

As the Oil & Gas World Churns

Hank Arnold

504.566.5204

harnold@bakerdonelson.com

Jan Hayden

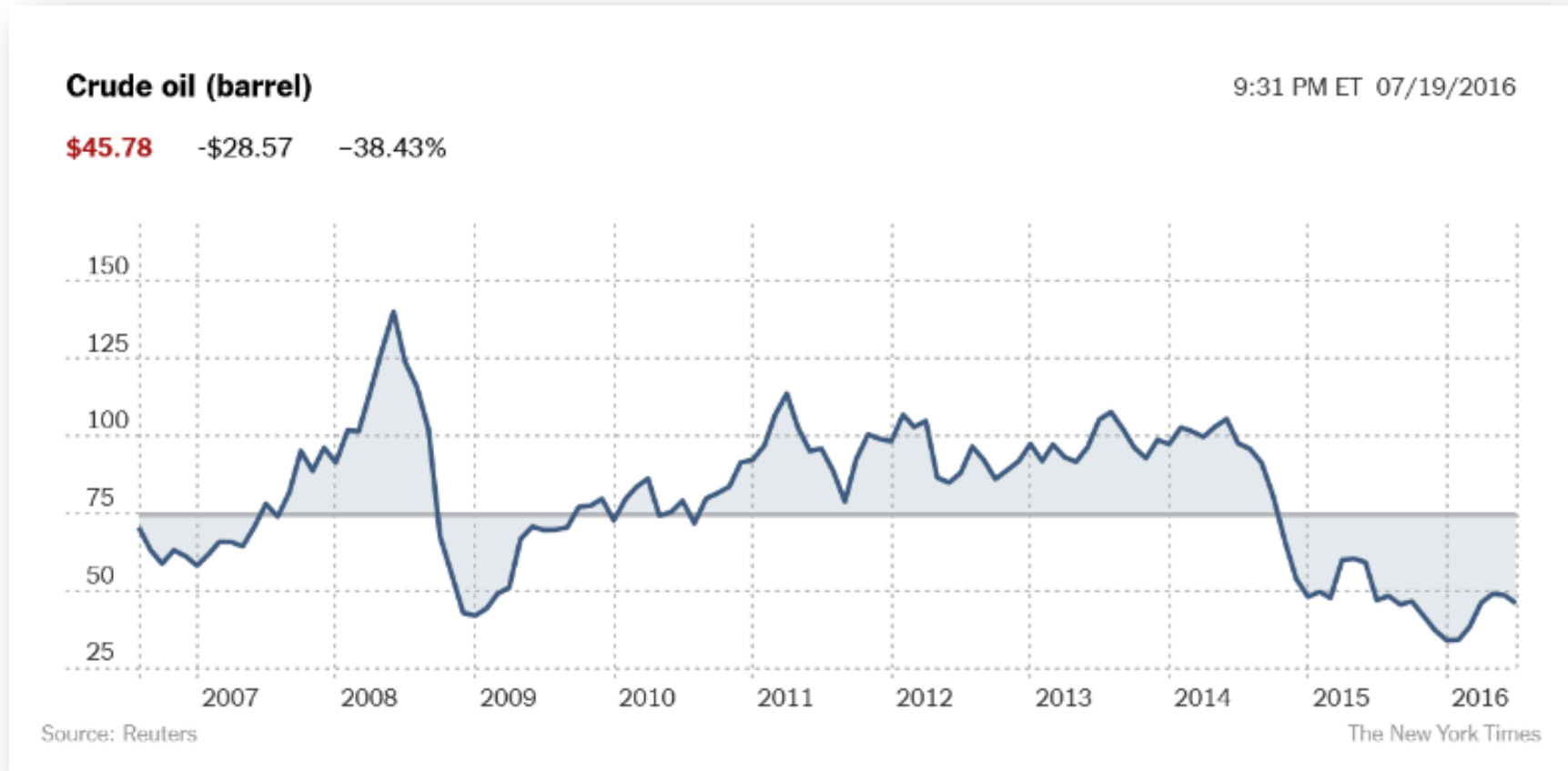
504.566.8645

jhayden@bakerdonelson.com

Discussion Topics

- How did we get here?
- Recent oil and gas bankruptcy outcomes
- Oil field servicer bankruptcies
- Mid-stream oil and gas bankruptcies
- Current issues in E&P bankruptcies
- Lessons learned
 - Where are we heading?

How did we get here?

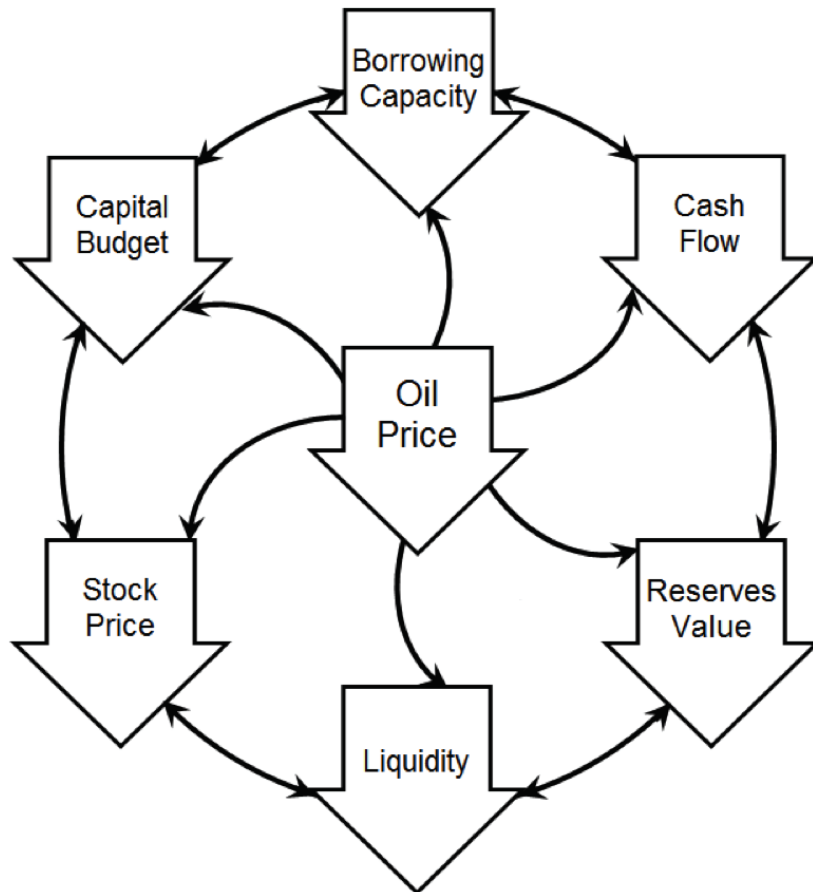


Source: Reuters as appearing in the New York Times

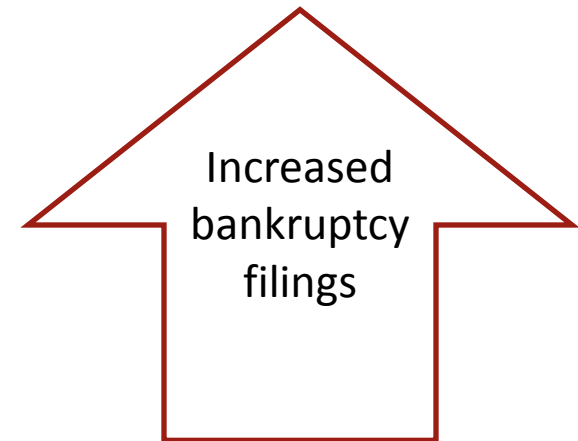
How did we get here? (continued)

- Increased U.S. production due to fracking
- Saudi increase in production = disaster
- Low prices = low cash flow
- Industry-wide belt tightening across the country = low cash flow
 - RBL borrowing base redeterminations reserves establish the borrowing base of the loan
 - A lender providing a RBL will make its own calculation of collateral value when determining the borrowing base at each redetermination date
- Covenant challenges/defaults in loan facilities
- Significant roll off of hedges, accelerating at year-end 2015
- Vendor issues
- Customer issues
- Litigation

Declining oil prices impact many corporate factors besides cash flows

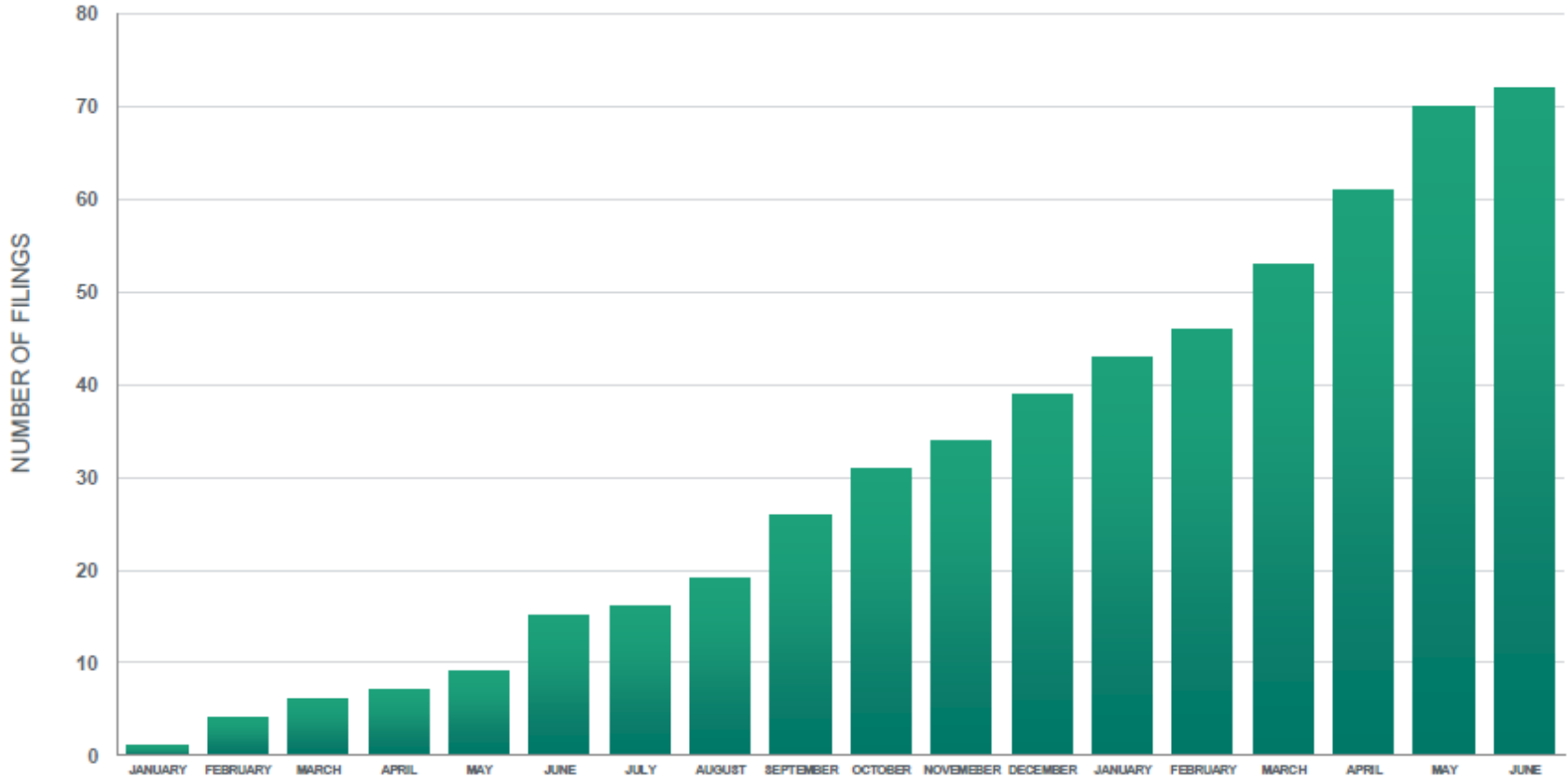


Current commodity prices have placed a severe strain on both oilfield service companies, mid-stream and E&P companies



Source: Decomworld Offshore Decommissioning Report 2015 Gulf of Mexico

2015-2016 Cumulative North American Oilfield Services Bankruptcy Filings



Source: Haynes and Boone Oilfield Services Bankruptcy Tracker

List of 2015 Bankruptcy Filings

	FILING DATE	COURT	CASE NUMBER	DEBTOR	SECURED	UNSECURED	TOTAL
1	1/15/2015	WD TEXAS	15-60161	GASFRAC ENERGY SERVICES, INC.**	\$ 24,872,458	\$ 47,340,908	\$ 72,213,366
2	2/5/2015	SD TEXAS	15-30786	CALMENA ENERGY SERVICES, INC.**	\$ 16,508,671	\$ 0	\$ 16,508,671
3	2/6/2015	WD PENN	15-20390	NORTH SHORE ENERGY SERVICES, LLC	\$ 45,000	\$ 1,429,550	\$ 1,474,550
4	2/19/2015	CANADA		LEADER ENERGY SERVICES**	\$ 9,379,928	\$ 8,384,929	\$ 17,764,857
5	3/3/2015	DELAWARE	15-10458	CAL DIVE INTERNATIONAL, INC.	\$ 199,800,000	\$ 111,539,932	\$ 311,339,932
6	3/4/2015	SD TEXAS	15-70116	SUMMIT WELL SERVICES, LLC	\$ 1,286,368	\$ 425,916	\$ 1,712,285
7	4/30/2015	NEW MEXICO	15-11137	HORIZON WELL SERVICES, LLC	\$ 2,912,058	\$ 1,266,464	\$ 4,178,524
8	5/17/2015	ND TEXAS	15-41974	FRAC SPECIALISTS, LLC	\$ 39,110,987	\$ 7,567,925	\$ 46,708,912
9	5/18/2015	WD OKLAHOMA	15-11872	LONESTAR GEOPHYSICAL SURVEYS, LLC	\$ 7,186,640	\$ 5,125,128	\$ 12,311,768
10	6/8/2015	CANADA		BIG EAGLE HYDRO-VAC, INC.	\$ 39,048,721	\$ 2,380,970	\$ 41,429,691
11	6/10/2015	WD TEXAS	15-70082	2 D'S OILFIELD SERVICES, INC.	\$ 2,291,571	\$ 819,280	\$ 3,110,851
12	6/11/2015	CANADA		HC PIPER MANUFACTURING, INC.**	\$ 2,218,286	\$ 805,015	\$ 3,023,301
13	6/12/2015	ND TEXAS	15-42370	ALL OUT ENERGY SERVICES, LLC	\$ 1,556,713	\$ 141,019	\$ 1,697,732
14	6/19/2015	DELAWARE	15-11326	CITADEL ENERGY SERVICES, LLC	\$ 149,719	\$ 3,251,848	\$ 3,401,567
15	6/21/2015	SD TEXAS	15-20241	TANK 1 SERVICES, LLC	\$ 3,969,381	\$ 2,255,207	\$ 6,224,588
16	7/17/2015	CANADA		TORRAC OILFIELD SERVICES, LTD.**	\$ 0	\$ 4,610,478	\$ 4,610,478
17	8/13/2015	DELAWARE	15-11685	HERCULES OFFSHORE, INC.**	\$ 0	\$ 1,306,971,541	\$ 1,306,971,541
18	8/18/2015	CANADA		AQUA-PURE VENTURES, INC.**	\$ 10,739,686	\$ 198,722	\$ 10,938,408
19	8/27/2015	WD TEXAS	15-52071	FOURWINDS LOGISTICS A/K/A FWLL, LLC***	\$ 0	\$ 5,516,047	\$ 5,516,047
20	9/1/2015	WD TEXAS	15-52159	JM OILFIELD SERVICES, INC.***	\$ 14,280,490	\$ 6,558,349	\$ 20,838,839
21	9/7/2015	SD TEXAS	15-34736	DIVERSE ENERGY SYSTEMS, LLC	\$ 18,848,379	\$ 29,915,797	\$ 48,764,176
22	9/18/2015	SD TEXAS	15-60070	HII TECHNOLOGIES, INC.	\$ 14,654,006	\$ 4,332,871	\$ 18,986,877
23	9/18/2015	WD TEXAS	15-52267	BMC OILFIELD SUPPLY, LLC***	\$ 0	\$ 2,201,359	\$ 2,201,359
24	9/18/2015	WD TEXAS	15-52270	NEW VOYAGE ENTERPRISES, LLC***	\$ 0	\$ 511,780	\$ 511,780
25	9/21/2015	WD LOUISIANA	15-11758	ELITE COIL TUBING SOLUTIONS, LLC***	\$ 12,000,000	\$ 11,402,567	\$ 23,402,567
26	9/25/2015	SD TEXAS	15-35003	ENERGY OILFIELD SERVICES, LLC***	\$ 3,260,142	\$ 1,586,327	\$ 4,846,469
27	10/2/2015	CANADA		GROUNDFORCE GEODRILLING SOLUTIONS, INC.**	\$ 10,110,076	\$ 7,014,059	\$ 17,124,135
28	10/12/2015	WD TEXAS	15-70136	TRINITY ENVIRONMENTAL SERVICES, LLC	\$ 186,468,226	\$ 726,624	\$ 187,194,850
29	10/16/2015	WD LOUISIANA	15-51336	A&B VALVE AND PIPING SYSTEMS, LLC	\$ 13,396,850	\$ 17,072,484	\$ 30,469,334
30	10/20/2015	SD TEXAS	15-35530	BLUEWATER INDUSTRIES LP***	\$ 0	\$ 133,281,714	\$ 133,281,714
31	10/23/2015	COLORADO	15-21821	ENSECO ENERGY SERVICES CORP.**	\$ 11,855,649	\$ 2,134,466	\$ 13,990,115
32	11/9/2015	WD PENN	15-70766	SOMERSET REGIONAL WATER RESOURCES, LLC	\$ 24,132,148	\$ 11,690,899	\$ 35,823,047
33	11/24/2015	WD TEXAS	15-70162	ANIMAS WELL SERVICES, LLC	\$ 5,056,648	\$ 1,562,558	\$ 6,619,206
34	11/24/2015	ED TEXAS	15-60796	TORQUED-UP ENERGY SERVICES, INC.	\$ 12,307,762	\$ 37,058,707	\$ 49,366,470
35	12/3/2015	DELAWARE	15-12422	VANTAGE DRILLING CO.*	\$ 2,629,230,429	\$ 143,924,728	\$ 2,773,155,157
36	12/14/2015	WYOMING	15-20821 / 15-20822	STRATA ENERGY SERVICES INC.*	\$ 19,875,810	\$ 3,203,555	\$ 23,079,366
37	12/16/2015	SD TEXAS	15-36563	NOVA DIRECTIONAL, INC.	\$ 4,065,119	\$ 530,825	\$ 4,595,945
38	12/16/2015	COLORADO	15-23704	CASCADE INTEGRATED SERVICES, LLC	\$ 5,017,133	\$ 1,257,827	\$ 6,274,960
39	12/17/2015	ARIZONA	15-15859	RDX TECHNOLOGIES COPORATION	\$ 2,280,000	\$ 38,425,221	\$ 40,705,221
TOTAL 2015					\$ 3,347,895,055	\$ 1,964,453,600	\$ 5,312,348,655

List of 2016 Bankruptcy Filings

	FILED DATE	COURT	CASE NUMBER	DEBTOR	SECURED	UNSECURED	TOTAL
40	1/19/2016	NEW MEXICO	16-10078	ALLIANCE WELL SERVICE, LLC	\$ 3,536,467	\$ 986,010	\$ 4,522,478
41	1/31/2016	DELAWARE	16-10221	EXTREME PLASTICS PLUS INC.	\$ 53,369,124	\$ 16,611,719	\$ 69,980,843
42	2/14/2016	DELAWARE	16-10386	PARAGON OFFSHORE PLC*	\$ 1,440,650,651	\$ 983,582,000	\$ 2,424,232,651
43	2/19/2016	COLORADO	16-11308	CRAIG ENERGY, LLC	\$ 38,471,000	\$ 6,958,952	\$ 45,429,952
44	2/26/2016	WD TEXAS	16-70028	DRM SALES & SUPPLY, LLC	\$ 11,465,408	\$ 7,715,498	\$ 19,180,906
45	3/1/2016	ND TEXAS	16-40956	GREENHUNTER RESOURCES, INC.	\$ 21,470,000	\$ 2,292,008	\$ 23,762,008
46	3/2/2016	ND TEXAS	16-40979	UNIVERSAL WELL SERVICE HOLDINGS, INC.	\$ 12,440,231	\$ 12,716,336	\$ 25,156,566
47	3/4/2016	SD TEXAS	16-31201	WELLHEAD DISTRIBUTORS INTERNATIONAL	\$ 7,116,106	\$ 24,615,688	\$ 31,731,795
48	3/4/2016	WD LOUISIANA	16-10383	S-3 PUMP SERVICE, INC.	\$ 4,056,686	\$ 9,470,720	\$ 13,527,407
49	3/10/2016	SD TEXAS	16-60020	ESP PETROCHEMICALS, INC	\$ 2,843,613	\$ 4,587,835	\$ 7,431,449
50	3/13/2016	ND TEXAS	16-41049	WELLFLEX ENERGY SOLUTIONS, LLC	\$ 1,639,599	\$ 2,317,930	\$ 3,957,529
51	3/14/2016	ND TEXAS	16-50062	DJ OILFIELD SERVICES, LLC	\$ 609,744	\$ 2,405,046	\$ 3,014,790
52	3/25/2016	SD TEXAS	16-31447	EAST AFRICAN DRILLING LTD.	\$ 40,000,000	\$ 5,358,389	\$ 45,358,389
53	3/28/2016	ND TEXAS	16-50070	CROSSFIRE MANUFACTURING, LLC	\$ 0	\$ 653,578	\$ 653,578
54	4/1/2016	WD TEXAS	16-70042	ATK OILFIELD TRANSPORTATION, INC.*	\$ 29,983,250	\$ 5,000,000	\$ 34,983,250
55	4/1/2016	WD LOUISIANA	16-10545	KEITHVILLE WELL DRILLING & SERVICES, LLC.	\$ 5,461,052	\$ 3,863,666	\$ 9,324,718
56	4/4/2016	WD TEXAS	16-50778	SANJEL INC.*	\$ 890,638,000	\$ 213,964,000	\$ 1,104,602,000
57	4/15/2016	ND TEXAS	16-41547	DIAMOND TANK RENTAL, INC.	\$ 6,700,731	\$ 2,227,896	\$ 8,928,627
58	4/15/2016	ND OKLAHOMA	16-10678	SHEEHAN PIPE LINE CONSTRUCTION COMPANY	\$ 13,069,790	\$ 55,345,948	\$ 68,415,738
59	4/21/2016	ED TEXAS	16-40742	FPUSA, LLC	\$ 0	\$ 2,365,457	\$ 2,365,457
60	4/26/2016	WD TEXAS	16-70059	WEST TEXAS POLY AND PUMP, LLC	\$ 1,620,000	\$ 2,116,023	\$ 3,736,023
61	4/29/2016	UTAH	16-23671	ENERGY DRILLING, LLC	\$ 0	\$ 657,872	\$ 657,872
62	5/3/2016	WD TEXAS	16-70066	CANDESCENT WELL SERVICE, LLC****	\$ 0	\$ 0	\$ 0
63	5/11/2016	WD TEXAS	16-51110	J P S COMPLETION FLUIDS, INC.	\$ 720,480	\$ 3,771,113	\$ 4,491,593
64	5/17/2016	SD TEXAS	16-50108	HAWK OILFIELD SERVICE, INC.	\$ 604,765	\$ 673,420	\$ 1,278,185
65	5/17/2016	WD TEXAS	16-70079	TALL CITY WELL SERVICE, LP	\$ 12,428,779	\$ 2,055,854	\$ 14,484,633
66	5/17/2016	NEW MEXICO	16-11222	HUNGRY HORSE, LLC	\$ 3,032,630	\$ 2,439,247	\$ 5,471,877
67	5/18/2016	MD PENN	16-02115	NUWELD, INC.*	\$ 8,000,000	\$ 2,200,000	\$ 10,200,000
68	5/23/2016	SD TEXAS	16-60056	ARMADA WATER ASSETS, INC. / WES-TEX VACUUM SERVICE, INC.*	\$ 6,798,928	\$ 18,142,639	\$ 24,941,567
69	5/24/2016	SD TEXAS	16-80149	MARK A. MARTINEZ, LLC****	\$ 0	\$ 0	\$ 0
70	5/31/2016	COLORADO	16-15466	FORT DRILLING, LLC****	\$ 0	\$ 0	\$ 0
71	6/5/2016	DELAWARE	16-11385	HERCULES OFFSHORE, INC.* ^	\$ 579,000,000	\$ 43,000,000	\$ 622,000,000
72	6/7/2016	DELAWARE	16-11409	SEVENTY SEVEN ENERGY, INC.*	\$ 625,000,000	\$ 1,100,000,000	\$ 1,725,000,000
TOTAL 2016					\$ 3,820,727,036	\$ 2,538,094,844	\$ 6,358,821,880
TOTAL 2015-2016					\$ 7,168,622,091	\$ 4,502,548,444	\$ 11,671,170,535

End Result in Recent Oil & Gas Bankruptcies

- **Sale**

- WBH Energy LP (WDTX)
- CalDive International (DE)
- Dune Energy (WDTX)
- BPZ Resources (SDTX)
- Quicksilver Resources (DE)
- Parallel Energy LP (DE)
- Luca International Group LLC (SDTX)
- Milagro Oil & Gas (DE)
- Magnum Green (NDTX)

- **Failed Sale/Reorganization**

- ERG Resources (NDTX)

- **Reorganization**

- Samson Resources (DE)
- Sabine Oil & Gas (SDNY)
- Miller Energy Resources (AK)
- RAAM Global Energy (SDTX)
- Hercules Offshore (DE)
- Magnum Hunter (DE)
- American Natural Energy Corporation (EDLA)

- **Sale/Liquidation**

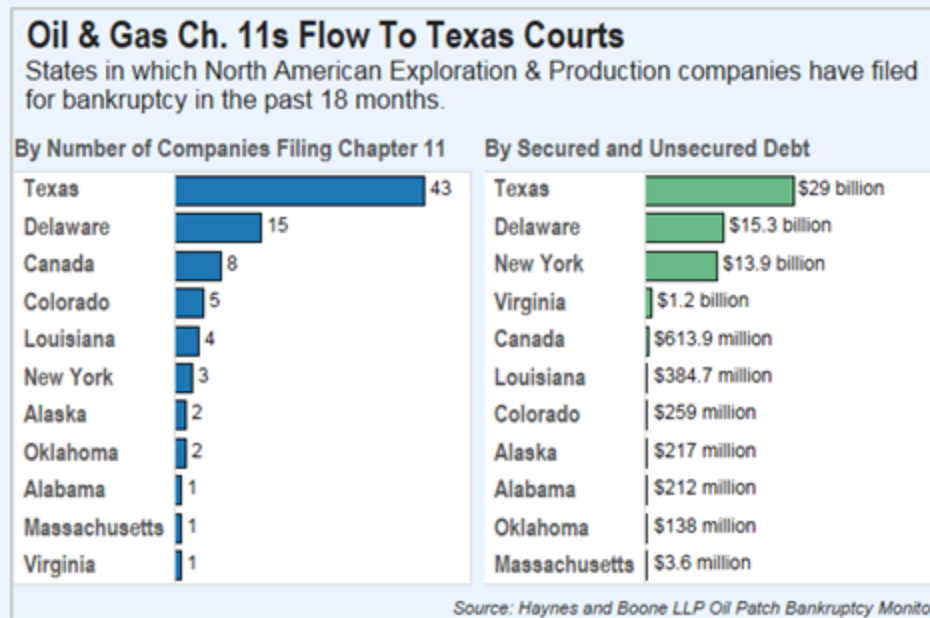
- Black Elk Offshore (SDTX)

- **Stalled Reorganization**

- Saratoga Resources, Inc. (WDLA)
- Graham Gulf Inc. (SDAL)

Trending towards Texas?

“[T]he Texas judiciary’s background and familiarity with oil and gas law and the potential reduced expense of going through a bankruptcy in Texas, the Lone Star State is today a far more popular venue for the wave of energy bankruptcy filings than Delaware or the Southern District of New York.”



Source Law360, July 22, 2016

Oilfield Service Bankruptcies

- Oilfield service company chapter 11 cases similar to typical cases
 - Appointment of statutory committees (unsecured, equity or both)
 - Negotiations with secured creditors
 - 363 assets sales are commonplace
 - Naked auction v. stalking horse
- Many “successful” cases have been prearranged deals either to sell or restructure pre-petition obligations

Mid-stream Oil and Gas Company Bankruptcies

- Not much restructuring/insolvency action in this sector... Yet
 - Recent ruling in *Sabine* indicative of trend that mid-stream agreements are not likely “covenants running with land”
- E&P companies may use 11 U.S.C. § 365 to reject mid-stream agreements (e.g., gathering and transportation agreements)
- Developments involving mid-stream agreements may leave this sector more vulnerable to insolvency risk amid E&P restructurings

Current Issues in E&P Bankruptcies

- Debt-for-equity swaps
- Counterparty considerations
- DIP Financing
- Sales
- Asset venue (regarding both perfection issues and profit margin)
- Oil & Gas Leases: A lease or a property interest?
- Covenants running with the land (versus 11 U.S.C. § 365)
- Treatment of joint operating agreements in bankruptcy
- Plugging and abandonment issues

Debt for Equity?

- **Energy XXI**
 - founded in 2005
 - aggressively expanded through acquisitions in LA and GOM
 - used debt to buy EPL Oil & Gas Inc. in a \$1.53 billion
 - became largest publicly traded producer of crude in the shallow waters of GOM
 - April 2016 filed Bankruptcy SDTX
 - reached \$1.45 billion debt-for-equity swap with a group of its bondholders
 - backing of 63 percent of the bondholders of a EXXI subsidiary
 - Note: Bankruptcy law requires approval from a group of creditors – two-thirds in amount and more than one-half in number – to agree to the deal

Debt for Equity? (continued)

- **C&J Energy Services Ltd**
 - Filed Chapter 11 bankruptcy SDTX in July 2016
 - struck agreement with its lenders (who hold 83 percent of its credit facility debt) to swap \$1.4 billion in debt for ownership of the reorganized company
 - Lenders will backstop a rights offering for up to \$200 million in stock in the reorganized company and provide a \$100 million loan, which will increase its liquidity
 - Equity holders will receive seven-year warrants that are convertible into six percent of the stock in the reorganized company
 - C&J said it expects to emerge from bankruptcy within six months
- **Atlas Resource Partners LP**
 - plans to file Chapter 11 bankruptcy by July 27, 2016
 - has entered into Restructuring Support Agreement backed by majority of noteholders, second lien lenders, and lenders under the company's revolving credit facility
 - plans to convert \$668 million of its outstanding senior notes into a 90 percent equity stake in the reorganized company
 - the plan will reduce Atlas' annual interest expenses by \$80 million
 - “prepack”

E&P Counterparty Issues

- Immediate bankruptcy considerations for counterparties to operating agreements, leases or other contractual arrangements:
 - Can payments due to the debtor be withheld?
 - Can those same payments be applied to the debtor's share of costs incurred pursuant to an operating agreement?
 - What actions should parties take to preserve their state law lien rights if they failed to file a lien affidavit or statement of privilege before the debtor filed bankruptcy?
 - What steps should be taken to enforce or preserve statutory liens rights after a case has been filed?

E&P Counterparty Issues: Setoff

- 11 U.S.C. §553 provides that the commencement of a bankruptcy case “does not affect the right of a creditor to offset a mutual debt owing by such creditor to the debtor that arose before commencement of the case ... against a claim of such creditor against the debtor that arose before the commencement of the case[.]”

E&P Counterparty Issues: Setoff (continued)

- **Requirements:**
 - amount the debtor owes its creditors and the amount the creditor owes the debtor must be “mutual”
 - mutually owed amounts do not need to arise out of the same transaction (Example: costs owed by the debtor on Well “X” can be offset against production due to the debtor from Well “Y.”)
- Both the claim of the creditor against the debtor (i.e., costs owed on Well “X”) and the debt owed by the creditor to the debtor (i.e., a share of production from Well “Y”) must arise before the debtor filed bankruptcy
- Must seek stay relief

E&P Counterparty Issues: Recoupment

- Unlike setoff, recoupment is only permissible when the creditor's claim arises from the same transaction as the debtor's claim
- Recoupment is a viable option when the money owed to the debtor relates to the same well or joint operating agreement as the debt
- No requirement to seek stay relief prior to exercising rights

Post-petition Perfection and Preservation of Statutory Liens

- State statutes protect parties in the oil and gas industry by granting such parties mineral liens or privileges over specified property to secure repayment of obligations incurred in upstream operations
 - Louisiana
 - LOWLA (La. Rev. Stat. § 9:4881 et seq.)
 - Texas
 - Title 52 of the Texas Property Code
- Incorporate relation back principle
 - perfected when debt incurred but creditor required to take additional steps to maintain perfection
- Failure to perfect as of petition date?
 - 11 U.S.C. § § 363(b)(3) & 546(b)

DIP Financing

- 11 U.S.C. § 364(d)(1)(b)
- A DIP financing arrangement has the potential to affect the entire case
 - A post-petition lender will most likely demand a lien on the post-petition cash and receivables of the debtor.
 - Priming issues
 - “roll-ups” – converts the lender’s prepetition indebtedness to a post-petition administrative expense
- Lender-friendly default and remedy provisions
 - may entitle the DIP lender to cease funding the case or even force a sale of the debtor’s assets
 - In re ATP Oil & Gas Corporation, Case No. 12-36187, United States Bankruptcy Court Southern District of Texas
 - DIP lenders were able to force a sale (effectively causing the administrative insolvency of the debtor) as a result of provisions they included in a DIP Order entered early in the case

DIP Financing – Counterparty Considerations

- What security granted as part of a DIP lending or cash collateral proceeding?
- Does granting of cash collateral security to the post-petition lender erode cash or security available to satisfy:
 - cash calls
 - capital calls
 - operating expenses
 - environmental liabilities
 - decommissioning liability
- Counterparty could be jointly liable with the debtor for environmental liabilities and may be compelled to advance the debtor's share of these expenses without security
- **Conclusion: increased counterparty issues makes 13 week cash flow budgeting less predictable**

Defensive Drawdowns

- Energy Companies Playing Risky game with Short Term Credit Grab?
- “The glut of energy companies using a borrowing strategy called a defensive draw – maxing out on credit before lenders can cut off access to cash – has taken the lending market by surprise and put exploration and production firms in the driver's seat in bankruptcy court. But experts say it could dramatically tighten the credit market for years to come and may spell long-term danger for the sector.”
- Lender should be monitoring for drawdowns

Source: Law360, July 15, 2016

Executory Contracts and Unexpired Leases

- 11 U.S.C. § 365
 - permits debtor “subject to court approval, [to] assume or reject an executory contract or unexpired lease of the debtor”
- Business judgment rule
- The debtor generally has until confirmation of its Chapter 11 plan to decide whether to assume or reject
- Counterparties to executory contracts and unexpired leases must perform during this period

“Countryman” Definition of Executory Contract

“[A] contract under which the obligation of both the bankrupt and the other party to the contract are so far unperformed that the failure of either to complete performance would constitute a material breach excusing the performance of the other.”

The Fifth Circuit applies the Countryman definition to an executory contract analysis. See e.g., *Phoenix Exploration v. Yaquinto (In re Murexco Petroleum)*, 15 F.3d 60, 62-63 (5th Cir. 1994)

Oil & Gas Leases as Executory Contracts in Bankruptcy

- Dependent on state law
- Louisiana – controversial and undecided (case law is mixed)
 - In re WRT Energy Corp., 202 B.R. 579 (W.D. La. 1996) (mineral leases neither executory contracts under Countryman definition nor unexpired leases)
 - Texaco, Inc. v. Louisiana Land & Exploration Co., 136 B.R. 658, 668 (M.D. La. 1992) (refusing to rule on issue as to whether or not mineral lease is an unexpired lease under section 365, but holding that it constitutes an executory contract)
 - Delta Energy Resources, Inc. v. Damson Oil Corp., 72 B.R. 7, 11 (W.D. La. 1985) (treating mineral lease as a real right which can be alienated and mortgaged to third parties although not conventional lease contemplated by section 365; allowing damages for rejection)

Oil & Gas Leases as Executory Contracts in Bankruptcy **(continued)**

- Texas, Oklahoma, New Mexico and others
 - Oil and gas leases convey to the lessee an ownership interest in real property, so 11 U.S.C. § 365 does not apply and cannot be used to reject oil and gas leases in these states
- Kansas and Ohio Oil and gas leases convey contract rights only (§ 365 applies)
- OCS Undecided issue (case law is uncertain)
 - Federal government taken position that an OCS lease is a true lease rather than an interest in real property

Consequences of Assumption

- Requirement to cure any defaults in an underlying contract
 - Counterparties to operating agreements should analyze the notice of cure promulgated by the debtor to ensure that it accurately accounts for all amounts required to bring the contract current
- Defaults occurring after assumption conferred priority status and treated as an administrative expense of the estate

Consequences of Rejection

- Rejection does not equate to termination
- General unsecured claim (no administrative priority)
- Predecessor liability for decommissioning and environmental obligations?
 - ATP Oil & Gas Corp
 - filed for bankruptcy protection in August 2012 and proposed to sell most of its assets in a 363 sale
 - sought to abandon certain OCS leases in Mississippi Canyon 711 for which ATP was responsible for decommissioning obligations estimated at \$115 million
 - bankruptcy court allowed DOI to take possession of the property and seek performance from Anadarko as predecessor in title of the lease

Sales “Free and Clear”

- Section 363 of the bankruptcy Code states that “[t]he trustee, after notice and a hearing, may use, sell or lease, other than in the ordinary course of business, property of the estate[.]”
- Additionally, the trustee may sell property of the estate “free and clear of any interest in such property of an entity other than the estate” if one of the following five conditions is met:
 - (1) applicable nonbankruptcy law (i.e., state law) permits sale of such property free and clear of such interest
 - (2) such entity consents
 - (3) such interest is a lien and the price at which such property is to be sold is greater than the aggregate value of all liens on such property;
 - (4) such interest is in bona fide dispute; or
 - (5) such entity could be compelled, in a legal or equitable proceeding, to accept a money satisfaction of such interest.

Current Upstream Sale Issues in Oil and Gas Bankruptcies

- 363 sale “free and clear”
 - Executory contract assumption
 - JIBS?
 - M&M liens?
 - Consent rights / rights of first refusal?
 - Ongoing vendor obligations / production proceeds?
 - Environmental concerns?
 - Lessor notice issues?
 - Estoppel
 - Indemnification issues

Strategy?

- Include language in any applicable orders, sale, or assignment agreements approved by the bankruptcy court making clear the legal undertaking by the purchaser or assignee of these obligations to satisfy in the future these obligations
- Otherwise the subsequent purchaser may argue that liability for obligations that accrued before the sale were discharged in debtor's bankruptcy

Dune Energy Inc.

- Filed Chapter 11 bankruptcy with two affiliates in WDTX in March 2015
- Listed assets at \$229.5 million and liabilities at \$144.2 million
- After lengthy sales process and infusion of \$10 million DIP, assets sold for \$19 million and assumption of P&A liability

Outer Continental Shelf Decommissioning

- Decommissioning:
 - General term referring to lease obligations required to be performed when facilities are no longer useful for operation
 - plugging wells
 - removing or reefing the platform
 - decommissioning pipelines
 - clearing the seafloor of all obstructions created by the lease and pipeline right-of-way operations
 - Federal law requires lessees to decommission wells and facilities located on OCS leases (30 CFR §§250.1700-1754)
 - Owners of leasehold interest, including record title interest and operating rights, are responsible for meeting decommissioning obligations during the relevant period of ownership

Source: Decomworld Offshore Decommissioning Report 2015 Gulf of Mexico

Responsibility for OCS Decommissioning Obligations

- The Outer Continental Shelf Lands Act (“OCLSA”) vests with the Secretary of the Interior the authority to require bonds or other forms of financial assurance for oil and gas exploration, development, and production activities on the OCS
- The Secretary has delegated authority over financial assurance to BOEM, which has promulgated regulations governing the financial assurance process

BOEM'S Bonding Requirements – Financial Assurance of Ability to Meet Decommissioning Obligations

- Currently BOEM's regulations require
 - general lease surety bond in an amount ranging from \$50,000 to \$3,000,000
 - supplemental bonds in an amount determined by the Bureau of Safety and Environmental Enforcement (“BSEE”) as appropriate to meet decommissioning liabilities

Primary Consumers of **OCS** Decommissioning Services 2015 – 2016

- The following companies operate half of the GOM active inventory (active wells and structures) in shallow water:
 - Fieldwood Energy, LLC
 - Chevron USA, Inc.
 - **EPL Oil & Gas, Inc. – filed April 2016**
 - **Energy XXI GOM, LLC – filed April 2016 (part of EXXI)**
 - **W&T Offshore, Inc. – wait and see**
 - credit line cut to \$150 million from \$350 million in March and the company has said it will pay off the loan in three monthly installments
 - Fieldwood Energy Offshore, LLC

Source: Decomworld Offshore Decommissioning Report 2015 Gulf of Mexico

NTL No. 2016-N01 – New BOEM supplemental bonding requirement

- Effective date: September 12, 2016
- Assigns **100** percent of decommissioning and other liability to a company for any lease, ROW, and RUE in which that company has an ownership interest or for which that company acts as a guarantor
 - joint and severable liability for co-holders of offshore leases
 - puts the onus on co-lessees to broker deals divvying up the liability, otherwise, it will hold each co-lessee liable for the full decommissioning
- **No more waiving supplemental bonding obligations**
- Allows companies to “self-insure,”
 - but only up to 10 percent of a company’s “tangible net worth,” which is defined as the difference between a company’s total assets and the value of all liabilities and intangible assets

NTL No. 2016-N01 – Effects

- If company is unable to satisfy the requirements of a BOEM supplemental bonding order, BOEM could issue civil penalties or request that BSEE order the company to immediately decommission its assets
- Smaller operators forced to sell assets to a larger companies that are better positioned to meet the significant costs of supplemental bonding
 - Would consolidation result in the end of the robust competitive market in the offshore oil and gas industry?
- Could lead larger E&P companies to conclude that the decommissioning costs too high to validate growth in frontier areas such as the Arctic and ultra-deepwater Gulf of Mexico

NTL No. 2016-N01 – Effects (continued)

- BOEM's orders also could drive certain companies to declare bankruptcy
- The bankrupt company would forfeit its general bond and any existing supplemental bond likely would not be sufficient to meet decommissioning obligations
- Trigger of BSEE's joint and several liability regulations
 - seek compliance with decommissioning obligations from another party in the lease, RUE or ROW chain of title
 - go after entity with deep pockets

State Decommissioning Law

- In Louisiana the plugging and abandonment activities on oil and gas wells are governed by the Commissioner of Conservation
- The party responsible for decommissioning obligations relating to abandoned wells is the “owner,” which includes any person who had a right to operate the well at any point in time starting with the original operator who installed the well or facilities
- Ultimately reaches the joint interest owners (“Responsible Parties”) who are in the chain of title through the Louisiana Oilfield Site Restoration Law

State Bonding Requirements

- In May 2015, the Office of Conservation amended its financial security requirement rules to effectively double the amount of financial security operators were required to post for wells they completed, drilled or took over from another operator
- On April 14, 2016, the Louisiana Office of Conservation issued a Declaration of Emergency
- Promulgated an Emergency Rule to decrease the amount of financial security certain oil and gas operators are required to post to obtain a permit to drill, recomplete or take-over a well
 - One stated reasons for Emergency Rule given by Louisiana Office of Conservation is “[t]he price of oil has dropped to historically low levels and most operators are unable to afford the increased financial security amounts promulgated in [La Rev. Stat. § 41:952].”

Source: Drill Deeper blog, April 19, 2016

Old Rules v. **New (Suspended) Rules**

- **For each well**
 - For land locations:
 - $\leq 3,000'$ = \$1.00 per foot (**New = \$2.00**)
 - 3,000-10,000' = \$2.00 per foot (**New = \$5.00**)
 - $\geq 10,000'$ = \$3.00 per well (**New = \$4.00**)
 - For inland water locations:
 - any depths = \$8.00 per foot (**New = \$12.00**)
 - offshore water locations:
 - \$12.00 per foot – no difference

Source: Drill Deeper blog, April 19, 2016

Old (Current) Rules v. New (Suspended) Rules

- Plus blanket security from each operator
- Land locations
 - ≤ 10 wells per operator = \$25,000 (New = same)
 - 11-99 = \$125,000 (New = same)
 - ≥ 100 = \$250,000 (New = same)
- Inland water locations
 - ≤ 10 wells per operator = \$125,000 (New = \$250,000)
 - 11-99 = \$625,000 (New = \$1,250,000)
 - ≥ 100 = \$1,250,000 (New = \$2,250,000)
- Offshore water locations
 - ≤ 10 wells per operator = \$250,000 (New = \$500,000)
 - 11-99 = \$1,250,000 (New = \$2,500,000)
 - ≥ 100 = \$2,250,000 (New = \$5,000,000)

Where are we heading?

- “Saudi Arabia could provide a glimmer of hope for those longing for an oil price rally.”
 - Nick Cunningham, OilPrice.com, July 24, 2016
- “The oil market is treading water for now, but the oil price overshoot to the downside earlier this year and this is clearly setting the stage for a bullish end to the decade.” and “[T]he pendulum is clearly swinging from the bears to the bulls.”
 - Analysts led by Ed Morse at Citibank, July 11, 2016, as reported by Bloomberg News

Where are we heading (continued)

- "You have to believe that there is a possibility that you will not necessarily go back above \$100, you know, ever[.]"
 - Vitol Group BV Chief Executive Officer Ian Taylor, February 8, 2016, as reported by Bloomberg
- "Gulf Oil, Gas Lease Sale Will Be First Streamed Online"
 - Law360, July 25, 2016
 - Sale date of August 24, 2016
 - 23.8 million acres in the Western GOM
 - The government estimates that the area up for sale has around 116 and 200 million barrels of oil and 538 to 938 billion cubic feet of natural gas
 - **Let's see who shows up!**

Questions?



Hank Arnold

Shareholder

201 St. Charles Avenue

Suite 3600

New Orleans, LA 70170

504.566.5204

harnold@bakerdonelson.com



Jan Hayden

Shareholder

201 St. Charles Avenue

Suite 3600

New Orleans, LA 70170

504.566.8645

jhayden@bakerdonelson.com