

June 5, 2007

Second Circuit Sends MTBE Actions Back to State Court

On May 24, 2007, the U.S. Court of Appeals for the Second Circuit ruled in *The People of the State of California v. Atlantic Richfield et al.* pending in *In Re: Methyl Tertiary Butyl Ether ("MTBE") Products Liability Litigation (M.D.L 1358)* that the district court did not have removal jurisdiction over the State of California's and the State of New Hampshire's actions against corporations that manufactured, refined, marketed, or distributed gasoline containing MTBE. The court remanded the actions from federal court back to the state courts in which they commenced. In doing so, the court rejected the oil industry defendants' argument in the state court below and on appeal that they were de facto compelled to use MTBE as an oxygenate by the federal government. The argument has been a principal defense in the underlying proceedings; the exact effect of this ruling remains to be seen but does not bode well for the defendants. Regardless, the ruling can be seen as a blow to industry efforts to deflect liability for the use of MTBE to meet the EPA oxygen mandate. Additionally, it frustrates industry hopes that a federal court would be more receptive to its arguments than a state court. The complete decision can be read [here](#).

Implications for Oil Industry Defendants

During the last several years, the major oil companies and others in the gasoline refining and distribution community have been the targets of lawsuits claiming that they are responsible for billions of dollars of damage to the nation's aquifers because of MTBE contamination, in large measure from leaking retail underground gasoline storage tanks. The cases typically have been filed in state court exclusively on state law causes of action. Most of these claims have been in regions that are required to use reformulated gasoline ("RFG"), which until recently was required to contain at least two percent oxygenates by weight (between 12 and 15 percent by volume). MTBE, although not yet proven to be a health hazard, causes noxious odors in drinking water, even when dispersed in very small amounts. Plaintiffs, who typically are states or municipalities and are represented by class action-type lawyers, contend that MTBE is an inherently defective product and that the oil industry knew or should have known about its hazards from the outset. Although several cases in California have settled, none has been decided by the courts.

The industry's main defense in the pending litigation is that it was required by the Clean Air Act ("CAA") to use oxygenates in RFG and that MTBE was the only practical option. This defense took a major blow from the Second Circuit as it rejected the argument in its examination of defendants' ability to remove cases filed by California and New Hampshire from state court to district court. The district court ruled that such removal was allowed, but the Second Circuit overturned that ruling. Additionally, for the numerous similar suits filed in state courts that have also been removed to federal court, the industry defendants can expect plaintiffs to pursue a remand to state court pursuant to this decision. This could result in divergent pre-trial rulings and an increased risk for high damage awards depending on the particular state's tort laws.

Removal to Federal Court was Improper

The key issue being determined by the Second Circuit was whether there was a proper basis for removal of the cases from state court. In making the determination, the court had to examine, among other issues, whether the industry defendants' acts in question were performed pursuant to a federal officer's orders or regulations. In other words, did the CAA direct the use of MTBE in gasoline. If the

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determination was yes, the CAA required the use of MTBE, then removal from state court could be authorized under the “federal officer removal statute.”

The Second Circuit reversed the district court’s holding that removal was proper under the federal officer removal statute. Under Supreme Court precedent, for a defendant to succeed under the federal officer removal statute, it must show that it was acting under federal direction to the extent that there was a causal connection between the alleged misconduct and the official authority. According to the Second Circuit, the district court erroneously reasoned that because the regulations under the CAA required the defendants to blend oxygenates into gasoline and because Congress and the EPA were deemed to be aware that defendants would likely use MTBE (instead of ethanol or other oxygenates) to comply with the CAA, the federal officer removal statute covered their conduct. The Second Circuit disagreed, noting that the EPA had identified six additives, other than MTBE, that would meet the regulations.

The Second Circuit also noted that the industry defendants had alleged in their filings for removal that Congress knew “industry would have to blend MTBE into at least some of the gasoline” in order to comply – an allegation that was only supported by references to congressional floor statements which provided little definitive insight into what Congress collectively anticipated would happen. In fact, the court found that the congressional floor statements demonstrated that industry made a determination to push for an oxygen requirement of 2.7 percent instead of the higher 3.1 percent. The higher requirement would have to be met through ethanol (MTBE alone could not meet the standard), while the 2.7 percent requirement could easily be met by the industry’s own product, MTBE. The court found that industry’s argument that ethanol capacity was insufficient is “a classic example of confusing the cart with the horse: ethanol supplies were low because the oil industry chose not to use it, not the other way around.”

The court vacated the order of the district court and remanded with directions to return these cases to the state forums from which they were removed.



Please feel free to contact the Sutherland attorney with whom you usually work or any of the attorneys listed below if you have any questions regarding this alert.

Gerald D. Higdon	713.470.6134	jerry.higdon@sablaw.com
Susan Grymes Lafferty	202.383.0168	susan.lafferty@sablaw.com
David P. Langlois	212.389.5007	david.langlois@sablaw.com
Gerald J. Pels	713.470.6135	gerry.pels@sablaw.com
Peter H. Rodgers	202.383.0883	peter.rodgers@sablaw.com
Paul B. Turner	713.470.6105	paul.turner@sablaw.com