The enforceability of indemnity clauses for oil pollution liability in offshore petroleum contracts

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1 Introduction

1.1 Introductory Remarks

One of the main functions of a commercial contract has always been to allocate risk. This is true of contracts used in almost any industry or commercial enterprise. The oil and gas industry however, presents a unique set of potential liabilities, which makes the allocation of risk of even greater importance. This is especially the case in complex deepwater drilling projects.

Arguably the most serious risk that companies in the oil industry expose themselves to is responsibility for a major oil spill. The problem though, is that the companies do not only expose themselves to the consequences of an oil spill. The blowout from a subsea oil well can have devastating consequences for the environment, the livelihoods of people in coastal areas and countless other third parties. This has never been more evident than it was in the aftermath of the 2010 Deepwater Horizon disaster in the Gulf of Mexico.

The Deepwater Horizon disaster resulted in the largest ‘accidental’ oil spill by volume in history and the second largest oil spill overall. This one incident, not only devastated marine environments and the livelihoods of thousands, it also threatened the very existence of BP, one of the richest corporations in the world. The extent of the financial consequences for BP is still far from known. Courts in the United States are currently establishing who will be held to account for the disaster and who will be made to pay compensation and civil fines. Will it be BP or one of its many contractors? This thesis will outline how the American courts will reach this conclusion and also how courts in the United Kingdom and Norway would reach a conclusion if presented with the same scenario.

1.2 Scope of Investigation

This thesis will analyse and compare the regulation of indemnity clauses, used in standard form petroleum service contracts; in the United States, United Kingdom and Norway. The investigation will focus on the domestic legislation and legal principles of each jurisdiction to establish how the
courts assess the enforceability and validity of indemnity clauses. The focus will be on oil pollution liability rather than liability for personal injury and property damage etc. Liability for oil pollution has been one of the main battlegrounds between BP and its contractors in the aftermath of the Deepwater Horizon disaster. Limiting the focus to this class of liability will provide a basis for consistent comparison of the various jurisdictions and will address the main type of risk that makes the petroleum industry stand out from other industry sectors.

The scope of this thesis will be limited to an investigation into the contractual relationship between BP and its main drilling contractor, Transocean. Although there were many other contractors involved in the project it is sufficient for the purposes of this investigation to focus on one.

One of the main legal concepts that will be considered in the context of all three jurisdictions is the freedom of contract. An attempt will be made to establish the extent to which the legislature and courts in each jurisdiction can intervene in contractual agreements between commercial entities. The pros and cons of indemnity provisions will be weighed against the public policy concerns of oil pollution, and finally an attempt will be made to highlight the potential effects that the Deepwater Horizon disaster might have on the status quo in the industry.

1.3 Sources of Law

The main focus of the investigation into the legal approach taken in the United States will be the Deepwater Horizon disaster. Provisions from the drilling contract entered into between BP and Transocean will be used as an example of a standard indemnity regime and the ongoing legal dispute between the two companies will be analysed to determine what principles regulate the enforceability of indemnity clauses for oil pollution liability under United States law. Other legal principles and doctrines will be drawn from Texas and Louisiana state law.

The main legal source in the investigation into the legal approach taken in the United Kingdom will be case law, with particular focus on the litigation that followed the 1988 Piper Alpha disaster. Legal principles and doctrines will be drawn from other cases to gain a deeper understanding of the legal principles that regulate the enforceability of indemnity clauses for oil pollution liability in the United Kingdom.
The main legal source of the investigation into the legal approach taken in Norway will be domestic legislation and legal principles drawn from case law. Although some Norwegian case law will be analysed, it will be more limited than the consideration of case law in the United States and United Kingdom. This difference in approach is mainly down to the fact that Norway is home to a civil law system where the sources of legal authority are classified differently than they are in the Anglo-American common law systems.

1.4 Method

This thesis will not only use the Deepwater Horizon as a case study in the investigation into the United States legal approach to indemnity clauses for oil pollution liability; it will transpose the scenario and surrounding circumstances into the legal jurisdictions of the United Kingdom and Norway. For the purpose of this thesis, three main examples of indemnity clauses will be used; all taken from standard form petroleum contracts in each jurisdiction.

The general legal principles and legislation of the United Kingdom and Norway will be analysed before applying the facts and contractual terms of the Deepwater Horizon incident to speculate on the likely outcomes, had an identical scenario been governed by English or Norwegian law. Applying English and Norwegian law to the same scenario that has been considered by courts in the United States will allow for a closer comparison to be drawn between the approaches taken in the different legal jurisdictions.

2 The need for risk allocation in the offshore petroleum industry

2.1 The Balance of Risk v. Reward
It has been said recently that; “[these] days contractors not only have to compete on price and product, but also on their willingness to accept risk.”\(^1\) By outlining the types of risk accepted by contractors in the oil and gas industry and the consequences such an acceptance may have, this section will present the main reasons why there is a need for risk allocation in the industry.

On 22 April 2010 the drilling rig Deepwater Horizon exploded in a ball of flames, killing eleven rig workers and resulting in the spill of an estimated 4.9 million barrels of oil.\(^2\) In the immediate aftermath BP, the owner and operator of the ill-fated Macondo oil well, was vilified by politicians and the media. Its stock price was halved and because of what happened on its watch, drilling in the Gulf of Mexico was temporarily banned.\(^3\) It has become clear in the time since the disaster that BP does not accept full responsibility for the incident. This thesis will show how, through the use of an indemnification agreement, BP hopes to share this responsibility.

In the United States alone, oil producers spent USD 123 billion on capital investment and exploration during 2009. The day rate paid by BP for the hire of Deepwater Horizon was USD 502,000. The rig itself was insured for USD 560 million.\(^4\) These figures are typical of the oil and gas industry and are quoted to provide context. It is easier to comprehend the magnitude of risk present in the offshore petroleum industry when one is aware of the investments that are on the line.

It is pertinent at this point to note the relative size of the companies involved in the Macondo project. This will serve to illustrate one of the main reasons why contractual risk allocation is required in the industry. As of 25 October 2012 the market capitalization of BP was USD 132 billion, while Transocean’s market cap was USD 17 billion. This significant difference in market value goes to the very core of the need for risk allocation in the petroleum industry. Contractors and operators are not on a level financial playing field and do not possess the same ability to pay for the consequences when, on rare occasion, disaster does strike.

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1 Bjørnstad (2012)
2 Polson (2011)
3 Moratorium lifted 12 October 2010
4 Kollewé (2010)
The market cap figures support an argument that says risk needs to be placed with the party whom can best manage it. They are also indicative of the reason why a balance must be found between potential risk and potential reward for the companies involved. For a long time after the Macondo blowout, BP’s survival hung in the balance, not to mention Transocean, if it was to be made financially responsible. So why would any company commit to explore and develop offshore oil and gas fields with these risks? If participation in one individual contract threatens the very existence of companies when disaster strikes, the industry would not function. Risk allocation is necessary in the oil and gas industry to ensure the production levels remain where they can meet the energy demands of society. At the same time, incidents like the Deepwater Horizon disaster also show how society is at the mercy of a small group of oil companies such as BP when things go wrong.

There is no doubt that production of oil from the Macondo well left BP with a much greater potential for profit when compared to Transocean; for the simple reason that BP’s profit is derived from production that could last for decades, while Transocean’s income is fixed by a multiple of the rig’s day rate. It does not seem entirely unreasonable therefore to say that the risk borne by BP should be higher also. Having said this however, in the case of the Deepwater Horizon, had a risk allocation regime not existed, Transocean could have been exposed to tens of billions of dollars in losses. If this were the norm, contractors such as Transocean would effectively be betting the company every time they performed work. BP on the other hand, a company with a much higher market cap and a stronger balance sheet, who are in a better position to pay for damages and also in a position where they have much more to gain, is left relatively unscathed. This imbalance portrays the situation that companies in the petroleum industry attempt to avoid when contracting with each other.

If contractors, who because of their business models always have smaller market caps than the so-called “supermajors,” are forced to gamble their company every time they enter into a service contract, they would not take on the jobs and the petroleum industry would be in stalemate. This is not the reality today however and is largely down to the existence of contractual mechanisms that maintain the balance of risk and reward.

5 The biggest oil companies by revenue (ExxonMobil, Shell etc.)
Insurance is also an important consideration when evaluating the reasons for risk allocation in the petroleum industry. A comprehensive indemnification regime ensures that each party involved in a project does not need to take out individual insurance policies for the same worst-case scenarios. Overlapping insurance for oil spill pollution would be too expensive for most contractors to obtain, and if all companies were required to purchase such insurance, project costs would be unsustainable. The costs would ultimately be passed on to the consumers and would result in a state of affairs that would not benefit anyone.

At the same time as risk and financial exposure must be balanced; incentive must remain for companies involved in offshore drilling projects to operate safely. This addresses a question of public policy. There is no doubt that society must be protected from the devastating consequences of an oil spill like the one caused by the Macondo blowout. This protection can only be ensured when companies are discouraged from taking unacceptable risks. This discouragement is characterised by the threat of penalty fines. Such fines will be discussed in greater detail below.

The Deepwater Horizon disaster has thrown the system for the allocation of liability into the spotlight and as a result, risk allocation models used in the industry are under scrutiny by the public, legislators and the judiciary. There have already been calls for changes to the way oil companies and contractors are allowed to deal with each other. This thesis will evaluate the powers of intervention possessed by courts, regulators and governments to determine the extent to which they can intervene in the closed contractual relationships between oil companies and contractors.

### 2.2 Potential Sources of Liability

The Deepwater Horizon disaster is an example of the worst-case scenario that companies in the oil industry fear most. The incident also highlights the types of risk that exist and the full range of consequences that could flow from such a devastating event.

The main sources of potential liability for companies in the offshore petroleum industry include negligence for property damage, personal injury and also breaches of contract. These types of liability tend to be covered by so-called “knock-for-knock” regimes however, where each party agrees
to bear the costs for damage to their own property. In the interest of providing a fuller picture of risk allocation, the “knock-for-knock” regime will be explained in Section 3.1.2 below.

The focus of this thesis is oil pollution liability, a type of risk with extreme consequences of a magnitude that is unique to the oil and gas industry. Liability for oil pollution could include clean-up costs as well as economic damages and payment of compensation. Governments also sometimes impose civil penalties on the responsible parties.

The Deepwater Horizon disaster shows how one incident alone can expose companies and contractors to the full range of liabilities mentioned above. Financial liabilities arising out of oil spills are highly unpredictable at best and sometimes even unlimited. This thesis will assess the risk allocation regimes used by companies in an attempt to make oil pollution liabilities somewhat more predictable.

3 How is risk allocated in the petroleum industry?

3.1 Types of Risk Allocation

Terms and phrases such as; exclusion of liability, release from liability, hold-harmless and indemnity, are used synonymously when discussing risk allocation regimes in petroleum contracts. Although the main focus of this thesis will be a specific type of risk allocation provision, known as an indemnity clause, it is also worth highlighting the “knock-for-knock” regime in the interest of providing a broader perspective on the practice. In this section key terms will be defined, and the use of indemnity and “knock-for-knock” clauses will be described in general terms.

3.1.1 Indemnity clauses

‘Indemnity’ is a term with multiple applications, not just in a contractual context. In its most basic form an indemnity is a type of insurance. It has been defined as “[a] duty to make good any loss,
damage or liability incurred by another,” or “the right of an injured party to claim reimbursement for its loss, damage or liability from a person who has such duty.”

Having provided a general definition for the concept of indemnity, it must be added that the exact content of an indemnity clause cannot be defined, nor can an exact formula for the construction of such a clause be provided. The form of an indemnity clause very much depends on its purpose and the context in which it appears. In many cases indemnity clauses will not be labelled as such. The existence of an indemnity clause is usually determined by its function, and as noted above; indemnification is the central function of an indemnity clause.

It is very important to understand indemnity clauses in the context of the oil and gas industry, where high risk is concentrated in capital-intensive environments. Indemnity clauses are used in the industry specifically for transferring and re-assigning liability and will usually appear as a mutual promises. The provisions have been described as a; “Private mode of re-allocation of risk and liabilities” that are used to replace the traditional fault-based liability found in common law tort. They do this by allowing parties to contractually discard the traditional consideration of fault that places liability with the tortfeasor. These contractual allocations are traditionally upheld by the principle of freedom of contract. It will become clear that this principle is the starting point in the consideration of the validity of such provisions in all three jurisdictions investigated in this thesis.

Indemnity clauses are to be distinguished from “knock-for-knock” clauses, described below, which are more correctly described as releases, or simple exclusions of liability; allowing parties to escape from pre-defined liabilities in certain situations. Indemnity clauses usually go one step further by establishing a positive duty to protect against or to pay or reimburse a claim for damages; such as paying compensation following an oil spill.

6 Black’s Law Dictionary
7 In a commercial scenario where a contract exists between two parties an indemnity is where A agrees to compensate B for third party claims addressed to B in respect of B’s contractual performance with A.
8 Ugwuanyi (2012) pg. 143
9 Ugwuanyi (2012) pg. 141
10 Ugwuanyi (2012) pg. 136 “Such arrangements could be said to be manifestations of the principle of (party autonomy and thus) freedom of contract.”
With regard to indemnity clauses in the oil and gas industry, it has been said that; “Until the Macondo oil spill in the Gulf of Mexico in [...] these standard models of liability allocation have been largely non-contested, and where reviewed before the courts, have been held to be enforceable.”11 This thesis will examine how this has changed somewhat, specifically under United States federal law.

3.1.2 The mutual hold-harmless regime ("knock-for-knock")

One of the classic types of risk allocation used in petroleum contracts is known as the mutual hold-harmless regime or “knock-for-knock” regime. This type of risk allocation covers only damage to the property interests of the contracting parties however, and does not extend to cover third party claims or oil pollution liability. The regime is worth highlighting in the interest of putting indemnity clauses in the broader context of risk allocation within the industry.

“Knock-for-knock” clauses are common in offshore construction and service contracts where there are hierarchies of contractors, all working in different capacities. The regime, in principle “provides that each contracting party agrees to assume responsibility for (and to indemnify the other party against) the risk of liability for loss or damage to its own property and for personal injury or death to its own personnel.”12 Without “knock-for-knock” provisions; small and independent service providers, suppliers and contractors would, in most situations, not assume the risk of providing services in the offshore industry.

There are two main benefits of “knock-for-knock” provisions. First, they provide certainty in that they outline a clear and unarguable allocation of liability. Second, they provide economic efficiency by eliminating the need for overlapping insurance policies. In summary, “knock-for-knock” provisions and indemnity clauses share some of the same benefits but cover different types of liability.

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11 Cameron (2012) pg. 207
12 Calnan (2012) pg. 6
4  The Deepwater Horizon Disaster

4.1  Facts – What happened that day?

On 20 April 2010 a blowout occurred in the BP owned and operated Macondo well in the Gulf of Mexico. The blowout, caused by a failure to contain hydrocarbon pressure in the well, resulted in an explosion on the Transocean owned drilling rig Deepwater Horizon that killed eleven rig workers and caused the total loss of the rig. The leak of oil was not stemmed completely until 15 July 2010. Of the estimated 4.9 million barrels of oil discharged into the seawater, 1.2 million were burned, captured or skimmed off the surface of the water. The oil that remained led to a major environmental catastrophe, the full effect of which will not be known for some time.

Although the actual facts of the disaster do not add to the analysis of indemnity clauses within the scope of this thesis, in the interest of providing sufficient background, it is worth summarising some of the findings made in the investigation by the National Commission set up by President Obama. The Commission summarised the cause as follows;

“…the Macondo blowout was the product of several individual missteps and oversights by BP, Halliburton, and Transocean, which government regulators lacked the authority, the necessary resources, and the technical expertise to prevent.”

The commission stressed that they would never know the precise details of the chain of causation leading up to the disaster, but outlined what they did discover in the following way;

“(1) each of the mistakes made on the rig and onshore by industry and government increased the risk of a well blowout; (2) the cumulative risk that resulted from these decisions

13 National Commission (2011) pg. 115
14 Polson (2011)
15 United States President Obama established the National Commission on the BP Deepwater Horizon Oil Spill and Offshore Drilling through Executive Order 13543 on May 21, 2010.
16 National Commission (2011) pg. 115
and actions was both unreasonably large and avoidable; and (3) the risk of a catastrophic
blowout was ultimately realized on April 20 and several of the mistakes were contributing
causes of the blowout.”

The complete set of facts and causes of the disaster will not be fully considered by a court until the
main action, brought by the United States against BP and its contractors, goes to trial in 2013.

4.2 The Applicable Law - United States Federal Maritime Law

4.2.1 Oil pollution liability legislation

Liability for oil pollution damage and civil penalties for oil spills on the United States Continental
Shelf (“USCS”) are imposed by the federal Oil Pollution Act (1990) (“OPA”)
and The Clean
Water Act (“CWA”) respectively. There has been no dispute between Transocean and BP as to
whether this legislation applied to the Drilling Contract.

Under OPA, the offending party responsible for an oil spill from an offshore facility is responsible
for economic damages up to USD$75 million, plus removal costs, provided it did not act with gross
negligence. If gross negligence is proved the statutory limit on liability is lifted.

The CWA imposes civil fines and penalties under s. 311 (b)(7) on “any person who is the owner,
operator, or person in charge of any vessel, onshore facility, or offshore facility from which oil or a
hazardous substance is discharged...” It is important to note that this provision does not limit lia-
bility to the owner of a well or licensee, and that a claimant can recover damages from all tortfear-

17 National Commission [2011] pg. 115
18 33 USC 2701
19 33 USC 1321
20 Summary Judgment [2012]
21 Section 2704 (a)(3)
sors responsible for causing pollution. This is the reason why the United States government has pursued both BP and Transocean for oil pollution liability.

The CWA states that a person who is guilty of such a discharge is “subject to a civil penalty in an amount up to [$32,000] 22 per day of violation or an amount up to [$1,100] 23 per barrel of oil or unit of reportable quantity of hazardous substances discharged.” 24 These penalties are increased significantly in cases of gross negligence or wilful misconduct. Section 7(D) states that:

“ In any case in which a violation…was the result of gross negligence or wilful misconduct…the person shall be subject to a civil penalty of not less [$130,000], 25 and not more than [$4,300] 26 per barrel of oil or unit of reportable quantity of hazardous substance discharged.”

Section 7(D), in particular, is of great concern to BP as on 5 September 2012 the Department of Justice accused BP of “gross negligence” in a document filed with the courts. If the prosecutor can prove gross negligence, BP may be liable to pay up to $21 billion in oil pollution damages alone. 27

4.2.2 Legal principles regulating the enforceability of indemnity clauses

The starting point when assessing the enforceability of indemnity clauses under United States law is the general principle of freedom of contract. A Fifth Circuit federal court judge summarized the principle in the following way;

“…men of full age and competent understanding shall have the utmost liberty of contracting…their contracts, when entered into freely and voluntarily, shall be held sacred, and

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23 $1,000 in original Act. Adjusted for inflation in 2004.
24 s. 7(A)
27 BBC News (2012)
shall be enforced by the courts of justice. Therefore you have this paramount public policy to consider: That you are not lightly to interfere with this freedom of contract.”

Relying on this principle it would seem that allocating risk through contractual indemnification agreements should be relatively straightforward in the United States. There are however; “a myriad of barriers, obstacles and snares in the form of specific legal hurdles and requirements”\(^{29}\) that regulate the validity and enforceability of these provisions. These limitations will be dealt with from the perspective of state law in Section 5 below.

4.2.3 Statutory limitations to indemnity provisions under federal maritime law

Some degree of statutory regulation of indemnification agreements in United States federal law is provided for in OPA §1010. The provision sets no limit on providing an indemnity to a party by agreement, but does stop short of allowing a full transfer of liability. OPA establishes a general statutory endorsement of indemnity clauses in the following way;

\[\text{§1010 (a) AGREEMENTS NOT PROHIBITED. Nothing in this Act prohibits any agreement to insure, hold harmless, or indemnify a party to such agreement for any liability under this Act.}\]

\[\text{ (b) LIABILITY NOT TRANSFERRED. No indemnification, hold harmless, or similar agreement or conveyance shall be effective to transfer liability imposed under this Act from a responsible party or from any person who may be liable for an incident under this Act to any other person […]}\]

This statutory endorsement of indemnification agreements is not something that is found in the United Kingdom, as will be discussed in Section 6 below, but does appear in a similar statute under Norwegian law, albeit with more limitations.

\(^{28}\) Mid-Continent Supply Co. v. Conway, 240 S.W.2d 796 (Tex. Civ. App. – Texarkana 1951) [taken from Transocean Indemnity Filing of 11 Nov 2012, pg. 10]

\(^{29}\) Bullock (2012) pg. 1
4.3 The Applicable Contract – “the Drilling Contract”

The document governing the contractual relationship between BP (“the Company”) and Transocean (“the Contractor”) is the contract for the provision of the drilling rig Deepwater Horizon (“the Drilling Contract”). This section will reproduce the key provisions and put them in context of the wider investigation.

The Drilling Contract is subject to federal maritime law. This is a legal requirement under the Outer Continental Shelf Lands Act (1952) and a fact that is not disputed in the litigation between Transocean and BP.

In Article 24.1 of the Drilling Contract, which outlines Contractor Responsibility, Transocean commits to “protect, release, defend, indemnify, and (hold harmless)” BP for any losses arising from pollution “originating above the surface of land or water.” The Articles appear exactly as follows;

24.1 CONTRACTOR RESPONSIBILITY

“CONTRACTOR [TRANSOCEAN] SHALL ASSUME FULL RESPONSIBILITY FOR AND SHALL PROTECT, RELEASE, DEFEND AND INDEMNIFY, AND HOLD COMPANY AND ITS JOINT OWNERS HARMLESS FROM AND AGAINST ANY LOSS, DAMAGE, EXPENSE, CLAIM, FINE, PENALTY, DEMAND, OR LIABILITY FOR POLLUTION OR CONTAMINATION, INCLUDING CONTROL AND REMOVAL THEREOF, ORIGINATING ON OR ABOVE THE SURFACE OF THE LAND OR WATER, FROM SPILLS, LEAKS, OR DISCHARGES OF FUELS, MOTOR OILS, PIPE DOPE, PAINTS, SOLVENTS, BALLAST, AIR EMISSIONS, BILGE SLUDGE, GARBAGE, OR ANY OTHER LIQUID OR SOLID WHATSOEVER IN POSSESSION AND CONTROL OF CONTRAC-
TOR AND WITHOUT REGARD TO NEGLIGENCE OF ANY PARTY OR PARTIES AND SPECIFICALLY WITHOUT REGARD TO WHETHER THE SPILL, LEAK OR DISCHARGE IS CAUSED IN WHOLE OR IN PART BY THE NEGLIGENCE OR OTHER FAULT OF COMPANY, ITS CONTRACTORS, (OTHER THAN CONTRACTOR) PARTNERS, JOINT VENTURES, EMPLOYEES, OR AGENTS...

In Article 24.2 of the Drilling Contract, the counterpart to Article 24.1 which outlines Company Responsibility, BP promises to “protect, release, defend, indemnify, and hold harmless” Transocean for amongst other things, third party claims linked to pollution “originating below the surface of the land or water.” The Article appears exactly as follows;

24.2 COMPANY RESPONSIBILITY

OPERATOR [BP] SHALL ASSUME FULL RESPONSIBILITY FOR AND SHALL PROTECT, RELEASE, DEFEND, INDEMNIFY, AND HOLD [TRANSOCEAN] HARMLESS FROM AND AGAINST ANY LOSS, DAMAGE, EXPENSE, CLAIM, FINE, PENALTY, DEMAND, OR LIABILITY FOR POLLUTION OR CONTAMINATION, INCLUDING CONTROL AND REMOVAL THEREOF, ARISING OUT OF OR CONNECTED WITH THE OPERATIONS UNDER THIS CONTRACT HEREUNDER AND NOT ASSUMED BY [TRANSOCEAN] IN ARTICLE 24.1 ABOVE, WITHOUT REGARD FOR NEGLIGENCE OF ANY PARTY OR PARTIES AND SPECIFICALLY WITHOUT REGARD FOR WHETHER THE POLLUTION OR CONTAMINATION IS CAUSED IN WHOLE OR IN PART BY THE NEGLIGENCE OR FAULT OF [TRANSOCEAN].

It is important to highlight the inclusion of “negligence” as an accepted head of damage under which the indemnity will still apply. The inclusion of this reference to negligence should in practice make it irrelevant whether or not the contractor has acted negligently, in a question of whether the indemnity should apply.

Article 25.1 of the Drilling Contract outlines BP’s indemnity obligations towards Transocean. It appears exactly as follows:
25.1 INDEMNITY OBLIGATION

EXCEPT TO THE EXTENT ANY SUCH OBLIGATION IS SPECIFICALLY LIMITED TO CERTAIN CAUSES ELSEWHERE IN THIS CONTRACT, THE PARTIES INTEND AND AGREE THAT THE PHRASE “SHALL PROTECT, RELEASE, DEFEND, INDEMNIFY, AND HOLD HARMLESS THE INDEMNIFIED PARTY OR PARTIES FROM AND AGAINST ANY AND ALL CLAIMS, DEMANDS, CAUSES OF ACTION, DAMAGES, COSTS, EXPENSES (INCLUDING REASONABLE ATTORNEYS FEES), JUDGMENTS AND AWARDS OF ANY KIND OR CHARACTER, WITHOUT LIMIT AND WITHOUT REGARD TO THE CAUSE OR CAUSES THEREOF, INCLUDING PREEXISTING CONDITIONS, WHETHER SUCH CONDITIONS BE PATENT OR LATENT, THE UNSEAWORTHINESS OF ANY VESSEL OR VESSELS (INCLUDING THE DRILLING UNIT), BREACH OF REPRESENTATION OR WARRANTY, EXPRESSED OR IMPLIED, BREACH OF CONTRACT, STRICT LIABILITY, TORT, OR THE NEGLIGENCE OF ANY PERSON OR PERSONS, INCLUDING THAT OF THE INDEMNIFIED PARTY, WHETHER SUCH NEGLIGENCE BE SOLE, JOINT OR CONCURRENT, ACTIVE, PASSIVE OR GROSS OR ANY OTHER THEORY OF LEGAL LIABILITY AND WITHOUT REGARD TO WHETHER THE CLAIM AGAINST THE INDEMNITEE IS THE RESULT OF AN INDEMNIFICATION AGREEMENT WITH A THIRD PARTY.

On the face of it, these clauses seems to protect Transocean against any third party claims arising from damages caused by its activities under the Drilling Contract. It is important to note that the phrase “gross negligence” is not included in Articles 24.1 or 24.2. This has become one of the main sources of dispute between BP and Transocean in their cross-claims for Partial Summary Judgment.31

31 See Section 4.4 below
4.3.1 The promises made by BP and Transocean

It is worth extracting the various obligations that both BP and Transocean agreed to take on. The list below shows what each company promised to indemnify the other for.

Transocean promised to “protect, release, defend, indemnify and hold harmless” BP for:
   i) Injury or death of its own employees
   ii) Pollution originating from the drilling unit
   iii) Damages to third parties during the mobilisation of the rig
       (Capped at USD$15 million)
   iv) Loss or damage to the drilling rig itself

BP promised to “protect, release, defend, indemnify and hold harmless” Transocean for;
   i) Civil fines and penalties.
   ii) Any claims relating to pollution except for claims connected with pollution originating from on or above the water.

These indemnities were to apply to damage and losses caused by negligence, “whether such negligence be sole, joint or concurrent, active, passive or gross.”

As stated in the introduction, this thesis will focus on the provision of indemnities for oil pollution liability originating from the reservoir itself. This is a source of liability, almost unique to the oil and gas industry in nature and magnitude, which has the greatest potential for serious financial ramifications. It is also the class of liability that induces the most public policy concerns.

4.4 The Claims

The ongoing litigation following the Macondo well blowout, classified as a multi-district litigation (“MDL”), is comprised of thousands of claims for death, personal injury and pollution damage.

32 Emphasis added (See Article 25.1)
There are two main parallel legal actions being pursued against BP and its contractors within the consolidated cases of the MDL. The following two cases provide the context for the decision that was given, in Summary Judgment, on the question regarding Transocean and BP’s indemnities towards each other.\textsuperscript{33}

The first case is a class action lawsuit brought by thousands of private individuals, claiming mainly for economic loss and loss of income; \textit{In re Triton Asset Leasing GmbH, et. al., No. 10-2771} (“the Limitation Action”). The claimants include fishermen, hotel owners and other small business owners on the Gulf Coast. This lawsuit was recently settled out of court and is awaiting approval by the federal court.\textsuperscript{34} The second case is a federal action pursued by the United States government against BP for oil spill pollution compensation and civil penalties; \textit{“United States v. BP Exploration & Prod. Inc., et al, No. 10-4536 (“the US Action”).}

Partial Summary Judgment was given, on the preliminary question of indemnities in both cases, by Judge Barbier in the United States District Court in Louisiana on 26 January 2012. This judgment will be the starting point in the analysis of United States law in this thesis.

\section*{4.5 The Summary Judgment}

\subsection*{4.5.1 The US Action}

In the US Action the government is suing BP and Transocean for penalties under section 311(b)(7) of the Clean Water Act and are seeking a declaration of liability for economic damages and removal costs under the Oil Pollution Act s. 2704 (a)(3). BP and Transocean were both named as

\begin{itemize}
\item \textsuperscript{33} Summary Judgment (2012)
\item \textsuperscript{34} In March 2012 BP reached a settlement agreement with the lawyers representing thousands of private individuals affected by the disaster worth $7.8 billion. The final ratification of the settlement is expected to be given by Judge Barbier 8 November 2012.
\end{itemize}
defendants in this case, and as a result they cross-claimed against each other in a motion for Partial Summary Judgment on the question of indemnity.\(^{35}\)

The Summary Judgment was a preliminary judgment given only on the specific question of indemnities. It is important to note that the court made no consideration of the facts, meaning that no position has been taken by the courts so far on the question of whether either party acted with gross negligence or wilful misconduct in causing the Macondo blowout. The main trial in the US Action, which was originally due to begin 27 February 2012, was postponed until 14 January 2013 in order to give BP more time to reach a settlement with thousands of private individuals in the Limitation Action.\(^{36}\)

### 4.5.2 The key issues

Transocean’s motion for Partial Summary Judgment asserts that the Drilling Contract requires BP to defend and indemnify Transocean from claims and liabilities (including compensatory damages, punitive damages and statutory penalties fines) related to pollution originating below the surface of the water, even when Transocean is strictly liable or the pollution was caused by Transocean’s negligence or gross negligence.\(^{37}\) Transocean admitted that the Drilling Contract does not provide indemnity in the event of intentional or wilful misconduct, in excess of gross negligence.\(^{38}\)

The main dispute was over the extension of the indemnity for acts of “gross negligence.” BP denied that it owed an indemnity towards Transocean for claims based on strict liability, such as a claim for seaworthiness or under the OPA or CWA, or where Transocean acted with gross negligence. BP did however accept that it must indemnify Transocean where there has been only simple “fault or negligence.”\(^{39}\)

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\(^{35}\) Summary Judgment was also provided in the same order in the case of In re Triton Asset Leasing GmbH, et. al. (no. 10-2771) ("the Limitation Action") but will not be considered under the auspices of this thesis.

\(^{36}\) Goldenberg (2012)

\(^{37}\) Transocean motion...

\(^{38}\) Summary Judgment (2012) pg. 3-4

\(^{39}\) Summary Judgment (2012) pg. 4
The arguments presented by both sides and the reasoning of the court is presented in the section below, where the decisions of Judge Barbier are outlined.

4.5.3 The decision

On 26 January 2012, the United States District Court issued an order requiring BP to indemnify Transocean, for pollution claims asserted by third parties, even if the claims were a result of Transocean’s own gross negligence. Judge Barbier was careful to state however that his ruling meant that such indemnities can be enforceable, not that such indemnities were per se enforceable. It was also stated that the court felt no additional need to define “gross negligence” or “wilful misconduct.”

Crucially, it was also held that BP did not have to indemnify Transocean for punitive damages or civil penalties imposed under the CWA. The decision was made on public policy grounds. Judge Barbier said that the public policy purpose behind punitive damages is to punish the defendant for “egregious conduct” and this purpose would be defeated if the burden of such damages was shifted by contractual indemnity; and like punitive damages; the primary purpose of CWA penalties is to punish and deter future pollution.

A final statement was made to provide for the possible scenario where Transocean might be found to have committed fraud. It was held that the indemnity agreements, to the extent they covered fraud, would in this case be void as against public policy. This is consistent with an exclusion of illegal acts in the principle of freedom of contract.

BP had mainly relied on a technical argument, claiming that the failure to include “gross negligence” as opposed to mere “negligence” in Article 24.2, meant that Article 25.1 did not cover Article 24.2. The court rejected this argument holding that the omission of one word was not sufficient in triggering the “specifically limited” language of Article 25.1, when specific limitations on the

40 US v. BP Exploration and Production Inc. et al (No. 10-4536) ("the US Action")
application of Article 25.1 were clearly stated in other articles. In reaching this conclusion it is clear that the court considered the construction of the contract as a whole.

Referring to the negotiations and drafting of the Drilling Contract, the court stated that BP and Transocean held roughly the same bargaining experience, insisting that they were both experienced and sophisticated entities who should have been aware of what they were doing. This consideration is also an important hallmark of judicial interpretation in Norway.

Another argument presented by BP was that Transocean, by alleged breaches of contract (e.g. not “properly monitoring the well, failing adequately to train its crew, and providing a vessel with poorly maintained equipment”) had materially increased BP’s risks as indemnitor. Thus, the Article 24.1 indemnity was voided. The court rejected this argument. It was held that Article 25.1 made clear that the indemnity covered the grossly negligent acts of the indemnified party. It was said that there might have been a breach of a “fundamental core obligation” but this could not be determined in Summary Judgment where the facts were not considered.

Another argument made by BP was that, even if Article 24.2 did cover gross negligence, it was ineffective as it was against public policy. Judge Barbier stated that he was indeed torn between public policy and freedom of contract in his decision and so weighed up BP’s argument in context of the two principles;

“The issue creates tension between two policies: freedom of contract, which weighs in favour of enforcing the indemnity, and a reluctance to encourage grossly negligent behaviour, which weighs against enforcing indemnity.”

In the end Judge Barbier balanced this concern by distinguishing between pollution claims made by third parties and penalties imposed by government. In doing this, Judge Barbier stated that there was no binding authority on an indemnity covering gross negligence and therefore declared that the court was free to decide the issue de novo. In other words there was a clean slate for judicial discretion to be applied. This assertion alone, emphasizes the importance of this judgment in the wider

41 Summary Judgment (2012) pg. 14
context and indicates the potential it possesses to have major consequences, not just in the main trial, but also in the industry in general.

In summary, the court found that the Drilling Contract “genuinely sought to allocate risk” arising from gross negligence but only when resulting in claims from third parties. The indemnity did not extend to penalties imposed by the government that sought to punish a guilty party, as this would be against public policy.

4.5.4 Possibility of appeal

Both Transocean and BP have said that they will not appeal the Summary Judgment before the main trial is complete. After judgment is given in the main trial in the US Action, they will be able to appeal against the Summary Judgment as part of a full appeal.

5 How are indemnification agreements regulated in the United States?

5.1 Introduction

Due mainly to their geographical proximity to the huge level of offshore drilling activity in the Gulf of Mexico, the bodies of state law that are most commonly encountered in offshore service contracts in the United States, are Texas and Louisiana state law. Federal admiralty law applies to activities on the United States Continental Shelf (“USCS”), with jurisdiction in such matters given to United States federal courts by the Constitution. Federal jurisdiction is not exclusive however, and matters relating to maritime law can be heard in both federal and state courts.

42 United States Constitution, Article 2, Section III
43 See “saving to suitors” clause in USC Title 28, Part IV, Chapter 85, § 1333
The sources of law, other than federal law, that apply to a particular contract usually depend on the jurisdiction agreed upon in a choice of law clause. This section will examine the judicial treatment given to indemnity clauses from the perspective of legal principles and interpretation methods used in Texas and Louisiana state courts. The section will conclude with speculation on the most likely outcome in the hypothetical scenario where the indemnity clauses in the Deepwater Horizon Drilling Contract were governed solely by Texas or Louisiana state law.

5.2 Legal Principles in Texas State Law

In general, Texas state law recognizes the enforceability of contractual indemnity provisions. Such provisions are construed pursuant to “well-settled principles that control the interpretation of contracts in order to give effect to the parties’ intent as expressed in the agreement.” The agreements are construed as a matter of law where “the court’s primary concern is to ascertain the true intent of the parties as expressed in the agreement itself.” The contract must be considered in full and the relevant clauses considered in context of the entire agreement. Actual knowledge of the indemnity regime can also be a determining factor under Texas law.

The standard for the interpretation of indemnity provisions is an objective one, and it is said that; “Simply because two opposing parties put forth differing interpretations of an agreement does not make it ambiguous…” It is accepted in Texas that an agreement is ambiguous “only if a provision is reasonably susceptible to more than one meaning or its meaning is simply uncertain.”

Two main sets of rules, applied in order to determine the enforceability of indemnity clauses, exist under Texas law.

44 The indemnity clauses in question are reproduced in full in Section 4(B) above.
45 Confirmed in Dresser Industries v. Page Petroleum Inc. 725 S.W.2d 705 at 708
46 Bullock (2012) pg. 4
47 Bullock (2012) pg. 4
48 J.M. Davidson, Inc v. Webster 128 S.W.3d 223
49 Bullock (2012) pg. 4
50 Bullock (2012) pg. 4 (J.M.Davidson 73-74)
5.2.1 The Fair Notice Requirements

The main common law principles that govern the enforceability of indemnification agreements in Texas state law, relate to interpretation, and are known as The Fair Notice Requirements (“the Requirements”). The Requirements establish that the other party to a contract must be given fair notice of an extraordinary shift in risk. The existence of fair notice is established by applying a two-prong test of express reference and conspicuousness. The Requirements provide relatively simple and straightforward guidelines that can be used when drafting commercial contracts to ensure that indemnity provisions are upheld in the event of an indemnitees’ own negligence.

The first test, known as the Express Negligence Doctrine, was adopted by the Texas Supreme Court in the seminal case of Ethyl Corp v. Daniel Construction Co. and makes an express reference to “indemnity,” in specific terms, a requirement for a clause that purports to cover the consequences of the indemnitees’ own negligence, to be valid. The best way of satisfying the rule is to label the relevant clause as an indemnity. Satisfaction of the express negligence doctrine is determined by the court on a case-by-case basis as a matter of law, and merely labelling a clause as an indemnity is not sufficient on its own.

The second test is one of conspicuousness and was addressed by the Texas Supreme Court in the key case of Dresser Industries v. Page Petroleum Inc. The rule requires that indemnity clauses be conspicuous within a contract. In other words, the rule states that; “an indemnity provision contemplating indemnification for the indemnitees’ own negligence will not be enforced where the provision itself is not conspicuous, within the overall agreement.” To determine if a clause is sufficiently conspicuous two considerations will be made by the court.

51 725 S.W.2d 705 at 708
52 Ethyl Corp. at 814
53 852 S.W.2d 505 at 508
54 Ibid. The court specifically set out the issue for consideration; “It is important to note that our decision today is limited solely to those types of releases which relieve a party in advance of liability for its own negligence”
55 Bullock (2012) pg. 6
The first consideration is based on an objective standard. The indemnity clause in question is generally found to be sufficiently conspicuous under the Fair Notice Requirements when a reasonable person should have noticed the provision.56

The second consideration, involves the court examining the actual appearance of the clause within the contract document. To achieve formal conspicuousness; larger type may be used or the words may be typed in capital letters or in a different colour.57 An exception to the formal appearance part of the conspicuousness requirement exists when the contract is an “extremely short document.” This exception applies when the contract is two-and-a-half pages or less, and if this is the case then the clause is conspicuous by default.58

5.2.2 The Actual Knowledge Exception

The Actual Knowledge Exception under Texas law eliminates the need for adherence to the Fair Notice Requirements when “the indemnitee establishes that the indemnitor possessed actual knowledge of the indemnity agreement.”59 The courts in Texas will look at a number of factors in order to establish the existence of actual knowledge. These factors include, but are not limited to; evidence of negotiations on the contract terms, evidence that the provisions had been brought to the indemnitor’s attention and also evidence of prior dealings between the parties.60

The Actual Knowledge Exception was also accepted by the Fifth District federal court in Cleere Drilling Co. v. Dominion Exploration & Production, Inc.61 The court emphasised the importance of taking parties’ history of dealings into account, saying in Campbell v. Sonat Offshore Drilling, Inc.62 that; “Where parties share a history of business dealings and standardized provisions have

57 Dresser Industries at 511
58 Philip Sean Murphy (2008) pg. 3
59 Dresser Indus., 852 S.W.2d at 508 (Confirmation Texas Supreme Court of prior holding in Cate v. Dover Corp.)
60 Bullock (2012) pg. 17 (See Cate v. Dover Corp., 790 S.W.2d 559 at 561 Tex. 1990)
61 351 F.3d 642 at 647 (5th Circuit 2003)
62 979 F.2d 1115 (5th Circuit 1992)
become part of those dealings, those provisions, even though issued after performance, are binding if they are accepted without objection.”

The ability of the courts to examine prior dealings and negotiations between the parties is a power that is found also in Norwegian law, as will be discussed in Section 7; but is not a feature of English law.

5.2.3 Deepwater Horizon outcome under Texas state law

If a state court in Texas considered the same issues addressed in the Deepwater Horizon Summary Judgment, to determine the enforceability of indemnity clauses for gross negligence; it is likely the outcome would have been very similar, if not the same. This is partly because of the close connection that exists between Texas state law principles and decisions of the Fifth District federal court, but also the result that an application of the Fair Notice Requirements and Actual Knowledge Exception would have.

The relevant clauses in the Drilling Contract (24.1, 24.2 and 25.1) satisfy the Fair Notice Requirements by appearing in capital letters and in bold, in contrast with the rest of the formatting in the contract. It seems likely that the requirements were known to the drafters and were intentionally adhered to.

Even in the absence of such conspicuous and express drafting, the Drilling Contract indemnity clauses would in all likelihood satisfy the Actual Knowledge Exception under Texas common law. There is no doubt that the parties share “a history of business dealings” and that standardized provisions have become part of those dealings.” This is a fact that was asserted by Transocean in their indemnity filing, in support of their motion for Partial Summary Judgment, and not disputed by

63 979 F.2d 1115 (5th Circuit 1992) at 1120
BP. It was asserted by counsel for Transocean that indemnity clauses like those found in the Drilling Contract had been used “before and also after Macondo.”

5.3 Legal Principles in Louisiana State Law

Similar to the approach taken in Texas, Louisiana courts will enforce contractual indemnification provisions where they are expressed in “specific and unambiguous terms.” The general rule in Louisiana also says that courts will enforce provisions purporting to provide and indemnify for damages and losses arising from the indemnitee’s own negligence, but like Texas law; this general rule comes with limitations. The burden for enforcement of such provisions is lesser in Louisiana however and, more than anything else, the issue comes down to the clarity of language used.

The clearest approach to the status of such provisions under Louisiana law was established in the key case of Polozola v. Garlock, Inc. where the Louisiana Supreme Court held that; “such a contract will not be construed to indemnify an indemnitee against losses resulting to him through his own negligence act, unless such an intention was expressed in unequivocal terms.” This approach shares a great deal with the clear language requirements imposed by English Courts, but does not go as far as upholding indemnities for wilful breaches.

5.3.1 Deepwater Horizon outcome under Louisiana state law

Based on the same reasons as in Texas, it is quite likely that a Louisiana state court would reach the same conclusion as the federal court did in the Deepwater Horizon Summary Judgment but is far from certain. The burden is not higher in Louisiana, than under Texas law or federal maritime law, but the approach taken by Louisiana courts is somewhat less predictable. This is true when con-

64 See Memorandum in Support of Transocean’s Motion for Partial Summary Judgment (2011) pg. 4
65 Ibid pg 4
66 Bullock (2012) pg. 6 (confirmed in Lee v. Allied Chem. Corp., 331 So.2d 608 (La. App. 1st Cir.)
67 Bullock (2012) pg. 6
68 343 So.2d 1000 (La. 1977)
69 Polozola at 1003
sidering the clear rules set out in the Fair Notice Requirements and the Actual Knowledge Exception in Texas. Indemnity clauses must be expressed in “unequivocal terms” to be enforceable under Louisiana law but in the absence of a more specific definition, enforceability is a question decided on a case-by-case basis. It should be questioned whether the exclusion of the word “gross” in Article 24.1 and 24.2 of the Drilling Contract would satisfy the requirement to express the indemnity in “unequivocal terms.”

6 How are indemnification agreements regulated in the United Kingdom?

6.1 Introduction

Most oil and gas activity on the United Kingdom Continental Shelf (“UKCS”) occurs off the coast of Scotland. For the avoidance of doubt it is noted however that although Scotland and England are home to separate legal systems; the legal principles applied to petroleum contracts are generally equivalent, therefore the distinction between English law and Scots law will not be discussed in this thesis.

6.2 Standard Indemnity Clause For Oil Spill Pollution

The standard form drilling contract used most often in the United Kingdom was drafted by a committee of contractors and company representatives for LOGIC, a not-for-profit industry funded subsidiary of Oil & Gas UK; the leading trade association for oil and gas companies operating on the UKCS.

70 General Conditions of Contract for Mobile Drilling Rigs (Dec 1997)
71 Membership is open to all companies active in the UK continental shelf, from super majors to large contractor businesses and from independent oil companies to SMEs working in the supply chain.
The indemnity provisions for oil pollution liability in the LOGIC drilling contract are found in clauses 18.3 and 18.4. As a starting point they uses the same language found in both Norwegian and United States counterparts. They appear as follows;

18.3 Notwithstanding the provisions of Clause 18.1(c) and except as provided by Clauses 18.1(a), 18.1(b) and 18.4 the COMPANY shall save, indemnify, defend and hold harmless the CONTRACTOR GROUP from and against any claim of whatever nature arising from pollution and/or contamination including without limitation such pollution and/or contamination emanating from the reservoir or from the property of the COMPANY GROUP including oil based muds or similar materials used on the instruction of the COMPANY, the discharge of contaminated cuttings or storage, use or disposal of radioactive sources arising from or related to the performance of the CONTRACT.\textsuperscript{72}

18.4 Notwithstanding the provisions of Clause 18.2(c) and except as provided by Clauses 18.1(a), 18.2(b), the CONTRACTOR shall save, indemnify, defend and hold harmless the COMPANY GROUP from and against any claim of whatever nature arising from pollution originating from the hull of the DRILLING UNIT located above or below the surface of the water and/or the other property and equipment of the CONTRACTOR GROUP located above the surface of the water (excluding oil based muds or similar materials used on the instruction of the COMPANY, the discharge of contaminated cuttings or storage, used or disposal of radioactive sources).\textsuperscript{73}

In these clauses, indemnification for oil spill pollution liability is dealt with in much the same way as it was in the Transocean Drilling Contract, with regard to the distinction made between pollution emanating from above and below the water, and also from the property of the respective parties.

\textsuperscript{72} Emphasis added
\textsuperscript{73} Emphasis added
The language used is also largely the same, with one notable exception. The LOGIC contract does not contain any reference to “gross” negligence. English courts have been reluctant to give any weight to the concept of “gross negligence” and it is said that English lawyers “have always had a healthy disrespect” for any distinction between simple negligence and gross negligence, considering the difference as merely one of degree. The term has been dismissed as “the same thing [as simple negligence] with the addition of a vituperative epithet”. The concept has been defined and imported in the settlement of disputes on occasion, but for the purposes of this thesis only the concept of simple negligence will be considered in the context of English law.

6.3 Legislation on Oil Spill Pollution Liability.

There exists no specific legislation in the United Kingdom comparable to the Oil Pollution Act or Clean Water Act in the United States and no counterpart to the Petroleum Act provisions on oil spill liability in Norway.

6.4 Principles of English Law

The traditional approach taken to contractual exclusions of liability in English law was established by the landmark case *Suisse Atlantique* in the 1967, which followed the “fundamental breach” doctrine. This doctrine stated that certain contractual terms were so critical to the performance of the contract that breaches of them could never be excused, even by agreement. However, this doctrine is no longer good law.

The modern approach is dictated by freedom of contract and party autonomy. The severity of breach is no longer the deciding factor in whether and exclusion of liability should be upheld. It is clear that under English law the principle of freedom of contract reigns supreme. It is the core-
stone of English contract law and a long line of case law precedent suggest that English courts will strive to uphold it. This is not to say that the basic limitations that exist in American and Norwegian law do not apply. The contracting parties must act within the limits of the law. They cannot agree to do something illegal and in this context, they cannot indemnify one another for a criminal offence.

Objectivity is the established starting point for the interpretation of indemnity clauses by English courts. English judges cannot, at their own discretion, add or take away from a clause to make it more fair or reasonable, and must construe only what is meant by the language in the provision.

6.4.1 Canada Steamship Lines Ltd. v The King AC [1952] 192 (House of Lords Privy Council on Appeal from Supreme Court of Canada)

An appropriate starting point in an assessment of the treatment of contractual risk allocation under English law is a case decided on before the Suisse Atlantique. The 1952 case Canada Steamship v. The King was heard by the Privy Council in the House of Lords; on appeal from the Supreme Court of Canada. The case concerned an indemnity provision in a contract for the lease of a freight shed on in Montreal, Canada. The appellants, Canada Steamship Ltd., leased the shed from The Crown. The Crown undertook to keep the shed in repair and by way of Clause 17, promised to indemnify the lessee from and against all claims arising out of damages to property of the lessee stored in the shed. A fire was caused by the negligence of the Crown’s servants and all contents, including the property of the lessee, were destroyed. Finding for the appellants, the Privy Council held that the Crown had failed to limit its liability in respect of negligence “in clear terms” and therefore; the Crown’s claim of indemnity under clause 17 was not established.

The clause in question included an indemnity for “any action taken or things done…by virtue hereof.” The court held that this language was too vague and therefore it was doubtful whether it could cover negligent acts. The court also stated that even if the clause was wide enough to cover negligence, “the head of damage might be based on some other ground than that of negligence”

78 Affirmed by Attorney General of Belize v Belize Telecom Ltd [2009] UKPC 10 at (16) per Lord Hoffman (see Cameron pg. 139)
79 Cameron (2012) pg. 4
precluding the need to consider negligence as a cause. Most importantly perhaps, the Lords stated that “the meaning and effect of clause 17 [was] far from clear, and such liability must be imposed by clear words.” This rule somewhat mirrors the Express Negligence Doctrine found in Texas. Lord Morton goes so far as to say;

“There would have been no difficulty in inserting...an express reference to negligence of the Crown’s servants if those clauses had been intended to protect the Crown against the consequences of such negligence.”

This rule establishes a formal requirement under English common law on the content of indemnification clauses, and is strongly indicative of the limited scope of aids to interpretation that will be employed by English courts when ruling on the validity of such provisions.

The counsel for the appellants neatly summarised the general rule on the validity of indemnification provisions for acts of negligence; “In English law, provided that it is expressed with sufficient clarity, the consequences of negligence can be excluded; even of gross negligence, falling short of fraud.” This statement still holds true today and clearly endorses freedom of contract. The principle that one cannot seek indemnity for fraudulent acts is consistent across all three jurisdictions considered in this thesis, and was affirmed by Judge Barbier in the Summary Judgment.

Even though gross negligence is not a concept much discussed by English courts, it was mentioned in Canada Steamship, as a reference to the language used in the original appeal case heard in the Supreme Court of Canada (faute lourde). This reference suggests that a consideration made to the concept of simple negligence can extend to any degree of negligence in English law.

The intention of the parties at the inception of the contract is brought into play by counsel for the appellants when he states; “The real question is what liability did the parties intend to exclude.” It has been established by the House of Lords that English courts will not go as far as to admit evi-

80 Canada Steamship Lines Ltd. v The King AC [1952] (193 at 214)
81 Ibid at 195
82 Ibid at 199
evidence of pre-contractual negotiations in the settlement of disputes however.\(^{83}\) This contrasts with the approach taken by Texas courts, who will admit correspondence and evidence of negotiations, when applying the Actual Knowledge Exception.

The guidelines for assessing the enforceability of an indemnification for the indemnitee’s own negligence has been extracted from Lord Morton’s judgment as a three-part test;\(^ {84}\)

i) If a clause contains language expressly exempting a party from the consequences of his negligence, effect must be given to the provision.

ii) If there is no express reference, the court must consider whether, given their natural meaning, the words would extend to cover negligence.

iii) If words are wide courts should consider whether there exists another “head of damage” apart from negligence that caused the damage.

Perhaps the most succinct way to summarise the rule established by Canada Steamship is as follows; “...the exemption must be express and clear, and beyond peradventure cover the negligence to which it was said to apply.”\(^ {85}\) This rule very much reflects the traditional English common law approach to assessing the enforceability of an indemnification agreement that purports to cover the indemnitees’ own negligence. It is a relatively limited test that focuses mainly on the language in the provision itself. The way in which this test has been broadened will be seen in a summary the A Turtle case in Section 6.4.3 below.

6.4.2 Piper Alpha Litigation

The Piper Alpha was a production platform operated by Occidental Petroleum Ltd. in the UK sector of the North Sea between 1976 and 1988. The operations at the platform accounted for approxi-

\(^{83}\) Chartbrook Ltd v Persimmon Homes Ltd [2009] UKHL 38
\(^{84}\) Cameron (2012)
\(^{85}\) Canada Steamship Lines Ltd. v The King AC [1952] (193 at 201)
mately ten percent of the oil and gas production in the North Sea during that era. On 6 July 1988 a leak of natural gas condensate ignited and caused a massive explosion destroying the rig and killing 167 crewmembers on board. In a series of cases following the disaster, Scottish and English courts considered various claims for indemnification by contractors and other service providers, in what was described as “the contractual aftermath” by Lord Bingham. Two key cases will be considered here to the extent that they dealt with allocation of liability and the validity of indemnification agreements in general. The cases are known as the Orbit Valve Case and the London Bridge Appeal.

6.4.2.1 E.E. Caledonia Ltd. v Orbit Valve Co. Europe 1 WLR [1994] 1515

In the Orbit Valve decision the Court of Appeal followed the general rule on the need for clear language outlined in Lord Morton’s dictum in Canada Steamship. Lord Justice Steyn stated that;

“The starting point must be the language…[the clause] contains no express reference to negligence. It contains no words synonymous with negligence, or words which in the case law has acquired a status equivalent to a reference to negligence.”

The judge emphasized a reluctance to take “an over-legalistic” approach to the language used in an indemnity clause agreed upon between two commercial entities however. Quoting LJ May in The Raphael he said;

“When two commercial concerns contract with one another, they do not, neither should they be deemed to, concern themselves with the legal subtleties of the law of private nuisance or the like. They in fact approach the problem, and so should the courts, with a much broader brush. They consider, or must be deemed to have in mind, their respective responsibilities to one another more from a factual standpoint than from a legalistic one.”

86 Caledonia North Sea Ltd. v British Telecommunications plc (and linked appeals) [2002] UKHL 4
87 Ibid 1520B
88 Lamport & Holt Lines Ltd. v. Coubro & Scrutton (M&I) Ltd. (The Raphael) [1982] 2 Lloyd's Rep. 42 (at pg. 50)
89 Caledonia North Sea Ltd. v British Telecommunications plc at 1521 H
Moving away from a narrow approach to interpretation, where only the natural meanings of the words are considered, LJ Steyn further quoted LJ May’s dictum where he endorsed a more pragmatic and commercial approach to assessing the enforceability of an indemnity clause by saying:

“We should look at the facts and realities of the situation as they did or must be deemed to have presented themselves to the contracting parties at the time the contract was made, and ask what potential liabilities the one had to the other did the parties apply their minds, or must they be deemed to have done so.”

It must be noted that LJ Steyn, in the present case, stated that he was “not convinced that these observations add much to what was inherent in what Lord Morton said [in Canada Steamship].” Nonetheless, he accepted the statement on the intention of the parties as a “gloss” on Lord Morton’s third test. This view highlights support for the freedom of contract in a commercial setting and also a purposive approach to interpretation.

The importance of reading the clause in context was summarised in the following statement where LJ Steyn insisted that it is “the ordinary meaning of the words in their contractual setting [that] is the dominant factor.” This assertion supports the view that, because the oil and gas sector is a specialised and unique “contractual setting,” it is not sufficient to construe the words in their ordinary meaning.

An inference can also be drawn from what LJ May was quoted as saying that consideration must be made of a certain asymmetry of knowledge between contractor and company. LJ May suggested that it must be questioned who knew what and when, during the drafting of the contract. In other words; what potential liabilities did the contractor know about at the inception of the contract? The asymmetry between company and contractor is highlighted again but this time with regard to the physical presence of employees, when LJ Steyn presented the inequality and imbalance of the parties’ roles and the resulting effect this has on their respective exposure to risk;

90 Caledonia North Sea Ltd. v British Telecommunications plc at 1522 A
91 Ibid at 1522 C
“…we know that the defendants had one engineer on board while the plaintiffs had 38 employees on board. The task of the defendants’ one employee was limited to overhauling some 13 valves. By contrast the functions of the plaintiffs employees were multifarious.”

This dictum shows how the court will take a matter-of-fact approach in their consideration of the parties’ intentions. It also shows how the court will take an objective approach in determining the intentions of the parties but does not confirm that the court will go as far as looking at pre-contractual negotiations, as courts in Texas and Norway will.

A further departure from the words on the page into a consideration of the practical reality was made when LJ Steyn stated that;

“…even in the case of a bilateral clause, such as the one before us, it is prima facie implausible that the parties would wish to release one another from the consequences of the other’s negligence and agree to indemnify the other in respect of such consequences.”

LJ Steyn took this approach one step further when assessing the parties’ exposure to risk and explained that; “As a matter of common sense the anticipated risk of death or injury through the negligence of the defendants’ employee must have been of a lesser order than the risk of death or injury through the negligence of the plaintiffs’ employees.” This view supports an argument that says, in a situation where there is an “imbalance and inequality” in consequences of negligence, the risk must be placed with the party best positioned to control it.

With the following statement LJ Steyn emphasised the need to keep commercial purpose in mind when assessing the clause; “It seems to me the right to approach the interpretation of article 10(b) not in a technical way but in the way in which the commercial parties to the agreement would probably have approached it.” This approach suggests that there is a need to consider the parties’ re-

92 Caledonia North Sea Ltd. v British Telecommunications plc at 1523
93 Ibid at 1523 C
94 Ibid at 1523F
95 Ibid at 1525 C
spective bargaining powers. This consideration was made in the Deepwater Horizon Summary Judgment where both Transocean and BP were deemed to be sophisticated and experienced parties of equal bargaining power. It was for this reason that Judge Barbier allowed himself a consideration of the companies’ intentions and not just the words in the clauses. This approach supports an argument that; if a company is able and willing to employee a team of lawyers to draft its contracts, it must know what its agreeing to.

LJ Steyn considered the rationale of the contract’s draftsmen and questioned why an express reference to negligence would be left out of an indemnity when a line of judicial decisions (such as Canada Steamship) makes express reference a requirement. He stated that the answer to such a question would almost certainly be that; “One does not want to frighten off one of the other parties.”96 With this insight the judge settles on a conclusion where he suggests that omissions of express references to negligence tend to be deliberate. This view takes into account the commercial reality of the situation and highlights what could be considered a drawback to the use of such language. It begs the question whether experienced commercial entities would in actual fact be concerned at the sight of a reference to negligence in an indemnity, as this is quite evidently standard industry practice.

6.4.2.2 Caledonia North Sea LD v British Telecommunications plc (and linked appeals) [2002] UKHL 4 – “The London Bridge Appeal”

In the London Bridge Appeal the House of Lords applied a test of reasonableness to distinguish an indemnity from a release for the purpose of showing objectively that no party would intentionally include acts of negligence in a clause containing situations where a party would be indemnified; “A party is even less likely to take on the other party’s liability for negligence than he is to exempt the other party from liability or negligence”97 This assertion presents a view of a parties’ intention but also questions how reasonable such clauses are.

96 Caledonia North Sea Ltd. v British Telecommunications plc at 1523 H
97 London Bridge 2000 SLT 1123 at 1148 (Cameron (2012) pg. 5)
The assertion also sums up the court’s aim when interpreting such provisions. The court clearly strives to establish what the parties’ intentions were when contracting on the issue in question. This being said however, the courts will not strike down an indemnity or exclusion clause because they think they are unreasonable following an objective consideration; no matter how unreasonable they may seem.

“The House of Lords has held that the court has no power under the common law to invalidate an exemption or indemnity clause simply because it is unreasonable. Not even when the consequences of the breach are serious will it have such power rather, it is a question of whether, as a matter of construction, the clause is apt to cover a given situation.”

This position again recognises and affirms freedom of contract. This is in direct contrast to Norwegian law, as will be established in Section 7.4.2 below, where the court has the power to “censor” a contractual provision should it be deemed unreasonable or in conflict with statutory rules of decency.

6.4.3 A Turtle Offshore v Superior Trading [2008] 2 CLC 953

This more recent case concerned a standard form of towage contract (“TOWCON”) for the towing of the drill rig “A Turtle” in which there was a mutual exemption from liability clause (Part II, Clause 25). The clause divided risk and responsibility between parties on a no fault basis. The rig was lost during towage when the tug owners cut the towline. The rig owners subsequently claimed damages from the owners of the tug for breach of contract. The tug owners denied any responsibility and claimed they could limit their liability under TOWCON Clause 25 as well as the 1976 Limitation Convention. Part of the judgment given was on the question of whether the breaches committed by the tug owner “were of a type for which the parties have agreed to exclude liability.”

98 Cameron (2012) pg. 5
99 A Turtle v Superior Trading (2008) (980 at 100)
The Court held that clause 25 of TOWCON provided a clear exemption in relation to damage to tow owner’s property, as part of the overall contractual “knock-for-knock” scheme, which was commercially well understood. Thus, despite the clear breach of contract, there was no liability.

The judge approached the question by considering the ‘commercial purpose’ of Clause 25, which was in his own words, “to make clear to the parties which one of them is to bear the risk of the loss, damage and liabilities which might arise during the towage and enable each to insure against them.”100

The words in the contract were not to be construed literally but instead, “in the context of the contract as a whole.”101 Provided sufficiently clear language was used however, a contracting party could rely on an indemnity for his own gross negligence or even wilful breach of contract.

“…the more radical the breach the clearer must the language be if it is to be covered…No formula will solve this type of question and one must look individually at the nature of the contract, the character of the breach and its effect upon future performance and expectation and make a judicial estimation of the final result.”102

The judge qualified this rule however by saying that a “strained construction must not be placed on words which are clear and fairly susceptible of one meaning only.”103 In support of this view the judge quoted Lord Diplock in Photo Production v. Securitor,104 in which the autonomy of parties with equal bargaining power is also emphasised as a key consideration;

“In commercial contracts negotiated between business-men capable of looking after their own interests and of deciding how risks inherent in the performance of various kinds of contract be most economically borne (generally by insurance) it is, in my view, wrong to place a strained construction upon words in an exclusion clause which are clear and fairly

100 A Turtle v Superior Trading [2008] (pg. 982 at 105)
101 Ibid pg. 982 at 109
102 Ibid pg. 983 at 111
103 Ibid pg. 983 at 112
104 Photo Production v. Securitor [1980] AC 827
susceptible of one meaning only after due allowance has been made for the presumption in favour of the implied primary and secondary obligations.”

This passage neatly summarises the key principles that characterize the treatment of indemnification provision by English courts. The emphasis on clear language has a lot in common with the principles found in the American principles of interpretation.

The relationship between the commercial purpose of the individual clause and the context provided by the contract as a whole is balanced by the judge in *A Turtle*, who stated that although he must give effect to the clause’s commercial purpose “of allocating risk between the parties on a no-fault basis,” a consideration of the contract as a whole makes it necessary to keep in mind that the contract places obligations upon the tug owners. The judge suggests that if it was intended that the tug owners should be excluded from liability for breach of key obligations “then very clear words would be needed because that would be a very radical breach indeed.” This requirement was satisfied in the court’s opinion.

With regard to the use of clear wording the judge referred to a clarification by Lord Atkin in which he said; “…a contracting party can be protected from liability even for wilful default if he used clear words to that effect.” This goes much further than what would be enforceable in the United States, where indemnification for wilful misconduct is not valid as against public policy. The tug owners in *A Turtle* must have understood on the balance of probabilities that the total loss of the rig was likely following their wilful breach. Nonetheless, the High Court upheld the indemnity. In allowing the indemnity to stand for wilful breach, *A Turtle* is perhaps the strongest possible endorsement the High Court could have given the freedom of contract.

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105 Photo Production v. Securitor [1980] AC 827 (at 851)
106 See Express Negligence Doctrine and the “clear and unequivocal” language requirements in Texas and Louisiana law.
107 Emphasis added
108 LJ Atkin at 984F
6.5 Deepwater Horizon Outcome Under English Law

In summary it is noted that under English law there is no general public policy limiting indemnities for negligence in statute. Freedom of contract, subject to clear wording, is the governing principle under English law. It is of fundamental importance that indemnity clauses are expressed in clear and unambiguous language. Case law confirms that English courts are very unlikely to enforce all-inclusive indemnity clauses where there is any doubt of the parties’ intention to include negligence. Where there is no doubt however, and following an objective approach to the parties’ intentions, indemnities for negligence and even wilful misconduct or breaches will be upheld.

It is almost certain that courts in the United Kingdom would uphold the indemnity clause for gross negligence in the Deepwater Horizon Drilling Contract. Following the precedent established by A Turtle, it is also likely that English courts would go one step further and also uphold an indemnity for wilful misconduct on the indemnitees’ part.

7 How are indemnification agreements regulated in Norway?

7.1 Introduction

There are currently fifty-one active oil and gas fields on the Norwegian Continental Shelf ("NCS"), where drilling activities are closely regulated by legislation that is enforced by the Norwegian Petroleum Directorate. This section will assess the regulation of indemnity clauses in petroleum contracts under Norwegian law.¹¹⁰

7.2 Standard Indemnity Clause for Oil Pollution Liability

¹¹⁰ Norway.org (2012)
The Norwegian Subsea Contract 2005 (“NSC 05”) is an example of a standard form contract used in the Norwegian petroleum industry. The indemnity clause for pollution contained in Article 34 of NSC 05 will be reproduced here as the basis for analysis in this section.

The creation of NSC 05 was initiated by The Norwegian Oil and Gas Association (“OLF”) and was drafted in negotiations between Statoil (the 67% state-owned oil company) on the operator side and Subsea 7, Technip Offshore Norge and Stolt Offshore on the contractor side. The contract is for use in the installation of pipelines, cables, umbilicals and other subsea structures where the use of vessels is involved. The contract aims to “address specific risks in connection with subsea work and the operation of vessels.”

Article 34.1 governs the limitation and exclusion of liability for oil pollution in the following way:

Article 34.1 Company shall indemnify Contractor Group from Company Group’s own indirect losses, and Contractor shall indemnify Company Group from Contractor Group’s own indirect losses. This applies regardless of any liability whether strict or by negligence, in whatever form, on the part of either group and – except as stated in Art. 17.3 and 24.2 – regardless of any other provisions of the contract.

Indirect losses according to this provision include but are not limited to loss or earnings, loss of profit, **loss due to pollution** and loss of production.

Article 34, and indeed NSC 05 as a whole, does not deal with reservoir pollution in the same way the Deepwater Horizon Drilling Contract and LOGIC Drilling Contract do. It is not necessary to include the same type of indemnification for pollution from the company’s well, as the Norwegian Petroleum Act imposes strict liability on the licensee (the operator) for this type of pollution.

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111 NSC 05 pg. 2
112 Emphasis added
113 PA 1996 (s.7-4)
114 See Section 7.4 below
In contrast, legislation in the United States and the United Kingdom do not contain specific limitations on what type of pollution can be included in a contractual indemnity. The statutory limitation on the use of indemnification agreements for reservoir pollution in Norway makes it essential to have an understanding of the Petroleum Act when construing the NSC 05.

### 7.3 Oil Pollution Liability Legislation

The Norwegian Petroleum Act §7.4 governs the allocation of liability for pollution damage between operators and contractors and imposes strict liability on the licensee. The provision establishes a statutory basis for the regulation of oil pollution liability on the Norwegian Continental NCS and states that such liability cannot be allocated by a contractual indemnity.

- **§7-4** The liability of a licensee for pollution damage may only be claimed pursuant to the rules of this Act. Liability for pollution damage cannot be claimed against:
  
  a) anyone who by agreement with a licensee or his contractors has performed tasks or work in connection with the petroleum activities.
  
  b) anyone who has manufactured or delivered equipment to be used in the petroleum activities […]

The provision goes on to limit the licensee’s ability to claim recourse from the contractor;

- **§7-5** The licensee cannot claim recourse for pollution damage against someone exempted from liability pursuant to the rules of Section 7.4, unless the person in question or someone in his service has acted wilfully or by gross negligence…

Any agreement on further recourse in respect of those against whom liability cannot be claimed pursuant to Section 7.4, second paragraph, shall be invalid.
It has been held that the phrase “in his service” shall include all employees of the contractor, but is not likely to include subcontractors.\(^\text{115}\)

### 7.4 Principles in Norwegian Law

#### 7.4.1 Norwegian contract law in general

Freedom of contract is also a fundamental principle of Norwegian private law, just as it is in the United States and United Kingdom. The principle is the starting point in commercial contracts, but exists with more qualification than its Anglo-American counterpart. Generally Norwegian courts have been known to emphasize considerations of fairness and reasonableness more than predictability and party autonomy, but deviations from this norm have been made in commercial cases where standard form contracts are interpreted.\(^\text{116}\)

#### 7.4.2 Limitation of liability in Norwegian law

The traditional and long established position on the exclusion of liability in Norwegian contract law is that one is able to exclude liability for any consequences whatsoever, as long as they are not caused by wilful misconduct or gross negligence.\(^\text{117}\) The basis of this general rule is found in the contractual Rules of Decency (“Ærbarhetsregelen”) in Norwegian civil code NL 5-1-2.\(^\text{118}\) This general rule has evolved somewhat as the result of an amendment to the Norwegian Contract Law Act

\(^{115}\) Thommessen (2012) pg. 31

\(^{116}\) Bjerketveit (2008)

\(^{117}\) See ND 1984.404 (Arbitration) – “Trans Tind” – Byggeverkstedets Mangleansvar

“It is presumed that a contractor who has acted with wilful or gross negligence, is prohibited from seeking enforcement of contractual exclusions of liability.” See also, ND 1989.225 (Arbitration) – “Harms-Dommen” - Use of exclusion of liability for deck cargo. “It is established Norwegian law that a party to a contract cannot validly exclude himself from liability for damage caused to another party to the contract through an act of wilful conduct or gross negligence…”

\(^{118}\) Hagstrøm (1996) pg. 421 (See Kielland (2008) pg. 115)
(“Avtaleloven”) in 1983 (“the 1983 statute”) however, and in the decisions of cases that will be summarised below.

The most significant deviation from the general rule comes in Section 36 of the 1983 statute, which states that a contract may, in whole or in part, be set aside if it is held to be unreasonable (“urime-lig”) or in conflict with sound business practices (“god forretningskikk”). Aspects that will be considered in an evaluation of the agreement in question include; the substantive content of the contract, the parties’ standing and relationship with each other and also latter agreements and any consequences that follow thereof.

A classic case on the exclusion of liability is The Berry Picking Judgment119 (“Bærturdommen”). The facts of this case seem trivial in the context of the modern petroleum industry but provide necessary background nonetheless. In this case an employer had organised an outing for his employees to pick wild berries. The employees were deemed to be passengers at their own risk and agreed in advance that they were participating “at their own risk, with regards to accidents and damages of any kind that may be incurred during or in connection with the outing.” In effect, the waiver acted as a simple exclusion of liability. In its decision the Norwegian Supreme Court established the general rule, also confirmed by NL-5-1-2; that one can exclude any type of liability by agreement, except for liabilities resulting from one’s own acts of gross negligence or wilful misconduct.120

In a landmark case that deviated from this general rule, and where an exclusion of liability was upheld for an act of gross negligence, The Dock Inspector Judgment (“Kaiinspektørdommen”)121 concerned a situation where an employee of the party seeking the exclusion had acted with gross negligence. In its judgment the Norwegian Supreme Court held that an agreement for the exclusion of liability in a standard form contract could be upheld where one of the company’s employees had acted with gross negligence. Considerations of clarity and predictability were central in the court’s judgment and it was of significant importance that the contract was a standard form contract negotiated between two commercial entities.

119 Rt 1948 pg. 370
120 Hagstrøm (1996) pg. 624
121 Rt. 1994 pg. 626
The judgment left two central questions unanswered. First, can an exclusion of liability clause be set aside for one’s own grossly negligent actions (or those actions of a company)? Second, is the rule that says an exclusion of liability for one’s own gross negligence will always be set aside absolute? The answers to these questions are not settled and it is uncertain whether decisions on these questions would be made on a case-by-case basis using the Section 36 test. There is a difference in opinion held by two authoritative writers on the matter. Viggo Hagstrøm argues that an absolute prohibition on excluding liability for one’s own wilful misconduct and gross negligence is established in the Norwegian Civil Code NL 5-1-2, whereas Knut Kaasen argues that a decision on the availability of such a limitation should follow an objective evaluation of the agreement and surrounding circumstances.

Even though the indemnity clauses in the most widely used Norwegian standard form petroleum contracts have not been considered by the courts, it could be speculated that they would be treated in the same way as in the Dock Inspector Judgment. The judge states in the decision that;

“…there seems to be the general understanding in legal theory that the responsibility for an employee’s grossly negligent actions can be excluded in an agreement between commercial entities and there is also exists a series of arbitration awards that suggest the same.”

In its verdict the Supreme Court points to four components that justify the enforcement of an exclusion of liability clause in spite of the presence of gross negligence. First, the agreement in question was a standard form contract drafted as a result of negotiations between organisations. Second, the allocation of responsibility is based on an evaluation of the balance of conflicted interests. Third, considerations are made of who is best placed to take out insurance for the various risks. Last, there is recognition of predictable and clear solutions, which should be encouraged.

123 Kielland (2008) pg. 116
124 Rt. 1994 pg. 626
125 BA-HR pg. 3
This decision represents a matter-of-fact approach to a commercial agreement where an objective interpretation has been made of the purpose of the allocation of liability and the intentions of the parties at the inception of the contract.

7.4.3 Gross negligence and wilful misconduct under Norwegian Law

Gross negligence (“grov uaktsomhet”) is an accepted concept under Norwegian law and can be defined as a ‘marked departure from simple negligence, where this departure is significantly more to blame than any simple negligence.’ Wilful misconduct is defined as “an intentional/deliberate disregard of the contract.” The intentional disregard must cover the breach itself, but most likely also the consequence of the breach.

7.4.4 The distinction between employee and management in Norwegian law

The key difference between the Norwegian and the Anglo-American approach to the enforceability of indemnity clauses, is a consideration of exactly whom, within the organisation of the party seeking an indemnity, has acted with gross negligence or wilful misconduct. Norwegian law distinguishes between actions at senior management level and those of lower level employees or servants. This is an extra layer that is not present in the law of the United States or the United Kingdom. Following the Dock Inspector Judgment, it is clear that gross negligence or wilful misconduct must be at a managerial level within a Norwegian company for an indemnity that purports to protect a company against such liability to be set aside. The distinction between management and employee is an objective test and depends on the person’s formal place within organisation’s central organs.

126 jf. Rt. 1989.1318 “In order for an act to be considered as grossly negligent, it must in my opinion represent a pronounced derogation from common proper behaviour. It must be a behaviour that is strongly blameable, where the person is substantially more to blame than where an act is only negligent.” [Supreme Court definition]

127 Thommessen (2012) pg. 27
The distinction can be illustrated in a scenario where a roughneck on the drill floor of a rig causes pollution by wilful misconduct. Under United States maritime law, public policy would bar a claim for contractual indemnity. Under Norwegian law, specifically a consideration under the Contracts Act §36 (par. 2), a claim for contractual indemnity would not be barred in this scenario.128

If it were found that the pollution was caused by the gross negligence of the company’s CEO, the outcome would be reversed. United States maritime law would not bar a claim for contractual indemnity in this case whereas Section 36 of the 1983 Statute would in all likelihood bar a claim for contractual indemnification in this case.

One approach suggested by Knut Kaasen is to say that; “…the contractor is identified with the organs of the organisation that has the duty to make decisions or act in a way that directly affects the fundamental prerequisites of the contract.”129 In other words, those who have real influence, power of attorney or executive authority are identified with the management and qualify as “the contractor” for contractual purposes.130

In the Dock Inspector Judgment the actual job description of the employee was considered; “The mere fact that during his work he made independent decisions on how the cargo should be stowed does not allow him to be identified with the management.”131 This shows how the court will take a matter-of-fact approach to determining actual influence on business decisions and seems to suggest an approach that may be best served in a case-by-case evaluation.

It follows that the current approach to contractual indemnity agreements in commercial contracts under Norwegian law can be summarised as follows; no indemnity or limitation of liability will be upheld in the event of gross negligence or wilful misconduct at a managerial level.

129 BA-HR pg. 9
130 BA-HR pg. 9
131 Rt. 1994 pg. 626


7.5 Rules of Enforceability Summary

It seems that the Norwegian judicial approach to exclusion of liability clauses seems to closely resemble the UNIDROT principle for interpretation where considerations of reasonableness of expectations, fairness and the purpose of the contract are central. Article 7.16 of the UNIDROT Principles of International Commercial Contracts states the following:

“A clause which limits or excludes one party’s liability for non-performance or which permits one party to render performance substantially different from what the other party reasonably expected may not be invoked if it would be grossly unfair to do so, having regard to the purpose of the contract.”

This approach mirrors the precedent established by Section 36 of the 1983 Statute, that allows a court to set aside a contractual provision if it is deemed to be “unreasonable.”

7.6 Deepwater Horizon Outcome Under Norwegian Law

It is likely that Norwegian courts would settle on the same decision as was made in the Deepwater Horizon Summary Judgment for Transocean’s gross negligence in non-pollution related claims. The validity of the indemnity clause would depend on the seniority of the offending employee within the contractor’s organisation however. Following The Deck Inspector Judgement, the indemnity would only be upheld if an employee who committed the grossly negligent act were not part of the senior management or a company director. Since Judge Barbier, in the Summary Judgment, did not take a stance on the cause or presence of gross negligence one cannot reach a definite conclusion on this point however.

The Norwegian approach to the question of liability for pollution liability and punitive damages differs from the approach applied in the Deepwater Horizon Summary Judgment. Liability for pollution damage would not be imposed on a contractor like Transocean in Norway unless the contrac-
tor, at a senior management level, committed the grossly negligent act or wilful breach. Norwe-
gian law does not recognise the concept of punitive damages so there is scope for speculation in this matter however.

8 Concluding Remarks

8.1 Benefits of Indemnity Clauses

There are two fundamental benefits to be gained from the use of indemnity clauses in a risk alloc-
a-ration regime for pollution liability in petroleum contracts. Both relate to the commercial reality of offshore drilling.

The first benefit is economic efficiency. It is quite evidently not realistic to expect a contractor with tight margins and limited capital to insure against the loss of a whole drilling operation and pollution damages. Mutual indemnity clauses allow projects to be completed with lower upfront costs for all involved. Lower insurance costs are a key benefit. Indemnity clauses, when drafted in a careful manner, with the laws of the relevant jurisdiction in mind, usually exclude the need for contractors to buy insurance for worst-case oil spill liability. These costs would be completely unsustainable and would prevent many potential offshore projects from reaching production. Ultimately lower insurance costs and economic efficiency benefits the consumers of oil, the general public.

The second benefit is certainty and predictability. One of the most important purposes of indemnity clauses in offshore drilling contracts is to, “allocate risk ahead of time in order that a certain degree of certainty may be brought to the risks inherent in that undertaking.” Such pre-determined allocations of risk, that makes legal and financial outcomes of an incident more predictable; allow com-

132 See s.7-4 and s.7-5 of The Petroleum Act
133 For further reading see comments by John Smith (former president of International Marine Contractors Association "IMCA," and CEO of Subsea 7) in Stuffing the Contractors (2004)
134 Todd Shipyards Turbine Serv., Inc. 647 F2d 401, 411 (5th Cir. 1982)
companies to contract and operate with more confidence. The absence of a need to establish blame and point fingers following an incident will also foster better working relationships between companies and contractors.

Excessive confidence is not always a beneficial trait for a contractor however, when it may lead to complacency. It follows therefore that public policy concerns that endorse the discouragement of irresponsible behaviour must be balanced against this benefit.

### 8.2 The Balance of Risk v. Reward

An argument in support of the need for risk allocation in the context of the Deepwater Horizon disaster is succinctly summarised as follows; “The risk is allocated in service contracts in such a way as to place the largest share with the party that is best able to control and prevent the risk and with the greatest upside: the operator.”¹³⁵ This statement acknowledges the asymmetry of potential upside versus potential downside that exists between contractors and companies and outlines the reasons why the balance of risk and reward must be established.

No contractor would, or should have to, take on risk that would leave them exposed to claims that might exceed their market capitalisation many times over. When liability is given to the party best placed to mitigate risk and pay for the financial consequences of oil pollution, public policy interests are safeguarded to a greater degree.

### 8.3 Achievable Legal Effects

The legal affect achievable by indemnity clauses used to allocate oil pollution liability is different in each jurisdiction. This is mainly down to legislation and the difference in weight given to public policy concerns and principles like the freedom of contract. The reality is that multinational companies such as BP and Transocean operate in all three jurisdictions considered in this thesis. The

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¹³⁵ Cameron (2012) pg. 13
Deepwater Horizon disaster illustrates the importance of exercising the highest possible due diligence and attention to detail when drafting petroleum service contracts. Special attention should be paid to choice of law clauses where applicable. Draftsmen negotiating contracts similar to the Deepwater Horizon Drilling Contract must keep in mind what legal effects they are trying to achieve while at the same time considering the limitations that are placed on the use of indemnity clauses by legislation and legal principles in the jurisdiction they are working in.

The care taken when drafting petroleum contracts becomes of crucial importance when one considers the different approaches taken to the enforceability of indemnity clauses for the indemnities’ own wilful misconduct for example. The fact that an indemnity for wilful misconduct is valid in the United Kingdom so long as the language used is sufficiently clear; while the same clause would never be valid in the United States, and would only be valid in Norway if the wilful breach were committed at employee level, brings the point home. The legal effects that are achievable by certain indemnity clauses in the United States, United Kingdom and Norway vary greatly, and may not satisfy the desired legal effects sought by the draftsmen. Sometimes this will be due to legislation that cannot be avoided, but can also be the result of careless drafting.

### 8.4 The Effect of the Deepwater Horizon Disaster

In finding for BP on the question of punitive damages, and deciding that Transocean must pay any fines and penalties levied by the government, Judge Barbier effectively cut through the indemnity Transocean thought it was protected by. This decision represents a threat to the established status quo in the opinion of Peter Cameron;

“…the service industry was shaken up by the position taken by Judge Barbier on fines and penalties. Before Macondo, it was assumed that regulators would only go after an operator in seeking damages, not a service company even if some applicable laws did not exclude such resources against contractors.”

136 Cameron (2012) pg. 2
The finding on punitive damages and penalties is a clear indication that the judiciary in the United States might be more prepared to step into private contractual arrangements in future. This represents a major shift in approach by American courts; “and has significant and potentially very adverse financial implications for the contractors and for the long term competitiveness and sustainability of the industry.”  

Indemnity clauses have long been, and can continue to be, useful tools for allocating risk in petroleum contracts but consideration of the limits on enforceability in the relevant jurisdictions, must be taken with greater care than ever in the post-Macondo era.

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