The ties that bind: Liabilities, Indemnities and Warranties after Macondo

The blowout at the Deepwater Horizon rig in the Gulf of Mexico has changed the face of the oil and gas industry forever, as did the ensuing battle between BP and its contractors.

In this post-Macondo world, companies have refocused their efforts on contract management, not least because of the cost the incident accrued. Tim Haïdar from Oil & Gas IQ said the economic loss for insurers from the Gulf of Mexico amounts to between $20 to 30 billion (£12.3 billion).

Aside from the fallout from the Gulf of Mexico leak, political unrest within the oil-rich MENA region has also served to highlight the importance of good contract management as companies expand into more politically and physically challenging locations.

Risk

"With diminishing investment in the sector and those kind of losses fresh in the mind, it has become more essential than ever that oil and gas firms entering into contracts are optimally insulated against risk through proficient risk management and risk allocation," Haïdar said.

As the oil industry looks to drill in more challenging environments, like the projects currently getting underway in the Arctic, the lessons learnt from the Macondo incident will take on even greater levels of importance.

These contractual changes come on top of the new regulations which the industry is now faced with, which are likely to mean greater sums need to be set aside to deal with a spill or leak occurring.

In the UK, for example, the Department of Energy and Climate Change sent out letters to members of the industry in late 2010 asking for confirmation that they had "sufficient finance or insurance/indemnity provision" in the event that relief wells needed to be drilled.

Across the pond in the United States, there is debate as to whether the liability limit should be lifted, which has been met with understandable concern from members of the industry.

Speaking to Drilling Contractor late last year, Brian Petty, executive director of government affairs at the International Association of Drilling Contractors (IADC), said: "Lifting the cap on liability for offshore spills would mean that independents, who represent the majority of companies drilling in the Gulf of Mexico, would not be able to continue… You can't insure against something like that."

Changes to the Contract Process

Legal experts working in the oil and gas field have also reported they have seen changes in the contract negotiations taking place.
Dr Lee Hunt, president of the IADC, told an audience at the IADC World Drilling 2011 Conference & Exhibition that he has seen little change within the force majeure provisions within contracts, however, he did note new considerations were being taken into account, including the period of time before termination right is triggered, the Wellsite Data Solutions blog reported.

Furthermore, commentary from legal firm Barlow Lyde and Gilbert, noted "the 'no gain, no loss' principle has however come under renewed pressure" post Macondo. Humphrey Douglas, Maurice Kenton and Wei Wu said the situation which arose with Anadarko and Mitsu with regard to the Deepwater Horizon costs demonstrates the fact that "contractual remedies are an imperfect risk transfer mechanism" when liabilities are on a scale of those from the Gulf of Mexico.

“We are also starting to see reallocation of certain risks under joint operating agreements and beyond, more time spent negotiating indemnities and liabilities (particularly in relation to negligence and nuisance claims), and we expect that there will be even fewer instances of commercial arrangements being left undocumented,” the legal experts noted.

Transocean has only released its internal report into the incident this month and the dust surrounding the incident has really only just began to settle.

In the longer term, it would seem experts believe companies will be looking to use the contract process to cover their backs more than ever before, making it essential for those in the industry to keep up with all the latest developments.