OILFIELD MASTER SERVICE AGREEMENT FUNDAMENTALS

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WHAT IS A MASTER SERVICE AGREEMENT?

- It is an agreement between an oil and gas company (operator) and an oilfield service company, other than a drilling contract, that establishes the basic terms of their relationship applicable to all goods and services provided to the oil and gas company by the service company

WHY ARE MASTER SERVICE AGREEMENTS USED?

- Resolve up front all of the basic terms so that, when goods or services are needed, all that needs to be addressed are the project-specific terms
  - When and where
  - Goods/services specifications/scope of work
  - Price/budget
- Confirm everyone has insurance

WHY ARE MASTER SERVICE AGREEMENTS USED?

- Insurance companies are urging their insureds to enter into these
  - Think about and manage risk
  - Reduce litigation over allocation of liability
  - Confirm everyone has insurance
- Part of an E&P company's risk management strategy

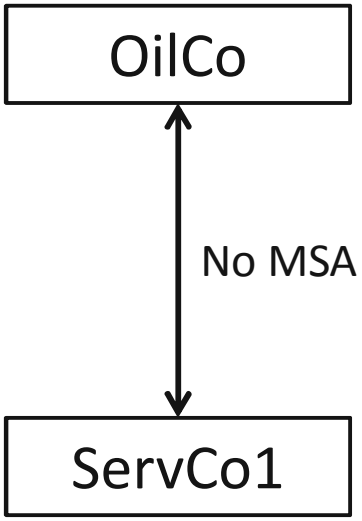
DEFINITIONS

- An indemnity agreement is an agreement by which one party agrees to pay another party if the latter experiences a loss
- Two basic indemnity structures in oilfield MSAs
  - Fault-based
  - Knock-for-knock (regardless of fault)

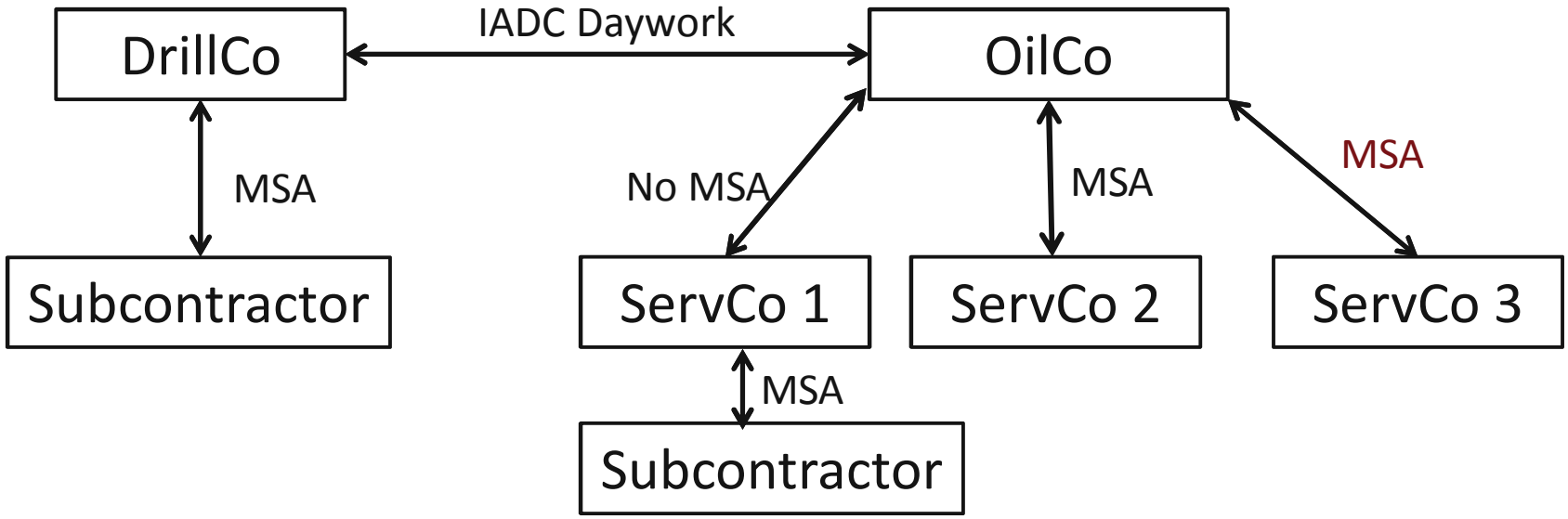
WHAT IF A MASTER SERVICE AGREEMENT ISN'T IN PLACE?

- The relationship is governed by tort law – generally a fault-based approach
  - In many instances, a fault-based indemnity structure is appropriate even for "oilfield" work.
  - Could be good. Could be bad. Depends on the facts.

HYPOTHETICAL



HYPOTHETICAL RECONSIDERED



WHAT IF A MASTER SERVICE AGREEMENT ISN'T IN PLACE?

- Far worse: the work is governed by the service company's basic "terms and conditions"
  - Often one-sided in favor of the service company
    - Onerous payment/collection terms
    - Broad warranty disclaimers
    - Lopsided indemnity obligations
      - Want to pay for a frac spread?
    - Waivers of rights by the operator

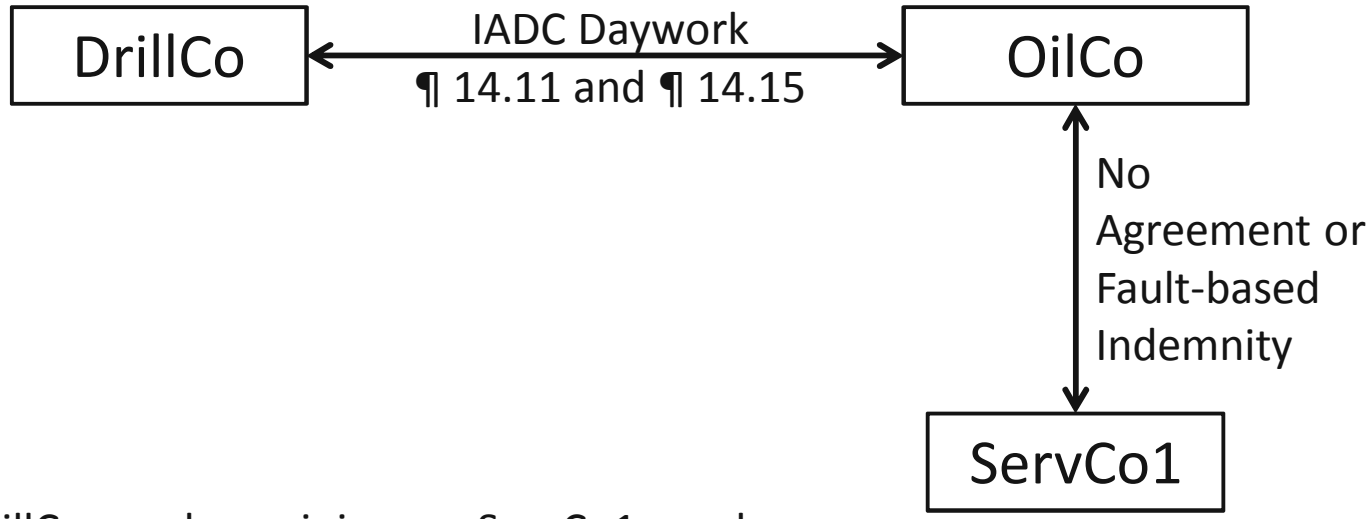
WHAT IF A MASTER SERVICE AGREEMENT ISN'T IN PLACE?

- Special Indemnity
  - **NOTWITHSTANDING ANYTHING TO THE CONTRARY HEREIN, CUSTOMER ASSUMES ALL LIABILITY FOR AND AGREES TO RELEASE, PROTECT, DEFEND, INDEMNIFY, AND HOLD CONTRACTOR GROUP AND ITS INSURERS HARMLESS FROM AND AGAINST ALL CLAIMS ARISING OUT OF OR IN CONNECTION HEREWITH FOR: (i) PROPERTY DAMAGE, PERSONAL INJURY OR DEATH OR LOSS THAT RESULTS FROM FIRE, EXPLOSION, BLOW-OUT, CRATERING, WILD WELL OR WORK PERFORMED TO CONTROL A WILD WELL. . .**
- Incidental or Consequential Damages
  - **IT IS EXPRESSLY AGREED THAT CONTRACTOR GROUP SHALL NOT BE LIABLE TO THE CUSTOMER GROUP FOR ANY PUNITIVE, INCIDENTAL, CONSEQUENTIAL, INDIRECT OR SPECIAL DAMAGES, INCLUDING, BUT NOT LIMITED TO, ANY LOSS OF PROFITS OR BUSINESS INTERRUPTION OR LOSS OF USE, LOSS OF PRODUCTION OR LOSS OF RIG TIME, REGARDLESS OF THE SOLE, JOINT CONCURRENT OR GROSS, ACTIVE OR PASSIVE, NEGLIGENCE OR OTHER FAULT OF CONTRACTOR GROUP.**

WHAT IF A MASTER SERVICE AGREEMENT ISN'T IN PLACE?

- A mess: incompatible indemnity structures

HYPOTHETICAL FURTHER RECONSIDERED



- DrillCo employee injures a ServCo1 employee
- Injured ServCo1 employee sues DrillCo
- DrillCo tenders the defense of the ServCo1 employee claim to OilCo
- OilCo gets stuck with the claim

FALSE COMFORT IN A "SMALL" PROJECT

- "It's only a one-well contract" or "It's only a $10,000 job"
  - That assumes the work is done properly and there are no accidents

BOTTOM LINE

- If you do not have master service agreements in place, there is a good chance you will be picking up risks you had not thought through
- It will likely be far more expensive to sort out liability

BOTTOM LINE (CONTINUED)

- Need to analyze the risks associated with work
  - Is it a common work site?
- Do not always assume that, just because the work is in the "oilfield," you should use a knock-for-knock structure

BASIC TERMS

- Scope
  - All goods and services
  - The MSA trumps work orders, service orders and purchase orders (the typical sources of the service company's standard T&C's)
  - Oral orders
    - Two schools of thought
  - Non-exclusive relationship
  - Prohibition on amendments

BASIC TERMS

- Payment terms
  - Right to challenge invoices/audit rights
  - Stale invoices
- Service company push-back
  - High interest rates on late payments
  - Be wary of credit applications
    - Short payment terms, broad collection rights

BASIC TERMS

- Warranties
  - Company specs; and free from defects in workmanship and material
  - Defective services and goods
  - Oil company remedies
  - Service company push-back
    - Short warranty periods
    - Limit dollar value of warranty work

BASIC TERMS

- Independent Contractor

Someone who is entrusted to undertake a specific project but who is left free to do the assigned work and to choose the method for accomplishing it… Unlike an employee, an independent contractor who commits a wrong while carrying out the work usually does not create liability for the one who did the hiring.

- BLACK'S LAW DICTIONARY (10th ed. 2014).

BASIC TERMS

- Compliance with company policies
  - Drugs, alcohol, and weapons
  - Environmental, health safety policies
  - Federal contracts
  - Radioactive sources
- Two schools of thought

BASIC TERMS

- Ethics (anti-kickback provisions)
- Insider trading (if the oil company is public)

BASIC TERMS

- Applicable law/venue
  - Service companies often push for Texas law and Harris County (Houston) venue

BASIC TERMS

- Attorneys' fees
  - Two schools of thought
  - Texas Civil Practice & Remedies Code, Section 38.001(8) allowing for the recovery of reasonable attorneys' fees in an action on an oral or written contract

BASIC TERMS

- Waiver of consequential damages
  - Two schools of thought

INDEMNIFICATION CLAUSES

DEAN MILLER

INDEMNIFICATION CLAUSES

- Goal: Allocate risk between contracting parties
- Often the most important provision in any contract
- There are many different types of indemnification clauses

KNOCK-FOR-KNOCK INDEMNITY

- Standard provision in oilfield MSAs involving operations in and on a well and the IADC daywork forms.
- Each party pays for illness, injuries, or deaths to “its” personnel and damage to or loss of its property regardless of fault.

KNOCK-FOR-KNOCK INDEMNITY

- Avoids disputes over loss allocation where multiple contractors are working at the same site.
  - No need to determine fault of each party.
  - Service companies typically want carve-outs for: (i) lost-in-hole equipment; (ii) catastrophic events; and (iii) rental equipment.

WHO IS INDEMNIFIED AND BY WHOM?

- Typical parties are Contractor and Company, but the respective indemnities protect each party's "Group."
  - "Contractor Group" shall mean Contractor, its affiliates, and their subcontractors of any tier, and their officers, directors, invitees, employees, agents, suppliers, vendors, successors, assigns, heirs and spouses.

WHO GETS INDEMNIFIED AND BY WHOM?

- Each party (i.e., Company and Contractor) indemnifies the other party's "Group."
- Groups do not indemnify.
  - Otherwise, officers, directors, suppliers, vendors, etc., are named as indemnitors.
  - Probably not enforceable because they are not parties to the MSA – but you don't want to fight about it.

WHO GETS INDEMNIFIED AND BY WHOM?

- If "Affiliate" includes a party's parent company, it is on the hook if a party's Group is the indemnitor.
  - Keep indemnity obligations as far down the corporate food chain as possible.
  - Parent guarantee can be negotiated separately if warranted.

KNOCK-FOR-KNOCK INDEMNITY

- CONTRACTOR shall defend, indemnify, release, and hold COMPANY Group harmless from and against all Claims arising out of or incidental to: (i) all injuries to, deaths, or illnesses of persons in CONTRACTOR Group; or (ii) all damages to or losses of any equipment, materials or other property of CONTRACTOR Group **EVEN IF CAUSED IN WHOLE OR IN PART BY THE NEGLIGENCE/FAULT OF ANY MEMBER OF COMPANY GROUP.**

KNOCK-FOR-KNOCK INDEMNITY

- Company shall defend, indemnify, release, and hold Contractor Group harmless from and against all Claims arising out of or incidental to: (i) all injuries to, deaths, or illnesses of persons in Company Group; or (ii) all damages to or losses of any equipment, materials or other property of Company Group EVEN IF CAUSED IN WHOLE OR IN PART BY THE NEGLIGENCE/FAULT OF ANY MEMBER OF CONTRACTOR GROUP.

OILFIELD ANTI-INDEMNITY STATUTES

- Several states have statutes providing that agreements relating to oil and gas operations in which one party is indemnified for its own negligence (e.g., knock-for-knock indemnities) violate public policy and are unenforceable
  - Texas
  - New Mexico
  - Wyoming
  - Louisiana

OILFIELD ANTI-INDEMNITY STATUTES

- Designed to (i) protect oilfield Contractors from bearing risk of Operator's negligence; and (ii) prevent the Operator from abdicating its responsibility for safety at a well site.
- Also protect Operators against Contractors' negligence.

TEXAS OILFIELD ANTI-INDEMNITY STATUTE

- Act applies to services that "bear a close nexus to a well and are directed toward the goal of obtaining or maintaining production from a well." *In re John E. Graham & Sons*, 210 F.3d 333, 343 (5th Cir. 2000).
- Does not apply to: (i) an agreement to repair an offshore drilling rig in a shipyard; (ii) an agreement requiring work to be performed inside the company's plant; and (iii) a terminal loading agreement between a trucking company and a petroleum refiner.

TEXAS OILFIELD ANTI-INDEMNITY STATUTE

- The Act allows:
  - Knock-for-knock indemnities that are mutual and supported with insurance
  - Unilateral indemnities up to $500,000

NEW MEXICO OILFIELD ANTI-INDEMNITY STATUTE

- New Mexico's statute applies only to "activities at the well head," such as drilling, deepening, reworking, repairing, improving, testing, treating, perforating, acidizing, logging, conditioning, altering, plugging or otherwise rendering services in connection with drilling an oil or gas well "or an act collateral thereto."
- Even acts "collateral thereto" must be related to activities at the well head. *Holguin v. Fulco Oil Servs., Inc.,* 245 P.3d 42, 48 (N.M. App. 2010).

WYOMING OILFIELD ANTI-INDEMNITY STATUTE

- Wyoming's statute covers "only those services closely related to well drilling. Not covered are services or activities having a remote or indirect connection to the kinds of services" enumerated in the Act. *Reliance Ins. Co. v. Chevron U.S.A. Inc.*, 713 P.2d 766, 770 (Wyo. 1986).

WYOMING OILFIELD ANTI-INDEMNITY STATUTE

- Knock-for-knock indemnities still common in Wyoming and New Mexico.
  - Parties may decide to honor them.
  - Large claim may cause one party (or its insurer) to challenge validity of indemnification provision in court.

LOUISIANA OILFIELD ANTI-INDEMNITY STATUTE

- Act applies to an agreement that: "(1) pertains to a well and (2) is related to exploration, development, production, or transportation of oil, gas, or water . . . ." *Transcontinental Gas Pipeline Corp. v. Transp. Ins. Co.*, 953 F.2d 985, 991 (5th Cir. 1992).

OILFIELD ANTI-INDEMNITY STATUTES

- Take away: All of these statutes apply only to operations closely related to drilling.
- Therefore, knock-for-knock indemnities remain viable for other service contractors in the oil patch.

OTHER ANTI-INDEMNITY STATUTES

- Anti-indemnity statutes applicable to construction and transportation industries may apply to oil and gas operations in some circumstances.
- Scope and effect of these statutes vary.

COLORADO CONSTRUCTION ANTI-INDEMNITY STATUTE

- Applies to "any provision in a construction agreement that requires a person to indemnify . . . another person against liability for damage arising out of death or bodily injury to persons or damage to property caused by the negligence or fault of the indemnitee" C.R.S. § 13-21-111.5 (2007)

COLORADO CONSTRUCTION ANTI-INDEMNITY STATUTE

- "Construction agreement" means a contract . . . for materials or labor for the construction, . . . repair, maintenance, design, planning, . . . inspection, testing, or observation of any . . . ***structure, . . . gas or other distribution system, or other work dealing with construction*** . . . .

COLORADO MOTOR CARRIER ANTI-INDEMNITY STATUTE

- Any provision of a transportation contract that "purports to indemnify . . . the indemnitee from or against any liability for loss or damage resulting from its own negligence or intentional acts or omissions [is] contrary to public policy and is therefore void." C.R.S. § 42-7-505.5 (2014)

COLORADO MOTOR CARRIER ANTI-INDEMNITY STATUTE C.R.S. § 42-7-103(16)(a)

- "Transportation contract" means a contract . . . between a motor carrier and another party regarding:
- (I) The transportation of property by motor vehicle for compensation or hire;
- (II) Entrance on property for the purpose of loading, unloading, or transporting property by motor vehicle for compensation or hire; or
- (III) Access or services incidental or related to an activity described in subparagraph (I) or (II).

DRAFTING AROUND ANTI-INDEMNITY STATUTES

- How do you craft an indemnification clause that may be applicable in multiple states, some of which have anti-indemnity statutes?
- Tiered or sliding-scale indemnity.

TIERED OR SLIDING-SCALE INDEMNITY

- First: Knock-for-knock indemnity
- Second: If first clause is not enforceable under applicable law, carve out claims arising from: (i) the gross negligence or willful misconduct of Company Group; (ii) the sole negligence of Company Group.
- Third: If second clause is unenforceable, include equitable allocation provision: allocate Claims/damages “to the extent caused” by the negligence of each party.

DUTY TO DEFEND

- The duty to defend is important
  - Defense costs can exceed cost to indemnify
  - Duty to defend can apply even for frivolous or otherwise unsuccessful claims
    - Similar to insurance policies

DUTY TO DEFEND

- If only duty to indemnify is specified, depending on which states law applies:
  - Duty to indemnify includes duty to defend.
  - Duty to indemnify includes duty to defend, but only if indemnitor's duty to indemnify is established.
    - No duty if no liability.
  - Duty to indemnify does not include duty to defend.

DUTY TO DEFEND

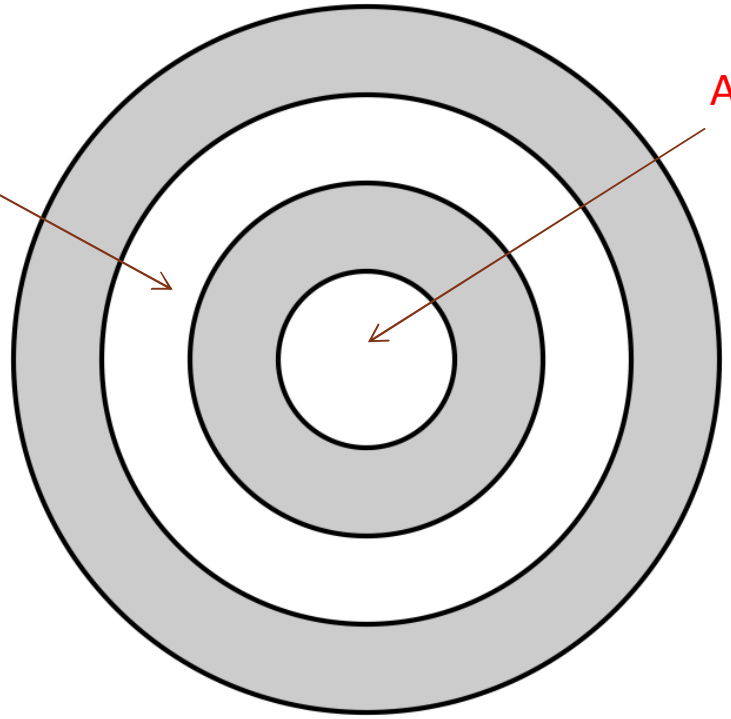
- Typical duty to defend language: “defend, indemnify, and hold harmless”
  - If the contract does not address duty to defend, significant costs can remain unallocated

INDEMNIFICATION AWAY FROM THE WELL

- If a knock-for-knock indemnity structure is imported into contracts for services away from the well, the Operator likely will assume more risk than is necessary.

INDEMNIFICATION AWAY FROM THE WELL

Away from the well.
Fault-based indemnity available.



At or in the well.
Knock-for-knock indemnities.
Anti-indemnity statutes apply.

INDEMNIFICATION AWAY FROM THE WELL

- The policies underlying the knock-for-knock indemnity do not apply to many oilfield services away from the well.
  - Contractor typically on location by itself or only with its subcontractors.

INDEMNIFICATION AWAY FROM THE WELL

- What type of indemnification clause is included depends on:
  - Relative strength of the parties' negotiating positions
  - Standards of commercial reasonableness in contractor's specific industry
    - Transportation, environmental consulting, spill response, laboratory services, etc.

WHAT IS COMMERCIALLY REASONABLE?

- It depends on the industry-specific risks, industry standards, and the geographic area.
  - E.g., environmental consulting and drilling present very different risks and have different industry standards.

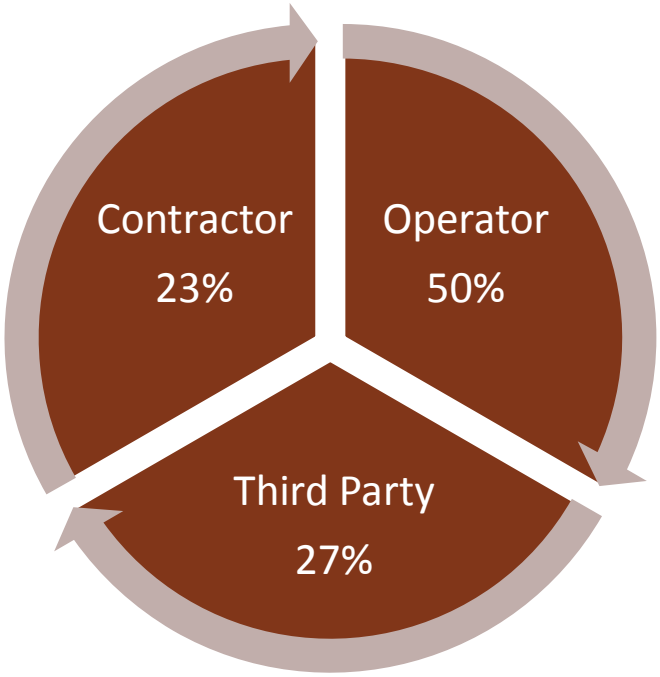
TYPES OF INDEMNIFICATION CLAUSES

- Many options are available
  - Knock-for-knock for injury, death, or illness of personnel?
    - Not for property damage or loss.
  - Each party indemnifies the other for its own proportionate share of fault.
    - The orphan share for insolvent jointly liable parties is not allocated by the contract.

TYPES OF INDEMNIFICATION CLAUSES

- Modified Limited Form Indemnity
  - Operator's liability always is limited to its proportionate share of fault.
  - Contractor liability excludes Operator's proportionate share of fault.
    - Contractor picks up liability for insolvent jointly liable third parties.

TYPES OF INDEMNIFICATION CLAUSES



TYPES OF INDEMNIFICATION CLAUSES

- How do you decide?
- Who has the leverage?

TYPES OF INDEMNIFICATION CLAUSES

- Don’t overlook strict liability.
- The most onerous environmental statutes are not negligence based.
  - CERCLA, Clean Water Act, etc.

CONTRACTORS' STANDARD TERMS AND CONDITIONS

- Be afraid, be very afraid!
- These typically contain very one-sided provisions, such as damages caps and liability-shifting provisions.
  - Hidden provisions can undercut indemnification and other provisions.

CONTRACTORS' STANDARD TERMS AND CONDITIONS

- In the MSA context, these typically are attached to proposals for specific projects.
- Make sure MSA trumps any such terms and conditions.

CONTRACTORS' STANDARD TERMS AND CONDITIONS

- Subtle variations in non-reciprocal indemnity provisions can be critical.
  - Operator indemnifies contractor for ***any actions or omissions*** or willful or reckless misconduct of the Company.
  - Contractor indemnifies Company for or any ***grossly negligent actions or omissions or willful or reckless misconduct*** of Contractor.

CAPS ON DAMAGES

- Many contractors' standard terms and conditions typically limit contractor damages to certain amount (e.g., $25,000) or cost of services set in project-specific work release/work order.
- Shifts risk of significant damages away from contractor to operator.
  - Operator essentially becomes contractor's excess insurance carrier.
- Basic Message: if we are a little negligent, we pay for it; if we are really negligent, you pay for it.

6. **LIMITATION OF LIABILITY**. CLIENT AND CONSULTANT HAVE EVALUATED THE RISKS AND REWARDS ASSOCIATED WITH THIS PROJECT, INCLUDING CONSULTANT'S FEE RELATIVE TO THE RISKS ASSUMED, AND AGREE TO ALLOCATE CERTAIN OF THE RISKS SO, TO THE FULLEST EXTENT PERMITTED BY LAW, THE TOTAL AGGREGATE LIABILITY OF CONSULTANT (AND ITS RELATED CORPORATIONS AND EMPLOYEES) TO CLIENT AND THIRD PARTIES GRANTED RELIANCE IS LIMITED TO THE GREATER OF $10,000 OR ITS FEEFOR ANY AND ALL INJURIES, DAMAGES, CLAIMS, LOSSES, OR EXPENSES (INCLUDING ATTORNEY AND EXPERT FEES) ARISING OUT OF CONSULTANT'S SERVICES OR THIS AGREEMENT REGARDLESS OF CAUSE(S) OR THE THEORY OF LIABILITY, INCLUDING NEGLIGENCE, INDEMNITY, OR OTHER RECOVERY. THIS LIMITATION SHALL NOT APPLY TO THE EXTENT THE DAMAGE IS PAID UNDER CONSULTANT'S COMMERCIAL GENERAL LIABILITY POLICY.

7. **Indemnity/Statute of Limitations.** Consultant and Client shall defend, indemnify, and hold harmless the other, their agents, and employees, from and against legal liability for all claims, losses, damages, and expenses to the extent such claims, losses, damages, or expenses are caused by their negligent acts, errors, or omissions. In the event such claims, losses, damages, or expenses are caused by the joint or concurrent negligence of Consultant and Client, they shall be borne by each party in proportion to its own negligence under comparative fault principles. Causes of action arising out of Consultant's services or this Agreement regardless of cause(s) or the theory of liability, including negligence, indemnity or other recovery shall be deemed to have accrued and the applicable statute of limitations shall commence to run not later than the date of Consultant's substantial completion of services on the project.

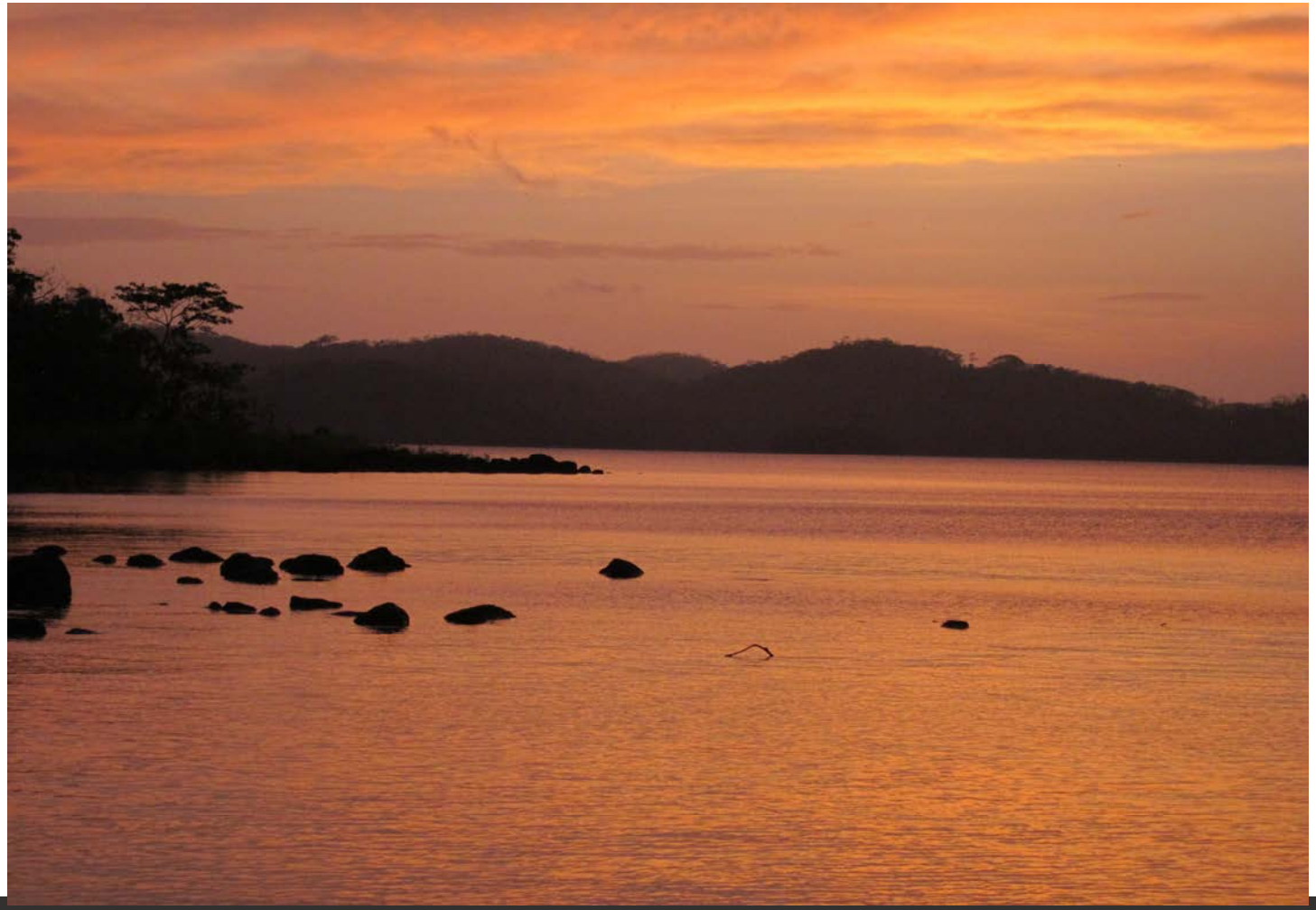
13. Testing and Observations. Client understands that testing and observation are discrete sampling procedures, and that such procedures indicate conditions only at the depths, locations, and times the procedures were performed. Consultant will provide test results and opinions based on tests and field observations only for the work tested. Client understands that testing and observation are not continuous or exhaustive, and are conducted to reduce - not eliminate - project risk. Client agrees to the level or amount of testing performed and the associated risk. Client is responsible (even if delegated to contractor) for notifying and scheduling Consultant so Consultant can perform these Services. Consultant shall not be responsible for the quality and completeness of contractor's work or their adherence to the project documents, and Consultant's performance of testing and observation services shall not relieve contractor in any way from its responsibility for defects discovered in its work, or create a warranty or guarantee. Consultant will not supervise or direct the work performed by contractor or its subcontractors and is not responsible for their means and methods.

15. Ownership of Documents. Work product, such as reports, logs, data, notes, or calculations, prepared by Consultant shall remain Consultant's property. Proprietary concepts, systems, and ideas developed during performance of the Services shall remain the sole property of Consultant. Files shall be maintained in general accordance with Consultant's document retention policies and practices.

17. Site Access and Safety. Client shall secure all necessary site related approvals, permits, licenses, and consents necessary to commence and complete the Services and will execute any necessary site access agreement. Consultant will be responsible for supervision and site safety measures for its own employees, but shall not be responsible for the supervision or health and safety precautions for any other parties, including Client, Client's contractors, subcontractors, or other parties present at the site.

LIABILITY-SHIFTING PROVISIONS

- May be called "Catastrophic Losses," "Special Events," or something else.
  - May apply to injury, death, blowout, fire, explosion, loss of well control, damage to third-party property.
  - Shifts liability back to Operator despite knock-for-knock indemnity.



INSURANCE

DAMIAN ARGUELLO

INSURANCE PROVISIONS IN MSA

- Purpose – back MSA indemnity obligations
- Contract language should coordinate with insurance policy language
  - If it doesn't, could create unsecured indemnity
  - Additional insured endorsement naming company or operator "group" on service company's policies provides best protection

INDEMNITY V. INSURANCE PROVISIONS

- Insurance provisions should be separate
  - Completely separate section, not part of indemnity or other sections
  - Specify indemnity not capped by insurance
- Two purposes for insurance provisions
  - Specify coverage parties should have for themselves
  - Provide coverage for service company's indemnity obligations

CONTRACTUAL INSURANCE REQUIREMENTS

- Insurance requirements should:
  - Be clear
  - Use current terminology
  - Reflect insurance industry practices

PUBLIC LIABILITY INSURANCE

COMPREHENSIVE GENERAL LIABILITY

OUTDATED LANGUAGE

- Other Examples
  - Broad form property damage
  - Contractual liability insurance
  - Combined single limit
- Current terminology is “commercial general liability”
  - Automatically incorporates broad form property damage, other coverages previously added through separate endorsements

CONTRACTUAL INSURANCE REQUIREMENTS

- Team approach to contract language & coverage:
  - Attorney
  - Risk manager
  - Broker
  - Others, e.g., CFO
- Customize to project
  - Mom & pop v. large service company
  - Commercially reasonable

CONTRACTUAL INSURANCE REQUIREMENTS

- Who and what is covered?
  - Named insured – the party who bought the policy
  - Party's own risk (make sure they can withstand loss and fulfill their contractual duties)
  - Additional insureds – how broad, e.g., "Company Group"
- How much insurance?
  - Appropriate limits, not too high or low, business judgment
  - Combination of primary and excess/umbrella
    - Multiple layers/tiers for larger exposures

COMMERCIAL GENERAL LIABILITY

- An important coverage
- "Standard" Insurance Services Office (ISO) form
- Contractual liability exclusion
  - "Insured contract" exception
  - Tort liability of another

ISSUES – GENERAL LIABILITY

- Non-ISO, proprietary forms
- Primary & Non-Contributory
  - Unclear – better language: "Service company's insurance shall be primary to, and shall not seek contribution from, any other insurance available to operator"
- Requiring precise limits of CGL and umbrella, rather than a general amount collectively

INSURED CONTRACT V. ADDITIONAL INSURED

- "Insured contract"
  - Pay indemnitee's defense costs as damages
    - Erode the limit
  - May have to share defense counsel with named insured
  - No direct contractual relationship with insurer
  - Defense costs could be in addition to limits if numerous conditions met

INSURED CONTRACT V. ADDITIONAL INSURED

- Additional insured status = direct contractual relationship between the insurer and the additional insured
- Defense usually in addition to limits
- Separation of insureds clause – policy applies to each insured separately
- Insurer owes duties to additional insured, including good faith

ENDORSEMENTS V. CERTIFICATES OF INSURANCE

- Endorsements are part of an insurance policy
  - Modify the coverage
- Certificates do not create coverage or legal obligation between insurer and certificate holder
  - “Snapshot” representation by agent/broker
  - Insurers do not usually see certificates
  - Don’t account for paid claims

EVOLUTION OF ADDITIONAL INSURED COVERAGE

- 1985 – Gold standard – "liability arising out of" named insured's work
  - "But for" causation standard, courts interpret broadly
  - Still required in many contracts, but hard to get
- Gradual evolution narrowed coverage
  - Coverage provided only "to the extent permitted by law"
    - Relates to anti-indemnity statutes
  - Coverage "will not be broader than which you are required by the contract or agreement to provide"
    - Expressly ties additional insured coverage to contractual requirements
  - Limits are lesser of contract requirement or policy declarations
    - Creates possibility of coverage gap if full primary limits not actually paid

EVOLUTION OF ADDITIONAL INSURED COVERAGE

- Some good news
  - Blanket additional insured form provides coverage to parties the named insured is required to name as additional insured, even if no contractual privity
    - Limited to vicarious liability of named insured
  - Optional "primary and noncontributory" endorsement when agreed to by named insured in writing
    - Still some issues with excess policies' other insurance provisions, which can require exhaustion of operator's primary policy first

SCOPE OF ADDITIONAL INSURED COVERAGE

- Temporal
  - Named insured's "ongoing operations"
- Drafting options
  - Request completed operations coverage
  - Define service company's operations broadly to bolster "ongoing" argument

SCOPE OF ADDITIONAL INSURED COVERAGE

- Monetary
  - Lesser of contract requirement or policy limit
- Drafting options
  - Specify limits of "not less than $X"
  - Specify aggregate dollar amount of primary & umbrella to be satisfied as service company chooses
    - Could create issues with defense as transition to excess occurs, particularly if primary limits are low

SCOPE OF ADDITIONAL INSURED COVERAGE

- Degree of liability
  - Limited to vicarious liability for named insured's conduct, or includes additional insured's sole or concurrent negligence?
- Drafting options
  - Specify that additional insured coverage be "at least as broad as" named insured's coverage under its policies
  - Permissible under anti-indemnity statutes?

SCOPE OF ADDITIONAL INSURED COVERAGE

- Contractual privity
  - Many contracts require named insured to name strangers as additional insured on policies, e.g., affiliated parties, officers, Company Group, etc.
  - Can be problem – certain additional insured forms limit coverage to party for whom named insured performs work
- Drafting options
  - Specify use of new forms, or issuance of separate additional insured endorsements for each required party

AI STATUS GONE WRONG

- Recent cases show insurers seek to narrow additional insured coverage
  - Limited to indemnity obligations in contract
  - Limited to named insured's liability
- Need to carefully coordinate indemnity and insurance provisions to ensure they work as intended when loss occurs

MIRAMAR PETROLEUM V. FIRST LIBERTY, 2015 WL 7301096 (S.D. TEX. NOV. 18, 2015)

- Daywork contract between Miramar (operator) and Nicklos (driller)
  - Nicklos to maintain insurance covering "the liabilities specifically assumed by [Nicklos]"
  - "[Miramar] and [Nicklos] shall cause their respective underwriters to name the other additionally insured but only to the extend [sic] of the indemnification obligations assumed herein."
- Blowout – Miramar sued, Nicklos counterclaimed for loss of drill string equipment and negligence for the loss of Nicklos' equipment

MIRAMAR PETROLEUM

- In contract, Nicklos assumed liability and agreed to indemnify Miramar for:
  - Nicklos' own surface equipment
  - Claims arising in favor of Nicklos' own employees, subcontractors, and invitees, and
  - Pollution originating above the surface from sources wholly within Nicklos' possession and control and associated with Nicklos' own equipment
- Claim did not involve these categories; no AI status

ADDITIONAL CONSIDERATIONS

- Specify strength/size of service company's carrier – solvency
- Build in verification methods, loss reporting, cancellation notices
  - Remember, insurers don't usually see certificates
- Get copies of endorsements and declarations pages
- Consider assignment and succession as changes occur
- Consider choice of law – policies not necessarily governed by same law as MSAs – separate choice of law analysis

INSURANCE TAKEAWAYS

- Insurance contracts are worth millions – need counsel and good brokers involved
- Take time to draft appropriate contract provisions, coordinate with policy language
- Don’t count on certificates – build in thorough verification process, repeat at renewal

CONTACT INFORMATION

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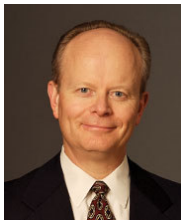

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