ENERGY & RESOURCES | JUNE 2021

ENGLISH HIGH COURT DECISION PROVIDES CLARITY ON OIL AND GAS DECOMMISSIONING REGULATIONS

The court examined the extent of decommissioning liability that would apply to a former licensee

In *Apache UK Investment Limited v Esso Exploration and Production UK Limited [2021] EWHC 1283 (Comm)*, parties were in dispute on the amount of security to be provided for decommissioning obligations in hydrocarbon producing fields in the North Sea.

Key Facts

- Under a LLC Sale and Purchase Agreement dated 21 September 2011 ("the **SPA**"), Apache UK Investment Limited ("**Apache**") acquired from Esso Exploration and Production UK Limited ("**Esso**") the sole legal and beneficial ownership in Apache Beryl I Limited ("**ABIL**"), then known as Mobil North Sea LLC ("**MNSL**"). ABIL holds licences in the Beryl, Buckland, Ness, Nevis, Skene and Maclure hydrocarbon producing fields in the North Sea (the "**Fields**").
- Apache and Esso entered into six Bilateral Decommissioning Security Agreements dated 31 December 2011 (the "**BDSAs**") in respect of the Fields.
- The BDSAs provide for security in respect of Apache's obligation under the SPA to indemnify Esso for all decommissioning related expenditures which Esso was or might become liable to incur whether such expenditures arose before, at or after the Effective Date of the SPA. The obligation to indemnify was further supported by a parent company guarantee provided by Apache Corporation, the ultimate parent company of Apache.
- On 26 March 2020, Apache Corporation ceased to be a "Qualifying Surety" under the BDSAs. The following day, Apache notified Esso of this, and indicated that it was arranging for the required letters of credit to be issued to Esso by 3 April 2020. The BDSAs provide a contractual process to determine the amount of the further security to be provided.
- On 23 June 2020 Apache sent its Proposed Plan for 2021 to Esso. Esso sent its formal objections to the Proposed Plan on 20 August 2020 and identified that 4 subsea wells relevant to the BDSAs and which were designated on the Fields had not been included in Apache's cost estimates ("**Additional Wells**"). These Additional Wells were drilled after Esso sold ABIL to Apache.
- Parties were in dispute over the operation of the process of determining the amount of security to be given by Apache, which involved 2 main issues:
  - construction of the BDSAs
  - the scope of liability for decommissioning costs under the Petroleum Act 1998 (the "**Act**")

Construction of BDSAs

When Apache Corporation ceased to be a "Qualified Surety" under the BDSAs, Apache was obliged to submit a proposed decommissioning schedule and budget (the "**Proposed Plan**") to Esso within 3 months. This was to cover an "*estimate of the highest net Cost during the immediately following Year (such immediately following Year being the ("**Relevant Year**")*)". It was intended that the Proposed Plan would provide a more accurate estimate of the security required by updating the historic figure provided in the BDSAs.

Apache provided a Proposed Plan for 2020 and 2021. However, Esso disregarded the 2020 Proposed Plan and only recognised the 2021 Proposed Plan on the basis that the definition of "Relevant Year" was the immediate following calendar year (i.e. 2021)

The High Court agreed with Esso's construction as it made more commercial common sense for the natural meaning of the Relevant Year to be the next calendar year, after the year in which the event occurs. Therefore, the Proposed Plan should be for 2021.

Extent of liability for decommissioning of Additional Wells

Parties' dispute over the security to be provided by Apache also engaged the issue of potential decommissioning obligations of Esso under the Act. The necessity to do so arose over a generally worded and wide indemnity in favour of Esso from Apache.

Esso identified that the Additional Wells should have been included in the Proposed Plan for 2021. This was due to its concern that one or more of the existing notices served under s29 of the Act might be deemed wide enough by the Secretary of State to require Esso to decommission the Additional Wells. Accordingly, unless provision was made for security of these Additional Wells under the Proposed Plan for 2021, there was a risk that Esso would be significantly unsecured.

In determining whether the pre-existing s29 notices were applicable to Additional Wells, the definition of "*offshore installation*" was relevant.

- S44(1) defines *"offshore installation"* as *"any installation which is or has been maintained or is intended to be established for the carrying on of any activity"* falling within s44(2) and (3). (emphasis added)
- S44(5) defines *"installation"* as that which includes any *"floating structure or devices maintained on a station by whatever means"*.

Agreeing with Apache's construction, the High Court held that “offshore installation” would naturally refer to equipment or structures within the field or sub-field such as a rig, instead of the entire field. This was especially so in light of the definition of "installation" as including a floating structure or device on a station.

The High Court also recognised that the s29 notices were dated between 2000 and 2005, long before the SPA was executed in 2011 and many years before the construction and existence of the Additional Wells. There was also no suggestion of an intention to construct the Additional Wells at the time of the notices. Therefore, these Additional Wells did not fall within the limits of s44. Accordingly, the Secretary of State would not have power to apply one of the pre-existing s29 notices to the Additional Wells and no security was required for them.

Conclusion

A compelling judgement which highlights how uncertainties can arise even in comprehensively drafted decommissioning agreements. The need to consider the scope of the Act was necessitated by the contractual indemnity. While in this matter a clear result was achieved, it may not have been the case had the regulations been less clear, and Apache might have found itself having to provide much wider security than anticipated.

For more information, please contact the authors of this alert,

CHANAKA KUMARASINGHE
Partner, Singapore
T +65 6411 5314
E chanaka.kumarasinghe@hfw.com
M +65 9170 3100

VANESSA KOH
Associate, Singapore
T +65 6411 5377
E vanessa.koh@hfw.com
M +65 9686 6879