**Fundamental Considerations When**

**Entering into a Master Service Agreement**

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1. **INTRODUCTION AND OVERVIE****W**

A Master Service Agreement (or “MSA”) is a single document that defines the overall relationship between an E&P company and its providers of goods and services. MSAs typically are supplemented by purchase orders or work orders for individual projects by service contractors, and the written or oral terms of those orders can cause a number of expensive headaches when they modify the terms of an MSA. This session will identify the source of those headaches and will provide a number of proposed solutions.

Even if you are not normally charged with drafting or approving MSAs for your company, it is still worth your time to understand how these agreements come together and how the provisions of an MSA work in practice. An ounce of attention to the contents of an MSA up front can save a pound of litigation headaches down the line.

1. **MSA** **BASICS**

An MSA provides a frame of reference and a means of retaining a contractor or a subcontractor to perform work on a given project on either a one-time or long-term basis.

1. An MSA is more of a *framework* than a standalone contract.
2. Work orders provide specific details and scope of work.
3. Oral or written orders subject to the MSA create the detailed contracts.
4. MSAs are particularly useful for defining broad concepts common to oil & gas operations.
5. An MSA unifies assumptions and expectations for multiple parties.
6. It avoids or minimizes misunderstandings and, consequently, litigation.
7. **MSA APPLICATIONS**
8. **When is an MSA Appropriate?**
9. Not appropriate for all operations.
10. Best in situations involving a common workplace where employees of multiple companies are working in a *single* location.
11. Where many contractors might interact or where one contractors’ work process might affect the work process of another.
12. Where allocating fault after an accident would be difficult, expensive, and time consuming.
13. Where allocating risk on the basis of ownership, not fault, is acceptable.
14. **When is an MSA NOT Appropriate?**
15. Where there is no common workplace. For example, tool rental companies under an MSA would obtain reciprocal indemnity benefits without much risk because their staff seldom travels to the worksite. Absence of a common workplace undercuts the basic fault allocation assumptions which justify the use of an MSA.
16. Where one party controls a common workplace. For example, under a construction contract, the contractor generally has full control of the worksite and what occurs there. To serves no purpose to allocate fault to anyone else under this circumstance. MSAs work best when several contractors share responsibility for and access to the same workplace.
17. **An MSA Program Must Be Integrated**
18. An MSA must not be considered in isolation.
19. More than a contract, it’s a program to standardize effort and to manage risk.
20. Most beneficial when companies have as few MSA forms as possible.
21. Least beneficial when poorly managed and when different contractors are bound by different MSA forms with different terms and conditions (at least on issues that may affect multiple parties, such as indemnity).
22. **Interplay between MSAs and Other Jobsite Documentation**
23. Operations subject to an MSA almost always involve additional agreements and documentation such as work orders, delivery tickets, and invoices that relate to particular task governed by the MSA.
24. That fine print can contain interest provisions, liability releases, and even insurance and indemnity requirements.
25. Always have a primacy clause in your MSA that specifically negates any provisions contrary to the basic indemnity scheme in the MSA.
26. Also specifically state that field personnel are not permitted to agree to any fundamental changes in the risk allocation scheme for a particular operation or job. Consider this approach:

**Company specifically objects to and rejects any terms contained within Contractor’s purchase orders, work orders, invoices or delivery tickets that (i) conflict with the terms of this MSA or (ii) purport to affect the risk allocation scheme of this MSA or to add further requirements.**

1. **INDEMNITY BASICS**
2. Oil and gas operators mitigate risk through indemnity, insurance, and other contractual provisions in order to foster certainty and reduce litigation costs.
3. MSAs often touch on several risk factors, but indemnity is a particularly tricky area.
4. Indemnity is a legal term of art, but the basic principle of indemnity is that one party (the “indemnitor”) has contractually agreed to take responsibility for the liability of another party (the “indemnitee”).
5. **Common Indemnity Risk Allocation Schemes**

Each has its own merits, and the best scheme is often determined by a company’s contracting philosophy, market leverage, and the applicable law.

1. *Broad reciprocal indemnity* is a condition where each party accepts responsibility for loss to its own people and property and for the people and property of its contractors and subcontractors.
2. *Narrow reciprocal indemnity* is a condition where each party accepts responsibility for loss to its own people and property. The protection is extended to the indemnitee and closely-related entities.
3. *Modified reciprocal indemnity* is a hybrid.
4. **Indemnity for One’s Own Negligence**
5. To be successful, risk allocation requires that indemnity obligations be enforceable.
6. Indemnity for one’s own negligence or strict liability is a common contractual provision, but it must be clearly expressed in “unequivocal terms.”
7. “howsoever arising in any way directly or indirectly” is not “unequivocal.”
8. A good example is the model terms of the IADC Daywork Contract:

**[I]t is the intent of parties hereto that all releases, indemnity obligations and/or liabilities assumed by such parties ... be without limit and without regard to the cause or causes thereof including, but not limited to, pre-existing conditions, defect or** **ruin of premises or equipment, strict liability, regulatory or statutory liability, products liability, breach of representation or warranty (express or implied), breach of duty (whether statutory, contractual or otherwise) any theory of tort, breach of contract, fault, the negligence of any degree or character (regardless of whether such negligence is sole, joint or concurrent, active, passive or gross) of any party or parties, including the party seeking the benefit of the release, indemnity or assumption of liability, or any other theory of legal liability.**

1. **“Pass through” Indemnity**
2. Contractual liability to a third party flows through indemnity agreements.
3. Ensure that all relevant contracts contain complementary terms.
4. Consider anti-indemnity acts applicable to subcontracts.
5. Express language required that the indemnity applies not only to tort liability of the party to be indemnified, but also (particularly for the E&P company) for contractual indemnity that the party to be indemnified may owe to a third party (e.g., another contractor)
6. The categories of persons or companies entitled to indemnity protection needs to be express. For example, considering including the indemnitee’s affiliates, partners, owners, agents, and, if appropriate, its contractors and subcontractors. Define for clarity in the MSA as the “Company Group” and the “Contractor Group.”
7. **Indemnity for Damage to Third Parties**
8. Many MSAs do not account for true third parties (landowners, passersby, etc.).
9. MSAs modeled after the IADC contract forms contain preambles that purport to allocate to the E&P company all risk or loss that is not specifically addressed in the contract. Watch out for those.
10. In some reciprocal provisions, each party agrees to indemnify the other for third-party damage, potentially deferring to applicable state law.
11. Alternatively, provide that each party shall be responsible for damage to third-parties to the extent, but only to the extent, caused by that party.
12. **Indemnity for Gross Negligence and Punitive Damages**
13. Area of tension and dispute: negligence v. breach of warranty.
14. Consider drafting the provision to take effect only upon the contractor’s *material* breach of specified safety regulations or other critical warranties or obligations.
15. Should a contractor be indemnified when it is 100% at fault? To do so would reward a contractor for an action or inaction that should be discouraged.
16. Consider a separate provision for “gross negligence,” particularly in cases of indemnity “carve-out.”
17. The law is muddled and arcane whether provisions that purport to indemnify or release a party for its own “gross negligence” are or are not enforceable.
18. “Punitive damages” clauses may not be enforceable and may affect other contract terms. Consider a provision where punitive damages that are awarded for one party’s conduct shall be borne by that party.
19. **Pollution Damages**
20. Under IADC drilling contract forms, the contractor accepts responsibility without regard to fault for “all claims, demands and causes of action of every kind and character” arising from pollution that originates from above the surface of the land, and which is “wholly in Contractor’s possession and control and directly associated with Contractor’s equipment and facilities.” Such broad language and nested conditions limit the scope of the indemnity.
21. Consider instead an approach that looks similar to the IADC form contracts but removes the words “wholly” and “directly,” as well as replacing the conjunctive “ands” with the disjunctive “or,” such that the contractor is allocated pollution responsibility if only *one* of the requirements is met (at least for equipment not used underground):

**Contractor shall assume all responsibility for control and removal of pollution or contamination, which originates above the surface of the land or water from spills of fuels, lubricants, motor oils, pipe dope, paints, solvents, ballast, bilge or garbage that is in Contractor’s possession or control or is associated with Contractor’s equipment and facilities.**

1. **Indemnity for Fines**

Particularly for operations on the outer continental shelf (OCS), it is important to recognize that the E&P company can be subject to fines for acts or omissions of its contractors. The new Safety and Environmental Management System (SEMS) regulations by the Bureau of Safety and Environmental Enforcement (BSEE) are explicit on this point.

1. These BSEE regulations require operators to have agreements in place relating to responsibility for these safety requirements.
2. MSAs should reference these “SEMS Bridging Agreements” (and generally should provide that they do not trump any such Bridging Agreement).
3. Consider an indemnity provision for the contractor to indemnity the E&P company for any fines and penalties the E&P company may incur for the contractor’s breach of its Bridging Agreement.
4. **Common Indemnity Carve-Outs**
5. A “carve-out” is an exception to the basic reciprocal indemnity standard in an MSA.
6. Typical carve-outs include tool damage, reservoir damages, and well-control costs.
7. Beware of “standard carve-outs” provisions because parties can manipulate them.
8. Carve-outs can be an exception that swallows the rule. Some carve-outs are preceded by the preamble: “Notwithstanding anything else contained in this Agreement to the contrary…” Those are extremely powerful words that can cancel all indemnities.
9. Consider a hypothetical well blow-out, where an MSA recites, that “notwithstanding anything else contained in this Agreement to the contrary, all well control and reservoir damages shall be charged to the company’s account, regardless of fault.” What if people were injured during well control operations? Since the carve-out declares “notwithstanding anything else contained in this Agreement to the contrary,” did the parties intend that the basic reciprocal indemnity scheme regarding personnel would no longer apply?
10. Be very mindful whether a particular carve-out provision should or should not control of the general indemnity provisions.
11. In tool carve-outs, be sure to specify whether a carve-out/exception applies to all tools or only tools that are actually being used down hole; consider liability during transport; consider replacement cost vs. actual cost; consider contractor’s sole fault.
12. Beware also of warranty disclaimer provisions that are overly broad; they can impact the general indemnity obligations of the contractor. Be sure to limit the scope of any such warranty disclaimer by declaring that it has no impact whatsoever on the indemnity obligations.
13. **LEGAL LIMITATIONS TO INDEMNITY**

Many states and offshore sites have laws that invalidate certain MSA provisions.

1. **Louisiana**
2. The Louisiana Oilfield Indemnity Act (“LOIA”) invalidates indemnification agreements “pertaining to a well” for death or bodily injury, but it does not affect property damage indemnity agreements.
3. There is a judicially-recognized insurance work-around, known as the “Marcel” exception. Consider a provision where the E&P company pays its share of the additional premium necessary for the contractor to include the company (and its group) as additional insureds under the contractor’s insurance relating to death or bodily injury.
4. **Other States**
5. The Texas Oilfield Anti-Indemnity Act (“TOAIA”) is broader in scope than the LOIA. It covers indemnity for property claims in addition to bodily injury and death and also apply to pipelines (rather than just wells).
6. The TOAIA (unlike the LOIA) allows exceptions if the parties agree in writing to reciprocal indemnity that is supported by insurance.
7. **Offshore**

1. To the extent maritime law applies, parties are generally free to contract indemnity for one’s own negligence.
2. On fixed platforms, the Outer Continental Shelf Lands Act applies, which imports adjacent state law to any offshore dispute arising from acts on those platforms.
3. Fact-based disputes (location of platform or vessel; is it a platform or a vessel; was the person on a vessel or a platform when the accident occurred; which state is “adjacent”) can determine which statutory scheme or law applies.
4. **Construction Anti-Indemnity Statutes in Many States**

Approximately 39 states have broadly-worded anti-indemnity statutes pertaining to the construction industry.  Be sure to plan for their potential application to an MSA.

1. **Savings Clauses Can Temper the Effects of Indemnity Statutes**

When faced with an illegal or invalid requirement in a contract, a court may invalidate the *whole clause*, not just the specific invalid portion. Consider including a savings clause, for example:

**In the event that any provision in this MSA is deemed by a court of competent jurisdiction to be unenforceable under applicable law, then that provision shall be adjusted to the extent, but only to the extent, required to comply with applicable law.**

1. **Insurance Provisions and Work-Arounds Relating to Indemnity**
2. Indemnity provisions are typically backed by insurance. Don’t get into a position where you have a valid indemnity claim against another party, but that party has no money, and no insurance.
3. Add insurance terms to your MSA, and be sure that they always reflect the MSA’s indemnity provisions and carve-outs, including the scope and extent of each indemnity obligation.
4. Every MSA should specifically require contractual liability insurance at least as broad as the indemnity provisions in the MSA. Consider the following approach:

**Contractor shall obtain and maintain contractual liability insurance that provides coverage for all of the release, defense, indemnity, and hold harmless obligations undertaken by Contractor in Section \_\_\_ of this Agreement.**

1. Expired or cancelled insurance policies are worthless. The parties to an MSA should have prior notice of any party’s change in insured status. But most insurers will not agree to give notice to additional insureds. Thus, consider providing that (i) the contractor’s insurance policies require advance notice to the named insured (contractor) and (ii) the contractor notify the E&P company of any cancellation or change in the contractor’s insurance policies.
2. In the event of an invalid or unenforceable indemnity obligation, an insurance policy could ensure that the parties’ intent can still be recognized. Preparing valid and enforceable insurance policies in this area is a complex matter, but it may be worth the effort.
3. **OTHER COMMON MSA PROVISIONS**
4. **Standard of Performance**

Many MSAs do not provide a “standard of performance,” describing the level of skill or standard by which the work should be performed. Add the terms “Contractor shall perform the work in a good and workmanlike manner.” Alternatively, include a provision such as follows:

**Contractor shall perform all Work in compliance with all applicable laws, rules, and regulations (including without limitation all safety codes, statutes, regulations, precautions, and procedures) and utilizing all necessary or desirable protective equipment and devices, whether suggested or required by safety associations, government agencies, municipalities or otherwise. All Work shall be done with skill, care, and diligence, in a good and workmanlike manner, in accordance with the terms of this Agreement and the industry standards of performance. All materials, goods, and tools, machinery, and equipment shall be of sufficient quality for their purposes, be free from defect, meet all engineering standards and specifications provided by Company; and shall be prepared, tested, and shipped in accordance with the provisions hereof and in all applicable orders. Contractor, its subcontractors and their employees shall be sufficiently experienced, well supervised, and suitably trained to perform the Work.**

Be sure that a standard of performance in an MSA won’t affect the overall risk allocation scheme by declaring that the risk allocation scheme is enforceable regardless of “breach of contract and/or warranty.”

1. **Independent Contractor**

An independent contractor provision can help minimize risks due to negligence claims by emphasizing that the contractor is in charge of the specific details of the work. A sample provision is as follows:

**Contractor shall at all times be an independent contractor, and nothing in this Contract shall be construed as creating the relationship of principal and agent, or employer or employee, between Operator and Contractor or between Operator and Contractor’s agents or employees. Contractor shall have no authority to hire any persons on behalf of Operator, and any and all persons whom Contractor may employ shall be deemed to be solely the employees of Contractor. Contractor shall have control and management of the Work, the selection of employees and the fixing of their hours of labor, and no right is reserved to Operator to direct or control the manner in which the Work is performed, as distinguished from the result to be accomplished. Nothing herein contained shall be construed to authorize Contractor to incur any debt, liability, or obligation of any nature for or on behalf of Operator.**

An “independent contractor defense” can be particularly important if the indemnity or insurance protection owed to the company is unenforceable.

1. **Louisiana Statutory Employer**

Under Louisiana law, a “statutory employer” is entitled to immunity from tort claims asserted by its “statutory employees.” A statutory employer provision creates a rebuttable presumption of statutory employer status. But to obtain this immunity, there generally must be an express language in the MSA along the following lines:

**In all cases where Contractor’s employees (defined to include contractor’s direct, borrowed, special or statutory employees) are covered by the Louisiana Worker’s Compensation Act, La. R.S. 23:1021 et seq., Company and Contractor agree (a) that all Work performed by Contractor and its employees pursuant to this Agreement are an integral part of and are essential to the ability of Company to generate Company’s goods, products and services for purposes of La. R.S. 23:1061A(1) and (b) that Company is the principal or statutory employer of Contractor’s employees for the purposes of La. R.S. 23:1061A(3). Irrespective of Company’s status as the statutory employer or special employer (as defined in La. R.S. 23:1031C or otherwise) of Contractor’s employees, Contractor shall remain primarily responsible for the payment of worker’s compensation benefits to its employees and shall not be entitled to seek contribution for any such payments from Company.**

1. **Choice of Law**

Consider the effects of state law including anti-indemnity and implied warranty acts, the location of the majority of work, and whether that selection of law will be enforceable under the state law where the work will be performed. Declare that the law chosen is the “substantive law of the state, exclusive of its conflicts of law principles.”

1. **Payment**
2. Require a standard of performance. Contractors must earn the rate they charge.
3. A company should be required to pay only “properly supported” invoices.
4. Lots of room for dispute. A company can pay only parts of an invoice that it feels are valid, while a contractor can refuse to work until it gets paid.
5. Consider a right to withhold a disputed payment, but also ensure that any termination provision in the favor of the contractor for non-payment is expressly *subject to* the right to withhold.
6. Consider a provision that allows the company to pay disputed invoices without waiving its right to contest the propriety of payment and seek reimbursement:

**Payment by Company of any invoice shall be without prejudice and shall not constitute a waiver of Company’s right to question or to contest the amount or correctness of said invoice and to seek reimbursement.**

1. **Termination**
2. Always include a termination clause. Consider the ability to terminate an MSA or a particular purchase order for “just cause” or “material breach of contract.”
3. Consider the right to deduct any amounts payable as necessary to “protect the company from loss” or to repair any damage resulting from breach.
4. Termination for cause may lead to an expensive, fact-intensive argument. Consider a provision that allows the company to terminate the MSA or purchase order “at will” and for whatever reason, including the company’s convenience.
5. **Consequential Damages Waiver**
6. Ensure that the definition of consequential damages is broad to include lost hire, lost rental, loss of business opportunity, and unabsorbed overhead.
7. Be attentive whether you want an indemnity within the waiver that requires one party to indemnify the other for the consequential damage claims of third parties. It is very important to the E&P company that these provisions be consistent among its MSAs; otherwise, it may be taking on a significant unprotected risk that it cannot “pass through” to other contractors.
8. **NEGOTIATING, DRAFTING, AND MANAGING MSAs**
9. **Battle of the Forms**
10. The party who begins negotiations with its own form is at an advantage because it understands the contents, the past areas of contention, and the way that the separate provisions relate to each other.
11. The opposing party may not propose too many changes in order to communicate as sense of trust and goodwill.
12. **Drafting Standards**
13. Keep it clear and simple—easier to negotiate and interpret.
14. Use defined terms, avoid legalese.
15. Conspicuous provisions as needed.
16. **No Frankenstein Contracts!**
17. MSA is more of a program than a contract.
18. Always match the voice, style, and content.
19. Contracts evolve. Be sure that amendments preserve the intent of every provision.
20. **Contract Administration**
21. Execution is the key to success.
22. Monitor compliance with terms and forms.
23. Send timely objection letters—silence may equal consent.
24. **CONCLUSION**
25. MSAs are an integral and important part of the oil & gas industry.
26. MSAs promote efficiency, common understanding, and certainty in risk calculations.
27. MSAs should not be used for every task.
28. MSAs must be employed as a part of a *program* with consistency and with due regard for the impact that other contracts may have on their operations.
29. Understand how the MSA will interact with other contracts and how the risk allocation provisions will be impacted by applicable law.
30. The best MSA is not in a form manual. It should be designed for the company’s own operations and culture, and it should complement the company’s other contracts.