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Regulation, Renegotiation, and Reform: Improving Transnational Public-Private Partnerships in the Wake of the Gulf Oil Spill[†]

JOHN J. MCKINLAY*

INTRODUCTION

On April 20, 2010, British Petroleum managers aboard the *Deepwater Horizon* congratulated the rig's workers for their stellar safety record: they had operated seven years without a single workplace injury.¹ A few hours after that evening's celebration, a high-pressure bubble of methane gas rose three miles through the *Deepwater Horizon*'s drill column, destroying a previously damaged blowout preventer on its way upward.² When the bubble reached the surface of the rig and ignited, the "blowout"³ caused a massive explosion that killed eleven rig workers, injured sixteen others,⁴ and unleashed the largest oil spill in American history.⁵ Regarding the physical mechanics of the blowout, the U.S. government and British Petroleum (BP) recognize that preexisting safety measures could have prevented the *Deepwater Horizon* disaster.⁶ Regarding the legal mechanics of regulation before and liability after the Gulf Oil Spill ("the Spill"), however, lawmakers are too willing to embrace the regulatory status quo.

In the wake of the disaster, BP; its partners Halliburton,⁷ Mitsui,⁸ Transocean,⁹ Anadarko;¹⁰ and the U.S. government scrambled to simultaneously contain the

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1. *Blowout: The Deepwater Horizon Disaster*, CBSNEWS (Sept. 21, 2010, 1:16 PM), <http://www.cbsnews.com/stories/2010/05/16/60minutes/main6490197.shtml>.

2. *Id.*

3. *Id.*

4. Carl Hoffman, *Investigative Report: How the BP Oil Rig Blowout Happened*, POPULARMECHANICS.COM (Sept. 2, 2010, 12:00 PM), <http://www.popularmechanics.com/science/energy/coal-oil-gas/how-the-bp-oil-rig-blowout-happened>.

5. Matthew Scott, *BP's Gulf Oil Spill Worst in U.S. History*, DAILY FIN. (May 27, 2010, 12:15 PM), <http://www.dailyfinance.com/2010/05/27/bps-gulf-oil-spill-worst-in-u-s-history/>.

6. See Henry Fountain & Tom Zeller, Jr., *Panel Suggests Signs of Trouble Before Rig Blast*, N.Y. TIMES, May 26, 2010, at A1.

7. Peter J. Henning, *Looking for Liability in BP's Gulf Oil Spill*, NYTIMES.COM (June 7, 2010, 9:30 AM), <http://dealbook.nytimes.com/2010/06/07/looking-for-liability-in-bps-gulf-oil-spill/>.

8. See Tom Bergin, *BP Cuts Oil Spill Burden with £677 Million Mitsui Deal*, REUTERS.COM (May 20, 2011, 10:40 PM), <http://uk.reuters.com/article/2011/05/20/uk-bp-mitsui-idUKTRE74J11I20110520>.

disaster and either reduce or avoid environmental and economic liability for it.¹¹ BP waged a public relations campaign,¹² likely aimed at keeping its stock price up¹³ and perception of the Spill's severity down.¹⁴ Undoubtedly, BP's managers calculated the company's potential criminal liability—based on the volume of oil spilled—under measures such as the Clean Water Act¹⁵ and Migratory Bird Treaty Act.¹⁶ The Obama Administration (“Administration”), which had recently exempted BP from key oversight and preparedness requirements,¹⁷ reprised its oversight role with a vengeance. President Obama declared a moratorium on deepwater drilling in coastal waters surrounding the United States.¹⁸ The government later lifted the moratorium after adopting “new regulatory measures.”¹⁹ Oil extractors and environmental groups alternatively praised and decried the Administration's reversal.²⁰ The Administration also quickly disbanded the Minerals Management Service (MMS)²¹ and rechristened it the Bureau of Ocean Energy Management, Regulation, and Enforcement (BOEMRE).²² The commission

9. See Hoffman, *supra* note 4.

10. See Chris Kahn, *BP Partners Refuse to Help Pay for Gulf Oil Spill*, HUFFINGTON POST (July 13, 2010, 4:56 PM), http://www.huffingtonpost.com/2010/07/13/bp-partners-moex-anadarko_n_645117.html.

11. See, e.g., John Schwartz, *BP Bills Its Partners for a Share of the Oil Spill Cost*, N.Y. TIMES, July 5, 2010, at A10 (discussing BP's attempts to spread liability costs among its partners and its insurer in the face of the U.S. government billing BP for costs associated with the Gulf Oil Spill).

12. See Cain Burdeau, *BP Ad Campaign Following Gulf Oil Spill Deemed 'Propaganda' by Some*, HUFFINGTON POST (Jan. 8, 2012, 11:38 AM), http://www.huffingtonpost.com/2012/01/08/bp-ad-campaign-gulf-oil-_n_1192600.html.

13. See *Oil Spill Hits BP's Stock, Threatens Its Future*, LAWYERS.COM, <http://securities.lawyers.com/Securities/Oil-Spill-Hits-BPs-Stock-Threatens-Its-Future.html>.

14. See Helen Pidd, *BP Oil Spill Estimates Double: US Government Figures Show Twice as Much Oil Spewing into the Gulf of Mexico Than Earlier Estimations Suggested*, THE GUARDIAN (June 11, 2010, 10:07 AM), <http://www.guardian.co.uk/environment/2010/jun/11/bp-oil-spill-estimates-double>.

15. 33 U.S.C. § 1319(c) (2006).

16. 16 U.S.C. § 707.

17. See Juliet Eilperin, *U.S. Exempted BP's Gulf of Mexico Drilling from Environmental Impact Study*, WASH. POST (May 5, 2010), <http://www.washingtonpost.com/wp-dyn/content/article/2010/05/04/AR2010050404118.html?hpid=topnews>. BP received a “categorical exclusion” from the National Environmental Policy Act's requirement for environmental impact studies due to the perceived unlikelihood of a large spill in the region. See *id.*

18. Bryan Walsh, *Obama Issues New Offshore Drilling Moratorium*, TIME.COM (July 12, 2010, 8:27 PM), <http://ecentric.blogs.time.com/2010/07/12/obama-issues-new-offshore-drilling-moratorium/>.

19. Peter Baker & John M. Broder, *U.S. Lifts the Ban on Deep Drilling, with New Rules*, N.Y. TIMES, Oct. 13, 2010, at A1.

20. See *id.* (discussing views of proponents and opponents of the moratorium).

21. See Perry Bacon Jr., David A. Fahrenthold & Steven Mufson, *Lawmakers Assail Minerals Management Service*, WASH. POST (May 26, 2010, 4:16 PM), <http://www.washingtonpost.com/wp-dyn/content/article/2010/05/26/AR2010052602787.html>.

22. Neil King, Jr., *Salazar Renames MMS, Adding 'Regulation and Enforcement'*,

tasked with investigating the Spill found that MMS's and BP's "shared failure" caused the Spill.²³

The centerpiece of Congress's reaction was the Big Oil Bailout Prevention Liability Act of 2010 ("the 2010 Act").²⁴ In light of the "laughably low liability level"²⁵ in place under the controlling Oil Pollution Control Act of 1990 (OPA),²⁶ Senator Robert Menéndez introduced the 2010 Act²⁷ to retroactively increase BP's liability cap to \$10 billion. Though the original Act was defeated in the Senate in September 2010,²⁸ Representative Rush Holt reintroduced the proposed legislation as the Big Oil Bailout Prevention Liability Act of 2011 ("the 2011 Act," or alternatively, "the Act") in the House in January 2011,²⁹ with Senator Menéndez following suit in the Senate.³⁰ The 2011 Act seeks to remove liability limits altogether.³¹ Though the 2011 Act has been stalled in committee since the Republican-controlled Congress was seated in January 2011,³² the very introduction of the Act indicates a systemic misalignment of incentives and raises important questions regarding the proper scope and mechanics of public-private partnership (P3) regulation.

The Act's proposed retroactive liability provision raises questions about prospective measures that could better implement public welfare and infrastructure development aims. This Note proposes that the present regulatory systems governing transnational P3s, as brought to light by the BP disaster, are costly, ineffective, and outdated. Furthermore, this Note argues that renegotiation as a corrective measure should be discontinued inasmuch as it may impose significant indirect costs on taxpayers—the true public side of a P3. The key to implementing a system that is efficient and beneficial to both parties of a P3 lies in realigning incentives of both parties and streamlining the regulatory process through more front-end participation and less back-end regulation. Part I of this Note examines

WALL ST. J. (June 21, 2010, 5:32 PM), <http://blogs.wsj.com/washwire/2010/06/21/salazar-renames-mms-adding-regulation-and-enforcement/>.

23. 'Shared Failure' in BP Spill Cited in Panel Report: Reforms Needed Since 'Oversight Utterly Failed,' Says Co-chair of Obama Commission, MSNBC.COM (Jan. 11, 2011, 11:34 AM), http://www.msnbc.msn.com/id/41020738/ns/us_news-environment.

24. Big Oil Bailout Prevention Liability Act of 2010, S. 3305, 111th Cong. (2010).

25. Katarzyna Klimasinska & Noah Buhayar, 'Laughably Low' Spill Liability Cap Spurs U.S. Debate After BP, STUART SMITH BLOG (Feb. 10, 2011) (citing Rep. Rush Holt), <http://www.stuarthsmith.com/'laughably-low'-spill-liability-cap-spurs-u-s-debate-after-bp>.

26. 33 U.S.C. § 2704(a)(3) (2006) (setting liability limits for offshore facilities such as the *Deepwater Horizon* at removal costs plus \$75 million).

27. S. 3305 (proposing a retroactive increase of the liability cap for deepwater oil spills from \$75 million to \$10 billion).

28. Geoff Holtzman, *Oil Spill Commission Suggests Raising Liability Cap*, TALK RADIO NEWS SERVICE (Jan. 11, 2011, 11:44 AM), <http://www.talkradionews.com/quicknews/2011/1/11/oil-spill-commission-suggests-raising-liability-cap.html>.

29. H.R. 492, 112th Cong. (2011).

30. S. 214, 112th Cong. (2011).

31. See H.R. 492 (proposing removal of liability cap effectuated at 33 U.S.C. § 2704(a)(3)).

32. The bill, with twenty-three Democratic co-sponsors and no Republican sponsors, was referred to the House Committee on Transportation and Infrastructure on January 26, 2011. See H.R. 492. No action on the bill has since been taken. See *id.*

the nature of P3s in the United States and that of the MMS/BP arrangement in particular. Part II discusses American P3 regulation, its limitations, and potential improvements that can be made. Part III addresses detrimental effects of the United States' actions and suggests reforms to benefit both public and private parties in future P3 arrangements. Part IV utilizes scholarship from corporate governance, transnational legal pluralism, and notions of the government as a fiduciary to anticipate objections to reform and suggest means to overcome them.

I. P3S: RATIONALES, RISKS, AND RENEGOTIATION

The rationale underlying the formation of P3s is that private companies partner with local governments to perform tasks deemed too operationally complex, capital intensive, or risky for the government to undertake alone.³³ Generally speaking, such arrangements enable public partners to limit expenditures and risks while receiving royalty payments from the private partner, whereas the private partner is able to deploy its expertise and capital in operational enterprises³⁴ that promise sufficiently large returns³⁵ to absorb risk the public partner would otherwise incur.³⁶ In effect, each partner in a P3 arrangement undertakes both public and private law functions.³⁷

Transnational extraction projects exist in part to implement national energy, economic, employment, or infrastructure development policies while reducing industrial development expenditures.³⁸ Within a transnational P3, implementation

33. See JOHN LOXLEY WITH SALIM LOXLEY, *PUBLIC SERVICE PRIVATE PROFITS: THE POLITICAL ECONOMY OF PUBLIC-PRIVATE PARTNERSHIPS IN CANADA* 176 (2010) (“The apparent motivation behind the approach [of creating P3s] has shifted to some degree from an attempt to move infrastructure spending and debt off the government books, to a desire to reduce costs through transferring risk to the private sector.”); see also MICHAEL B. LIKOSKY, *LAW, INFRASTRUCTURE, AND HUMAN RIGHTS* 27–28 (2006) (noting that the Panama Canal and trans-American railroad construction projects were P3s).

34. See LOXLEY WITH LOXLEY, *supra* note 33, at 2–3 (“With P3s, the large up-front capital costs associate with infrastructure projects can . . . be offset and spread over a number of years through a lease . . . Private firms can assume responsibility for things that may go wrong, such as project over-runs, problems resulting from poor construction, etc.”).

35. As Loxley notes, “P3s offer important opportunities for profit-making.” *Id.* at vii.

36. See R. PRESTON MCAFEE & JOHN MCMILLAN, *INCENTIVES IN GOVERNMENT CONTRACTING* 9 (1988).

37. See LIKOSKY, *supra* note 33, at 23 (“Within PPPs, the interests of governments and companies are intertwined.”); see also *id.* at 24 (“[I]n the context of specific PPPs, companies might combine public and private law powers.”).

38. See *id.* at 24 (“Commentators have long complained that private companies, for example, have taken on too many political powers.”). This is especially true in the case of large companies. See *id.* It would seem even more relevant in discussing transnational companies with presumably less incentive to enhance the foreign host country’s public welfare. See Nick Beermann, *Legal Mechanisms of Public-Private Partnerships: Promoting Economic Development or Benefiting Corporate Welfare?*, 23 SEATTLE U. L. REV. 175, 204 (1999) (“Economic development is often advanced as a reason for creating public-private partnerships.”); G. Allen Brooks, *Musings: Future of the Gulf of Mexico Oil & Gas Industry*, RIGZONE (Nov. 12, 2010), http://www.rigzone.com/news/article.asp?a_id=101257

of public policy is effectively outsourced to a foreign entity. Ensuring that transnational partners adequately promote domestic public welfare aims is a formidable challenge to P3 regulators. One potential solution—exemplified by the Act—is the threat of renegotiation.³⁹ This Note argues that renegotiation should be a disfavored mechanism in transnational P3s insofar as it ultimately increases the costs of business and sustains a regulatory regime unlikely to avert disasters such as the Spill.

For economic and historical reasons, transnationals like BP are increasingly important players in capital-intensive industries like mineral extraction.⁴⁰ In accordance with the American policy of reducing dependence on foreign oil,⁴¹ the United States tasked BP with accessing its deepwater oil reserves. Typical of such oil and gas exploration arrangements, BP's lease to drill for oil in the Gulf of Mexico is a concessionary lease from the U.S. government agency tasked with oversight of the arrangement—the MMS/BOEMRE.⁴² Events surrounding the Spill demonstrate two dangers inherent in poorly supervised transnational P3 leases: the private entity may find itself in a position to ignore the host country's public welfare aims in light of the company's profit motive,⁴³ and the public goals of cost saving and revenue generation incentivize the overseeing agency to become a

(explaining, from the oil industry's perspective, why deepwater drilling is necessary for American energy policy).

39. In this context, renegotiation is a unilateral action undertaken by the stronger party. Prior to the formation of a P3, the government negotiates for favorable conditions based on anticipated benefit to the country as a stakeholder. See J.J. Boddewyn, *Multinational Business-Government Relations: Six Principles for Effectiveness*, in *MULTINATIONAL CORPORATIONS AND GOVERNMENTS: BUSINESS-GOVERNMENT RELATIONS IN AN INTERNATIONAL CONTEXT* 193, 196 (Patrick M. Boorman & Hans Schollhammer eds., 1975). Risks are assigned as under any contract, and such losses are insured by the insurance carriers. See generally Ronald J. Daniels & Michael J. Trebilcock, *Private Provision of Public Infrastructure: An Organizational Analysis of the Next Privatization Frontier*, 46 U. TORONTO L.J. 375 (1996). Because of public parties' sovereign power to rescind a lease under its own law, expel the private party from its borders, nationalize, or otherwise take advantage of its relative power, the government may act opportunistically or legitimately to increase the benefit to the country or allay the damage created by the private partner. See MICHAEL LIKOSKY, *OBAMA'S BANK: FINANCING A DURABLE NEW DEAL* 333 (2010) (noting that many renegotiations are driven by the inequitable flow of benefits to private partners and risks to the public partners).

40. LOXLEY WITH LOXLEY, *supra* note 33, at vii (“P3s . . . draw[] on private sector technical expertise, private sector organizational and management experience and private sector capital to deliver public services.”).

41. See Kerri Shannon, *United States Lifts Oil Drilling Ban to Reduce Foreign Energy Dependence*, MONEY MORNING (Apr. 1, 2010), <http://moneymorning.com/2010/04/01/drilling-ban/>.

42. See Dane Hahn, *Unraveling BP's Oil Lease in the Gulf*, ENGLEWOOD EDGE (June 8, 2010, 2:19 AM), <http://www.engagewoodedge.com/2010/06/08/unraveling-bps-oil-lease-in-the-gulf/>. A concessionary contract is one in which the “government cedes a mix of ownership and control over a public activity to a private-sector entity.” See LIKOSKY, *supra* note 39, at 189.

43. See Boddewyn, *supra* note 39, at 196 (noting that successful P3s demand “focusing on the integration of the guest company into the host economy and society through the obeying of laws”).

rubber stamp for the private parties' wishes.⁴⁴ The lines between public policy and profit motive become uncomfortably blurred in a P3, removing incentives for either party to act in the public interest and instead pursue only monetary gain.⁴⁵ Leading up to the Spill, BP avoided meaningful regulation⁴⁶ to increase its profits and reduce cost overruns resulting from delays.⁴⁷ As the world learned in the wake of the Spill, existing administrative regulations leading up to the disaster were ill equipped to avoid an otherwise preventable economic and environmental disaster.⁴⁸

The existence of the 2011 Act indicates the degree to which contract terms and administrative regulations inadequately accounted for risk to the public.⁴⁹ Such shortcomings can only be inferred *ex post*, however, since the Freedom of Information Act (FOIA) generally exempts from public scrutiny sensitive business information reified in extraction contracts.⁵⁰ Beyond the structural opaqueness

44. Hahn, *supra* note 42 (noting that the United States received \$34 million as a prepayment on the lease and was to collect 12.8% of revenues generated from producing wells drilled by BP in the Macondo tract); *see also* LOXLEY WITH LOXLEY, *supra* note 33, at 175 (“One of the most disturbing aspects of P3s is the uniformly abysmal record of accountability and transparency.”); JULIA STEETS, ACCOUNTABILITY IN PUBLIC POLICY PARTNERSHIPS 39 (2010) (“Public-private policy partnerships must be accountable if they are to fulfill policy objectives successfully.” (quoting Pauline Vaillancourt)); Eilperin, *supra* note 17 (noting the superficial review given BP’s operations before exempting BP from a mandatory environmental impact study).

45. *See* LIKOSKY, *supra* note 33, at 24 (“In each case, the concern is that private companies are too intermingled with governments and are thus acting as political bodies exceeding their private law remit.”); *see also generally* Klaus Dingwerth & Tine Hanreider, *Public Markets and Private Democracy? The Renegotiation of Public and Private in Global Politics*, in DEMOCRACY AND PUBLIC-PRIVATE PARTNERSHIPS IN GLOBAL GOVERNANCE 81 (Magdalena Bexell & Ulrika Mörth eds., 2010) (discussing the blurred distinction between public and private actors and tasks in P3s).

46. *See* Mark Clayton, *BP Oil Spill: MMS Shortcomings Include ‘Dearth of Regulations,’* CHRISTIAN SCI. MONITOR (June 17, 2010), <http://www.csmonitor.com/USA/Politics/2010/0617/BP-oil-spill-MMS-shortcomings-include-dearth-of-regulations>.

47. *See* Kevin Spear, *Documents Show BP Chose a Less-Expensive, Less-Reliable Method for Completing Well in Gulf Oil Spill*, ORLANDO SENTINEL (May 23, 2010), http://articles.orlandosentinel.com/2010-05-23/news/os-florida-oil-spill-unspeakable-risks-20100522_1_oil-company-bp-rig-oil-spill.

48. *See* Clayton, *supra* note 46; *see also* ‘Shared Failure’ in BP Spill Cited in Panel Report, *supra* note 23.

49. *See* LOXLEY WITH LOXLEY, *supra* note 33, at 3 (“The desirability and effectiveness of any P3, from the point of view of the various actors, is directly related to the specific content of the contract, the way it is implemented and the vision behind it.”). This statement of course assumes that BP and the MMS were economically rational actors at the time the lease originated.

50. *See* ALFRED C. AMAN, JR., THE DEMOCRACY DEFICIT: TAMING GLOBALIZATION THROUGH LAW REFORM 89 (2004). Congressman Issa requested information on behalf of the House Committee on Oversight and Government Reform, but was denied access to communications between the Interior Department and private sector entities. *See* Letter from Darrell Issa, U.S. Rep. for Cal., to Kenneth Salazar, Sec’y Interior (May 3, 2010), available at <http://www.boemre.gov/deepwaterreadingroom/>; Letter to Darrell Issa, U.S. Rep. for Cal.

engendered by broad FOIA protection, parties usually conduct P3 contract negotiations without public participation,⁵¹ often antithetical to public welfare interests,⁵² and subcontracted to multiple parties outside the host country.⁵³ The implications of extraction P3s for the host country's environment, labor sector, taxpayers, and business climate are far reaching, though the process of negotiating such arrangements is generally designed to exclude these interests,⁵⁴ thus substituting contracts negotiated behind closed doors for public policy referenda.⁵⁵ The host country's public welfare aims are further jeopardized by the tendency of savvy transnational contractors to take advantage of inherent economic and jurisdictional limitations by subcontracting riskier aspects of projects to other transnationals.⁵⁶

Private partners also bear substantial risks in transnational P3s. When extraction contracts are inadequate for unforeseen real-world developments, state actors engaged in P3s may seek to renegotiate contracts—changing the terms to reassign downside risk away from the public partner and its constituents.⁵⁷ Renegotiation in this instance can be thought of as the sword wielded when the shield fails. The Act clearly demonstrates the dangers renegotiation poses to the private P3 party. Through the 2011 Act,⁵⁸ the U.S. government seeks unlimited liability in order to recover from its P3 partner in excess of the original terms—the \$75 million liability cap under the OPA which BP's insurer, Jupiter Insurance, Ltd., ostensibly relied upon at the time BP negotiated its lease.⁵⁹ As an ad hoc remedy in extraction industry P3s, renegotiation is recognized as a necessary evil despite its adverse

from Christopher P. Salotti, Legislative Counsel, Office of Cong. and Legislative Affairs (July 21, 2010), *available at* <http://www.boemre.gov/deepwaterreadingroom/>.

51. *See* LIKOSKY, *supra* note 39, at 176 (“P3 planners typically oppose efforts at deliberative participatory decision-making.”).

52. *Id.* at 180 (noting that participatory planning by non-parties is seen as a financial risk to be mitigated).

53. *See* AMAN, *supra* note 50, at 197.

54. *See, e.g.,* B. Guy Peters & Jon Pierre, *Public-Private Partnerships and the Democratic Deficit: Is Performance-Based Legitimacy the Answer?*, in *DEMOCRACY AND PUBLIC-PRIVATE PARTNERSHIPS IN GLOBAL GOVERNANCE*, *supra* note 45, at 41, 46 (“[T]he operative efficiency of partnerships hinges to some extent on seclusion from public debate.”).

55. *See* LIKOSKY, *supra* note 39, at 180–81.

56. *See* Kahn, *supra* note 10 (noting that arbitration is the only legal option for BP to collect from its partners).

57. *See supra* note 39.

58. Big Oil Bailout Prevention Liability Act of 2011, H.R. 492, 112th Cong. (2011).

59. *See* Michael Cessna, *Insurance Implications of the Deepwater Horizon Disaster*, LEXISNEXIS.COM (May 17, 2010, 1:43 PM), <http://www.lexisnexis.com/community/insurancelaw/blogs/insurancelawblog/archive/2010/05/17/insurance-implications-of-the-deepwater-horizon-disaster-by-michael-cessna-of-counsel-lathrop-amp-gage-llp.aspx> (noting the liability limits of the insurance underwriter). As Cessna notes, the liability requirements in place at the time of negotiation were fixed by the Oil Pollution Act of 1990, which was itself a response to the disastrous *Valdez* spill in Prince William Sound. *See id.* The government's punitive damages recovery was limited by the United States Supreme Court after MMS's March 2008 lease with BP was entered into. *See Exxon Shipping Co. v. Baker*, 554 U.S. 471 (2008).

effects on business.⁶⁰ The amount the government seeks to recover from BP will likely exceed \$50 billion,⁶¹ though potential sanctions under the Clean Water Act, private securities actions, and negligence suits may well double BP's costs.⁶² Other estimates put the number as high as \$100 billion after cleanup and litigation costs are taken into account.⁶³ BP is in turn seeking to recover from its investors,⁶⁴ though BP does not have as much negotiation leverage as the U.S. government does through its sovereign powers.

As long as P3s have existed, renegotiation has existed.⁶⁵ Renegotiation essentially imposes new, unfavorable contract terms on the private partner that is otherwise powerless to continue its business without accepting the renegotiated terms. Large transnationals are especially vulnerable to renegotiation given their structural lack of political representation in the host country, the potential for adverse public sentiment toward foreign entities,⁶⁶ and the typically large investment and liability exposure associated with the massive infrastructure projects in which they are most likely to participate.⁶⁷ Because the proposed Act would apply retroactively, it is a form of unilateral renegotiation of the contract terms by the United States.⁶⁸ While electoral politics compel the host country in a transnational P3 to shift the economic burden from their constituent taxpayers to the transnational operators after a disaster such as the Spill,⁶⁹ relying on renegotiation as a viable alternative to adequate negotiation at the P3's formation

60. See YINKA OMOROGBE, *THE OIL AND GAS INDUSTRY: EXPLORATION AND PRODUCTION CONTRACTS* 5 (1997) (acknowledging renegotiation as a function of inevitable changes).

61. Tom Bergin, *How BP's Gulf Oil Disaster Costs Could Double*, *INS. J.* (Dec. 1, 2010), <http://www.insurancejournal.com/news/national/2010/12/01/115279.htm> (showing that total costs of the BP disaster are being adjusted continuously upward, and are presently estimated to be around \$50 billion).

62. *Id.*

63. See Daniel Bates, *'The Most Incompetent CEO in Living Memory': BP Chief Tony Hayward Demoted After Public Flogging as Clean-up Cost Could Reach \$70bn*, *MAIL ONLINE* (June 19, 2010, 9:37 AM), <http://www.dailymail.co.uk/news/article-1287685/BP-oil-spill-Shares-rise-Louisiana-puts-cost-100billion.html>.

64. Schwartz, *supra* note 11.

65. See LIKOSKY, *supra* note 39, at 287–88 (discussing renegotiation as a measure typically undertaken by governments); see also *id.* at 292 (“In fact, efforts to renegotiate projects result in revision of material contract terms.”).

66. See *After Dubai Ports World*, *WASH. POST* (Mar. 4, 2007), <http://www.washingtonpost.com/wp-dyn/content/article/2007/03/03/AR2007030301029.html>.

67. See Cessna, *supra* note 59 (noting some of the larger P3 arrangements undertaken and that BP's insurer is capable of underwriting up to \$700 million of liability insurance).

68. LOXLEY WITH LOXLEY, *supra* note 33, at 3 (“[Q]uestions arise about . . . who is bearing the costs of these arrangements. It is at that point that P3s potentially become controversial, as not everyone involved may be a winner, and then the details of any arrangement become crucial.”).

69. *Id.* at 176–77 (“Indeed, without evidence of risk transfer, there is, in general, no case for the P3 approach.”).

reduces or eliminates the economic benefits of vital P3 arrangements and increases the ultimate costs to both sides of P3s.⁷⁰

Clearly accidents will happen regardless of how well-negotiated future contracts are; however, renegotiation is a symptom of a failed process as well as a predicate to indirect future costs. If existing regulatory and negotiation structures in P3 arrangements are not reformed, increasing direct and indirect costs may jeopardize the efficacy of transnational P3s.⁷¹ The Act seeks to resolve the question of who should pay for the cleanup of the Gulf, but it raises the issue of what mechanisms can prospectively eliminate the need for such measures by aligning business and public welfare aims with the government's goal of reducing costs through P3 arrangements.⁷²

II. REGULATORY MODELS IN TRANSNATIONAL CONTEXTS

The administrative environment in which the parties operate is an important consideration when examining P3 contracts. It stands to reason that weak regulatory regimes would prefer to rely upon highly-negotiated contract terms (or renegotiation) to ensure the private party is held liable for risk or harm to the host country's interests. Unfortunately, such contracts are expensive to negotiate and invariably fail to address at least some material concerns.⁷³ On the other hand, strongly enforced regulations effectively incorporate a wide range of statutory and administrative laws into the contract, necessitating significant expenditures in the form of oversight and enforcement.⁷⁴ BP's disregard of public regulations without consequence indicates poor enforcement,⁷⁵ whereas the necessity of ex post renegotiation indicates lack of adequate bargaining during the negotiation phase.⁷⁶ In looking to improve the balance between contract and administrative law, the nature of regulation itself is in question: what should it look like? Professor Aman identifies three models of administrative regulation: market-based regulation, strong regulatory state, and efficient-state regulation.⁷⁷

A. The Ideological Methods: Market-Based and Strong Regulatory State Models

In many ways, these two models mimic "traditional political debates between conservatives and liberals, at least regarding issues within U.S. borders."⁷⁸ Each

70. *Id.* at 3 ("[P3s] might . . . impose costs on taxpayers that may not always be evident.").

71. See LIKOSKY, *supra* note 33, at 31–42 (discussing the historical development of P3s and their present necessity).

72. See LOXLEY WITH LOXLEY, *supra* note 33, at 176 ("The apparent motivation behind the approach [of creating P3s] has shifted to some degree from an attempt to move infrastructure spending and debt off the government books . . .").

73. See OMOROGBE, *supra* note 60, at 122.

74. See AMAN, *supra* note 50, at 97–98.

75. See Clayton, *supra* note 46.

76. See OMOROGBE, *supra* note 60, at 5–6.

77. See generally AMAN, *supra* note 50, at 118–24.

78. *Id.* at 119.

model is a relic of an earlier paradigm and not particularly well suited to the global marketplace.⁷⁹

Market-based regulation treats contracts as the superior form of governance and propounds two goals: maximum autonomy for the contracting parties and minimal government intervention or oversight.⁸⁰ While reducing the burden of regulation is a legitimate aim of both private and public parties,⁸¹ the danger of market-based regulation is that it is inherently incapable of recognizing a public interest beyond what the market itself may provide.⁸² In a market-based regulatory scheme involving transnational P3s, the government delegates its public-welfare duty and provides the foreign entity incentive to skirt regulations inasmuch as the cost-benefit balance compels it to do so.⁸³ The danger of allowing transnational, private corporations organized outside the United States to determine the degree to which they should uphold the government's aims should be self-evident. Market-based regulation is not without merit in some instances; public bodies may sanction non-self-enforcing private regulations for the sake of convenience and efficiency.⁸⁴ But even in smaller industries where some degree of private self-policing has proven effective, public regulation is almost always a necessary backstop to voluntary self-regulation.⁸⁵ As a practical matter, it is very difficult to imagine a set of effective, voluntary measures BP would have been more likely to follow than the public regulations it ignored at the peril of its workers and the environment.⁸⁶ As noted in the context of the 2008 financial collapse, "voluntary regulation does not work."⁸⁷

79. *See id.* at 117 (noting that both methods "clearly resonate with long-standing political assumptions and public-law theories").

80. *See id.* at 120; *see also* Karin Svedberg Helgesson, *Partnerships, Boundary Blurring, and Accountable Actorhood*, in *DEMOCRACY AND PUBLIC-PRIVATE PARTNERSHIPS IN GLOBAL GOVERNANCE*, *supra* note 45, at 24, 24 (noting that under a market regulation scheme, "the business sector is expected to help produce frameworks for governing itself by creating industry standards, codes of conduct, and other rules as a complement to, or even substitute for, intra- and interstate regulation").

81. *See supra* text accompanying note 36. The purpose of P3s is to reduce costs and create profits. Costs imposed by government regulation necessarily hamper both.

82. Peters and Pierre pithily note that market-based regulation creates a "private-private partnership." Peters & Pierre, *supra* note 54, at 42–43.

83. AMAN, *supra* note 50, at 119.

84. *See supra* text accompanying note 81.

85. *See* Mark Levinson, *Wishful Thinking*, in ARCHON FUNG, DARA O'ROURKE & CHARLES SABEL, *CAN WE PUT AN END TO SWEATSHOPS?* 54 (Joshua Cohen & Joel Rogers eds., 2001) (critiquing the optimism of an article which claims viable private or self-regulating measures are possible absent government enforcement).

86. *See, e.g.*, Dina Cappiello, *Another Report Says BP Ignored Warning Signs on Doomed Deepwater Horizon Well*, AL.COM (Nov. 17, 2010, 9:59 AM), http://blog.al.com/wire/2010/11/report_bp_ignored_warnings.html (noting that in the months leading up to the disaster, BP recklessly disregarded a multitude of regulations, norms, and warnings).

87. STEVEN M. DAVIDOFF, *GODS AT WAR: SHOTGUN TAKEOVERS, GOVERNMENT BY DEAL, AND THE PRIVATE EQUITY IMPLOSION* 159 (2009) (citing former SEC Chairman Christopher Cox remarking upon the failure of market-based, voluntary regulation in

Expansive bureaucracies regulating even privatized and global industries typify the strong regulatory state model.⁸⁸ As evidenced by circumstances surrounding the BP spill, an expansive regulatory regime may result in costly, redundant oversight functions and an overgrown bureaucracy that compromises the effectiveness of the administrative system as a whole.⁸⁹ As studies and reports concerning the BP disaster have surfaced, the degree to which regulations were in place but unenforced has become clear.⁹⁰ The inspector general's office found that MMS regulators were "heavily reliant on industry to document and accurately report on operations, production, and royalties."⁹¹ The administrative bureaucracy overseeing BP metastasized to the point that even the various agencies tasked with oversight were not sure of their responsibilities.⁹² While overseeing BP's operations, MMS regulators failed to review data submissions by the operators regarding deepwater drilling,⁹³ seek sufficient information prior to approving drill permit applications,⁹⁴ specify well design and materials requirements,⁹⁵ require tests for the prevention system implicated in the disaster,⁹⁶ or notice obvious clerical and mathematical errors on BP documents.⁹⁷ In addition, the investigating commission found that MMS regulators had violated ethical rules and disregarded safety guidelines.⁹⁸ As the facts surrounding the Spill indicate, having numerous agencies tasked with oversight does not ensure effective oversight,⁹⁹ especially where overlap creates confusion regarding each agency's responsibilities.¹⁰⁰

Balancing operational efficiency for private parties and effective regulation by public parties demands rethinking existing administrative structures. A cornerstone of such a reform is eliminating incentives that tend to result in captured regulators and opaque governance agencies in which ineffectual oversight is hidden from public view until disaster strikes.¹⁰¹ The "major implication of this broader

preventing the collapse of Bear Stearns and Lehman Brothers).

88. AMAN, *supra* note 50, at 120 ("To strong regulatory state advocates, the public sphere, particularly when it comes to the economic and environmental well-being of individuals should be a broad one . . .").

89. *See, e.g., Deepwater Horizon Spill Report Blames BP, Contractors, Government*, ENVTL. NEWS SERV. (Nov. 17, 2010) [hereinafter *Deepwater*], <http://www.ens-newswire.com/ens/nov2010/2010-11-17-01.html> (describing confusion among agencies tasked with regulating the oil drilling industry).

90. *See, e.g., id.*

91. Clayton, *supra* note 46 (quoting Mary Kendall, Acting Inspector General, U.S. Department of Interior).

92. *See* Laura Strickler, *BP Rig Missed 16 Inspections Before Explosion*, CBS NEWS (June 11, 2010, 5:39 PM), http://www.cbsnews.com/8301-31727_162-20007514-10391695.html.

93. NAT'L COMM'N ON THE BP DEEPWATER HORIZON OIL SPILL AND OFFSHORE DRILLING, CHIEF COUNSEL'S REPORT 253 (2011).

94. *Id.*

95. *Id.* at 254.

96. *Id.* at 256 (noting "the lack of any regulation requiring negative pressure tests").

97. *Id.* at 259.

98. *Id.* at 261.

99. *See* Eilperin, *supra* note 17.

100. *See* Strickler, *supra* note 92.

101. *See, e.g.,* Peters & Pierre, *supra* note 54, at 46–47 (discussing the detrimental effects

reconfiguration seems to lie in a renegotiation of what is or should be governed by market competition, what is or should be governed by democratic procedures, and how these two mechanisms (should) interrelate.¹⁰²

B. The Pragmatic Method: The Efficient-State Regulation Model

Reforming the regulatory system challenges lawmakers to find “a balance between the use of official standards bodies and market forces to set standards.”¹⁰³ The efficient-state regulatory model borrows from principles of modern corporate governance’s emphasis on streamlining and internal cooperation,¹⁰⁴ as well as the focus on public welfare interests and effective oversight that are hallmarks of strong regulatory states.¹⁰⁵ As the name suggests, the model emphasizes efficient, as opposed to expansive, regulation.¹⁰⁶ The strengths of this model are its task rather than process orientation, and its fluidity rather than parochialism.¹⁰⁷ The primary drawbacks of this model are the potential for increased front-end costs, as well as structural and procedural obstacles to implementing such a system.¹⁰⁸

The efficient-state regulatory model emphasizes transparency, accountability, and efficiency. Effectively implementing an efficient-state model encourages input from a broad range of interests in order to best assign the numerous responsibilities inherent in complex transactions.¹⁰⁹ Under an efficient-state model, BP and the MMS would negotiate a lease with input from subcontractors, independent scientists and engineers, the Environmental Protection Agency, labor unions, nongovernmental organizations (NGOs), and foreseeably affected industries such as fisheries, coastal businesses, and oil refineries, among others. By including a greater cross-section of interested parties, the front-end negotiations will greatly improve the assignment of responsibilities and liabilities, ultimately reducing the need for back-end regulatory measures and contract litigation or renegotiation.

An expanded roster of contract participants further increases transparency.¹¹⁰ In practice if not by design, the current regulatory model keeps citizens uninformed¹¹¹ and is largely unable to prevent self-interested technocrats and managers, whose

to public welfare interests engendered by opaque governance structures); *see also* LIKOSKY, *supra* note 33, at 25 (“What is worrisome is when mixing is obscured from public view.”).

102. Dingwerth & Hanreider, *supra* note 45, at 97.

103. Peter Grindley, *Regulation and Standards Policy: Setting Standards by Committees and Markets*, in *THE REGULATORY CHALLENGE* 210 (Matthew Bishop, John Kay & Colin Mayer eds., 1995).

104. *See* AMAN, *supra* note 50, at 121–22.

105. *See id.* at 120 (“To strong regulatory state advocates, the public sphere, particularly when it comes to the economic and environmental well-being of individuals should be a broad one . . .”).

106. *See id.* at 121.

107. *See id.*

108. *See infra* Part IV.B.

109. *See id.* at 141–44 (stating that the inclusion of non-participants is the best way to ensure representation of public welfare interests, as well as to sufficiently develop and assign contract liabilities during the negotiation process).

110. *See id.* at 143–44.

111. *See* AMAN, *supra* note 50, at 141 (“Openness, accountability, and citizen participation are vital to new governance regimes now emerging.”).

interests are often aligned against transparency, from dictating the deal's terms in derogation of the public welfare interests or third parties' economic concerns.¹¹² The present regulatory model often operates to reduce or eliminate the influence of public-interest actors even though public money is being spent to oversee the projects.¹¹³ Within P3s, opaqueness tends to benefit the private parties, who negotiate self-interestedly before complaints can be registered, depend on the rational apathy or ignorance of the public, and "firefight" the problem with the most cost-effective measures if necessary.¹¹⁴ This paradigm is reflected the circumstances leading up to the *Deepwater Horizon* disaster.¹¹⁵ The lifting of the moratorium on deepwater drilling not long before the Spill, over strenuous protests by NGOs, raises a suspicion that the government failed to adequately weigh the public interests at stake.¹¹⁶ Governance of P3s with the potential to cause so much damage to the public should necessitate greater participation by public-interest advocates.¹¹⁷ Given the high financial stakes at play in large transnational P3s,¹¹⁸ economic rather than public welfare consideration may be overemphasized in negotiating and regulating P3 arrangements.¹¹⁹ However, the Act demonstrates public welfare costs are both monetizable and substantial,¹²⁰ and should therefore not be ignored.

Aside from implicating democratic ideals,¹²¹ the government's failure to represent the public interest overlooks potentially serious consequences, as evidenced by the lives lost aboard the *Deepwater Horizon* and the negative commercial impact of the Spill.¹²²

112. See LIKOSKY, *supra* note 39, at 176 ("P3 planners typically oppose efforts at deliberative participatory decision-making."); see also *id.* at 182 (noting that citizens are not partners, their interests are a cost to be mitigated).

113. See *id.*; see also AMAN, *supra* note 50, at 144 (noting that once the bargaining enters the administrative agency phase, bargaining with NGOs and public interest groups is limited).

114. See LIKOSKY, *supra* note 39, at 180–83.

115. See *Deepwater*, *supra* note 89.

116. See Shannon, *supra* note 41 (discussing how energy policy concerns led to the decision to lift the deepwater drilling ban, over protests from NGOs); see also Eilperin, *supra* note 17 (noting that the government granted BP a categorical exclusion from submitting an environmental impact analysis only eleven days prior to explosion).

117. See Peters & Pierre, *supra* note 54, at 52 ("[G]overnance of [P3s] has to be embedded in public values and must serve under sufficient political control to meet minimal requirements of transparency.").

118. See Hahn, *supra* note 42 (noting the United States collected \$6.5 billion in royalties from extraction leases in 2009).

119. See AMAN, *supra* note 50, at 144 ("[E]conomic discourse . . . increasingly dominates regulation . . .").

120. In this instance, the costs to BP may exceed eight to sixteen times the total amount of extraction lease royalties the United States received in 2009. See *supra* text accompanying notes 60–63.

121. See STEETS, *supra* note 44, at 48 ("[W]herever power is exercised there should be mechanisms of accountability . . ." (citations omitted)).

122. See *supra* text accompanying notes 4 and 61–63.

While transparency primarily involves the public side of a P3, accountability should be of primary concern to both sides¹²³—public negotiators depend upon reelection for their positions of power and the private negotiators have come to recognize the necessity of positive public relations.¹²⁴ As noted generally in transnational contexts, “accountability is largely driven by public interest groups,”¹²⁵ and in the absence of accountability mechanisms, P3s are prone to abuse or corruption.¹²⁶ A poignant example of moral hazard in an environment of minimal accountability is the MMS’s exemption of BP from an environmental impact study over NGO objections and based only on BP’s self-serving report to the MMS.¹²⁷

Effective accountability mechanisms require clear internal rules and predictable oversight.¹²⁸ Participation by a wider range of parties should increase accountability and benefit all parties through better-defined responsibilities and oversight roles. Clear standards and rules reduce the likelihood of costly litigation and enforcement proceedings; predictability and stability entice other private parties to form P3s with the host country; and predictability should operate to reduce insurance costs as risks are better defined.¹²⁹ The Act seeks to impose an unpredictable standard of liability. The moratorium paralyzes business to the detriment of both P3 parties and the consumers. The Spill cost BP billions of dollars, and litigation will only increase the expenses. The costs to the United States are undetermined. The quantifiable costs from unpredictable accountability standards are massive and likely still growing.¹³⁰ More effective accountability mechanisms may well have prevented an extremely costly accident in this instance,¹³¹ and could prevent future disasters.

Efficiency likewise concerns both business and government entities, to the extent it often predominates transparency and accountability concerns.¹³² BP’s costs from the Spill are in the tens of billions of dollars; the cost of enhanced oversight and negotiation could hardly reach this level. A public law system that is both effective and efficient benefits P3s and justifies the market-based regulatory

123. LIKOSKY, *supra* note 33, at 25 (“As a matter of policy, if a government promotes certain corporate groups, then the government should be accountable for the actions of such groups.”).

124. PHILLIP I. BLUMBERG, CORPORATE RESPONSIBILITY IN A CHANGING SOCIETY: ESSAYS ON CORPORATE SOCIAL RESPONSIBILITY 94 (1972) (noting that businesses’ acceptance of corporate social responsibility norms are so entrenched as to be beyond debate).

125. LIKOSKY, *supra* note 39, at 176.

126. *Id.* at 163.

127. *See* Eilperin, *supra* note 17.

128. *See* STEETS, *supra* note 44, at 105–06.

129. This benefit is most applicable to smaller transnationals as BP’s subsidiary underwriter, Jupiter Insurance, Ltd., will not underwrite liability in excess of \$700 million, well below BP’s estimated liability in this instance. *See* Cessna, *supra* note 59.

130. *See supra* note 120.

131. *See generally* NAT’L COMM’N ON THE BP DEEPWATER HORIZON OIL SPILL AND OFFSHORE DRILLING, *supra* note 93, at 225–61 (detailing the many ways in which the Spill might have been prevented and implicating a lack of accountability as a primary cause of the accident).

132. *See supra* note 119.

measures adopted by some agencies.¹³³ Devising a fluid system subject to government control is the best means of ensuring efficient and effective regulation.¹³⁴ However, third-party participation at the planning stages and high standards of accountability should be part of the system for it to remain effective in the long term.¹³⁵ Effective, as opposed to expansive, oversight is necessarily better equipped to avoid financial and environmental disasters and associated government costs than are voluntary measures or labyrinthine regulatory structures. The challenge is in adopting structural changes that encourage efficient oversight and safeguard against inefficiencies and entrenched special interests in the regulatory process.

In light of the incentives and realities of global business and public welfare, an efficient-state system is the most realistic means of increasing accountability and transparency in P3s while maintaining efficiency. The three goals of efficient-state model are interrelated. Increased accountability encourages transparency and reduces the costs associated with uncertainty and instability. Increased transparency creates opportunities to bargain for public welfare¹³⁶ and thereby reduce oversight costs through greater contractual participation and accountability assignment.

III. THE EFFICIENT-STATE SOLUTION

In negotiating a P3 arrangement, the government assumes both public welfare aims and private contract party responsibilities.¹³⁷ Risk taking is implicit in P3 arrangements generally, and extraction industry arrangements in particular, so a significant function of the negotiation phase is to equitably assign risk among the parties while protecting each party's broader interests.¹³⁸ The private side seeks to

133. See AMAN, *supra* note 50, at 141–43 (noting methods the Administrative Procedure Act uses to set standards rather than rules).

134. See Peters & Pierre, *supra* note 54, at 52–53 (“For such [transnational] partnerships to become useful instruments, they have to cater to public and collective objectives. This requires some degree of external control . . .”).

135. See, e.g., Capiello, *supra* note 86 (noting that in the months leading up to the disaster, BP recklessly disregarded a multitude of regulations, norms, and warnings).

136. See STEETS, *supra* note 44, at 48 (“[A]dequate governance mechanisms [...] must be more inclusive and participatory—that is, more democratic—than in the past.” (alteration in original) (quoting COMM’N ON GLOBAL GOVERNANCE, OUR GLOBAL NEIGHBOURHOOD: THE REPORT OF THE COMM’N ON GLOBAL GOVERNANCE (1995))); see also *id.* at 47–48 (discussing the democracy deficit in transnational P3s).

137. See LIKOSKY, *supra* note 33, at 23–24.

138. The efficacy of risk transfer is debated, however. Compare LOXLEY WITH LOXLEY, *supra* note 33, at 176 (“The empirical case for cost reduction and risk transfer, however, has not been established, and some suggest that ‘In infrastructure projects, it rarely makes sense to try to transfer large amounts of risk to the private sector.’” (citation omitted)), with STEETS, *supra* note 44, at 40 (“Trust reduces transaction costs and thereby enables institutions to work more efficiently.” (footnote omitted)). If risk transfer is indeed an exercise in futility, it makes the public welfare negotiation even more important as the financial risks cannot be sufficiently assigned or even estimated. See LOXLEY WITH LOXLEY, *supra* note 33, at 175 (“Transaction costs of the P3 route are often not accurately or fully recorded.”).

reduce the risk it absorbs and insure against the risk it undertakes; the public side seeks to minimize its risk exposure and inure benefits to its constituency.¹³⁹ As with all negotiations, a fundamental concern is reducing the overall transaction costs relative to the benefits inuring under the contract. Assigning risk and evaluating transaction costs within the P3 context implicate the same concerns as the efficient-state model: how to best assign risk in light of transparency, accountability, efficiency, and public welfare concerns.

A. Transparency, Accountability, Public Welfare, and Efficiency

Bäckstrand notes that bringing third parties to the table encourages greater consideration of risks inherent in nonpublic arrangements,¹⁴⁰ overcoming the perception that “[d]eliberative processes [in P3s] tend to be cosmetic and symbolic, and are often added on or serve to legitimize decisions already made.”¹⁴¹ Transparency in the negotiation process assures greater representation of interests than will occur in closed negotiations between the government and special interests, or “peak organizations.”¹⁴² Narrowing the interests represented in the negotiation phase is more apt to produce a final contract in which the parties regard public welfare interests as externalities.¹⁴³ Conversely, a contract that assigns the widest possible range of duties and responsibilities should reduce the overall cost of administration and enforcement.¹⁴⁴

The government’s responsibility to safeguard the public welfare should inform the negotiation process.¹⁴⁵ If the government does not adequately bargain for public welfare, the contract terms will not likely ensure such aims are met, especially given the practical and procedural problems of indemnified or inadequately insured transnational subcontractors.¹⁴⁶ Furthermore, where the government fails to

139. See LOXLEY WITH LOXLEY, *supra* note 33, at 176 (“The apparent motivation behind the approach [of creating P3s] has shifted to some degree from an attempt to move infrastructure spending and debt off the government books, to a desire to reduce costs through transferring risk to the private sector.”).

140. See, e.g., Karin Bäckstrand, *From Rhetoric to Practice: The Legitimacy of Global Public-Private Partnerships for Sustainable Development*, in DEMOCRACY AND PUBLIC-PRIVATE PARTNERSHIPS IN GLOBAL GOVERNANCE, *supra* note 45, at 145 (examining the effects of greater stakeholder participation on transparency and accountability in the CDM and Johannesburg partnerships).

141. *Id.* at 159.

142. AMAN, *supra* note 50, at 143.

143. See, e.g., LIKOSKY, *supra* note 39, at 170 (“[O]ur domestic economy sees aspects of the public interest as risks to be mitigated. By reformulating public interest concerns as risks to project profitability, financial institutions in effect domesticate the common good.”).

144. See *id.* at 191.

145. See, e.g., AMAN, *supra* note 50, at 143 (“[T]he state . . . seeks to assert its view of the public interest in the course of bargaining.”).

146. See David Phillips, *It Lost an Oil Rig, but Transocean May Easily Ride Out the Gulf Oil Spill*, BNET (May 13, 2010), <http://www.bnet.com/blog/sec-filings/it-lost-an-oil-rig-but-transocean-may-easily-ride-out-the-gulf-oil-spill/360?tag=content> (describing Transocean’s insurance and indemnification against losses); see also Kahn, *supra* note 10 (describing the difficulty BP had in recovering from its subcontractors).

negotiate public welfare aims, it creates a moral hazard in the private entity; BP received little warning that its numerous violations would impel government sanctions.¹⁴⁷ Reducing the private party's moral hazard at the negotiation stage is a government's public welfare responsibility.¹⁴⁸

Government should adopt a more risk-averse posture in negotiation and a more aggressive compliance-enforcement posture. Risk aversion by the government will incentivize greater negotiation by both parties to efficiently spread costs to insurers and seek input from NGOs and other interested parties to better understand those costs. On the downside, including a wider range of participants could raise costs of bidding, planning, and negotiating,¹⁴⁹ although there is at least some debate as to whether these costs are permanent.¹⁵⁰ From a short-term transaction cost perspective, the administrative issues of bringing more parties to the table are a disincentive, as is the willingness of P3s to undertake additional public responsibilities as part of the contract.¹⁵¹ Requiring BP to negotiate on a wider range of issues and with more parties would give contract signatories enforcement power through the agreement's terms, while creating strong incentives for BP to insure against its losses at the outset. Though BP could always disregard regulations at its own peril, expanding the roster of participants in the negotiation and embedding them in the oversight mechanism would enable policing by interested parties and thus reduce enforcement costs.

B. Renegotiation and Its Costs

After a disaster like the Spill, the government is likely to impose harsh measures such as an industry-chilling moratorium on drilling¹⁵² or renegotiation as in the form of the Act.¹⁵³ The effects of the moratorium and renegotiation on business, policy, and consumer interests are likely to have far-reaching indirect effects, destabilizing investment and increasing regulation costs.¹⁵⁴

147. See Strickler, *supra* note 92 (noting BP's repeated failure to meet inspection requirements without significant adverse consequences).

148. MCAFEE & MCMILLAN, *supra* note 36, at 17 ("Moral hazard, like risk aversion, is an element that the government agency must consider in designing the optimal contract."); see also Boddewyn, *supra* note 39, at 196 ("Ongoing operations, on the other hand, require a type of government relations focusing on the integration of the guest company in to the host economy and society through the obeying of laws . . .").

149. See LIKOSKY, *supra* note 39, at 170 ("[P]articipatory planning is reformulated as a financial risk to the interest of planners, a risk that must be mitigated at the least possible cost to the project's commercial interests.").

150. See STEETS, *supra* note 44, at 40 ("Trust reduces transaction costs and thereby enables institutions to work more efficiently." (footnote omitted)).

151. See LIKOSKY, *supra* note 39, at 170.

152. A seven-year moratorium was imposed on deepwater drilling, which is almost certain to stifle oil exploration and American energy policy for its duration. See John M. Broder & Clifford Krauss, *U.S. Drops Bid to Explore Oil in Eastern Gulf*, N.Y. TIMES, Dec. 2, 2010, at A1.

153. See *supra* text accompanying note 68.

154. See Brooks, *supra* note 38 (discussing the likely harmful effects to the oil industry in light of government actions taken in response to the Gulf Oil Spill).

Renegotiation portends many hidden costs that ultimately harm the public as well as the private industries.¹⁵⁵ Renegotiation is likely to impose oppressive terms on the private partner as the public side renegotiates only when it recognizes a deficiency in its perceived benefits under the contract.¹⁵⁶ In the present instance, U.S. taxpayers have funded the cleanup and seek to recover from BP. As undesirable as the outcome that taxpayers foot the bill for BP's negligence is, the prospective costs to taxpayers of renegotiation are likewise substantial, if indirect. There is a fierce competition for transnational partnerships in the extraction sector, and private parties will disfavor contracting with a country that negotiates for oppressive terms, leaving the host country's core industries underdeveloped.¹⁵⁷

Renegotiation's unpredictable nature increases the political risk of the country that utilizes it. The more political risk—or likelihood of acting unpredictably against the private party's interests—a country holds, the less likely transnational actors will invest in that country, depriving the country of revenue, infrastructure, and access to cheaper resources.¹⁵⁸ Transnational industries will look closely at BP's liability for the Spill, especially costs imposed by the Act. If the United States punishes BP harshly, future partners in P3s will seek greater assurances in the negotiation process in order to do business within the United States. Accordingly, the United States could be forced to make more front-end concessions to remain a competitive foreign investment destination, further eroding its bargaining position vis-à-vis public welfare interests.¹⁵⁹ Increasing the risk or cost of doing business in the United States may dissuade transnational extraction companies from contracting with United States altogether. Fewer P3s with transnationals will result in more of those contracts going to domestic industries, which will likely increase costs to the public side through greater overhead, insurance, and tax subsidy costs.¹⁶⁰ The ancillary effects of fewer transnational P3s will likely include higher insurance costs, less market participation from smaller firms, and reduced overall foreign investment in American infrastructure.¹⁶¹ In order to avoid negative perceptions stemming from the Act, the United States would be well served to decrease regulatory compliance costs and enhance P3 stability through an efficient-state regulatory model. The rationale behind transnational P3s is to reduce the host country's development costs, but inadequate negotiation, poor regulation, or renegotiation could inadvertently increase both the economic and external costs

155. *See id.*

156. *See* LIKOSKY, *supra* note 39, at 333 (“Governments may take on too many downside risks. . . . Many renegotiations are driven by [this] feature[] of partnerships.”).

157. *See* OMOROGBE, *supra* note 60, at 25.

158. *See id.* at 45; *see also* LIKOSKY, *supra* note 39, at 311 (“[R]enegotiations may decrease foreign appetite for investment . . . driving down efficiency and overall revenue into the country.”).

159. *See, e.g.,* OMOROGBE, *supra* note 60, at 18 (noting that environmental regulation in the United States “greatly increases costs for the companies”). Increased costs to businesses will predictably result in higher costs to consumers, the true public side of a P3. *See id.*

160. *See* LIKOSKY, *supra* note 39, at 264.

161. *See* Brooks, *supra* note 38.

of such arrangements past the point at which it is rational to form such relationships.¹⁶²

Inasmuch as the proposed Act is a renegotiation of BP's liability at the lease's inception, and insofar as the effects of such a renegotiation are harmful to the oil industry, consumers, and American taxpayers, the U.S. government should avoid similar measures in the future. As a complement to efficient-state regulatory measures, an effective way to avoid such costly measures is an enhanced contract negotiation process that brings the responsibilities of the parties closer to self-enforcing than they are under the existing regulatory model. Enhanced accountability, transparency, and consideration of the public welfare ultimately increase efficiency and serve to preclude measures such as the Act and the moratorium, both of which are toxic to transnational investment in, and development of, the United States' vital industries.

IV. THE FUTURE OF REGULATION AND CONTRACT IN TRANSNATIONAL P3 CONTEXTS

The Act raises important questions regarding effective regulation and public welfare. Retroactive measures, such as the Act and its predecessor the OPA, are necessary and meaningful only in the wake of disasters, but such measures cannot retroactively prevent or rectify disasters.¹⁶³ BP can pay costs even in excess of \$50 billion.¹⁶⁴ However, smaller oil drilling companies are not so profitable and future measures may not be possible with a less wealthy P3 partner.¹⁶⁵ Recognizing that some disasters will always be inevitable, liability may still be more cheaply and effectively negotiated for ex ante by improving the contract bargaining process and streamlining the administrative role—hallmarks of an efficient-state theory. Despite the benefits of enhanced accountability, public welfare protection, transparency, and efficiency, realizing an efficient-state regulatory system will not be possible without overcoming entrenched perceptions and structural impediments to reform.

162. See *supra* text accompanying notes 33–36. As the formation of P3s is motivated by economic incentives, excessive costs in creating or maintaining a P3 necessarily undermine the rationale for such arrangements.

163. See generally Brad Marten, *Brad Marten on Fighting the Last War: The Relevance (and Irrelevance) of the Exxon Valdez Oil Tanker Spill to the Deepwater Horizon Oil Rig Spill*, LEXISNEXIS.COM (May 6, 2010, 7:37 PM), <http://www.lexisnexis.com/community/litigationresourcecenter/blogs/litigationblog/archive/2010/05/07/brad-marten-on-fighting-the-last-war-the-relevance-and-irrelevance-of-the-exxon-valdez-oil-tanker-spill-to-the-deepwater-horizon-oil-rig-spill.aspx>.

164. See Bergin, *supra* note 61 (showing that total costs of the BP disaster are being adjusted continuously upward, and are presently estimated to be around \$50 billion).

165. See Nicholas Graham, *BP's Profits Far Outweigh the Cost of Cleaning Up Gulf Oil Spill*, HUFFINGTON POST (May 27, 2010, 1:18 PM), http://www.huffingtonpost.com/2010/05/27/bps-profits-far-outweigh_n_591992.html.

A. Perception Obstacles

The Act raises questions about how to create more effective regulatory processes so that measures like the Act are not required again.¹⁶⁶ The U.S. government's fumbled response to the Spill is an indictment of the present regulatory model's limitations.¹⁶⁷ Reforming the regulatory paradigm and moving from the inertia of the present regulatory system to that of an efficient-state system requires more than mere persuasion; it requires the will to transform perceptions of American regulation, not only domestically but also abroad.

1. Transnational Perceptions

The Act increases political risk by raising the possibility that retrospective increases in liability limits will become the paradigm of future regulation.¹⁶⁸ The United States is presently a prime destination for P3s in large part for its perceived willingness to underwrite risk to the benefit of the private parties.¹⁶⁹ The Act's loss reassignment to BP may be politically defensible, but such ex post measures are capricious considering the government is not without blame for the disaster.¹⁷⁰ The United States's increase in BP's liability limits cannot inspire confidence in other transnationals bidding for extraction leases.

In crafting better-defined public welfare responsibilities within P3s, front-end participation of public interests and NGOs is desirable, not a cost to be avoided.¹⁷¹ The irony of risk allocation in transnational P3s is that most of the transnationals active in extraction industries are from well-developed countries that have public welfare aims strongly entrenched in their native business climate.¹⁷² In its hidebound insistence on mitigating nonmarket costs¹⁷³ the U.S. government overlooks the possibility that foreign operators are not so hostile to costs associated with safeguarding the public welfare. It is not unthinkable that the U.S. government could bargain for greater public benefits in P3s without completely overwhelming the incentives presently inherent in the U.S. business climate. Rather than renegotiate ex post, the United States is in a prime position to bargain ex ante with

166. See Daniels & Trebilcock, *supra* note 39, at 378 (“[V]ery little attention is paid to the design of the institutional processes surrounding public/private sector infrastructure partnerships or the complex contracting problems that they present.”).

167. See Tim Dickinson, *The Spill, the Scandal, and the President*, ROLLING STONE, June 24, 2010, at 54.

168. See OMOROGBE, *supra* note 60, at 45.

169. LIKOSKY, *supra* note 39, at 184–85.

170. See, e.g., NAT’L COMM’N ON THE BP DEEPWATER HORIZON OIL SPILL AND OFFSHORE DRILLING, *supra* note 93, at 253–61; ‘Shared Failure’ in BP Spill Cited in Panel Report, *supra* note 23.

171. See LIKOSKY, *supra* note 39, at 176 (“[A]ccountability is largely driven by public interest groups.”).

172. Transocean (Switzerland), Enso (U.K.), and Seadrill (Norway) are among the largest drilling companies in the world and are based in countries with traditionally strong regulatory systems. See e.g., INTERNATIONAL HANDBOOK ON ECONOMIC REGULATION (Michael Crew & David Parker eds., 2006).

173. See LIKOSKY, *supra* note 39, at 182.

transnationals to more effectively assign liability while better protecting American public policy concerns.

2. Domestic Perceptions

Domestic perceptions of regulatory reform will depend largely on the scope of reform adopted. On the unlikely end of the scale is the American government opting to turn P3s into publicly held corporations as in the European model, rather than creating extraction leases subject to administrative oversight as it presently does.¹⁷⁴ Adopting the European model would make the P3 a government operation, ostensibly creating avenues for greater transparency and concomitantly reducing the need for secrecy.¹⁷⁵ Furthermore, the government could appoint watchdog directors from outside industries such as NGOs and labor unions to reduce its administrative costs. A likely insurmountable obstacle to such reform is legitimizing such a socialized structure in the American business environment.¹⁷⁶

The most likely result will be business as usual, with both sides hoping disaster will not befall them and relying on renegotiation and litigation if it does. But the tremendous public welfare and financial costs associated with this paradigm make it undesirable. The most formidable obstacle to implementing efficient-state regulatory measures is not a cost assessment, but the political reality of the present system: most politicians in a competitively democratic system crave the chance to make headlines, not to work behind the scenes. A well-publicized act by Congress may garner more votes than a quiet, effective one that averts disasters like the Spill. Furthermore, efficient measures offer fewer justifications for taxes and spending, while any reduction in the bureaucratic state means entrenched interests must first be defeated.

The predominant approach for a government aided by the possibility of renegotiation is to approach initial negotiations as a win-win situation.¹⁷⁷ As the Act demonstrates, the U.S. government may anticipate gaining from the contract as written or rely upon a later renegotiation to the detriment of investors, third parties, and its P3 partners. Since the government is capable of controlling the administrative information disseminated to the public and could thus refuse to disclose facts surrounding its negotiations, few incentives are in place to encourage the government to approach P3 negotiations with the care a truly private party would.¹⁷⁸

To sustain P3 arrangements and the public welfare interests of its citizens, the U.S. government must shift its fundamental assumptions in negotiating P3s. Rather than engage in its own form of firefighting, or ad hoc damage control, the government should bargain as a private party unable to rely upon unilateral renegotiation as a viable alternative to due diligence. Though this simple shift in

174. See AMAN, *supra* note 50, at 87–88 (comparing the U.S. and European P3 models).

175. See *id.*

176. See *id.*

177. See LIKOSKY, *supra* note 39, at 184 (“[T]he presentation of P3 accountability in the U.S. context is a nonissue because of the win-win nature of the approach is a naive projection of joviality on what must be hard-nosed bargaining.”).

178. See *id.* at 163–64 (discussing lack of transparency from the government in P3s).

negotiation tactics would result in an immediate return, it is difficult to predict if it would be sufficient in itself, and even its implementation would require overcoming the structural tendency toward a neocorporatist¹⁷⁹ negotiation process.¹⁸⁰

B. Structural Issues

A common shortcoming of P3 leases is their failure to anticipate conflict resolution, the need for adaptation, or the true costs of renegotiation.¹⁸¹ Such failures are contract issues that could be avoided through better agreement structuring. Though many details of BP's lease are unavailable to the public, apparently neither the BP lease nor the statutory limitations on liability sufficiently anticipated the scope of the Spill's damage or the legal and financial costs of recovery.¹⁸² Omorogbe notes that "[w]hat a fluctuating investment climate needs is not contract revision whenever fundamental changes occur. Instead . . . the fluctuating nature of the investment climate should be taken into account."¹⁸³

Omorogbe also suggests that "the right agreement for any HC [host country] is first and foremost one that is capable of managing and supervising efficiently."¹⁸⁴ Incentives to cut costs through reduced safety expenditures and compliance are likely highest where costs, risks, and uncertainty are highest—fixed-price contracts for exploratory drilling. For example, the BP lease was in the form of a fixed-price contract, more specifically, a royalty-bearing license.¹⁸⁵ In fixed-price leases, profits accruing to the private partner vary inversely with development costs.¹⁸⁶ Since every additional dollar spent by BP on compliance, safety, or research is subtracted from its bottom line, this form of contract strongly encourages cost cutting. A typical production-sharing agreement¹⁸⁷ likewise incents the explorer to cut all possible costs in bringing oil to the surface.¹⁸⁸ Participation agreements and joint ventures can be desirable alternatives to concessionary contracts as they are highly negotiated at each stage, rely largely on self-enforcing regulations, and allow the host country greater control over the extraction process.¹⁸⁹ The United States should consider various forms of leases designed to ensure, in each case, that

179. Neocorporatism is a system or process in which the government bargains with a select group of special interests and "peak organizations" with respect to public policy. *See* AMAN, *supra* note 50, at 143–44.

180. *See id.*

181. OMOROGBE, *supra* note 60, at 5.

182. *See* Gloria Gonzales, *BP Oil Spill Damages To Stretch Insurance Coverage*, OILPRICE.COM (Aug. 2, 2010, 3:51PM), <http://oilprice.com/Environment/Oil-Spills/BP-Oil-Spill-Damages-to-Stretch-Insurance-Coverage.html>.

183. OMOROGBE, *supra* note 60, at 5–6.

184. *Id.* at 70.

185. Hahn, *supra* note 42.

186. *See* MCAFEE & McMILLAN, *supra* note 36, at 23.

187. *See* OMOROGBE, *supra* note 60, at 60–61.

188. Because companies in production-sharing agreements bear all the risk associated with exploration, the companies have maximum incentive to minimize exploration costs. *See id.*

189. *Id.* at 64–65.

oversight “objectives are satisfied, adequate financial benefits are accruing to the state, and the company is assured of an acceptable level of profits at all times.”¹⁹⁰

Limited market-based regulation is also desirable provided the government structurally implements sufficient oversight *ex ante*. Private, or market-based, regulations require less input, draw from a narrow range of generally aligned interests, can respond quickly to change, and encourage the private party to participate in creating mutually beneficial standards for compliance.¹⁹¹ Because of these advantages, both governments and private parties are likely to find such private or nonlegal regulations more workable in complex projects involving transnational actors, multiple subcontractors, a host of regulations from overlapping industries, and a nexus of publicly traded companies whose stock prices are in permanent flux.¹⁹² Purely public laws are potentially obstructive in such complex arrangements, where participants attempt to minimize the effect of complicated regulatory mechanisms while maximizing profits.¹⁹³ The key to effective market-based regulations is that they should not be a last resort in lieu of regulation or intended to circumvent oversight; the parties should agree upon clear standards and judiciously assign responsibility.¹⁹⁴ For example, fixing contract terms through extensive negotiation, aligning incentives through a joint-venture agreement for extraction, assigning third-party interests to assist in enforcement, and tying economic incentives to compliance can all be used in conjunction with market-based regulations. Similar provisions in transnational P3 contracts will cost less to implement and maintain than the status quo, while better safeguarding American public welfare interests.

Integrating the benefits of private and public regulatory schemes is the principle underlying the call for enhanced contract negotiation procedures and efficient-state regulatory processes. To achieve these ends, public lawmakers can draw lessons from the theories that gave rise to private regulations in the first instance: corporate legal models, transnational legal pluralism, and notions of the government as a fiduciary. In recognition of common underlying aims in calls for efficient-state regulation, aspects from these models may enhance the operation of P3s and preserve the public and private benefits contemplated by those arrangements.

190. *Id.* at 70.

191. See Helgesson, *supra* note 80, at 24 (noting that under a market regulation scheme, the “business sector is expected to help produce frameworks for governing itself by creating industry standards, codes of conduct, and other rules as a complement to, or even substitute for, intra- and interstate regulation”). For discussion of private regulation and its development, see generally Susan Strange, *The Declining Authority of States*, in *THE GLOBAL TRANSFORMATIONS READER: AN INTRODUCTION TO THE GLOBALIZATION DEBATE* 127 (David Held & Anthony McGrew eds., 2d ed. 2003).

192. For a discussion of private actors’ incentives to private or market-based regulations, see Julia Steets & Laura Blattner, *Partnership Accountability Need Not Be Democratic Accountability*, in *DEMOCRACY AND PUBLIC-PRIVATE PARTNERSHIPS IN GLOBAL GOVERNANCE*, *supra* note 45, at 55, 58–59.

193. *Id.*

194. See *id.*; see also AMAN, *supra* note 50, at 96 (praising the Environmental Protection Agency’s model of delegation).

1. Corporate Legal Models and Transnational Legal Pluralism

In response to globalization and the need for businesses to operate across many jurisdictions simultaneously, many private actors and the entities that regulate them have rethought the necessity of centralized control and the nature of regulation.¹⁹⁵ Corporate models involve less parochialism, tend to be task oriented rather than process oriented, and emphasize cooperation and efficiency.¹⁹⁶ Such models are especially beneficial in transnational contexts, where labyrinthine layers of regulation may create only an illusion of process while inhibiting effectual oversight.¹⁹⁷ The desirability of voluntary, or private, regulations has arisen from public law's inability to keep pace with the necessities of commerce, as well as the absence of a universal enforcement framework—indeed, the unworkability of such a framework.¹⁹⁸ The scholarship of transnational legal pluralism deals extensively with transparency and accountability in transnational industries, as well as means of realizing these goals.¹⁹⁹ The primacy of these goals intends to bring business and privately regulated industries back under the umbrella of regulation by creating an avenue for a democratic citizenry, through its government, to supervise actions affecting national policy aims.²⁰⁰ The following suggestions for structural changes to P3 arrangements foster stability and efficiency—with the resultant profitability—that produced functional governance standards in the corporate and transnational contexts.²⁰¹

Where rights and duties are not defined in the contract or enforceable within juridical or administrative frameworks, private parties may compensate by developing unsanctioned, private regulations with attendant transparency and accountability issues,²⁰² or by disregarding outright costly or inconvenient regulations.²⁰³ In either case, this neocorporatist process endangers the P3's democratically sanctioned public welfare aims.²⁰⁴ The keys to successful corporate governance are its cooperative nature and horizontal integration, whereas the present regulatory system relies heavily on vertical integration.²⁰⁵ Corporate

195. See, e.g., IAN HARDEN, *THE CONTRACTING STATE* 14–26 (Norman Lewis & Cosmo Graham eds., 1992).

196. See AMAN, *supra* note 50, at 121–22.

197. See, e.g., Andrew D. Mitchell & John Farnik, *Global Administrative Law: Can It Bring Global Governance to Account?*, 37 *FED. L. REV.* 237, 250 (2009).

198. See generally *id.* at 237–58.

199. See, e.g., *id.*

200. See LIKOSKY, *supra* note 39, at 298.

201. See LIKOSKY, *supra* note 33, at 23.

202. See LIKOSKY, *supra* note 39, at 298; see also STEETS, *supra* note 44, at 48 (“[W]herever power is exercised there should be mechanisms of accountability.” (citation omitted)).

203. See *supra* text accompanying notes 89–97.

204. See AMAN, *supra* note 50, at 143 (“Neocorporatist mentality sidesteps traditional democratic processes with technocratic and managerial solutions. . . . [I]t is a risk to democracy.”); see also Boddewyn, *supra* note 39, at 196 (“The major point here is that government relations have to be intelligently managed like any other function of the enterprise, rather than neglected, improvised, or let go wild.”).

205. See DAVID G. FREDERICKSON & H. GEORGE FREDERICKSON, *MEASURING THE*

governance networks, or horizontally integrated structures, have not entirely replaced vertical integration but, when adopted, have shifted the paradigm of regulation.²⁰⁶ Horizontal integration offers promising efficiency incentives to private parties in P3s: greater participatory planning in regulatory measures²⁰⁷ and less-restrictive oversight mechanisms through industry-wide, competitive self-policing measures.²⁰⁸

Other useful measures derived from corporate legal models are tax and subsidy incentives tied to stringent compliance standards, thus enhancing efficiency while reducing costs and burdens to both public and private parties.²⁰⁹ By embedding watchdog overseers able to quickly approve or disapprove critical measures, or establishing ex ante unlimited liability for contractors who either fail to institute or conform to reasonable standards, the government could align BP's interests with its own public welfare interests. As an added benefit, the noninvasive and efficient nature of the regulations will entice future extractors to comply with the regulations.

In order to align public and private interests, public partners must create incentives that make compliance desirable and profitable to the private party, not simply an obstacle to business. In BP's case, ignoring safety measures was preferable to regulatory compliance due to cost overruns that resulted from construction delays.²¹⁰ Structuring the Macondo lease as a joint venture rather than a fixed-price contract could have included cost-sharing provisions for exploration in exchange for greater share of profits than were available under the fixed-price contract.²¹¹ This measure would have reduced BP's incentive to cut exploration costs. The United States may also align public and private incentives by changing its assumptions when entering the negotiation process.²¹² Shorter contract periods will require more frequent assessments of the parties' goals and demand a greater

PERFORMANCE OF THE HOLLOW STATE 12–13 (2006).

206. See AMAN, *supra* note 50, at 96–98.

207. The commission tasked with determining the causes of the Spill and making recommendations for reform have propounded at least one aspect of a horizontally integrated strategy in recommending that independent scientists from federal agencies be consulted at the negotiation stage. See 'Shared Failure' in *BP Spill Cited in Panel Report*, *supra* note 23.

208. See Helgesson, *supra* note 80, at 24 (under a market regulation scheme, the "business sector is expected to help produce frameworks for governing itself by creating industry standards, codes of conduct, and other rules as a complement to, or even substitute for, intra- and interstate regulation"); see also AMAN, *supra* note 50, at 96 (discussing the positive results of the Environmental Protection Agency adopting horizontal governance mechanisms).

209. See LIKOSKY, *supra* note 39, at 164.

210. Joe Carroll & Katarzyna Klimasinska, *BP Cost-Cutting, Conflicts Preceded Gulf Disaster*, *U.S. Says*, BLOOMBERG.COM (Sept. 14, 2011, 4:26 PM), <http://www.bloomberg.com/news/2011-09-14/bp-transocean-halliburton-faulted-by-u-s-in-2010-gulf-spill.html>.

211. See OMOROGBE, *supra* note 60, at 65 (noting that the Nigerian government is entitled to 60% of profits in its joint ventures); see also Hahn, *supra* note 42 (noting the United States bargained for roughly 12% of profits in its lease with BP).

212. See LIKOSKY, *supra* note 39, at 184 ("[T]he presentation of P3 accountability in the U.S. context is a nonissue because of the win-win nature of the approach is a naive projection of joviality on what must be hard-nosed bargaining.").

degree of transparency. The BP lease was for five years,²¹³ whereas a shorter term could allow for an easier adjustment of priorities and policies. More flexible contracts are also a means of reducing the cost and volatility of unscheduled renegotiation.²¹⁴ By negotiating directly with smaller players rather than allowing the primary to engage them as subcontractors, the United States can enter into horizontally integrated agreements regulated by task-oriented entities created for the purpose. Another reform would be to contract on as comprehensive a range of issues as possible. The result of inadequate drafting makes litigation more likely, increasing costs and relegating questions of accountability to the postdisaster environment rather than the negotiation phase.²¹⁵ The measures listed here intend to align incentives and ensure that regulation is both effective and noninvasive.

The key to adopting corporate legal models in P3 arrangements is to promote cooperation and align the parties' incentives to meet public welfare aims. Not all of the suggestions above should be applied in every case, but each is an option to be weighed in transnational P3s when economic stakes are high, moral hazard exists, and a potentially burdensome regulatory structure may incent bad behavior with disastrous consequences.

2. Government as Fiduciary: Stronger Bargaining for Public Welfare

In addition to its role as a private contractor seeking to maximize its economic benefit under the P3 arrangement,²¹⁶ the government has a duty to bargain for the public welfare.²¹⁷ The unwillingness of the United States government, under the present paradigm, to negotiate more strenuously with prospective transnational partners is a major concern.²¹⁸ This Note advocates more proactive use of the government's inherent powers to control operators within its jurisdictional reach.

Government responsibility for public welfare entails aggressive bargaining not only for direct economic benefits, but also for indirect benefits such as labor, employment, natural resource protection, and infrastructure development, as well as other national interests that maximize economic development.²¹⁹ Though the Act is an ex post acknowledgment of this duty, effective ex ante measures may include

213. See Braden Reddall, *Transocean Rig Loss's Financial Impact Muddled*, REUTERS (Apr. 22, 2010, 4:37 PM), <http://www.reuters.com/article/idUSN2211325420100422>.

214. Extraction contracts in the oil and gas industry are notoriously poor at providing for conflict resolution and adaptation mechanisms. See OMOROGBE, *supra* note 60, at 5.

215. LIKOSKY, *supra* note 39, at 191.

216. See, e.g., LOXLEY WITH LOXLEY, *supra* note 33, at 176 ("The apparent motivation behind the approach [of creating P3s] has shifted to some degree from an attempt to move infrastructure spending and debt off the government books, to a desire to reduce costs through transferring risk to the private sector."); Beermann, *supra* note 38, at 204 ("Economic development is often advanced as a reason for creating public-private partnerships.").

217. See LIKOSKY, *supra* note 33, at 23–25 (arguing that where the government assigns public duties to a private party, it retains the duty to supervise that entity).

218. See *supra* notes 177–80.

219. See LIKOSKY, *supra* note 39, at 298 ("[T]he government has a fiduciary duty to ensure the advancement of its domestic constituency.").

delineating policy goals and devising structures to ensure these goals are voluntarily embraced by the private partner as well.²²⁰ Contracting horizontally with the subcontractors rather than vertically through primary contractors can ensure that all parties are aware of the public policy goals contemplated by the P3 arrangement.²²¹ Cross-subsidization of less-attractive aspects of the project may reduce the desirability of subcontracting to parties who are difficult to regulate or reach, and operate as another means to align private and public welfare interests by evenly distributing the wealth generated by the P3.²²² Broader horizontal integration and contracting directly with parties rather than primaries that subcontract are means of keeping enforcement costs down and public/private interests aligned.²²³

Enhanced ex ante negotiation is not immune from one major drawback of the Act: indirect costs to the public side from burdensome terms imposed upon the private party. The United States' desirability as an investment location may diminish if private transnationals perceive third-party input at the negotiation stage as inimical to their interests.²²⁴ However, the United States is presently the home to the thirteenth-largest proven oil reserves in the world.²²⁵ Neither the Act nor the measures proposed in this Note will eradicate the geographic benefits of drilling in the United States. In light of this, a logical question is: why worry about renegotiation at all? The public party should seek to eschew the moral hazard and concomitant disregard for public welfare aims enabled by a renegotiation regime. Private parties also stand to gain when the public party's incentives to renegotiate are minimized. A predictable regulatory system is ultimately more efficient and cheaper for private parties than the Russian-roulette style liability in place now, where the private party can flout rules until the resultant liability threatens the survival of the company itself.²²⁶ In addition, renegotiation exacerbates volatility, which acutely affects securities prices.²²⁷ When volatility results in part from the

220. See Boddewyn, *supra* note 39, at 196 ("The major point here is that government relations have to be intelligently managed like any other function of the enterprise, rather than neglected, improvised, or let go wild.").

221. LIKOSKY, *supra* note 39, at 164 (calling for articulation of public policy interest applicable to all contractors).

222. *Id.* (suggesting cross-subsidization as one inducement to responsible behavior as a means to avoid the contractors' competition for the most profitable aspects of a project and thereby balkanizing the whole).

223. See *supra* text accompanying notes 205–08.

224. See Peters & Pierre, *supra* note 54, at 45 ("[P]ublic sector actors are increasingly dependent on financial resources from the private sector for public investment, but private sector interests have fewer and fewer incentives to engage the public sector, for instance in public-private partnerships.").

225. CIA WORLD FACTBOOK (2011), available at <https://www.cia.gov/library/publications/the-world-factbook/geos/us.html>.

226. BP's stock price was so harmed by the Gulf Oil Spill that BP was susceptible to a takeover. Loren Steffy, *The Return of BP Takeover Speculation*, CHRON.COM (Dec. 17, 2010, 11:26 AM), http://blogs.chron.com/lorenstefly/2010/12/the_return_of_b_1.html.

227. Hans Wagner, *Volatility's Impact on Market Returns*, INVESTOPEDIA.COM (May 7, 2008), <http://www.investopedia.com/articles/financial-theory/08/volatility.asp> ("When volatility increases, risk increases and returns decrease.").

security issuer's own negligence, it may create further costs in the form of security holders' litigation.²²⁸ A more effective regulatory scheme would greatly reduce the risk of volatility in large-capitalization extractors' stock prices, protecting wealth and domestic investments.²²⁹ In a real sense, regulation can operate as a form of insurance for these companies, whereas renegotiation is a gamble that public industries, such as massive transnationals, would be better off avoiding.²³⁰

For the time being, the United States enjoys significant geographical advantages, with profits realizable independent of modest cost increases in the negotiation process. Private and public parties tend to profit handsomely from successful P3s in the United States²³¹ and can prospectively negotiate for a more balanced arrangement if costs are anticipated to increase as the result of structural changes. By bargaining for a wider range of public interests at the negotiation stage, the United States will reduce the likelihood of unpredictable, indirect economic and environmental costs associated with a regime that sanctions renegotiation as a viable alternative to inclusive, *ex ante* negotiation.

The efficacy of the efficient-state model depends in part on willingness by the government to strenuously negotiate for public welfare interests,²³² to take its difficult-to-monetize public welfare interests as seriously as its economic interests.²³³ The participation of subcontractors, NGOs, independent advisory experts, and representatives from local industries in the negotiation process could serve to effectively outsource the monetization studies to those industries, making a project's cost-benefit analysis more reliable than one derived solely from either P3 party. The present model is that of a state acting largely on behalf of entrenched economic and administrative interests to the detriment of broader public welfare interests.²³⁴ Overall, the implementation of even some of the ideas suggested in this Note will increase the efficiency of the process, reduce back-end costs for both public and private parties, and increase the likelihood that future negotiations will better represent a broader scope of public welfare aims while maximizing long-term profitability for both parties to transnational P3s.

228. See *Oil Spill Hits BP's Stock, Threatens Its Future*, *supra* note 13; see also Bates, *supra* note 63 (discussing costs of securities litigation stemming from material misstatements from BP).

229. See Wagner, *supra* note 227.

230. LIKOSKY, *supra* note 39, at 288 (“[I]t is not always clear that shifts in the nature of partnerships [due to renegotiation] result in more equitable outcomes.”).

231. See Hahn, *supra* note 42 (noting that the United States received over \$6.5 billion from exploratory leases in 2009); see also Graham, *supra* note 165 (noting that BP's profits should be sufficient to pay clean-up costs).

232. See *supra* text accompanying notes 177–80.

233. See *supra* text accompanying notes 117–20.

234. As noted by the executive director of an environmental group at the time of the Spill, “[MMS’s] oversight role has devolved to little more than rubber-stamping British Petroleum’s self-serving drilling plans.” Eilperin, *supra* note 17 (quoting Kieran Suckling, Executive Director, Center for Biological Diversity).

CONCLUSION

The Gulf Oil Spill and its aftermath, including the moratorium and the Big Oil Bailout Prevention Unlimited Liability Acts, throw into relief the inadequacy of existing forms of regulation and P3 contract negotiation. Not merely reforming, but rethinking the American regulatory model is necessary to better ensure the representation of both public and private aims in transnational P3 arrangements. By embracing an efficient-state regulatory model, the administrative, litigation, and implementation costs of P3s can be greatly reduced, saving the public money. Unexpected costs to taxpayers can be more equitably absorbed by insurers and private parties when negotiated for *ex ante*. The model would also increase transparency, accountability, efficiency, and participation while giving public welfare actors more input into P3 negotiations.

An enhanced bargaining process with representatives from the widest practicable range of affected third parties benefits the private parties of P3s in that it will better contemplate risk assignment and thereby reduce the likelihood of unilateral renegotiations, increase the likelihood that well-defined policy goals will be included in the contract, and create more-detailed information for the private parties' insurer. Enhanced contract negotiations will reduce volatility in the P3 arrangement and reduce the need for invasive regulation, thus stabilizing private parties' expectations and increasing overall efficiency. Even if private parties are reluctant to adopt higher front-end costs that may arise from participation of a wider range of interests in the negotiation process, the government has tools to enhance cooperation: tax subsidies for compliance with safety standards; cost-sharing agreements; delegation of market-based regulatory measures through horizontal integration of subcontractors, contractors, public interest groups, and oversight agencies; shorter contract periods; structuring the agreement based on responsibly assessed risk preferences; and the threat of higher insurance requirements, among a multitude of other possibilities.

The Big Oil Bailout Prevention Unlimited Liability Act of 2011 represents much of what is wrong in the regulatory system in the United States. It is a backward-looking measure that does little to safeguard the public interest beyond mitigating financial losses²³⁵ arising from a preventable disaster.²³⁶ Backward-looking measures like the Act are inevitable only where *ex ante* measures are insufficient to adequately safeguard both public and private aims. In order to avoid such ineffectual measures in the future, the U.S. government must adopt more efficient regulatory and negotiation processes. Winston Churchill once quipped that "democracy is the worst form of government except for all the others that have been tried . . ."²³⁷ It could also be said today that renegotiation is the worst form of contract remedy except for all the others that have been tried.

235. LIKOSKY, *supra* note 39, at 166 ("To make transparency backward-looking embraces a concept of forensic accountability that is not suited to progressive public interest minded planning.")

236. See generally NAT'L COMM'N ON THE BP DEEPWATER HORIZON OIL SPILL AND OFFSHORE DRILLING, *supra* note 93, at 225–26.

237. JAMES C. HUMES, THE WIT & WISDOM OF WINSTON CHURCHILL 28 (Harper Perennial 1995) (1994).

Efficient-state regulation will reduce administrative costs as compared to those of the present regulatory paradigm. Furthermore, the enhanced contract negotiation process fundamental to efficient-state regulation will better protect American public welfare interests and reduce costs for transnational parties by protecting against unpredictable policy shifts. Effective administration and efficient contracting will greatly reduce or eliminate the financial, environmental, public relations, business disruption, and compliance costs associated with measures like the moratorium and the Big Oil Bailout Prevention Unlimited Liability Act of 2011.