# The Deans of Oil & Gas Law

**Remarks of**
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## *"Responsible Energy"*

Good afternoon ladies and gentlemen. It is my very great pleasure to be with you here today in Houston. The invitation to deliver this speech came to me as a wonderful surprise, and I am humbled at the prospect of speaking to you. This program, as you know, brings together the "whose who" of the American energy bar – veterans of the major controversies facing our industry…true experts in the field.

As many of you know, I am a complete newcomer to this area, having spent my entire career prior to ChevronTexaco as an antitrust lawyer in Washington, DC. Even though I started my career in the Petroleum Section of the Federal Trade Commission working on the infamous and ill-fated shared monopoly case, In re Exxon et al, energy was never a significant part of my law practice before joining ChevronTexaco.

As an aside, I am often asked to speak about antitrust in the technology field, which used to be a sub-specialty of mine. Last year I appeared on a panel of Silicon Valley general counsel. When the moderator introduced my counterparts from various computer industry law departments, he said that Charles is not really in a "technology" business, but he knows a great deal about the topic. I replied that anyone who has ever tried to extract high pressure oil out of 6000 feet of water knows that the oil business is as "high-tech" as it gets. The oil business is not just bits and bytes; it is technology in action.

Now, I find myself racing to learn many of the things that you veterans of the oil and gas industry already know all too well. I do, however, bring an outsider's perspective to many of the issues facing our industry, and it is very often the case that a new viewpoint, albeit somewhat naïve, can be at least interesting, and perhaps even useful. With that in mind, I thought I would talk about the topic of "responsible energy" – the challenges we all face in delivering a vital commodity to the world in a very hostile legal and political environment. I will end my remarks with a few suggestions on how our industry might better position itself for success in the legal battles we must fight.

**Misperceptions of the Oil Industry**

Many of you here today live and work in Houston, an oil industry town. I, on the other hand, live in California, where many are dubious of, if not outright antagonistic to, our business. While the "real politique" of California perhaps represents an extreme, I think we all understand that our industry is misperceived and unduly vilified.

Our industry is routinely castigated for high prices. Yet in the period since the first oil shocks of the 1970's, gasoline has been, in real terms, one of the most inflation-proof mass commodities. In fact, a gallon of premium unleaded gasoline, even in California, actually costs less at retail than a gallon of fancy spring water. Nevertheless, we can count on any significant upward movement in gasoline prices to prompt transparently political government investigations

that will never be closed with the same fanfare as attends their commencement.

Before coming to the oil industry, I had never worked in an atmosphere so preoccupied with occupational and environmental safety. We at ChevronTexaco aspire to move beyond world class status in the safety arena, and have set the ambitious goal of achieving incident-free operations. Workplace safety and spill performance are among our most important and closely-monitored operational metrics. In striving to be world class, we understand the outstanding safety and environmental performance of our peer group companies, and know that your companies are as devoted to incident-free operations as we are.

Most Americans cannot routinely get a cup of coffee from the kitchen to their favorite chair without a calamity, yet our industry regularly transports huge volumes of oil and gas across vast distances with relatively few significant discharges into the environment. The ChevronTexaco shipping company just celebrated its second consecutive year of operations without a single spill. Few Americans, however, understand the effort our industry makes to operate in a safe and environmentally responsible manner, preferring instead to blindly cast us as environmental villains.

It is a cruel fact that many of the world's most significant concentrations of hydrocarbon resources reside in some of the most politically and economically challenged regions of

the globe. Many who live in the most resource-rich nations experience crushing poverty and seemingly endless political instability. Our companies make huge investments in those countries, and in so doing bring the prospect of economic development and social reform. Intellectual elites, however, speak of something they call the "curse of oil," asserting that the income streams that flow into troubled governments from oil development necessarily encourage public corruption and exacerbate political acrimony.

ChevronTexaco has built itself on the conceptual trilogy of "people, partnership and performance." We seek to be a welcomed partner in the countries where we operate, and in the under-developed world we are devoting considerable resources to building human capacity. Our $25 million pledge in Angola is a case in point. We are proud to have received the State Department's Corporate Excellence Award for our work in Africa and to have been honored by the Organization of American States for our work in Latin America.

ChevronTexaco is not alone. We recognize and salute the socially responsible stands that others in our industry have taken in the areas of environmental stewardship, financial transparency and public health, to name just a few. Our industry, however, is not broadly recognized for its positive contributions. Quite the contrary, we are often blamed for the adverse conditions that exist in the oil producing regions, and we face an aggressive community of NGOs

who oppose almost any form of energy development in the third world.

Even the economics of our business are broadly misunderstood. Few in the public understand the huge economic rents the oil producing nations extract from the international oil companies in the form of leasing costs, production sharing, royalties, taxes and bonuses. While the industry is presently enjoying strong profits, long-term returns in our industry are cyclical and rather modest, tied as they are to growth trends in the world economy.

The competition in our industry is fierce, particularly as a growing list of competitors, including the emerging national oil companies, vies for access to a narrowing field of development opportunities. Just last week, the New York Times ran an article describing the investment conundrum facing the industry. Despite high crude oil prices and tight processing capacity, the industry has been slow to launch into major new investments, in part because of the cost of high-impact investment opportunities and corresponding concerns about future prices and margins.

**The Legal Landscape**

Make no mistake about it, oil and gas is a tough business, and it is made even tougher by the challenges we face on the legal front. In the contractual arena, our co-parties are powerful governments, who control not only the hydrocarbon resources that exist in their countries, but also their own legal, regulatory and taxation systems. Just

sustaining the basic benefit of the bargain over the course of a long-lived project is difficult under the best of circumstances. Increasingly, we are seeing international oil companies having to resort to arbitration and other legal challenges to enforce basic contractual rights. Lawsuits of this nature are no bargain, particularly when they must be fought out in local courts. Just last year, we were pleased to prevail in an environmental suit contested before the Supreme Court of Kazakhstan, reducing a fine of approximately $70 million to just $7 million. In contrast, our predecessor company, Texaco, litigated a series of contract disputes against the Government of Ecuador. Those suits, which represent hundreds of millions of potential benefit to our company, have been pending in the courts of Ecuador for 10 to 12 years, with no movement toward resolution in sight.

We also face a challenging regulatory environment – here in the United States and around the world. I began my career in government in the Reagan Administration, and those of us working in the economics sphere back then envisioned a clear path toward deregulation and free market globalization. Globalization, of course, faces a constant battle with economic nationalism, and the events of 9-11-2001 have been a complicating factor. For the last several years, deregulation as an economic movement, has fallen into disrepute in the wake of the corporate scandals in the U.S. and elsewhere. Congress and the American public have become distrustful of business, and the self-policing forces of the market are not presently regarded as being sufficient.

Over the last few years, the regulatory community in Washington has been empowered with new legislation – Sarbanes-Oxley being the most notable example. I was the head of the Antitrust Division when Sarbanes-Oxley was passed, and I recall receiving a call from a Senate staffer asking me whether I wanted anything for the Antitrust Division in the bill. He described it as though there was a blank check for anything, no matter how extreme, that could be characterized as strengthening white collar criminal enforcement.

The agencies have been largely re-loaded, with new funding and increased staffs, and many now have adopted an "in-your-face," take-no-prisoners approach to their work. We see this in the ever-increasing assault on the attorney-client privilege and in the expectation that "cooperation" with a government inquiry will consist of total supplication, as though it is somehow "bad form" to mount a legal defense.

Because some of the conduct that has prompted this regulatory renewal has been so utterly indefensible, the corporate community has been forced to stand mute through all of this. Any call for moderation could be misinterpreted as support for corporate vice. Just now, we are seeing the first signs of people questioning whether all of this new regulatory oversight is prudent or advisable.

Turning more specifically to the oil and gas industry, we have come to expect a steady diet of basic environmental and business litigation as a basic fact of life in our business.

For the major international oil companies, however, we now also face an increasing onslaught from a combination of plaintiffs lawyers and anti-development activists -- sometimes separately, sometimes together, and now increasingly in league with state attorneys general.

To be sure, our industry has been targeted by these groups. We see this in the class action royalty suits. We saw it when plaintiffs' lawyers rushed to file MTBE suits in so-called magic jurisdictions just ahead of the relatively modest MTBE litigation reforms contained in last year's proposed energy bill. We see it in the way state and local governments are "bountying-out" more and more of their environmental litigation to personal injury lawyers – the wave of new actions in the NORM and NRD areas being an example. We see it in the politicized actions brought under the Alien Tort Claims Act.

We are targeted in this manner because we are politically unpopular and are perceived to represent a convenient deep pocket. Moreover, these types of suits against us can be fought in the media, which is almost always favorably disposed toward a story that can be told in the David versus Goliath paradigm. The formula is simple: file suit in a favorable forum, claim big numbers, attack the company's reputation in the media, and press for a quick settlement. The litigation we face relating to Texaco's former operations in Ecuador is a case in point.

## The Rain Forest Litigation

From 1964 to 1992, Texaco participated in a production consortium in the Oriente region of Ecuador. Through a series of transactions, PetroEcuador came to own 62.5 percent of the consortium, while Texaco Petroleum owned 37.5 percent and initially served as the operator. The consortium worked under a joint operating agreement, containing fairly standard indemnification and arbitration provisions. As the majority partner, PetroEcuador had complete approval over most operational matters. As the underlying concession wound down, PetroEcuador exercised its right to become operator for the final two years, and declined Texaco's offer to extend the concession.

To wind up the concession, the parties commissioned environmental audits and agreed upon a plan that called upon each party to perform its proportionate share of the necessary remediation. Texaco submitted a plan that received full governmental approval, and performed a multi-year $40 million remediation program under close government supervision. Every aspect of the plan was checked, tested and approved by Ecuadorian authorities. At the conclusion of the remediation, Texaco Petroleum received full releases from any further environmental liability from various agencies of the Ecuadorian government, and from local tribal organizations. PetroEcuador, however, did not perform its share of the remediation, and has continued to operate on the consortium sites until today.

Notwithstanding these efforts to leave Ecuador on positive terms, our company has come under attack from rain forest activists, working in close association with US-based trial lawyers. Their initial suit in New York under the Alien Tort Claims Act was dismissed. Thereafter, essentially the same groups filed suit in Ecuador under a statute that did not even exist during the time that Texaco operated in Ecuador and which the courts of Ecuador have already ruled does not apply retroactively.

The plaintiffs in these actions are not at all interested in the legal releases Texaco Petroleum obtained from the Ecuadorian government, or in the fact that the environmental damage that presently exists there comes either from PetroEcuador's failure to perform its share of the remediation or from PetroEcuador's ongoing production operations. Instead they are waging a public relations battle in the media that is almost totally devoid of facts or science. Each year, as we approach our annual shareholders meeting, we watch the plaintiffs' lawyers and their allies gear up their misinformation machine, in an effort to pressure the company for what they should not be able to achieve under the rule of law.

One of their favorite tactics is to take media and investor groups on tours of the PetroEcuador's production sites, where they stand in front of presently operating facilities – bear in mind that is has been nearly 15 years since Texaco Petroleum operated there – and blame Texaco for the damage they observe.

In the mean time, we are conducting a multi-front legal battle, with a defense of the case in Ecuador, and arbitration we have commenced in New York to enforce the indemnification provisions of the joint operating agreement and the releases we obtained under the remediation agreement. The effort is costly and distracting corporate resources. Interestingly, these plaintiffs have never once asked PetroEcuador to perform any form of environmental remediation for the benefit of the indigenous people they purport to represent. The entire thing is "Kafka-esque."

**The Path Forward**

I do not want my remarks to consist totally of a rant against the evil forces that attack our industry. I want to offer some views about how we can make things better. To that end, I offer the following five suggestions.

First and foremost, the companies in our industry should become tireless supporters of tort reform. In the last 2-4 years, the tort reform movement has gained considerable momentum at the state level, and Senate passage of the Class Action Reform Act last week is the first major step toward federal reform. The successful efforts in Mississippi and here in Texas to win broad-based tort reform were monumental victories. The very visible defeat of Judge Maag in Illinois and the successful campaign in California to rationalize the infamous 17200 statute also are noteworthy. These victories, particularly those won at the polls, indicate that the American public understands the

social costs of a broken tort system, and that change can occur when this misbehavior becomes subject to close public scrutiny.

Sadly, tort reform has become a costly endeavor. The plaintiffs' bar, flush with their winnings in asbestos and tobacco litigation, has invested heavily in creating and preserving the status quo. It will take an equal level of investment to win change. In the last two years, ChevronTexaco has significantly increased its financial and sweat-equity commitments to tort reform, through the Civil Justice Reform Group, the Chamber's Institute for Legal Reform and other organizations. I urge you all to consider the value of tort reform to your businesses and to increase your support.

Second, and of equal importance, oil and gas companies must urge other forms of legal reform. Even beyond the procedural problems in our civil justice system, our industry often falls victim to bad laws or good laws misapplied. The Alien Torts Claims Act is a wonderful example. No one can seriously contend that the Alien Torts Claim Act was intended to be what it has, in fact, become. Despite the welcomed limitations imposed by the Supreme Court in the Sosa case, it will take federal legislation to stop these frivolous attempts to make US companies responsible for the conduct of foreign governments. Similarly, legislation to address things like MTBE would be of tremendous benefit to the oil companies and to the public, as well. The cost of rectifying

MTBE contamination is likely to be small when compared to the likely cost if the plaintiffs' bar has its way.

We now have a President who ran against a noted personal injury lawyer and actively campaigned on legal system reform. He has already helped to deliver a major overhaul of the class action quagmire. Now, more so than ever before, is the time to press for meaningful tort and legal reform.

Third, our industry should be united in insisting that the trade policy of the United States continue to press for effective legal reform and adherence to the rule of law by all of our foreign trading partners. Given the magnitude of our investments throughout the developing world, we must be able to count upon basic legal protections and the fair adjudication of legal disputes. These battles cannot be fought on an ad hoc basis by individual companies. Trading status is one of the most important points of leverage that can be exerted upon developing nations. The U.S. stand on this must not be compromised.

Fourth, while our industry is absolutely correct to work with responsible non-government organizations to promote economic sustainability and transparency in the developing world, we must be wary of efforts to impose undue burdens upon private business. It is in the nature of our business that sovereign governments control the resources to which we seek access, and we must contract with those governments largely on their terms. Our industry, however, should not be held hostage to attempts to reform

foreign governments, nor should our companies be expected unilaterally to solve the economic and social problems that exist in certain countries as a cost doing business. As we are asked to sign on to the endless array of initiatives, compacts, protocols and guidelines being promoted by various groups, we must be mindful of our roles as private companies, and of the risks that these well-meaning efforts might become the source of future regulatory regimes and legal disputes.

Finally, when our industry comes under attack, we should be as united as possible in our defense. As a general counsel new to the industry, I have been surprised to see how fractious our industry can be when we are confronted with a broad-based attack against us. We know that our adversaries in the plaintiffs' bar are highly organized and manage to cooperate with each other at least right up until the time that fees are to be divided. I would like to see our industry equally united. We should make the greatest possible use of joint defense techniques, judgment sharing and the like. So far in the MTBE litigation the joint defense strategy has been highly successful, and I am certain that it can work in other situations, as well.

**Conclusion**

In the movie *Pulp Fiction*, the Samuel L. Jackson character quotes a biblical passage to the effect . . . "The Path of the Righteous is Beset on All Sides by the Tyranny of Evil Men." I am not yet prepared to declare our industry the righteous, but I know that our companies almost uniformly

make conscientious efforts to do things the right way. I am proud to be in the oil and gas business, and I am very proud to work for ChevronTexaco. Our companies make the energy that sustains our way of life. We are in the business of producing "responsible energy." Over the years to come, I am hoping that the impediments to fair resolution of the legal issues facing our industry can removed, so that legal issues can become a smaller and more manageable component of our businesses. Legal disputes involving energy companies should be fought out on a level playing field; not one that either assumes guilt or presumes that companies in our industry can absorb the cost of imperfections in the legal system.

From my perspective, lawyers have been forced to become far too important in the life of the modern corporation. And I am looking forward to a day when the job of the general counsel involves quiet days and a low handicap.

Thank you for patiently listening to the views of a non-expert and for allowing me to share my perspectives.