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The Jones Walker Energy E*Zine reviews and discusses developments in the energy industry, with a particular focus on matters that affect Louisiana. It addresses all legal disciplines within the energy industry, including the exploration and production of oil, gas, and other hydrocarbons; as well as the processing, marketing, and valuation of these products.

LOUISIANA SUPREME COURT AFFIRMS \$33 MILLION PROPERTY RESTORATION DAMAGE AWARD AGAINST LESSEE

Corbello v. Iowa Production, et al., 02-C-0826 (La. 2/25/03), __ So.2d __, 2003 WL 536727, *reh'g granted in part for the sole purpose of clarification, otherwise den'd*, __ So.2d __, 2003 WL 21417579 (La. 6/20/03).

In a decision that prompted immediate reaction by the Louisiana State Legislature, the Louisiana Supreme Court recently affirmed a \$33 million award against Shell Oil Company for its failure to reasonably restore property it leased to its original condition. The Louisiana Supreme Court also affirmed an award of damages stemming from Shell's unauthorized disposal of saltwater on the property and based on Shell's failure to vacate the leased premises after the lease had expired. Responding to the decision, during its 2003 Regular Session, the Louisiana Legislature enacted legislation, which has now been signed by the Governor, directed to claims seeking damages for the remediation of usable ground water.

The Case:

The centerpiece of the case was Shell's 1961 surface lease, which contained the following language:

“Lessee further agrees that upon termination of this lease it will reasonably restore the premises as nearly as possible to their present condition.”

The Louisiana Supreme Court rejected Shell's argument that its liability for reasonable restoration was limited to the “market value” of the property (\$108,000), stating: “[i]n this case, Shell, a sophisticated company with vast experience in negotiating oil and gas contracts, bound itself by contract to reasonably restore plaintiff's property as near as possible to current condition.” Addressing the proper measure of damages, the Court did note that Louisiana courts “have consistently restrained property damage awards in tort cases” by limiting the awards based on the market value of the property. But,

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refusing to apply the tort-case approach, the Court held that the measure of damages “in breach of contract cases is governed by the four corners of the contract” and thus refused to tether the damage award to the market value of the property in light of the explicit contractual provision in the lease imposing a restoration obligation.

The Louisiana Supreme Court also disagreed with Shell’s argument that the private award erroneously included an award for damages to the Chicot Aquifer, which was a public injury, even though the plaintiffs had no legal duty to use the award to restore the property. The Court framed the issue as whether it had “authority to modify a breach of contract damage award to a private landowner because the landowner has no duty to actually use the money to clean and restore the land where the legislature has not chosen to mandate remediation or restoration.” The Court held that “the fact that the contamination of the groundwater, for which the plaintiff recovered \$28 million in restoration damages, is a public injury as well as a private injury, does not prevent plaintiffs from collecting damages for cleanup of the groundwater.” In reaching its decision, the Court specifically found that the Oilfield Site Restoration Law, La. R.S. 30:80, *et seq.*, did not preclude a private landowner’s right to seek redress against oil companies. In finding that Louisiana law allowed a private party to recover damages for groundwater cleanup, the Court further observed that “Private landowners in Louisiana have no duty to seek relief from an administrative agency before filing suit against an oil company.” (This part of the Court’s decision prompted the enactment of the legislation discussed below).

The Court also examined plaintiffs’ claim for damages arising from Shell’s alleged unauthorized disposal of saltwater. First, the Court concluded that plaintiffs were entitled to damages resulting from the unauthorized disposal because the lease contained – and Shell breached – a specific provision, separate from the restoration provision, regarding saltwater disposal. Second, the Court rejected Shell’s argument that the cause of action for the unauthorized disposal had prescribed, concluding that “plaintiffs’ breach of contract claims against Shell, including the claim for unauthorized disposal of saltwater, arose upon termination of the . . . surface lease, at which time Shell was to tender the property back into plaintiffs’ possession.” The Court, however, rejected the lower courts’ \$16.7 million damage calculation for the unauthorized disposal of saltwater, reversing and remanding for a determination of the proper award of damages. The Court did so because it disagreed with the lower courts’ use of an investment/inflation factor in arriving at the award, finding instead that the prejudgment interest rate was the proper method to calculate the present value of the damages. In reversing the award,

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the Louisiana Supreme Court held that, “Unlike judgments in *ex delicto* actions wherein legal interest attaches from judicial demand, interest is recoverable on debts arising *ex contractu* from the time they become due, unless otherwise stipulated.”

Concluding that exemplary damages under former Louisiana Civil Code article 2315.3 did not apply to breach of contract claims, the Court rejected plaintiffs’ demand for punitive damages, finding that plaintiffs’ claims sounded solely in contract. Finally, the Court upheld the \$4 million award of attorneys fees to plaintiffs.

Partial Rehearing:

Granting partial rehearing for the sole purpose of clarification, the Louisiana Supreme Court addressed Shell’s argument that the evidence submitted to establish damage to the Chicot Aquifer was speculative. In doing so, the Court held that “Proof of actual damages by a preponderance of evidence is required to be entitled to compensation for environmental damages.” The Court then found that the specific evidence presented established that the “threat to the aquifer is real; the pollution on plaintiffs’ property is undisputable.” So, although granting Shell a partial rehearing, in the end, the Louisiana Supreme Court left unchanged its original decision.

Some Effects of the Decision:

- The Court’s decision to affirm a damage award grossly disproportionate to the value of the land leaves unresolved the issue of the scope of a lessee’s liability for failure to restore when a surface lease (or a mineral lease, for that matter) does not contain a specific contractual provision obligating the lessee to restore the property. Even absent a specific contractual obligation to restore the leased premises, the Louisiana Mineral Code imposes an obligation on a mineral lessee “to develop and operate the property leased as a reasonably prudent operator,” from which an implied obligation to restore the leased property arises. *See* La. R.S. 31:122, comments (“It is established that the mineral lessee must restore the surface even though the lease contract is silent.”) So, it is unclear whether courts will tether damages against a lessee for failure to restore the leased property to the “market value” of the land when the obligation to restore arises solely from the lessee’s implied obligation and not from a specific contractual obligation. In rejecting the tort-case approach that tethers the award of property damages to the market value of the land, the Louisiana Su-

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preme Court relied heavily on the explicit contractual term to which Shell agreed to be bound. Moreover, the comments set forth in the Mineral Code related to the implied obligation note that “There is apparently an economic balancing process which limits this duty” and that “it appears that in effect the obligation to restore the surface is limited by a standard of reasonableness which balances the cost of perfect restoration against the value to which the land is being put to use.” La. R.S. 31:122, comments. Accordingly, even after *Corbello*, a mineral lessee that operated under a lease that was silent on the duty to restore and that faces a failure to restore claim continues to have a viable argument that any damages awarded must be balanced by the market value of the property. Under Louisiana’s newly enacted statute (which is outlined below), however, there appears to be no room to argue that market value should limit a lessee’s liability for ground water contamination.

- The Court’s finding related to Shell’s prescription argument that the plaintiffs’ cause of action did not arise until the lease terminated may provide a “prematurity” defense to oil companies when landowners bring suits alleging restoration damages while the lease remains in effect. A successful prematurity defense may afford the oil company time to perform reasonable restoration measures in an effort to avoid litigation down the road.

The Legislation:

Act 1166 (La. R.S. 30:2015.1), now signed by Governor Foster, addresses litigation involving claims seeking damages for remediation of usable ground water. Generally, the Act requires parties seeking damages for ground water contamination to notify two Louisiana State agencies, the Department of Natural Resources (“DNR”) and the Department of Environmental Quality (“DEQ”), granting the agencies the opportunity to intervene in the litigation. It also requires a court that finds that ground water contamination exists to adopt a plan for remediation and to administer the funding for the remediation. The Act further includes a provision indicating that it is to be applied retroactively (with certain exceptions) to all cases filed after August 1, 1993.

Specifically, the Act:

- requires any litigant seeking to recover damages “for the evaluation and remediation of any contamination or pollution that is alleged to

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impact or threatens usable groundwater” to provide written notice to the State of Louisiana through both DNR and DEQ.

- provides that DNR and DEQ “shall have the right to intervene” in the litigation.
- requires the court, upon its determination that contamination of usable ground water exists, which poses a threat to public health, and, upon its determination of the party responsible, to adopt a plan to evaluate or remediate the contamination consistent with the health, safety and welfare of the people.
- requires the court, in adopting a remediation plan, to provide DNR and DEQ with an opportunity to provide input into the formulation of the plan and requires the court to consider any input provided by DNR and DEQ before adopting the plan.
- requires the court to order the party responsible for the contamination to fund implementation of the plan by depositing funds into the court registry and specifies that all damages awarded for the evaluation and remediation of contamination of usable ground water shall be paid exclusively into the court registry (excluding damages for personal injury), regardless of whether DNR or DEQ becomes a party.
- authorizes the court to issue all orders necessary to ensure that the funds are “actually expended for the evaluation and remediation of the contamination . . .”
- provides that a party providing evidence that another party is responsible for contamination is entitled to recover costs, including expert witness fees and reasonable attorney fees, from the party cast in judgment.
- provides that DNR and DEQ shall recover, from the party cast in judgment, all costs, including evaluation and review costs, expert witness fees and reasonable attorneys fees, when DNR or DEQ, either as a party or through witnesses, provides evidence or contributes to a determination of responsibility.
- provides for “expedited” review or appeal of any judgment adopting a plan of evaluation or remediation of contaminated usable ground water.

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- expresses the Legislature's intent that the Act "shall be interpretive, remedial and procedural and shall be applied both prospectively and retroactively only to cases filed after August 1, 1993."

Some Effects of the Legislation:

- Historically, parties in the oil and gas industry facing suits by landowners for alleged property damage have sought to involve administrative agencies by raising exceptions based on the landowners' failure to exhaust administrative remedies. The legislation, by requiring litigants seeking damages related to contaminated ground water to notify DNR and DEQ and then authorizing agency intervention in the lawsuits, pushes agency involvement to the front burner. It also does so by requiring courts to request agency comment when formulating and adopting remediation plans. What remains to be seen is how active a role DNR and DEQ will take in ground water contamination suits now that the legislature has extended the invitation.
- The new statute also specifically addresses one of the concerns raised by Shell in *Corbello*. Shell's concern was that, by paying a private award to redress a public injury, a party cast in judgment may subject itself to paying double upon later receiving a state order requiring remediation. Shell's theory was that, in the event that a defendant did not receive statutory credit for payment of private restoration damages under La. R.S. 30:89.1, the defendant could pay double for the same injury. The Louisiana Supreme Court ultimately rejected Shell's argument on the basis that the legislature had not declared that a private party's recovery for public injury prevented the private party from collecting damages. By enacting the statute, the legislature has now declared that a private landowner cannot pocket the damages recovered; ground water remediation damages must be spent to redress ground water contamination.
- The statute may also affect the venue of ground water contamination suits. Depending on whether DNR or DEQ elect to intervene and on the circumstances of a particular case, litigants may find themselves in the 19th JDC.
- Further, by requiring the courts to adopt and oversee the funding of environmental remediation plans to redress ground water contamination, the statute imposes a burden on the courts that falls outside of the traditional functions of the judiciary. The statute, however, plainly

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contemplates involvement by DNR and DEQ, agencies with expertise in the environmental field. Again, whether DNR and DEQ will accept the invitation to intervene in ground water litigation and what level of assistance they will lend in formulating the requisite plans remains to be seen.

- Finally and perhaps most importantly, the statute closes a significant loophole by mandating that all damages recovered for ground water evaluation and contamination must be used to evaluate and remediate the contamination, to the benefit of the welfare of the citizens and environment of the State of Louisiana.

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- Author and Editor, Alida C. Hainkel, Partner, Energy

Remember that these legal principles may change and vary widely in their application to specific factual circumstances. You should consult with counsel about your individual circumstances. For further information regarding these issues, contact:

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