look to see what natural forces and what human conduct should have appeared likely to come upon the scene, and we weigh the dangerous consequences likely to flow from the challenged conduct in the light of these interventions. And in this inquiry foreseeability is not to be measured by what is more probable than not, but includes whatever is likely enough in the setting of modern life that a reasonably thoughtful man would take account of it in guiding practical conduct. (citations omitted.) 373 F. Supp. at 844.

The district court then found that the Coast Guard had fallen below the standard expected of a private person although the "natural forces" and "human conduct" that "intervened" with clean-up were not explained.

The circuit court -- in an opinion designated Tamano II -- vacated that ruling. It found that negligence by a pilot aboard the M/V TAMANO had been a contributing cause to the initial spill; that the shipowner had to take responsibility for the pilot's negligence; and, that the government was not liable for any damages because it was not solely responsible for the initial spill. Accordingly, the ship's owner became liable for all costs notwithstanding the government's negligent clean-up activities.

A significant distinction between the district court opinion and the circuit court opinion is that the former relied on maritime common law (i.e. Indian Towing) while the latter relied on the Clean Water Act (CWA). The district court was correct when it opined that maritime law imposed liability on the government for negligent clean-up. The circuit court was correct when it opined that the CWA imposed liability on the ship's owner because the government was not "solely" responsible for the wreck and consequential spill. 33 U.S.C. § 1321(f)(1)(C). The question not answered by the circuit court is why imposition of this statutory liability on the ship's owner should eliminate the common law liability of the government. In other words, if the ship owner is liable under the CWA, and the government is liable under the principles of Indian Towing, it seems both possible and reasonable for a reviewing court to secure partial payment from each.

Such joint liability is not possible, however, if a statute so comprehensively covers a particular issue that the common law is deemed preempted. *Illinois v. City of Milwaukee*, 406 U.S. 91, 107 (1972). Thus the circuit court in Tamano II must have assumed that maritime law was preempted by the CWA. This may or may not have been true in 1977. Given the comprehensive nature of the Oil Pollution Act of 1990 (OPA), federal common law on oil spills has, in all probability, been preempted now.

In any event the two Tamano decisions point up the importance of asking what law would apply in the absence of AS 46.03.825. If AS 46.03.825 was repealed, the OPA or CWA may be deemed to set the standard. In such a case the circuit court's ruling in Tamano II provides an appropriate guide. However, if maritime common law is deemed controlling, the district court's ruling in Tamano I may be the appropriate guide.

- II. *United States v. Gavagan*, 280 F. 2d 319 (5th Cir., Florida, 1960), *cert. denied*, 364 U.S. 933 (1961).

This is a case in which the U.S.C.G. was found liable notwithstanding good Samaritan doctrines. This case, like Tamano I turned on maritime common law.

In 1956 the federal government established a national Search and Rescue Plan (SAR). In many ways the SAR is similar to the National Contingency Plan (NCP) which governs oil spill response activities. Both allocate responsibilities among federal agencies. Both provide for the U.S.C.G. to be on-scene-commander. Both establish a hierarchal command system to enhance efficiency of governmental response in emergency situations.

In Gavagan the SAR failed. Thus Gavagan provides some guidance on how a court would handle failure of the NCP.

In Gavagan the shrimp boat Donald Ray was disabled by rough seas. Radio communication was established, the Coast Guard was notified and the SAR was put into action. By 4:17 p.m. the Donald Ray had been positively spotted by a SAR airplane. Due to a compendium of human errors no rescue had been accomplished by 7 p.m. when darkness fell. Come morning the ship and her crew were gone.

Relatives of deceased crew members sued the U.S.C.G. for botching the rescue. In defense, the government claimed that it was a good Samaritan and, as such, it could not be liable because it did not leave the injured party in worse condition. Remember, the good Samaritan rule holds that the Samaritan is not liable unless his negligent conduct aggravates or worsens the condition of the injured party.

The Coast Guard's position was simple. Donald Ray was lost at sea when the Coast Guard began its rescue. Donald Ray was still lost at sea when the Coast Guard completed its "rescue." Since the ship's condition was not worsened by the Coast Guard's

action (or inaction), the Guard could not be liable for damages caused when the ship sank.

This argument was rejected by the court. It said:

In addition we are also of the opinion that the facts fully meet the requirements of the good Samaritan doctrine. The only element of any doubt is that of "worsening" the plight of the crew members of the Donald Ray. We think that adequately established.

The members of the families of the crew of the Donald Ray and . . . fishermen on the other fishing vessels in Mayport were greatly exercised. They were maintaining a very close contact with the Coast Guard. The Coast Guard was likewise anxious to keep in contact with them. Had these persons known the true facts, steps could have been taken to reach the Donald Ray in the time remaining up to 7:00 p.m. when darkness set in and visual contact was lost. As we pointed out, the SS Henry M. Dawes was in the vicinity -- not over five or six miles and 30 minutes away -- and ready to respond to a search. And the other fishing vessels in Mayport were available to go out as one did later that night and as several did during the succeeding days.

All of these interested persons were standing by, as they properly might, while the extensive, experienced facilities of the Coast Guard-directed search went on. But they were ignorant of several critical facts [namely, that the Coast Guard operation had gone awry.] Ignorance of these facts and continued reliance upon the Coast Guard's celebrated skill made independent action unnecessary. But it kept them from taking action which, in all probability, would have been successful.

The Coast Guard was liable for the loss of lives and property.

A set of facts like those presented in Gavagan probably constitutes "gross negligence." As such, AS 46.03.825 provides no protection. Furthermore, if AS 46.03.825 was repealed and a case similar to this one occurred, good Samaritan laws would provide no protection. The moral then is this. If a response action contractor makes a show of responding such that others are dissuaded from acting, and the contractor turns out to be totally incompetent, the contractor may well be liable for all spill-related damages.

Also, bear in mind that the U.S.C.G. was a volunteer, not a contractor, and it was acting pursuant to an approved contingency plan. In that light, Gavagan provides insight into the liabilities of all responders, not just contractors. Gavagan stands for the proposition that any responder can be liable for failing to properly implement a contingency plan, especially when there exists only a brief period of time in which to act and the responder's actions dissuade others from acting. Gavagan also stands for the proposition that a good Samaritan may be deemed to have worsened a situation even if he does not physically alter the injured party's condition.

III. *Patentas v. United States*, 687 F.2d 707 (3rd Cir., Penn., 1982)

On April 9, 1974, the Greek tanker ELIAS exploded while discharging its cargo of crude oil at the Fort Mifflin terminal in Philadelphia. The vessel was destroyed, thirteen people were killed and property damage totalled millions of dollars. One of the many consequential lawsuits focused upon the Coast Guard, claiming that the Guard had failed to exercise due care when it undertook to inspect the ELIAS shortly before the explosion.

Two days before the explosion, ELIAS had caught fire. The Coast Guard was aware of this fire -- which had been extinguished without injury -- and therefore two Guardsmen inspected the ship to see if it could operate safely. The Guard failed to locate the cause of the fire and a short time later the vessel exploded. Plaintiffs contended that the Guardsmen failed to properly carry out the inspection and, therefore, were liable for explosion-related damages.

The court found that the Coast Guard's risk of liability was no less nor greater than the risk of a private person acting as a good Samaritan. It also noted:

"The good Samaritan doctrine incorporates two theories of recovery, depending on whether the injured person is the direct beneficiary or a foreseeable third party beneficiary of gratuitously rendered services . . ."

Applying the Restatement (Second) of Torts § 324A (1965) -- which does not distinguish between a good Samaritan who acts for free (i.e. a volunteer) and one who acts for compensation (i.e. a paid response action contractor) -- the court found that plaintiffs were foreseeable third party beneficiaries of the inspection but that the Coast Guard had not increased their risk of harm. "Increased risk", said the court, "means some physical change to the environment or some other alteration of circumstances." The Coast Guard was not liable.

Patentas then, is important for two reasons. First, it introduces the concept of direct and foreseeable beneficiaries. Second, it shows a different approach to the "worsening" element. Where Gavagan did apply liability, Patentas did not. Perhaps this is because the injured persons in Gavagan were direct beneficiaries of the Coast Guard's rescue attempt while the injured persons in Patentas were merely foreseeable third party beneficiaries of the Coast Guard's inspection. Perhaps this is because the casual nexus in Gavagan was much easier to pinpoint. Everyone knew that someone had to rescue the Donald Ray or it certainly would be lost. No one suspected that the fire in Patentas was going to lead to an explosion. Or, perhaps this is an example where Samaritans are not liable for simple negligence (Patentas) but are liable for gross negligence (Gavagan).

IV. *Berg v. Chevron, U.S.A., Inc.* 759 F.2d 1425 (9th Cir.,
Alaska, 1985)

Ogie Berg was the master of the CAPELLA, bound for the waters of King Cove, Alaska. He struck the rocks at Cape Lazaref, puncturing CAPELLA's hull. The ALASKA STANDARD, owned by Chevron, responded to Berg's distress signal and began towing CAPELLA toward a port. Due to deteriorating weather the ALASKA STANDARD was forced to anchor off Fox Island. During the anchorage CAPELLA sank and most of her crew drowned.

Berg's estate sued Chevron for wrongful death (a personal injury tort). Although the federal district court imposed liability on Chevron, awarding Berg's estate 1.2 million dollars, the circuit court reversed. The circuit court held "that the proper standard of care is that a rescuer will be held liable only (1) for negligent conduct that worsens the position of the victim or (2) for reckless and wanton conduct in performing the rescue."

Inasmuch as this was a case involving Alaskan waters, it shows that -- absent statutory law -- the maritime good Samaritan doctrines define the scope of a responder's liability in Alaska. Of course, a response action contractor's liabilities are also defined by his contract and, at this time, by statute.

Berg is also helpful in pointing out that the occurrence of tragedy does not necessarily mean someone was negligent. The master of ALASKA STANDARD had been in nearly constant radio communication with Ogie Berg; had repeatedly offered to take Berg and crew on board but Berg had refused; had offered to bring the CAPELLA alongside but Berg had declined that invitation; and, generally, had endeavored to minimize the risk to CAPELLA's crew. After CAPELLA sank, ALASKA STANDARD's master had failed to undertake any rescue operations. But, this failure was excused due to the dangerous weather conditions. These considerations by the Berg court show that the question of whether a good Samaritan was or was not negligent turns on the specific facts and circumstances making up the incident in question.

V. *Wright v. United States*, 700 F. Supp. 490 (N.D. Cal. 1988)

Jack Wright's wooden boat came apart while at sea. The Coast Guard provided bilge pumps via helicopter and -- when a U.S.C.G. rescue boat arrived -- saved the crew. However, the Coast Guard was unable to save the boat. Wright sued the Coast Guard for the value of the boat. Wright lost.

In denying Wright's claim, the court attempted to outline parameters of the maritime good Samaritan doctrine. It said:

1. The Coast Guard has no affirmative duty to render aid to a vessel or person in distress;
2. If the Coast Guard does respond, it is not required to provide any particular kind of equipment;
3. The Coast Guard is not held to any higher standard of care in its rescue operations than a private person;
4. The standard of care exhibited by rescuers is measured by the unique circumstances of the rescue.

Some of these maxims are widely accepted. Others are not. Maxim #1 is widely accepted. Applying it to the oil spill context, we can say that in the absence of a statutory or contractual requirement no one is obliged to assist the oil-releasing vessel.

Maxim #2 is called into question by *Petition of the United States*, a case discussed *infra*. Wright's point may or may

not be valid. Assuming, for the sake of argument, that it is valid, a responder could respond with any equipment, no matter how ineffective. (Again, this is only true under common law. Alaska's statutes have, and contract provisions might, alter this maxim.)

Wright's third maxim raises a question. What standard (common negligence or gross negligence?) is a private person held to? Several cases discussed below attempt to answer this question and they appear to differ in their conclusions. Also, one of those cases, *Miller v. United States*, disagrees with Wright's third maxim, whatever the standard may be. But, if Wright is correct, governmental responders (local, state or federal) have neither more nor less protection than any other responder. Municipal corporations that join response cooperatives will want to note the benefits provided by this rule.

The validity of Wright's fourth maxim is confirmed by the *Berg case*; the issue of a good Samaritan's liability is highly fact-specific.

VI. *Grigsby v. Coastal Marine Service of Texas, Inc.*, 412 F.2d 1011, 1021 (5th Cir., Louisiana, 1969), cert. dismissed, 396 U.S. 1033 (1970).

When does a lack of due care by a Samaritan expose the Samaritan to liability? Is he liable for negligence or only gross negligence? In a broad discussion of "the Amphibious Good Samaritan" law, this court said:

"Of all branches of jurisprudence, the admiralty must be the one most hospitable to the impulses of man and law to save life and limb and property

[T]o eliminate a deterrent to voluntary, impulsive response to need as the forces of nature or man, or both, imperil ship or seamen, the law accords a considerable latitude in the standard of performance of the salvage service."

This suggests that a Samaritan is only liable for gross negligence. However, it may be that times have changed. Given the next case, Miller, it may be that a responder will -- in the absence of AS 46.03.825 -- find that courts no longer afford such "considerable latitude."

VII. *Miller v. United States* 614 F. Supp. 948 (D.C. Me. 1985)

This is a case where the Navy, acting as a good Samaritan, was held liable for simple negligence. Miller and his companion were attempting to sail a small wooden boat from New York to Washington via the Panama Canal. They ran out of water off the

coast of North Carolina but failed to stop and replenish their supply.

On the next day they hailed a Navy vessel, the U.S.S. GUADALCANAL, seeking water and a position fix. Due to a series of misunderstandings and miscommunications, GUADALCANAL's captain thought Miller and his companion were in need of rescue. He succeeded in bringing the adventurers aboard but inadvertently sank their boat in the process. Miller sued the Navy.

The court employed a simple negligence standard. Navy lawyers argued that they should only be liable for gross negligence and that the captain's conduct was not gross negligence. Quoting another case, the Miller court responded:

In seeking exoneration, the government makes much of the principle that a salvor who is a "good Samaritan" is not held to ordinary standards of care. Whatever may be the limits of this principle with respect to volunteered salvage, we believe that if the Navy accepts a mission it should conduct its share of the proceedings with acceptable seamanship. We refuse to take the government's view, and be party to adding to the honored motto, 'Semper Paratus' [Always Ready] the words 'Interdum Prudens' [Sometimes Careful].^{5/}

^{5/} 614 F. Supp. at 954. Citations omitted.

Thus it appears that at least some good Samaritans can be held liable for simple negligence. If this is the case, AS 46.03.825 -- which only imposes liability for gross negligence -- provides significant protection over common law.

The Miller court also applied principles of contributory negligence. It is unclear whether, and to what extent, notions of contributory or comparative negligence apply in Alaska in any context. In the context of response action contractors those notions are muddled even more. However, as exemplified by this case, contributory negligence may be applied under maritime common law.

VIII. *Petition of the United States*, 255 F. Supp. 737 (D. Mass. 1966) (Petition I); *aff'd in part, reversed in part by United States v. Sandra & Dennis Fishing Corp.*, 372 F.2d 189 (1st Cir. 1967) (Petition II); *cert. denied* 389 U.S. 836 (1967).

Like Gavagan, this case exemplifies gross negligence. As the story unfolds Gerald H. McManus is commander of a 95 foot Coast Guard patrol boat assigned to the busy fishing district of George's

Bank, off the shores of Massachusetts. By the end of the story he is stationed at a desk, studying loran, on St. Paul's Island, Alaska. His grossly negligent "rescue" of a disabled fishing vessel would have been comical in a pathetic way but for the loss of lives that resulted. Suffice it to say that Commander McManus unquestionably left the persons he was "saving" in worse condition than when he found them. Given that fact the district court had no difficulty finding liability notwithstanding "good Samaritan" doctrines and concepts of sovereign immunity.

Unlike Wright, this court appears to agree with Miller that the Coast Guard can be held to a higher standard than private party responders. 255 F. Supp. at 748, 372 F.2d at 197. If that is true, (and Wright's third maxim is false), governmental responders who qualify as "response action contractors" within the meaning of AS 46.03.826 are afforded very substantial protection by AS 46.03.825. While common law holds governmental responders to a higher standard and imposes liability for simple negligence, Alaska's law holds all response action contractors to the same standard: gross negligence.

Another point where Petition I differs from Wright is in its holding that negligence arises if a responder does not have adequate equipment on hand, irrespective of how adeptly available

equipment is used. In this case the Coast Guard vessel was equipped with a defective loran, a defective gyro compass and repeater, a defective fathometer and a totally inoperative radio direction finder. In sum, this "rescue" ship was completely unable to fix its position at sea. The district court held that it was negligent for the Coast Guard even to send such an ill-equipped ship on a rescue mission, irrespective of the outcome of that mission.

The appellate court took a somewhat more conservative approach. It held that the government was not required to place any particular equipment on board its rescue vessels but that if the vessel was so poorly equipped as to be unable to effectuate its mission, the ship commander had a duty to make that shortcoming known to those who sought his assistance. 372 F.2d at 195-196. Under either interpretation, it seems clear this case differs from Wright's second maxim. Given Petition's concept, a response action contractor may be negligent if he fails to equip his vessel with such response equipment as is reasonably necessary.

It is unclear whether a lack of operative equipment constitutes "gross negligence." Assuming that it does not, AS 46.03.825 in its current form insulates the responder from Petition's concept. Absent AS 46.03.825, a court might apply the

Petition concept and impute liability to a responder whose lack of equipment increased the risk of loss.

LEGISLATIVE HISTORIES

The Oil Pollution Act of 1990

Section 4201 of the Oil Pollution Act (OPA) amended subsection 311(c) of the Clean Water Act (CWA). Section 311 deals with oil spills on navigable waters. Section 4201 empowers the President to ensure effective and immediate removal of oil or hazardous substances which have been discharged into the environment. The OPA goes on to add an exemption from liability for those persons engaged in such removal activities.

Exemption from liability -- (A) A person is not liable for removal costs or damages which result from actions taken or omitted to be taken in the course of rendering care, assistance, or advice consistent with the National Contingency Plan or as otherwise directed by the President.

It then goes on to limit the scope of this exemption but the concept of exempting RACs from liability remains.

Congressmen and Senators generally touted § 4201, "Federal Removal Authority" as a critical feature of the OPA. 6/ Of course the exemption provision is a critical feature of § 4201; it does little good to authorize the Coast Guard to commandeer clean-up workers if no workers are willing to clean up. The significance of this provision is evidenced by the fact that it was included in the earliest drafts of the OPA. 7/

Despite the importance of this provision, there is scant legislative history to explain it. All that I could locate was a brief comment by the conference committee that:

This section reflects the conferees' intention that responses to oil spills be immediate and effective. Without such a provision the substantial financial risks and liability exposures associated with spill response could deter vessel operators, cleanup contractors, and cleanup cooperatives from prompt, aggressive response. 8/

6/ E.g. Comments of B. Clement (D-TN), 135 Cong. Rec. H7965 (Nov. 2, 1989).

7/ See comments of Thomas A. Luken (D-OH) 135 Cong. Rec. H 7959 (Nov. 2, 1989) in which he explains how § 4201 of the OPA has been modified so as not to run afoul of § 119 of CERCLA.

8/ 136 Cong. Rec H6273 (August 1, 1990).

The Comprehensive Environmental Response Compensation and Liability
Act

Section 119 of this Act, 42 U.S.C. § 9619, exempts response action contractors from liability for damages or losses resulting from a release or threatened release of hazardous substances unless the release is caused by the contractor's negligent or intentional misconduct. The provision also allows persons in charge of a response to indemnify response action contractors for those risks not covered by insurance.

Section 119 was added to CERCLA in 1986 after six years of experience with the Superfund clean-up program. Congress became aware that RACs, despite the exercise of due care and satisfactory performance of contract specifications, could be deemed a "potentially responsible party" and liable under Superfund. 9/ Because of such contingent liabilities, RACs were unable to insure their response activities and, absent insurance, were unable to obtain many response action contracts. 10/ Monopolies were inadvertently created for a few large contractors who could afford

9/ EPA Interim Guidance on Indemnification of Superfund Response Action Contractors Under Section 119 of SARA, from J. Winston Porter, Assistant Administrator to Regions I - X (April 1, 1987).

10/ Joint Explanatory Statement of the Committee of Conference on Superfund Amendments and Reauthorization Act of 1986, reprinted in Superfund Deskbook (ELI 1986) at 153.

to self insure. This, in turn, drove up the costs of clean-up as monopolistic opportunists were able to increase their rates. 11/ To ensure a competitive marketplace of insured contractors, RACs were exempted from liability.

The Oversight Council should note that CERCLA § 119(c)(8) required the Comptroller General to study and report on the use of CERCLA's response action contractor provision. That report was scheduled to be filed with Congress by September 30, 1989. If it has not done so already, the Council may wish to acquire and review that report as preparation for their HB 196 report.

CONCLUSION

A review of caselaw and legislative history for the OPA and CERCLA unearthed no specific instance where a response action contractor was held liable for non-negligent response activities. Case studies do reveal that common law concepts of limited liability for a good Samaritan will not protect against gross negligence or intentional misconduct and -- at times-- will not

11/ Armstrong, T.M.; Rock, W.G.; Butler, A.L., "Contractor Liability for Environmental Assessments and Remedial Action", Real Estate Law and Practice Course Handbook Series, The Impact of Environmental Regulations on Business Transactions 1989 (Practicing Law Institute 1989), available on westlaw, ENV-TP, 342 PLI/Real 435.

even tolerate negligence. CERCLA's history reveals that common law concepts are not adequate to assuage the concerns of insurers and therefore tend to restrict the market of available response action contractors.

At a minimum, then, Alaska's provision achieves two goals. First it protects contractors from liability for simple negligence. Second, it enhances insurability and thereby increase the number of available contractors.

THE STATE OF ALASKA'S PARTICIPATION
IN SPILL RESPONSE AND PREPAREDNESS IN THE STATE

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This report summarizes the indirect expenditures that the State of Alaska is currently making for oil spill response and preparedness in the state. The primary expenditure that the state makes is the loss in wellhead value -- and therefore in state royalties and severance taxes -- incurred when spill response expenditures are included in the transportation costs used to arrive at wellhead value. The summary does NOT include direct budget expenditures such as those incurred by the Department of Environmental Conservation for contingency plan development and review.

I. THE STATE'S ROLE IN CRUDE OIL PRODUCTION AND TRANSPORTATION IN ALASKA

The State of Alaska occupies two distinct roles with respect to oil production. On the one hand, the state is unique among oil producing states in that it is the owner of almost all of the land from which oil currently is produced. The state's role as landowner is a proprietary role. The state is in the same position as would be any private entity that owned the land. It is through this proprietary interest that the state retains a royalty interest in oil produced from leases on state land.

On the other hand, Alaska, like every other oil producing state, exercises sovereign power over activity within the borders of the state. It is through this sovereign power that the state levies taxes, like the severance tax, and exercises regulatory control, like requiring contingency plans, over activities.

Because almost all oil production in Alaska has been from state leases, the state's sovereign interest and its proprietary interest are often considered together and, as a result, confused. But the powers, rights and responsibilities flowing from these two roles are very different. If oil development occurs on federal lands, such as in the Arctic National Wildlife Refuge, Alaska may see the first significant production within its borders in which the state does not have a proprietary interest.¹ Thus, it is important to understand and consider the differences between the two roles.

A. The State's Proprietary Interest in Oil Production.

Oil and gas leases on state lands -- like virtually all oil leases in the United States on public or private land -- are written to include a royalty obligation to compensate the landowner for its ownership. Royalty obligations vary on different leases; the state has generally offered its leases on a straight percentage of the oil produced, but has occasionally leased oil on a net

¹The land in the Refuge is federally owned. Under current law, the federal government would be required to share royalties from production on federal leases within the Refuge with 90% going to Alaska and the federal government retaining 10%. Thus, if the federal leases provide for a 12.5% royalty, the state's share would be 11.25%. However, Congressional proposals to open the Refuge to leasing have considered changing or eliminating this split.

profit share basis. Table I sets out the royalty obligation for the oil fields in Alaska, and the amount of production from each field. As can be seen from the table, almost of the oil currently being produced in Alaska carries a 12.5% royalty obligation. Two producing fields in Cook Inlet are on federal leases; federal law provides that the state receive 90% of the 12.5% royalty on these leases. At Milne Point, on the North Slope, most of the leases carry a 20% royalty, as do some leases at Endicott.²

The state's role as landowner on state leases is exactly the same as it would be if the state were a private party. The state enjoys no particular advantage over private parties in the same position. Thus, when the state litigates over royalty obligations, it is a contractual dispute in which the state enjoys no presumptions in its favor.

Table I shows that the total annual production of oil in Alaska in 1990 was 647.3 million barrels. The state's average royalty percentage of this oil is 12.7%. Thus, 82.21 million barrels produced in 1990 belonged to the state as royalty owner. The state may take its royalty oil "in kind" or "in value". That is, the state may take possession of the actual barrels of oil and dispose of them itself, or it may require the producer to pay the state the value of the royalty oil. The state takes almost all of its oil in value, but does take some in kind, which it sells to

²Approximately 80% of the oil produced at Milne Point carries a 20% royalty obligation. The remainder carries a 12.5% obligation. The average royalty at Milne Point is 18.3%. At Endicott, about 25% of the oil carries a 20% royalty, with the remainder at 12.5%; the average royalty is 14.4%.

local refineries. When the state does take its royalty in kind, its actual physical possession of the barrels exists for only an instant. When oil is produced, it is assumed that the royalty obligation will be satisfied in value. Thus, if a producer produces 100 barrels, theoretically all of the 100 barrels "belong" to the producer, but each barrel is encumbered by a 12.5% value obligation to the state. If the state then notifies the producer that it will take certain of its royalty barrels in kind, it does so only after having arranged for the disposal of those barrels. The state takes possession of the barrels at the lease automatic custody transfer (LACT) meter; it simultaneously transfers the oil to the royalty purchaser at that moment. Thus, the state is never in actual physical possession of the oil, so as to expose the state to liability if the oil spilled.

Even though the state never actually physically possesses royalty oil, the state's royalty interest places it in substantially the same position as any other producer of oil. Policy makers may want to consider the state's ownership of this oil when reviewing the impacts on state revenue of spill prevention expenses. It may be seen as appropriate that the state absorb the costs associated with spill preparedness commensurate with its ownership interest.

B. The State's Sovereign Interest in Oil Production.

The state is exercising its sovereign powers when it taxes and regulates oil production and transportation activities in the state. This power extends to the borders of the state,

regardless of the status of land ownership. Thus, oil produced from federal or private lands within the state is taxed the same as oil produced from state lands.³ Similarly, the state may exercise its police power to regulate all oil activities within the state, regardless of ownership. However, offshore oil produced outside the three mile limit is not subject to the state's sovereign power to tax or to regulate, except as offshore activities have near shore or onshore impacts.

The taxes applicable to oil activities in the state are:

1) the Oil and Gas Properties Production Tax (AS 43.55)(the severance tax) which includes the Conservation Surcharge; 2) the Oil and Gas Conservation Tax (AS 43.57); 3) the Corporate Income Tax (AS 43.20); and 4) the Oil and Gas Properties and Pipeline Transportation Property Tax (AS 43.56).

1. The Oil and Gas Properties Production Tax (AS 43.55).

Alaska's production tax, or severance tax, is levied on value at the point of production.⁴ For most fields, the nominal tax is 15% of value.⁵ This nominal rate is reduced by the Economic Limit Factor (ELF), which is a formula that is sensitive to well and

³On federal leases, the state taxes the oil produced by the private leaseholder. It may not, of course, tax the federal royalty.

⁴ The severance tax has a cents-per-barrel "floor" that becomes the tax if it exceeds the percent of value amount. The cents-per-barrel tax is also subject to the ELF. However, prices have never fallen to the point that the cents-per-barrel alternative was used, although they approached the point in 1986.

⁵ The nominal rate is 12.5% in a new field for the first five years.

field productivity. The higher the field productivity the closer the severance tax approaches the nominal rate of 15%. The actual severance tax rate for oil producing fields in Alaska is set out in Table I. This rate is levied against the non-royalty production in the field. In 1990, oil and gas producers paid \$972.3 million in severance taxes. State Department of Revenue, "Revenue Sources Book" Spring 1991, p. 50 (hereafter, Revenue Sources Book).

The severance tax includes a "conservation surcharge" of \$.05 cents per barrel on the same barrels taxed by the severance tax. AS 43.55.200. The legislature may appropriate the proceeds of the surcharge to the Oil and Hazardous Substance Release Fund; if the amount in the fund exceeds \$50 million, the surcharge is suspended. AS 43.55.210-240. Since its inception in 1989, the surcharge has not been suspended. In 1990, oil and gas producers paid \$26.9 million under this tax. Id.

2. The Oil and Gas Conservation Tax (AS 43.57). The conservation tax is 4 mills (\$.004/bbl) on the same production taxed under the severance tax. Conceptually, the tax pays for the Alaska Oil and Gas Conservation Commission. In 1990, \$2.4 million was collected under this tax from oil and gas producers. Id.

3. The Corporate Income Tax (AS 43.20). The corporate income tax rate is 9.4% for income above the threshold level of \$90,000. Every corporation organized for profit in the state is subject to the tax. Corporations that do business in more than one taxing jurisdiction apportion their income to Alaska for tax purposes by use of the apportionment formula set out in AS 43.19 (the

Multistate Tax Compact). An apportionment formula estimates in-state income by starting with the entity's overall income, and then apportioning a part of that income to the state through the use of formula indicators of business activity (such as payroll, property and sales). Overall income is multiplied by the average percentage of the factors in the state to arrive at taxable state income. Corporations engaged in the production or pipeline transportation of oil use a special formula set out in AS 43.20.072.

Spill prevention and response expenditures are deducted from gross income by every entity that incurs them, if that entity is organized for profit. However, calculating the impact of these deductions on state revenue cannot be done without access to the confidential tax returns of the taxpayers. This is because the use of apportionment formulas makes the relationship between expenditures and impact indirect. If a corporation does business only in Alaska, and deducts a spill related expense, then the revenue impact is simply 9.4% times the amount of the deduction. But most corporations, especially oil companies, do business in many jurisdictions. The spill expense is then deducted from worldwide income, and a fraction of that income is apportioned to Alaska.⁶ Depending upon the magnitude of the corporation's out-of-state activities, the impact of the deduction is diluted to a greater or lesser degree. (At the same time, spill related expenditures in other jurisdictions reduce income tax collections

⁶ In 1991, the legislature repealed "worldwide unitary" apportionment for most taxpayers. HB 12. However, it retained the worldwide unitary approach for oil and gas taxpayers.

in Alaska.) An accurate analysis, or even a rough estimate, of impact cannot be done without access to tax returns.

For this reason, income tax impacts are not analyzed in this report. However, unlike the wellhead value reductions in severance taxes and royalties which reflect only spill expenditures in certain areas of the state, income tax deductions are taken everywhere that they occur. Thus, while Alyeska's expenditures impact severance taxes and royalties and Tesoro's expenditures do not, the expenditures of both Alyeska and Tesoro impact income taxes. Corporate income taxes collected from oil and gas taxpayers in 1990 were \$117.2 million. Revenue Sources Book at 50.

4. The Oil and Gas Production and Pipeline Transportation Property Tax (AS 43.56). The oil and gas property tax is a 20 mill tax levied on the "hardware" associated with oil and gas production and pipeline transportation. Although the tax is a state tax, municipalities are permitted, with certain restrictions, to levy property taxes on the same property. Taxpayer payments to a municipality are a credit against the state tax.

Oil spill equipment that is associated with production or pipeline transportation activities is taxed under this law. Thus, Alyeska's expenditures for pipeline and terminal spill protection are presumable taxed, as are the North Slope producers' expenditures, including those of Alaska Clean Seas. However, because of the set-off provision for municipal taxes, the state receives only a small portion of the revenue produced by this tax. While it would appear at first glance that the state should see

increased revenue as a result of a property tax on pollution equipment, in fact, as described below, the revenue effects can be negative. The state collected \$89.8 million from this tax in 1990. Id.

II. THE NET-BACK METHODOLOGY AND STATE REVENUES

An Alaska oil producer's liability for both the state's severance tax (the Oil and Gas Properties Production Tax (AS 43.55) and the state's royalty is based on the value of the oil at the point of production. Because most Alaska oil is not sold at the point of production, a "net-back" methodology is used to establish this value. Sales in the lower 48 states are netted back to the wellhead by deducting the costs of transporting the oil between Alaska and the market. This calculation generates a value at the point of production. Those sales that are made at the wellhead or elsewhere in Alaska are generally valued by reference to the price received for the oil sold in the lower 48 states.

Use of this methodology means that there is a direct relationship between transportation expenditures (including spill prevention and response expenses) and wellhead value. The revenue effect of transportation expenditures for Alaska North Slope crude (ANS) is approximately 25%. That is, for every \$1.00 deducted by a producer as a transportation cost, state revenues from severance taxes and royalties are reduced by \$.25.⁷ Thus, if spill response equipment and operating expenses are included in the costs of transporting oil, state revenues are reduced accordingly, and the

⁷ Horst (see note 9, post), Table 2, line 36.