CLIENT ADVISORY

New Technology Creates New Insurance Issues for Oil and Gas Lease Operators

Over the last two years, new technology has made unconventional drilling a viable, cost-effective way to extract oil and gas from shale. This new technology is based on advanced horizontal drilling techniques that enable pinpoint accuracy combined with complex multi-stage hydraulic fracturing (“fracking”) techniques over significant distances horizontally. This shift has resulted in new insurance issues that often go unaddressed.

The new fracking technology has advanced to 40-stage fracking operations on 10,000-foot horizontal laterals. This game-changing technology and its impressive results have led to a re-evaluation of the oil and gas resources available in the United States. A Congressional Research Service report released on March 25 of this year indicates that the United States now has the largest hydrocarbon resources in the world.[1]

Drilling activity is up, and the use of this new technology is now common.

This shift to unconventional drilling and heavy multi-stage fracking has created new insurance issues for the industry:

- Increase in blowouts during the completion/fracking stage.
- Increase in blowouts involving communication between multiple wells.
- Increase in blowouts caused by casing/cementing failure.
- Increase in blowouts caused by surface events.

In addition to these blowout trends, we are seeing:

- An increase in blowouts involving producing wells.
- An increase in blowouts involving plugged and abandoned wells.

While fracking has been the cause of some of the blowout increases, producing wells and plugged and abandoned wells are experiencing underground blowouts from the failure of old and corroded casings. These underground blowouts can lead to cratering events that are costly and difficult to bring under control. Underground blowouts can be much more expensive to bring under control than surface blowouts, yet many operators do not insure these wells or have high enough limits for them.

Another issue that has arisen from fracking is an increase in surface and water table pollution events that can result in expensive claims and erode the Control of Well limit rapidly, if not entirely. As a result, many of the blowouts that are now occurring are under-insured.

Well control costs have significantly increased over the past ten years. Setting Control of Well limits requires being mindful of the Combined Single Limit for the Control of Well coverage components, which include:

- Well Control Costs
- Relief Well (if required)
- Seepage & Pollution
- Evacuation Costs
- Restoration & Re-drill

Also important to keep in mind is that Control of Well limits scale to a client’s interest in the well. If a client has a 10% interest in a well with a $10,000,000 limit, the limit scales to the owner’s interest, resulting in a $1,000,000 limit for Control of Well insurance for that well.

Considering the impact of this new technology, now may be a good time to review the Control of Well limits for your client and provide options for higher limits as necessary.

1 “U.S. Fossil Fuel Resources: Terminology, Reporting, and Summary.” Congressional Research Service. <http://epw.senate.gov/public/index.cfm?FuseAction=Files.View&FileStore_id=04212e22-c1b3-41f2-b0ba-0da5eaead952>

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