Responding to $50 oil through collaboration, combination and innovation

In responding to the 2014 oil price collapse, oilfield services companies, or OSCs, have engaged in a range of novel contracting and ownership structures. Glenn Kangisser and Teena Grewal from law firm Haynes and Boone CDG LLP, take us through a number of industry examples that defy traditional thinking.

Traditionally, oil companies are generally either awarded a petroleum production licence by the State or enter into a production sharing contract with the State. The field operator then contracts with a range of OSCs to perform the work for the agreed day rates and fees.

Reservoir risk and oil price risk is traditionally borne by the oil companies. In return, the day rates and fees payable to the OSCs do not typically reward the OSCs in a high oil price environment. Although there may be some incentives, these are typically focused on rewarding safety and efficiency in the conduct of operations.

However, the increased willingness of OSCs to engage in a broader range of novel contracting and ownership structures has been evident in recent months.

Collaboration

On October 6th 2017, Borr Drilling and Schlumberger, announced they had teamed up to offer integrated performance-based drilling contracts in the offshore jack-up drilling rig market.

Borr's CEO, Simon Johnson, highlighted the fact that as drilling contractors effectively manage the workflows undertaken by a multitude of OSCs, it means they have a lot to offer in terms of improving performance and efficiency.

"Time is the most critical element in the drilling process... if we are incentivised to be as efficient as possible then we will focus our efforts accordingly," stated the CEO. In his view, there are many models that support this approach, ranging from a lumpsum/turnkey approach to day-rate bonuses based on a time/depth curve and/or well objectives curve.

This is an interesting development as under the traditional drilling contract model, offshore drilling contractors are paid a day rate for the provision of their services based on the period of time spent in performing drilling activities. This structure does not reward the drilling contractor for efficiencies in reducing the time involved in performing drilling work (save possibly in the case of bonuses agreed as a "top up" to the day-rate).

A further example of collaboration was announced on November 21st 2017 when Aker BP entered into two separate alliance agreements. The first agreement with Maersk Drilling and Halliburton is in respect of jack-up drilling rigs; the second is with Halliburton and Odfjell Drilling for semi-submersible drilling rigs.

The alliances are intended to provide a "one for all, all for one" collaboration model. Under the alliance arrangement, Aker BP intends to "plan and execute sanctioned production and exploration activities by using an integrated well delivery model; a "Drilling & Well Alliance". Halliburton will provide well construction activities to support jack-up (Maersk) or semi-submersible (Odfjell) operations.

Combination

On July 3rd 2017, a merger was concluded between GEC's oil and gas business and Baker Hughes, resulting in the world's second largest oilfield services company. This merger blurs the lines between the traditional oilfield equipment manufacture business and the oilfield services element.

In the merger announcement, it was noted that the merged entity, known as BHGE, would provide a "fullstream offering" of capabilities "across the full value chain of oil and gas activities".

Innovation

OSCs have also embarked on innovative schemes to respond to the changed market conditions. As Schlumberger's production business has grown, it has also negotiated deals which include equity in oil and gas fields, as well as deals which give Schlumberger a firm payment based on oil and gas output.

For example, Argentina's state-run oil company, YPF SA, and Schlumberger AG have agreed a deal to invest $390 million in the Vaca Muerta shale formation. Schlumberger will invest the full amount and obtain a 49% stake in the Bandurria Sur concession, where the two companies will develop a two-phase shale oil pilot project.

Moving away from tradition

It is clear that a low oil price environment has motivated OSCs to find innovative ways of reducing costs and increasing profit, including an exploration of a wider range of contracting and ownership structures, which blur the traditional roles between oil companies and OSCs. We anticipate that greater innovation in contracting, ownership and risk/reward structures will continue in the offshore oil and gas sector while the low oil prices persist. ■