Risk Shifting in the Oil Patch: A Guide to Extraordinary Risk Shifting

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There are a variety of risks associated with the exploration and production of hydrocarbons. Such risks include the potential for property damage, personal injury, and higher than expected costs (*i.e.*, business losses). When any of these risks turn from a possibility into a reality, there is ultimately one question left to be answered: "Who is going to pay for the damage?" This paper will address issues related to the allocation of risk among working interest owners and contractors so that we can determine who is going to pay for "that."

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The State of Texas is by far the largest producer of onshore hydrocarbons in the United States, and production is trending higher.[1] For example, Texas produced 7,531,365 MMCF of onshore natural gas and 2,543,000 barrels per day of onshore oil in 2013.[2],[3] The next highest hydrocarbon-producing states were Pennsylvania with 3,259,042 MMCF of onshore natural gas and North Dakota with 860,000 barrels per day of onshore oil in 2013. Moreover, according to the Baker Hughes Rig Count, as of November 14, 2014, Texas had 901 onshore active rotary rigs; the next highest state was Oklahoma with 207 onshore active rotary rigs.[4],[5],[6],[7] Therefore, this article will be centered around Texas law and will make occasional note of some of the differences in other hydrocarbon-producing states.

I. COMMON LAW INDEMNITY

Common law indemnity in Texas is extremely limited and largely replaced by a modified comparative fault scheme.

At one time, Texas common law provided indemnity in at least three situations.[8] First, Texas common law allowed indemnity between joint tortfeasors if they were not *in pari*

1. U.S. Energy Info. Admin., *Crude Oil Production*, EIA.Gov, http://www.eia.gov/dnav/pet/pet_crd_crpdn_adc_mbblpd_a.htm (last visited Oct. 13, 2014) [hereinafter EIA, *Crude Oil Production*]; U.S. Energy Info. Admin., *Natural Gas Gross Withdrawals and Production*, EIA.Gov, http://www.eia.gov/dnav/ng/ng_prod_sum_a_EPG0_VGM_mmcf_a.htm (last visited Oct. 13, 2014) [hereinafter EIA, *Natural Gas Gross Withdrawals and Production*].
2. EIA, *Natural Gas Gross Withdrawals and Production*, *supra* note 1.
3. EIA, *Crude Oil Production*, *supra* note 1.
4. EIA, *Natural Gas Gross Withdrawals and Production*, *supra* note 1.
5. EIA, *Crude Oil Production*, *supra* note 1
6. The Baker Hughes North American Rotary Rig Count is a weekly census of the number of drilling rigs actively exploring for or developing oil or natural gas in the United State and Canada. To be counted as active, the rig must be on location and drilling. The rig is considered active from the moment the well is spudded until it reaches its target depth. Baker Hughes Investor Relations, Rig Count FAQs, http://phx.corporate-ir.net/phoenix.zhtml?c=79687&p=irol-rigcountsfaqs (last visited Oct. 13, 2014).
7. Baker Hughes Investor Relations – North America Rig Count, Rigs by State, http://phx.corporate-ir.net/External.File?item=UGFyZW50SUQ9NTYxMzMzfENoaWxkSUQ9MjYwMzI0fFR5cGU9MQ==&t=1 (last visited Nov. 16, 2014).
8. Strakos v. Gehring, 360 S.W.2d 787, 798 (Tex. 1962).

delicto or "in equal fault."[9] Second, Texas common law allowed indemnity where the injury forming the basis for the judgment against the joint tortfeasors resulted from a violation of a duty which one of the tortfeasors owed to the other.[10] The latter would have a claim for common law indemnity against the former.[11] And third, Texas common law allowed indemnity where one party was vicariously liable by operation of law.[12] Vicarious liability is liability placed upon a person for the conduct of another, based solely upon the relationship between the two.[13] For example, under the doctrine of *respondeat superior*, an employer is exposed to liability not because of any negligence on its part, but because of the employee's negligence in the scope of his or her employment.[14] Therefore, the employer has a common law claim for indemnity against the employee.[15]

Today, the availability of common law indemnity in Texas is extremely limited.[16] Common law indemnity survives only in negligence actions to protect a defendant whose liability is purely vicarious in nature and in products liability actions to protect an innocent retailer in the chain of distribution.[17] Common law indemnity is an all-or-nothing concept. "Generally

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9. *Id.* at 797. For example, two defendants are not in equal fault if they are sued by a plaintiff for the same injury, and one defendant is liable for breaching a heightened duty of care and the other defendant is liable for breaching the ordinary duty of reasonable care. *Id.* The defendant liable for a more aggravated species of negligence would owe common law indemnity to the defendant who was liable for a less aggravated species of negligence. *Id.*
10. *Id.*
11. *Id.* For example, in *Renfro Drug Co. v. Lewis*, the plaintiff was injured by falling at the entrance of a drug store. 235 S.W.2d 609, 614–15 (Tex. 1950). The plaintiff sued the landlord and the tenant of the premises, and both were found negligent. While holding that the tenant was entitled to indemnity from the landlord, the Court used the following rule: "Where the injury forming the basis for the judgment against the joint tortfeasors results from a violation of a duty which one of the tortfeasors owes to the other, the latter, at common law, is entitled to contribution or indemnity from the former." *Id.* at 623. In that case, the landlord breached a duty to the tenant because, under the lease, the landlord had reserved at least joint control over the entrance and had expressly obligated himself to the tenant to keep the entrance in repair. *Id.*
12. S*trakos*, 360 S.W.2d at 797.
13. Affordable Power, L.P. v. Buckeye Ventures, Inc., 347 S.W.3d 825, 833 (Tex. App.—Dallas 2011, no pet.).
14. *Id.*
15. *Id.*
16. *Id.*
17. *Id.*

speaking, a person who, without personal fault, has become subject to tort liability for the unauthorized and *wrongful* conduct of another is entitled to full indemnity from the other for expenditures properly made to discharge the liability."[18]

Except for vicarious liability and products liability, common law indemnity was abolished by Tex. Rev. Civ. State. Ann. Art. 2212a, now codified at Tex. Civ. Prac. & Rem. Code §§ 33.001 *et seq*.[19] For tort claims, Chapter 33 of the Texas Civil Practice and Remedies Code allows the trier of fact to determine the percentage of responsibility of each claimant, defendant, settling person, and responsible third party with respect to each person's contribution to causing the claimant's damages.[20] A claimant is barred from recovery if his percentage of responsibility is greater than fifty percent.[21] If the claimant is not barred from recovery, the court will reduce the amount of damages recoverable by the claimant by a percentage equal to the claimant's percentage of responsibility.[22] If the claimant has settled with one or more persons, the court will also reduce the amount of damages recoverable by the claimant by the sum of the dollar amounts of all settlements.[23]

Generally, in Texas, a defendant is only liable to a claimant for the percentage of damages found by the trier of fact equal to that defendant's percentage of responsibility with respect to the claimant's recoverable damages.[24] However, a defendant will be jointly and severally liable for all recoverable damages if (1) the percentage of responsibility attributed to that defendant is greater than fifty percent; or (2) the defendant acted in concert with another person to violate certain provisions of the Texas Penal Code.[25] If a defendant who is jointly and severally liable pays a percentage of the damages greater than his percentage of responsibility, that defendant has a right of contribution for the overpayment against each other liable defendant to the extent that the other liable defendant has not paid for his own

18. Humana Hosp. Corp. v. Am. Med. Sys., Inc., 785 S.W.2d 144, 145 (Tex. 1990) (emphasis added).
19. Ethyl Corp. v. Daniel Const. Co., 725 S.W.2d 705, 708 (Tex. 1987).
20. Tex. Civ. Prac. & Rem. Code Ann. § 33.003 (West 2014).
21. *Id.* § 33.001.
22. *Id.* § 33.012(a).
23. *Id.* § 33.012(b).
24. *Id.* § 33.013(a).
25. *Id.* § 33.013(b).

percentage of responsibility.[26] Other hydrocarbon producing states have enacted similar comparative fault schemes.[27]

II. CONTRACTUAL INDEMNITY

Contractual indemnity is a method contracting parties may use to determine which party will be held responsible for certain losses. "An indemnity agreement is a promise to safeguard or hold the indemnitee harmless against either existing and/or future loss liability."[28] As a result, contractual indemnity allows contracting parties to manage and shift risks that are associated with a particular venture. Contractual indemnity is most closely associated with shifting the risk of damage to persons or property.

Indemnity agreements are construed and analyzed under the same principals applicable to any other contract.[29] Thus, the primary goal is to ascertain and give effect to the parties' intent as expressed in the contract.[30] When the contract is worded so that it can be given a certain or definite legal meaning, it is not ambiguous, and the court will construe the contract as a matter of law.[31]

A. Indemnity Provisions Come in All Shapes and Sizes

Indemnity provisions can take many different forms. More narrow indemnity provisions may require the indemnitor to indemnify the indemnitee only to the extent that the indemnitor is at fault for causing or contributing to the loss. In addition, it may only apply to personal injury or property damage or both. Intermediate indemnity provisions may require that the indemnitor indemnify the indemnitee relating to the subject of the

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26. TEX. CIV. PRAC. & REM. CODE ANN. § 33.015 (West 2014).
27. LA. CIV. CODE ANN. art. 2323 (2014) (Louisiana's pure comparative fault scheme); OKLA. STAT. ANN. tit. 23, § 13 (West 2014) (Oklahoma's modified comparative fault scheme); 42 PA. CONS. STAT. ANN. § 7102 (West 2014) (Pennsylvania's pure comparative fault scheme); N.D. CENT. CODE ANN. § 32-03.2-02 (West 2014) (North Dakota's modified comparative fault scheme).
28. Dresser Indus., Inc. v. Page Petroleum, Inc., 853 S.W.2d 505, 508 (Tex. 1993); *see also* Okla. Stat. Ann. tit. 15, § 421 (West) ("Indemnity is a contract by which one engages to save another from a legal consequence of the conduct of one of the parties, or of some other person.").
29. Crimson Exploration, Inc. v. Intermarket Mgmt., *LLC*, 341 S.W.3d 432, 441 (Tex. App.—Houston [1st Dist.] 2010, no pet.).
30. Gulf Ins. Co. v. Burns Motors, Inc., 22 S.W.3d 417, 423 (Tex. 2000).
31. *Id.*

agreement, except for injury or loss caused by the indemnitee's sole negligence. In addition, it may protect against injury or loss caused by other contractors. The broadest form of indemnity provisions may require that the indemnitor indemnify the indemnitee for all losses regardless of fault, including losses caused by the sole or concurrent negligence of the indemnitee. In addition, the indemnitor may indemnify the indemnitee's other contractors or protect against injury or loss caused by the sole negligence of the indemnitee's other contractors or both.

Indemnifying third parties to the contract is called "pass-through" indemnity. There are different ways to accomplish pass-through protection. One method is for the indemnitor to agree to indemnify the indemnitee from any contractual liability to third parties.[32] A second method would be to specify that the indemnity obligation is owed to the indemnitee and anyone to whom the indemnitee owes contractual indemnity.[33] A third method would be to expand the categories of persons or companies entitled to indemnity protection to include the indemnitee and its contractors and subcontractors.[34]

The language of the contract will determine the breadth of the indemnity obligation, whether there is indemnity from damages or from liability, whether there is a duty to defend in addition to the duty to indemnify, and thus the amount of risk shifted from one party to another.[35]

B. Extraordinary Risk Shifting and Fair Notice

The broader an indemnity provision is written, the more risk is shifted, and the more value it will have to an indemnitee. As a practical matter, from a personal injury or property damage standpoint, a defendant is usually sued because it allegedly did something wrong. Many times it is alleged that the defendant was negligent. As a result, in the oil and gas industry, broad-form indemnity provisions known as "knock-for-knock" provisions are often used. In broad-form knock-for-knock indemnity provisions, the indemnitor agrees to indemnify the in-

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32. Nabors Drilling USA, L.P. v. Encana Oil & Gas (USA) Inc., No. 02-12-00166-CV, 2013 WL 3488152, at *5 n.5 (Tex. App.—Fort Worth July 11, 2013, pet. denied) (mem. op.) (citing William W. Pugh, *A Strategic Look at the Bigger Picture—Risk Allocation in Oil and Gas Operational Agreements*, 45 Rocky Mtn. Min. L. Found. J. 349, 354 (2008)).
33. *Id.*
34. *Id.*
35. *Gulf Ins. Co.*, 22 S.W.3d at 423.

demnitee for injury or damage to personnel or property of the indemnitor (or indemnitor's contractors), including injury or damage caused by the sole or concurrent negligence of the indemnitee. Many times, these broad knock-for-knock provisions will also indemnify the other party's contractors against injury or damage caused by the sole or concurrent negligence of the other party's contractors.

While Texas courts recognize that most contractual provisions operate to transfer risk, they consider the indemnification of a party for its own negligence an extraordinary shifting of risk.[36] As a result, Texas courts have developed fair notice requirements that apply to these types of agreements.[37] The Texas Supreme Court was concerned with contracting parties drafting indemnity provisions that were broad enough to indemnify one party for its own negligence, but just ambiguous enough to conceal the true intent from the indemnitor.[38] The result was a flood of litigation to construe those ambiguous contracts.[39] The Court held that "the better policy is to cut through the ambiguity of those provisions and adopt the express negligence doctrine."[40]

Therefore, any indemnity provision that attempts to indemnify one party for its own negligence (an "extraordinary indemnity provision") must (1) be conspicuous and (2) satisfy the express negligence rule.[41] Other states use variations of the less stringent "clear and unequivocal" test.[42]

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36. *Dresser Indus., Inc.*, 853 S.W.2d at 508.
37. *Id.*
38. *Ethyl Corp.*, 725 S.W.2d at 707–08.
39. *Id.* at 708.
40. *Id.*
41. Audubon Indem. Co. v. Custom Site-Prep, Inc., 358 S.W.3d 309, 319 (Tex. App.—Houston [1st Dist.] 2011, pet. denied).
42. *See, e.g.*, Polozola v. Garlock, Inc., 343 So.2d 1000, 1003 (La. 1977) ("A contract of indemnity whereby the indemnitee is indemnified against the consequences of his own negligence is strictly construed, and such a contract will not be construed to indemnify an indemnitee against losses resulting to him through his own negligent act, unless such an intention was expressed in unequivocal terms."); Bridston by Bridston v. Dover Corp., 352 N.W.2d 194, 196 (N.D. 1984) ("It is almost universally held that an indemnity agreement will not be interpreted to indemnify a party against the consequences of his own negligence unless that construction is very clearly intended."); Noble Steel, Inc. v. Williams Bros. Concrete Const. Co., 49 P.3d 766, 770 (Okla. Civ. App 2002) ("To be enforceable, the agreement must meet the following three conditions: (1) the parties must express their intent to exculpate in unequivocally clear language; (2) the agreement must result from an arm's-length transac-

The conspicuous requirement mandates "that something must appear on the face of the [contract] to attract the attention of a reasonable person when he looks at it."[43] "Language is conspicuous if it appears in larger type, contrasting colors, or otherwise calls attention to itself."[44] Whether an extraordinary indemnity provision meets the conspicuous requirement is a question of law for the court.[45]

An extraordinary indemnity provision that does not satisfy the conspicuous requirement is generally unenforceable as a matter of law.[46] However, an extraordinary indemnity provision that is not conspicuous can still be enforced if the indemnitee establishes that the indemnitor "possessed actual notice or knowledge of the indemnity agreement."[47] Merely reading the contract is not enough to trigger the actual notice exception; otherwise, the exception would swallow the rule.[48] Something more needs to be shown, such as the initialing of a specific change to the extraordinary indemnity provision in the contract.[49]

The other half of the fair notice requirement is called the "express negligence rule." The express negligence rule provides that a party seeking indemnity from the consequences of its own negligence must express that intent in specific terms.[50] The intent to release a party from the consequences of its own negligence must be unambiguous and stated in the four corners

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tion between parties of equal bargaining power; and (3) the exculpation must not violate public policy."); Ruzzi v. Butler Petroleum Co., 588 A.2d 1, 4 (Pa. 1991) ("The law has been well settled in this Commonwealth for 87 years that if parties intend to include within the scope of their indemnity agreement a provision that covers losses due to the indemnitee's own negligence, they must do so in clear and unequivocal language. No inference from words of general import can establish such indemnification.").

43. Am. Home Shield Corp. v. Lahorgue, 201 S.W.3d 181, 184 (Tex. App.— Dallas 2006, pet. denied); s*ee Storage & Processors, Inc. v. Reyes*, 134 S.W.3d 190, 192 (Tex. 2004) (quoting *Dresser Indus., Inc.*, 853 S.W.2d at 508).
44. *Am. Home Shield Corp.*, 201 S.W.3d at 184 (citing *Dresser Indus., Inc.*, 853 S.W.2d at 508).
45. *Dresser Indus., Inc.*, 853 S.W.2d at 509.
46. *Am. Home Shield Corp.*, 201 S.W.3d at 184.
47. *Id.* at 186 (quoting *Dresser Indus., Inc.*, 853 S.W.2d at 508 n.2).
48. *Id.* at 186–7.
49. Chesapeake Operating, Inc. v. Nabors Drilling USA, Inc., 94 S.W.3d 163, 169 (Tex. App.— Houston [14th Dist.] 2002, no pet.).
50. *Ethyl Corp.*, 725 S.W.2d at 708.

of the document.[51] Courts have interpreted this to mean that the contract must include the word "negligence" or some synonym thereof.[52] The Texas Supreme Court has specifically blessed language to the effect that the indemnitor agrees to indemnify the indemnitee "in any matter arising from the work performed hereunder, including but not limited to *any negligent act or omission of* [indemnitee]."[53] Absent language stating a clear intent to indemnify a party for its own negligence, there is no obligation to do so.[54] Whether the express negligence rule is satisfied is also a question of law for the court.[55]

These fair notice requirements will come into play any time an indemnitee attempts to shift any portion of the risk or consequences of its own negligence onto the indemnitor.[56] Even comparative indemnity provisions must comply with the fair notice requirements.[57] However, the fair notice requirements do not apply where the indemnitee is not attempting to shift the consequences of its own negligence onto the indemnitor. For example, in *DDD Energy, Inc. v. Veritas DGC Land, Inc.*, DDD Energy owned a working interest in an oil and gas lease.[58] DDD Energy contracted with Veritas DGC Land to conduct field geophysical surveys and related services on the lease.[59] The contractual indemnity provision stated,

> [Veritas DGC Land] shall protect, indemnify, defend and save [DDD Energy], . . . harmless from and against all claims, . . . and causes of actions . . . asserted by third parties on account of . . . damage to property of such third parties, which . . . damage is the result of the negligent act or omission, breach of this Basic

51. *Ethyl Corp.*, 725 S.W.2d at 708; Oxy USA, Inc. v. Sw. Energy Prod. Co., 161 S.W.3d 277, 282 (Tex. App.—Corpus Christi 2005, pet. denied).
52. Lee Lewis Const., Inc. v. Harrison, 64 S.W.3d 1, 21 n.13 (Tex. App.—Amarillo 1999), *aff'd*, 70 S.W.3d 778 (Tex. 2001).
53. *Atl. Richfield Co. v. Petroleum Pers., Inc.*, 768 S.W.2d 724, 726 (Tex. 1989).
54. *Ethyl Corp.*, 725 S.W.2d at 708.
55. *Dresser Indus., Inc.*, 853 S.W.2d at 509.
56. *Ethyl Corp.*, 725 S.W.2d at 708.
57. *Id.* ("Indemnitees seeking indemnity for the consequences of their own negligence which proximately causes injury jointly or concurrently with the indemnitor's negligence must also meet the express negligence test.").
58. DDD Energy, Inc. v. Veritas DGC Land, Inc., 60 S.W.3d 880, 882 (Tex. App.—Houston [14th Dist.] 2001, no pet.).
59. *Id.*

> Agreement or the Supplemental Agreement, or willful misconduct of [Veritas DGC Land] . . . . Likewise, [DDD Energy] shall protect, indemnify, defend and save [Veritas DGC Land], . . . harmless from and against all claims, . . . causes of action . . . asserted by third parties on account of . . . damage to property of such third parties, which . . . damage is the result of the negligent act or omission of willful misconduct of [DDD Energy].[60]

Veritas DGC Land hired a third party to conduct brush-clearing operations on the lease.[61] Those operations resulted in destruction of numerous oak and mesquite trees.[62] The lessor filed suit against DDD Energy asserting claims for (1) breach of duty to manage and administer the lease, (2) breach of contract, (3) negligence, (4) malicious trespass, (5) negligent misrepresentation, (6) breach of fiduciary duty, (7) gross negligence, and (8) intentional tort.[63] DDD Energy then sought a declaratory judgment stating that Veritas DGC Land was obligated to defend and indemnify DDD Energy from the claims asserted by the landowner.[64] The trial court ruled that the indemnity provision was unenforceable as it failed to comply with the fair notice requirements; DDD Energy appealed the trial court's ruling on the duty to indemnify.[65]

The appellate court held that the express negligence rule was directly implicated because the landowner in the underlying lawsuit asserted several negligence-based claims against DDD Energy.[66] The indemnity provision at issue contained no hint that DDD Energy was to be indemnified for its own negligence.[67] As a result, DDD Energy was not entitled to indemnity from Veritas DGC Land for the landowner's claims based on DDD Energy's negligence.[68]

However, DDD Energy was entitled to indemnity from Veritas DGC Land for the landowner's non-negligence-based claims

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60. *Id.*
61. *Id.*
62. *Id.*
63. *Id.*
64. *DDD Energy, Inc.*, 60 S.W.3d at 882.
65. *Id.*
66. *Id.* at 884.
67. *Id.*
68. *Id.* at 884–85.

against DDD Energy.[69] The case was sent back to the trial court to determine which of the other claims asserted by the landowner against DDD Energy fell within the purview of the indemnity agreement between DDD Energy and Veritas DGC Land.[70] Therefore, the indemnity provision was not as valuable as DDD Energy originally thought.

The bottom line is that people and entities generally get sued because they allegedly did something wrong. Indemnity agreements that attempt to shift the risk of the indemnitee's negligence onto the indemnitor, yet fail to comply with the fair notice requirements in Texas, or "clear and unequivocal" requirements in other states, will be of little or no value when the indemnitee is sued for negligence. Although, as shown in *DDD Energy, Inc.*, that same indemnity agreement may still cover other claims against the indemnitee.

C. Anti-Indemnity Statutes

In addition to common law hurdles, the Texas and Louisiana legislatures, among others, have enacted anti-indemnity statutes to remedy the perceived inequity of indemnity provisions on contractors performing work on oil or gas wells.[71] In general, these statutes declare indemnity provisions attempting to indemnify the indemnitee for its own negligence void.[72] However, there are exceptions, so understanding how these statutes operate is essential to draft an effective indemnity agreement.

i. Texas Oilfield Anti-Indemnity Act

The Texas Oilfield Anti-Indemnity Act ("TOAIA") invalidates indemnity agreements that purport to indemnify a person against loss or liability for damage that is caused by or results from the sole or concurrent negligence of the indemnitee and arises from personal injury, property damage, or related expenses.[73] The TOAIA applies if the indemnity obligation is con-

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69. *Id.* at 885; *see Audubon Indem. Co.*, 358 S.W.3d at 320.
70. *DDD Energy, Inc.*, 60 S.W.3d at 885 (*DDD Energy, Inc.* did not involve whether or not Veritas DGC Land had a duty to defend DDD Energy or the scope of that duty.); *English v. BGP Intern., Inc.*, 174 S.W.3d 366, 375 (Tex. App.—Houston [14th Dist.] 2005, no pet.).
71. TEX. CIV. PRAC. & REM. CODE ANN. § 127.002 (West 2014); LA. REV. STAT. ANN. § 9:2780A (2014).
72. TEX. CIV. PRAC. & REM. CODE ANN. § 127.003 (West 2014); LA. REV. STAT. ANN. § 9:2780B (2014).
73. TEX. CIV. PRAC. & REM. CODE ANN. § 127.003 (West 2014).

tained in, collateral to, or affecting an agreement "pertaining to" a well for oil, gas, or water, or to a mine for a mineral.[74] An agreement pertains to a well for oil, gas, or water, or to a mine for a mineral if it concerns the rendering of well or mine services, an agreement to perform a part of those services, or an act collateral to those services. Collateral acts to these services include furnishing or renting equipment, incidental transportation, or other goods and services furnished in connection with the services.[75]

The TOAIA does not apply to loss or liability for damages arising from (1) personal injury, death, or property damage that results from radioactivity; (2) property damage that results from pollution, including cleanup and control of the pollutant; (3) property damage that results from reservoir or underground damage, including loss of oil, gas, other mineral substance, or water, or the wellbore itself; (4) personal injury, death, or property damage that results from the performance of services to control a wild well to protect the safety of the general public or to prevent depletion of vital natural resources; or (5) cost of control of a wild well, underground or above the surface.[76]

The TOAIA does not apply to an indemnity agreement if the parties agree in writing that the indemnity obligation will be supported by liability insurance coverage to be furnished by the indemnitor.[77] With respect to mutual indemnity obligations, the indemnity obligation is limited to the extent of the coverage and dollar limits of insurance or qualified self-insurance each party as indemnitor has agreed to obtain for the ben-

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74. *Id.*

75. *Id.* § 127.001. "Well or mine service" includes drilling, deepening, reworking, repairing, improving, testing, treating, perforating, acidizing, logging, conditioning, purchasing, gathering, storing, or transporting oil, brine water, fresh water, produced water, condensate, petroleum products, or other liquid commodities, or otherwise rendering service in connection with a well drilled to produce or dispose of oil, gas, other minerals, or water. *Id.* It also includes designing, excavating, constructing, improving, or otherwise rendering services in connection with a mine shaft, drift, or other structure intended for use in exploring for or producing a mineral. *Id.* However, it does not include purchasing, selling, gathering, storing or transporting gas or natural gas liquids by pipeline or fixed associated facilities or construction, maintenance, or repair of oil, natural gas liquids, or gas pipelines or fixed associated facilities. *Id.*

76. *Id.* § 127.004.

77. *Id.* § 127.005(a).

efit of the indemnitee.[78] With respect to unilateral indemnity obligations, the amount of insurance required may not exceed $500,000.00.[79] Moreover, the TOAIA does not invalidate insurance obligations that are independent from the indemnity provision.[80]

Also, the TOAIA does not apply to joint operating agreements.[81] Finally, the TOAIA does not prevent an owner of the surface estate from securing indemnity from a lessee, operator, contractor, or other person conducting operations for the exploration or production of minerals on the owner's land.[82]

ii. Louisiana Oilfield Indemnity Act

The Louisiana Oilfield Indemnity Act ("LOIA") invalidates indemnity agreements to the extent that it provides for defense or indemnity to the indemnitee for death or bodily injury to persons caused by the indemnitee's sole or concurrent negligence or fault.[83] The LOIA also invalidates any provision that requires waivers of subrogation, additional named insured endorsements, or any other form of insurance protection that would frustrate the LOIA.[84] The LOIA applies if two conditions are

78. *Id.* § 127.005(b). "Mutual indemnity obligation" means an indemnity obligation in an agreement pertaining to a well for oil, gas, or water or to a mine for a mineral in which the parties agree to indemnify each other and each other's contractors and their employees against loss, liability, or damages arising in connection with the bodily injury, death, and damage to property of the respective employees, contractors or their employees, and invitees of each party arising out of or resulting from the performance of the agreement. *Id.* § 127.001(3).
79. TEX. CIV. PRAC. & REM. CODE ANN. § 127.005(c) (West 2014). "Unilateral indemnity obligation" means an indemnity obligation in an agreement pertaining to a well for oil, gas, or water or to a mine for a mineral in which one of the parties as indemnitor agrees to indemnify the other party as indemnitee with respect to claims for personal injury or death to the indemnitor's employees or agents or to the employees or agents of the indemnitor's contractors but in which the indemnitee does not make a reciprocal indemnity to the indemnitor. *Id.* § 127.001(6).
80. Getty Oil Co. v. Ins. Co. of N. Am., 845 S.W.2d 794, 804 (Tex. 1992).
81. TEX. CIV. PRAC. & REM. CODE ANN. §§ 127.001(1)(B), 127.002(c) (West 2014).
82. *Id.* § 127.007.
83. LA. REV. STAT. ANN. § 9:2780B (2014).
84. LA. REV. STAT. ANN. § 9:2780G (2014); Babineaux v. McBroom Rig Bldg. Serv., Inc., 806 F.2d 1282, 1283–84 (5th Cir. 1987). In the insurance context, an exception is available where the indemnitee pays for its coverage. For example, in *Marcel v. Placid Oil Co.*, the Fifth Circuit Court of Appeals recognized that if the principal pays for its own liability cov-

met.[85] First, there must be an agreement "pertaining to a well for oil, gas, or water, or drilling for minerals."[86] "The decisive factor in most cases has been the functional nexus between an agreement and a well or wells."[87] Second, the agreement must be related to the exploration, development, production, or transportation of oil, gas, or water.[88]

The LOIA does not affect the validity of an operating agreement or farm out agreement to the extent it purports to provide for defense or indemnity to the indemnitee for death or bodily injury to persons caused by the indemnitee's sole or concurrent

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erage, no risk shifting occurs. *Marcel v. Placid Oil Co.*, 11 F.3d 563, 459 (5th Cir. 1994). Therefore, such arrangements fall outside of the LOIA. Notably, in order for this exception to apply, no material part of the cost of insuring the indemnitee can be borne by the indemnitor procuring the insurance coverage. *Id.* at 570.

85. Fontenot v. Chevron U.S.A. Inc., 95-1425 (La. 7/2/96), 676 So.2d 557, 564.

86. LA. REV. STAT. ANN. § 9:2780B (2014); *Fontenot*, 95-1425 (La. 7/2/96), 676 So.2d 557, 564.

87. Verdine v. Ensco Offshore Co., 255 F.3d 246, 252 (5th Cir. 2001). Other factors include

> whether the structures or facilities to which the contract applies or with which it is associated, e.g. production platforms, pipelines, junction platforms, etc., are part of an in- field gas gathering system; (2) what is the geographical location of the facility or system relative to the well or wells; (3) whether the structure in question is a pipeline or is closely involved with a pipeline; (4) if so, whether that line picks up gas from a single well or a single production platform or instead carries commingled gas originating from different wells or production facilities; (5) whether the pipeline is a main transmission or trunk line; (6) what is the location of the facility or structure relative to compressors, regulating stations, processing facilities or the like; (7) what is the purpose or function of the facility or structure in question; (8) what if any facilities or processes intervene between the wellhead and the structure or facility in question, e.g., "heater treaters," compressor facilities, separators, gauging installations, treatment plants, etc.; (9) who owns and operates the facility or structure in question, and who owns and operates the well or wells that produce the gas in question; (10) and any number of other details affecting the functional and geographic nexus between "a well" and the structure or facility that is the object of the agreement under scrutiny.

Transcon. Gas Pipe Line Corp. v. Transp. Ins. Co., 953 F.2d 985, 994–95 (5th Cir. 1992).

88. LA. REV. STAT. ANN. § 9:2780C (2014); *Fontenot*, 95-1425 (La. 7/2/96), 676 So.2d 557, 564.

negligence or fault.[89] However, this exception will not apply if the work is performed pursuant to a different agreement.[90]

The LOIA also does not apply to loss or liability for damages or any other expenses resulting from (1) bodily injury or death to persons arising out of or resulting from radioactivity; (2) bodily injury or death to persons arising out of or resulting from the retainment of oil spills and clean-up and removal of structural waste subsequent to a wild well, failure of incidental piping or valves and separators between the well head and the pipeline, or failure of pipelines, so as to protect the safety of the general public and the environment; or (3) bodily injury or death arising out of or resulting from performance of services to control a wild well so as to protect the safety of the general public or to prevent depletion of vital natural resources.[91]

Another exception to the LOIA is reimbursement of defense costs in the event of a meritless suit.[92] In *Meloy v. Conoco, Inc.*, the contract stated that the "Contractor further agrees to have any such claim, demand, or suit instigated, handled, responded to and defended at no cost to Company, . . . even if such claim, demand, or suit is groundless, false or fraudulent."[93] The Louisiana Supreme Court held that a contract provision for defense costs in the event of agroundless or meritless lawsuit is outside the scope of the LOIA.[94] As a result, an indemnitee may seek defense costs if there is a judicial finding that the indemnitee was neither negligent nor at fault.[95]

Finally, the LOIA does not prevent a royalty owner from securing an indemnity from any lessee, operator, contractor, or

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89. La. Rev. Stat. Ann. § 9:2780D(2) (2014). An "operating agreement" is defined as "any agreement entered into by or among the owners of mineral rights for the joint exploration, development, operation, or production of minerals." *Id.* § 9:2780D(2)(a). A "farmout agreement" is defined as "any agreement in which the holder of the operating rights to explore for and produce minerals, the 'assignor,' agrees that it will, upon completion of the conditions of the agreement, assign to another, the 'assignee,' all or a portion of a mineral lease or of the operating rights." *Id.* § 9:2780D(2)(b).
90. *Id.* § 9:2780D(2).
91. *Id.* § 9:2780F(1)–(3). "Wild well" means "any well from which the escape of salt water, oil, or gas is unintended and cannot be controlled by the equipment used in normal drilling practices." La. Rev. Stat. Ann. § 9:2780F.
92. Meloy v. Conoco, Inc., 504 So. 2d 833, 839 (La. 1987).
93. *Id.* at 836 n.4.
94. *Id.* at 839.
95. *Id.*

other person conducting exploration and production operations with the reserved mineral rights.[96] For this exception to apply, the royalty owner cannot retain a working interest or an overriding royalty interest convertible to a working interest.[97]

iii. Wyoming Act

The Wyoming Oilfield Anti-Indemnity Act ("WOAIA") invalidates indemnity agreements to the extent that they relieve the indemnitee from loss or liability for personal injury or property damage, or loss, damage, or expenses from either, arising from (1) the negligence of the indemnitee or the agents or employees of the indemnitee or any independent contractor who is directly responsible to such indemnitee or (2) any accident which occurs in operations carried on at the direction or under the supervision of the indemnitee or an employee or representative of the indemnitee or in accordance with methods and means specified by the indemnitee or employees or representatives of the indemnitee.[98] The WOAIA applies if the indemnity obligation is "contained in, collateral to, or affecting any agreement pertaining to any well for oil, gas, or water, or mine for any mineral."[99]

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96. LA. REV. STAT. ANN. § 9:2780B (2014).
97. *Id.*
98. WYO. STAT. ANN. § 30-1-131 (2014).
99. *Id.*

> The term "agreement pertaining to any well for oil, gas, or water, or mine for any mineral" as used in W. S. 30-1-131, means any agreement or understanding, written or oral, concerning any operations related to drilling, deepening, reworking, repairing, improving, testing, treating, perforating, acidizing, logging, conditioning, altering, plugging, or otherwise rendering services in or in connection with any well drilled for the purpose of producing or disposing of oil, gas or other minerals, or water, and designing, excavating, constructing, improving, or otherwise rendering services in or in connection with any mine shaft, drift, or other structure intended for use in the exploration for or production of any mineral, or an agreement to perform any portion of any such work or services or any act collateral thereto, including the furnishing or rental of equipment, incidental transportation, and other goods and services furnished in connection with any such service or operation.

Id. § 30-1-132. *See also Reliance Ins. Co. v. Chevron U.S.A. Inc.*, 713 P.2d 766, 770 (Wyo. 1986) (holding that a party contracting to dig pits to

An indemnity provision violating the WOAIA is not void and unenforceable in total, but only to the extent that it violates the statute.[100] In addition, indemnification is not prohibited except for the indemnitee's own negligence.[101] As a result, the WOAIA is not applicable when the indemnitee is not negligent but is liable only under the theory of *respondeat superior*.[102]

The WOAIA specifically exempts agreements in which an owner of the surface estate seeks indemnity from any lessee, operator, contractor, or other person conducting operations for the exploration or production of minerals on such owner's land.[103] However, the WOAIA applies to unit operating agreements even when the agreements do not use the term "indemnity."[104]

iv. New Mexico Anti-Indemnity Act

The New Mexico Anti-Indemnity Act ("NMAIA") invalidates an indemnity agreement that "purports to indemnify the indemnitee against loss or liability for damages arising from" (1) the sole or concurrent negligence of the indemnitee or its agents or employees, (2) the sole or concurrent negligence of an independent contractor who is directly responsible to the indemnitee, or (3) an accident that occurs in operations carried on at the direction or under the supervision of the indemnitee or in accordance with methods and means specified by the indemnitee.[105] The NMAIA applies to "an agreement pertaining to a well for oil, gas, or water, or mine for a mineral, within New

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collect waste fluids from a fire at a separation plant was not "rendering services" in connection with a well for oil or gas).

100. Gainsco Ins. Co. v. Amoco Prod. Co., 53 P.3d 1051, 1075 (Wyo. 2002).

101. *Id.*

102. *Id.*

103. WYO. STAT. ANN. § 30-1-133 (2014).

104. Bolack v. Chevron, U.S.A., Inc., 963 P.2d 237, 242 (Wyo. 1998) ("While the contractual provisions at issue may be enforceable under other circumstances, in this instance they are being used to enforce the Unit Operating Agreement in a manner which patently violates Wyo. Stat. § 30–1–131.") In *Bolack*, Chevron attempted to charge non-negligent interest owners its "costs" to compensate workers who were seriously injured by Chevron's negligence. *Id.*

105. N.M. STAT. ANN. § 56-7-2 (West 2014).

Mexico."[106] Unlike other anti-indemnity statutes, the NMAIA is limited in scope to services at the well.[107]

D. Indemnity Against Liability vs. Indemnity Against Damages

The issue of indemnity for damages as opposed to indemnity for liability relates to timing. When can the indemnitee seek payment from the indemnitor? As soon as the indemnitee becomes liable, or only after the indemnitee has made the payment and actually suffered the loss?

"The traditional rule of strict indemnity requires the indemnitor to reimburse only actual loss and not to discharge the liability of the indemnitee."[108] Therefore, indemnity would only be owed after the indemnitee has suffered damage or injury by being compelled to pay the judgment or debt.[109] This is a firmly established part of the law of indemnity contracts and is consistent with the favoritism the law has for indemnitors.[110] For example, in *Russell v. Lemons*, the Amarillo Court of Appeals held that an indemnity provision stating "I here and now guarantee to hold M. W. Lemons harmless and to protect him against whatever judgment, if any, may be entered against the said M.

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106. *Id.* An "agreement pertaining to a well for oil, gas or water, or mine for a mineral" means an agreement:

> concerning any operations related to drilling, deepening, reworking, repairing, improving, testing, treating, perforating, acidizing, logging, conditioning, altering, plugging or otherwise rendering services in connection with a well drilled for the purpose of producing or disposing of oil, gas or other minerals or water;
> for rendering services in connection with a mine shaft, drift or other structure intended for use in the exploration for or production of a mineral; or
> to perform a portion of the work or services described in Paragraph (1) or (2) of this subsection or an act collateral thereto.

107. *Id.*; Holguin v. Fulco Oil Services L.L.C., 245 P.3d 42, 48 (N.M. Ct. App. 2010).
108. Hernandez v. Great Am. Ins. Co. of New York, 464 S.W.2d 91, 93 (Tex. 1971).
109. Tubb v. Bartlett, 862 S.W.2d 740, 750 (Tex. App.—El Paso 1993, writ denied); *See also* Okla. Stat. Ann. tit. 15, § 427 (West 2014) ("Upon an indemnity against claims or demands, or damages or costs, expressly, or in other equivalent terms, the person indemnified is not entitled to recover without payment thereof.").
110. *Hernandez*, 464 S.W.2d at 93.

W. Lemons in said [lawsuit]" was an agreement to indemnify Lemons only after he suffered actual loss.[111]

However, as we have seen above, the indemnitor may contractually agree to indemnify the indemnitee from liability for a loss. With regard to indemnity against liability, indemnity is owed when the liability has become fixed and certain, as by rendition of a judgment.[112] It does not matter whether or not the indemnitee has suffered actual damages, such as actual payment of the judgment.[113] "Broad language . . . that holds the indemnitee 'harmless' against 'all claims' and 'liabilities' evidences an agreement to indemnify against liability."[114] However, the word "liability" is not necessary. For example, in *Tubb v. Bartlett*, the El Paso Court of Appeals held that an agreement "to indemnify JIM BARTLETT against all debts and obligations, claims and demands, arising out of BIG HORN ENERGY, OTEC, INC. and its subsidiaries" was an agreement to indemnify Bartlett whenever the liability was certain.[115]

E. Duty to Defend vs. Duty to Indemnify

Many indemnity provisions include the time tested language that the indemnitor will "defend, indemnify and hold harmless" the indemnitee or a slight variation thereof.[116] Texas courts have held "indemnify" and "hold harmless" to be synonymous.[117] Generally, the duty to indemnify includes the duty to

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111. *Russell v. Lemons*, 205 S.W.2d 629, 631-32 (Tex. Civ. App.—Amarillo 1947, writ ref'd n.r.e.).
112. Ingersoll-Rand Co. v. Valero Energy Corp., 997 S.W.2d 203, 207 (Tex. 1999).
113. *Id.*
114. *Id.*; *see also* Okla. Stat. Ann. tit. 15, § 427 (West 2014) ("Upon an indemnity against liability, expressly, or in other equivalent terms, the person indemnified is entitled to recover upon becoming liable.").
115. *Tubb*, 862 S.W.2d at 750.
116. *See*, *e.g.*, Spawglass, Inc. v. E.T. Services, Inc., 143 S.W.3d 897, 901 (Tex. App.—Beaumont 2004, pet. denied) (using "defend, hold harmless and unconditionally indemnify"); *DDD Energy, Inc.*, 60 S.W.3d at 882 (using "shall protect, indemnify, defend and save [DDD Energy] . . . harmless").
117. MG Bldg. Materials, Ltd. v. Moses Lopez Custom Homes, Inc., 179 S.W.3d 51, 64 (Tex. App.—San Antonio 2005, pet. denied) ("The language used in the assignment of lien provision providing that Lopez agreed to 'hold MG harmless' from any loss, claim, or expense arising out of construction of the Gonzales home constitutes an indemnity agreement. . . ."); Bank of El Paso v. Powell, 550 S.W.2d 383, 385 (Tex. Civ. App.—El Paso 1977, no writ) ("The net effect of the [hold harmless]

pay for all costs and expenses associated with defending suits against the indemnitee.[118] In *Fisk Electric Co. v. Constructors & Associates, Inc.*, the Texas Supreme Court addressed the issue of "whether an indemnitor . . . must pay attorney's fees and other expenses incurred by an indemnitee . . . when the indemnitee is accused of negligence, but not found to be negligent, and the indemnity agreement does not meet the express negligence test."[119] The court held that "[a]bsent a duty to indemnify there is no obligation to pay attorney's fees."[120] The general rule in Texas is simple: if you are entitled to indemnity, you are entitled to costs and expenses associated with defending the underlying lawsuit; if you aren't entitled to indemnity, you are not entitled to such costs and expense associated with defending the underlying lawsuit.[121]

However, in Texas, the duty to defend is a completely separate obligation from the duty to indemnify.[122] When an indemnity provision states that an indemnitor will *defend* an indemnitee, it raises the distinct obligation to defend.[123] The duty to defend is determined by the language in the indemnity agreement and the factual allegations in the underlying pleadings.[124] The indemnitor is not required to defend a suit against the indemnitee if the underlying pleadings do not allege facts within the scope of the indemnity agreement.[125] In determining whether there is a duty to defend, the focus of the inquiry is on

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agreement was that the customer agreed to indemnify the Bank for any loss it incurred, but not to discharge the liability of the Bank.").

118. *English*, 174 S.W.3d at 371.
119. Fisk Elec. Co. v. Constructors & Associates, Inc., 888 S.W.2d 813 (Tex. 1994).
120. *Id.* at 815.
121. *But c.f. Meloy*, 504 So. 2d at 839 (stating the Louisiana Supreme Court has held that parties may agree to provide costs of defense in the event a meritless suit is brought against the indemnitee and that such an agreement is outside the scope of the LOIA; in such a case, whether the indemnity is negligent or not can only be determined after a trial on the merits: "If it is established at trial that there is no 'negligence or fault (strict liability) on the part of the indemnitee,' the [LOIA] does not prohibit indemnification for cost of defense.").
122. *English*, 174 S.W.3d at 371.
123. *Id.* at 373; *cf.* Okla. Stat. Ann. tit. 15, § 427 (West) ("An indemnity against claims or demands, or liability, expressly or in other equivalent terms, embraces the costs of defense against such claims, demands or liability incurred in good faith, and in the exercise of reasonable discretion.").
124. *English*, 174 S.W.3d at 372.
125. *Id.*

the facts alleged, not the theories alleged.[126] The duty to defend for an indemnitor is the same as the duty to defend for an insurer.[127] And just as with insurers, an indemnitor may have a duty to defend but, eventually, no duty to indemnify.[128]

When some theories of liability give rise to a duty to defend but others do not, the indemnitor is still required to provide a defense.[129] Under the duty to defend, the indemnitor must defend against all claims—those that are covered and those that are not covered by the indemnity agreement.[130] To be sure, the express negligence rule will not relieve an indemnitor from providing a defense to negligence claims as long as there is a duty to defend and some of the underlying claims are covered by the indemnity contract.[131]

To avoid the obligation to defend in Texas, the word "defend" should be left out of the indemnity agreement.[132] Conversely, parties may expressly provide that one party will hold the other party harmless for any expenses, including attorneys' fees, incurred in connection with claims, without regard to whether indemnitor will ever be obligated to provide indemnification for the underlying loss.

III. JOINT OPERATING AGREEMENTS

A joint operating agreement ("JOA") is an agreement between working interest owners to explore for and produce oil and gas in certain lands. The JOA will, among other things, identify the property interests of the parties, commit the parties to participate in operations, provide how costs will be shared, and designate the operator.

As to sharing costs, under most JOAs, each party is responsible only for its percentage of costs. This intention is confirmed by the following paragraph in model form JOAs issued by the American Association of Professional Landmen:

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126. *Id.* at 373.
127. *See English*, 174 S.W.3d at 372 n.6 ("[W]e find little reason why the principles regarding an insurer's duty to defend should not apply with equal force to an indemnitor's contractual promise to defend its indemnitee.").
128. *See id.* at 371.
129. *Id.*
130. *Id.* at 374.
131. *Id.* at 375-76.
132. *Id.* at 374.

> The liability of the parties shall be several, not joint or collective. Each party shall be responsible only for its obligations, and shall be liable only for its proportionate share of the costs of developing and operating the Contract Area. . . . [N]o party shall have any liability to third parties hereunder to satisfy the default of any other party in the payment of any expense or obligation hereunder. It is not the intention of the parties to create, nor shall this agreement be construed as creating, a mining or other partnership, joint venture, agency relationship or association, or to render the parties liable as partners, co-venturers, or principals. In their relations with each other under this agreement, the parties shall not be considered fiduciaries or to have established a confidential relationship but rather shall be free to act on an arm's-length basis in accordance with their own respective self-interest, subject, however, to the obligation of the parties to act in good faith in their dealings with each other with respect to activities hereunder.[133]

In designating the operator, the JOA will generally provide that the operator shall conduct and direct and have full control of all operations on the contract area as permitted and required by, and within the limits of the JOA. All of the other working interest owners are imaginatively called "non-operators."

A. Cost Overruns

Before operations begin, the operator will typically issue an authorization for expenditure ("AFE") detailing the anticipated cost of the work, whether it is drilling, completing, or reworking a well. As one court stated:

> An AFE is a form which is widely used in the oil and gas industry when wells are drilled by multiple parties. The AFE sets forth the location of the well, its objective geological formation, an estimated depth at which that formation will be encountered, the estimated costs of drilling and completion, and miscellaneous other information. It is prepared by the "operator" of the well,

133. In re Great W. Drilling, Ltd., 211 S.W.3d 828, 832 n.1 (Tex. App.—Eastland 2006, no pet.).

> and execution of the AFE by the non-operating owners of the working interests in the underlying leaseholds is a written manifestation of their consent to participate in the well. It is axiomatic that drilling costs cannot be estimated with certainty and that an AFE is at best a good-faith estimate.[134]

It is common for actual costs to exceed those estimated in the AFE, often by substantial amounts.[135] This may cause the non-operators to question whether the operator acted appropriately and whether the non-operator should be liable for its share of the unanticipated costs.

The JOA will typically contain language to the affect that the operator will conduct "all such operations" or "its activities" in a good and workmanlike manner, but it shall have no liability as operator to the other parties for losses sustained or liabilities incurred except such as may result from gross negligence or willful misconduct, known as the exculpatory clause.[136] The Texas Supreme Court has held that this language will exempt an operator from liability for operations under the JOA unless the liability arises from gross negligence or willful misconduct.[137] Therefore, the operator and non-operators would all pay their share of any cost overruns unless the non-operator can prove that the cost overruns were the result of gross negligence or willful misconduct.[138] The exculpatory clause shifts at least some of the risk of cost overruns—even those resulting from the operator's negligence—onto the non-operators.

B. Third Party Litigation

Another situation that may arise under a JOA is that a third party may bring a suit against the operator for personal injury arising out of the operations conducted under the JOA.[139] The operator will incur costs defending the claim and possibly

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134. M&T, Inc. v. Fuel Resources Development Co., 518 F. Supp. 285, 289 (D. Colo. 1981).
135. *Id.*
136. Reeder v. Wood County Energy, LLC, 395 S.W.3d 789, 793 (Tex. 2012), opinion supplemented on reh'g (Mar. 29, 2013).
137. *Id.* at 797.
138. *Id.* at 794-95.
139. Scott Lansdown, *B. Reeder v. Wood County Energy LLC and the Application by Texas Courts of the "Exculpatory Clause" in Operating Agreements Used in Oil and Gas Operations*, 8 Tex. J. Oil Gas & Energy L 202, 220 (2013).

settling or paying a judgment.[140] JOAs recognize that such costs are the joint responsibility of the parties to the JOA.[141] For example, many JOA forms provide that the operator has authority to settle uninsured claims up to a certain dollar amount if the payment is in complete settlement of such claim or suit.[142] The JOA will further provide that "[a]ll costs and expenses of handling, settling, or otherwise discharging such claim or suit shall be at the joint expense of the parties participating in the operation from which the claim or suit arises."[143] Here, again, the exculpatory clause may come into play.[144] If the plaintiff was injured as a result of the operator's ordinary negligence, the exculpatory clause may save him from bearing all of the defense costs.[145] However, if a plaintiff claims and proves that he was injured as a result of the operator's gross negligence or willful misconduct, the operator may not be able to share the costs to defend and resolve the claim.[146] Similarly, if the exculpatory clause does not apply at all, the operator may not be able to share the costs to defend and resolve the claim merely because he acted negligently and failed to perform in a good and workmanlike manner.[147] As with cost overruns, the exculpatory clause shifts at least some of the risk of claims by third parties resulting from the actions of the operator onto the non-operators.

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140. *Id.*
141. *Id.*
142. *Id.*
143. *Id.* at 220–21.
144. *Id.* at 221–22.
145. Lansdown, *supra* note 139, at 222.
146. *Id.*
147. *Id. See Reeder*, 395 S.W.3d at 794 (The reach of the exculpatory clause depends on the language used in the JOA. Exculpatory clauses using the phrase "such operations" have been limited to claims arising out of operations in the field, excluding claims for mere breach of contract.) Thus, the operator would not be protected by an "operations" exculpatory clause and may bear the entire cost to defend and resolve a breach of contract claim by a third party. *See* Lansdown, *supra* note 139, at 222.

    Alternatively, exculpatory clauses using the phrase "its activities" have been interpreted to include claims for breach of the JOA. *Reeder*, 395 S.W.3d at 794. As a result, under an "activities" exculpatory clause, to recover damage from an operator for breach of the JOA, a non-operator would not only have to prove that the operator breached the JOA, but that the operator did it via gross negligence or willful misconduct. *Id.* at 794–95.

IV. CONCLUSION

Risk shifting is an integral function of contracts in the oil patch. This paper can only introduce some of the many facets as to how risk may and may not be shifted between contracting parties. Drafting enforceable indemnity provisions requires familiarity with the particular state's common law (fair notice requirements) and statutory law (anti-indemnity statutes). For one to have an understanding of risk shifting under a JOA means having an understanding of the difference between "such operations" and "its activities." This paper does not cover all aspects of Texas law, let alone those of other hydrocarbon-producing states. It does, however, introduce common issues that arise when people in the energy industry ask, "who is going to pay for that?!"