Legal Backgrounder

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SUPERFUND LAW PREEMPTS CONTINGENT FEE ARRANGEMENTS IN NATURAL RESOURCE DAMAGES SUITS

by

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Inspired by the financial bonanza of tobacco litigation, state attorneys general in a number of states have recently focused on natural resource damages ("NRD") litigation as the next potential revenue source for state treasuries. Following the tobacco model, some of these attorneys general have retained private plaintiffs' lawyer firms to pursue NRD claims on a contingent fee basis. In New Jersey, for example, the State Attorney General announced plans to use private attorneys to pursue natural resource damages claims at 4,000 environmental sites across the state. In New Mexico, a federal district court recently dismissed a multi-billion dollar natural resource damages claim brought by private attorneys on behalf of the State Attorney General involving a single Superfund site.[1]

The use of contingent fee arrangements to retain private attorneys in tort litigation has been the subject of significant controversy. Critics argue that vesting power in private attorneys with a direct financial interest in maximizing monetary recoveries distorts government priorities at the expense of other legitimate state interests, and creates serious conflicts of interest for attorneys general who often receive large campaign contributions from these same attorneys.[2] Thus far, legal challenges to contingent fee arrangements have focused on state law issues regarding the separation of powers and government attorneys' ethical obligations of neutrality, with mixed results.[3] This LEGAL BACKGROUNDER focuses on an

[1] *See New Mexico v. General Electric Co.*, 322 F. Supp. 2d 1237 (D.N.M. 2004), *appeal pending.*

[2] *See, e.g.*, John Beisner, *et al.*, *Bounty Hunters on The Prowl: The Troubling Alliance of State Attorneys General and Plaintiffs' Lawyers*, Institute for Legal Reform, available at www.legalreformnow.com (May 26, 2005).

[3] *Compare Clancey v. Superior Court*, 705 P.2d 347 (Cal. 1985) (contingent fee arrangement for private attorney to bring abatement actions under public nuisance ordinance antithetical to standard of neutrality); *Meredith v. Ieyoub*, 700 So. 2d 478 (La. 1997) (attorney general use of contingent fee arrangements to enforce environmental laws violates separation of power) *with Phillip Morris Inc. v. Glendening*, 709 A.2d 1230 (Md. 1998) (allowing contingent fee arrangement in state tobacco litigation); *State v. Hagerty*, 580 N.W.2d 139 (N.D. 1998) (allowing contingent fee arrangement in state asbestos litigation); Order Regarding

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additional problem with the use of contingent fee arrangements in NRD litigation that has not yet been addressed by the courts — the conflict between such arrangements and the Comprehensive Environmental Response, Compensation, and Liability Act ("CERCLA"), 42 U.S.C. § 9607(f)(1).

CERCLA Provides that Natural Resource Damages Recoveries Be Used Only for Restoration of Resources. Under CERCLA, Section 107(f), designated state officials have statutory authority to seek financial recoveries for loss of services caused by injuries to natural resources under their trusteeship. Congress' purpose in enacting Section 107(f) was the restoration or replacement of natural resources damaged by unlawful releases of hazardous substances. *See* H.R. Rep. No. 255 (IV), 99th Cong., 1st Sess. 50 (1985); *Ohio v. Dept. of Interior*, 880 F.2d 432, 444 (D.C. Cir. 1989). Thus, CERCLA expressly provides that designated state trustees may use NRD recoveries "*only* to restore, replace, or acquire the equivalent of such natural resources." 42 U.S.C. § 9607(f)(1). As the D.C. Circuit explained, "[b]y mandating the use of all damages to restore the injured resources, Congress underscored in § 107(f) its paramount restorative purpose for imposing damages at all." *Ohio v. Dept. of Interior*, 880 F.2d 432, 444 (D.C. Cir. 1989).

The legislative history makes clear that natural resource damages recoveries may not be diverted for uses other than restoration of the natural resource:

> The amendment of Section 107(f) clarifies that sums recovered by trustees are to be used only to restore the natural resources without further appropriation. ... The natural resource regime is not intended to compensate public treasuries. Nor are recoveries to be diverted for general purposes.

132 Cong. Rec. H9561, H9612-13 (Daily Ed. Oct. 8, 1986). At least two courts have thus concluded that natural resource damages recoveries may not be diverted to private parties. In *Alaska Sport Fishing Assoc. v. Exxon Corp.*, 34 F.3d 769 (9th Cir. 1994), the Ninth Circuit rejected an attempt by an association of sport fisherman to recover damages for the lost use of fisheries due to the Exxon-Valdez oil spill:

> Given the restorative purposes behind ... CERCLA, it simply makes no sense to reserve a portion of [natural resource] damages for recovery by private parties. Unlike trustees, private parties are not bound to use recovered sums for the restoration of natural resources, or the acquisition of equivalent resources.

Id. at 722. The D.C. Circuit adopted this reasoning in *Kennecott Utah Copper Corp. v. U.S. Dept. of Interior*, 88 F.3d 1191, 1228 (D.C. Cir. 1996), noting that the restorative purposes of CERCLA require that courts "funnel damage recovery through public trustees rather than to private litigants."

Contingent Fee Arrangements in NRD Litigation Should Be Preempted. Under a contingent fee arrangement, the state is agreeing to divert a portion of any NRD recovery into the hands of private attorneys and away from restoration of the resource. This diversion of NRD recoveries is contrary to CERCLA and any claimed authority under which a state attorney general would enter into such arrangements should be barred by conflict preemption. "Conflict preemption occurs where it is impossible to comply with both the federal and state law, or the state law stands as an obstacle to the accomplishment of Congress' objectives." *United States v. Denver*, 100 F.3d 1509, 1512 (10th Cir. 1996). As the United States Supreme Court has explained "it is not enough to say that the ultimate goal of both federal and state law is to eliminate water pollution. A state law is also pre-empted if it interferes with the methods by which the federal statute was designed to reach this goal." *International Paper v. Oullette*, 471 U.S. 481, 491-92 (1987).

Special Counsel Issues and Transferring Remaining Issues to the Appellate Division, *New Jersey Society for Environmental & Economic Development v. Campbell*, No. MER-L-343-04 (N.J. Super. Ct., Mercer County June 17, 2004) (upholding contingent fee agreements in NRD litigation under state law, subject to certain conditions).

While CERCLA's savings provisions preserve certain types of state causes of action for environmental damage, *see* 42 U.S.C. §§ 9614(a) & (b), 9652(d), those provisions do not allow for state actions that conflict with CERCLA's purposes. *See Denver*, 100 F.3d at 1513; *PMC, Inc. v. Sherwin Williams Co.*, 151 F.3d 610, 618 (7th Cir. 1998). The Supreme Court has "refused to read general 'saving' provisions to tolerate actual conflict" between state and federal law. *Geier v. American Honda Motor Co., Inc.*, 529 U.S. 861, 874 (2000); *see also American Tel. & Tel. Co. v. Central Office Telephone, Inc.*, 524 U.S. 214, 227-28 (1998) (same). Accordingly, federal circuit courts have repeatedly preempted state laws that interfere with CERCLA's purposes. *See Bedford Affilliates v. Sills*, 156 F.3d 416, 427 (2d Cir. 1998) (state law claims for restitution and indemnity that "would bypass [CERCLA's] carefully crafted settlement system" held preempted); *Matter of Reading Co.*, 113 F.3d 111, 1117-19 (3d Cir. 1997) (same); *PMC*, 151 F.3d at 617-18 (state law claims for recovery of cleanup costs barred by CERCLA held preempted); *Denver*, 100 F.3d at 1512-14 (local zoning ordinance that conflicted with CERCLA-approved cleanups held preempted).

The conflict between CERCLA § 107(f) and contingent fee arrangements in NRD litigation is unambiguous. Section 107(f)(1) requires that any NRD recovery be used "only" for the restoration or replacement of the affected resources. There is no exception allowing for a fixed portion of the recovery to be diverted to pay the contingent fees of private attorneys.[4]

In an analogous setting, the Louisiana Supreme Court rejected the argument that contingent fee arrangements could co-exist with such a statutory scheme. *Meredith v. Ieyoub*, 700 So.2d 478 (La. 1997). In *Ieyoub*, the Louisiana Attorney General contracted with private law firms to prosecute state environmental laws on a contingent fee basis. The state's environmental statute, however, provided that "all sums" recovered through environmental litigation be deposited into a special "Hazardous Waste Site Cleanup Fund." *Id.* at 482. The Louisiana Supreme Court held that this statutory scheme does not allow for contingent fee arrangements:

> [T]his provision expressly mandates that all recoveries in cases involving environmental legislation must be paid into the state treasury. The language of the statute is clear and unambiguous: '[a]ll sums recovered through judgments' means *all* sums, not all sums remaining after the Attorney General has paid his contingency fee lawyers. If the Legislature had intended to allow the Attorney General the right to deduct the fees of contingency fee lawyers from judgments or settlements in environmental cases before paying the remainder into the state treasury, surely it would not have clearly directed that 'all sums recovered' be paid into the state treasury.

Id. Likewise, had Congress intended to allow state trustees to deduct the fees of contingent fee lawyers from NRD recoveries, it would not have directed that those recoveries be used "only" for restoration or replacement of natural resources. *See also City of Modesto Redevelopment Agency v. Dow Chemical Co.*, Nos. 999345 & 999643, 2005 WL 1171998, at * 14 (Cal. Super. Apr. 11, 2005) (state law claims preempted where "there are no binding commitments that plaintiffs will spend the proceeds of any judgment in this action on [the] proposed remediation").

The Department of Justice Has Recently Provided Amicus Guidance Arguing for Preemption of State Law Claims that Would Improperly Divert NRD Recoveries. The Department of Justice recently filed an *amicus* brief in the *In re Tutu Wells CERCLA Litigation* that addresses the need for preemption of claims that would divert a portion of NRD recoveries away from resource restoration. The DOJ's *amicus*

[4]Courts have repeatedly rejected the argument that litigation costs can be considered part of the cost of remediation. *See, e.g., Ellis v. Gelatin Steel Co.*, 390 F.3d 461 (6th Cir. 2004).

position is entitled to deference[5] and provides further support for preemption of state attorneys general's use of NRD contingent fee agreements.

In *Tutu Wells*, the Virgin Islands Department of Planning and Natural Resources ("DPNR") sought under territorial law to use a portion of its NRD recovery for lost groundwater services at the Tutu Wellfield to purchase a beach property on another part of the island. On February 14, 2005, DOJ filed an *amicus* brief arguing that territorial law is preempted to the extent it would allow DPNR to divert NRD trust money for anything other than restoration of the injured natural resources.[6] DOJ explained:

> Congress' goal in enacting CERCLA's NRD regime was to ensure that injured natural resources be restored or replaced, and an essential component of that regime is the requirement that NRD recoveries be used to restore, replace or acquire the equivalent of the natural resource. Clearly, allowing DPNR to use the Tutu NRD recovery ... for some purpose other than to restore, replace or acquire the equivalent of the injured natural resource at Tutu would undercut Congress' goal.

DPNR Amicus, at 12.

DOJ rejected DPNR's argument that CERCLA Section 107(f)(1) did not apply because a portion of the recovery was based on territorial law rather than on CERCLA:

> In most CERCLA NRD cases, the fact that an NRD claim may be premised upon state law in addition to CERCLA would not increase the total amount of the recovery. The NRD recovery would be limited to the actual amount of the natural resource damages, regardless of the fact that there may be multiple legal bases for the underlying NRD claim. Thus, if a portion of the NRD recovery hypothetically could be earmarked for the state law claim ... and that portion is used for non NRD-related expenses, the remaining NRD recovery would be insufficient to restore the injured natural resources. This clearly would be an obstacle to the Congressional intent underlying the NRD provisions.

DPNR Amicus, at 13. This same reasoning applies to NRD contingent fee agreements. To the extent that any portion of an NRD recovery is used for payment of private attorneys, the remaining NRD recovery would by definition be insufficient to restore the injured natural resources. Contingent fee agreements accordingly conflict with the congressional intent underlying the NRD provisions.

Conclusion. State attorneys general's use of contingent fee arrangements in NRD litigation improperly diverts NRD recoveries away from the restoration of natural resources and is in direct conflict with CERCLA Section 107(f)(1). These arrangements should be preempted.

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[5] *See, e.g., Horn v. Theratec Corp.* 376 F.3d 163, 170-71 (3d Cir. 2004) (FDA's views on preemptive effect of its regulations as set forth in *amicus* brief entitled to deference); *Union Pacific RR Co. v. California Public Utilities Comm'n*, 346 F.3d 851, 866 (9th Cir. 2003) ("[a]n agency's interpretation of the preemptive effect of its regulations is entitled to deference").

[6] *See* Brief of the United States as *Amicus Curiae* Regarding Federal Preemption, *DPNR v. Esso Standard Oil, S.A.*, No. 1998/206 (D.V.I. Feb. 14, 2005) ("*DPNR Amicus*"). The case subsequently settled without a ruling on this issue.

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