

# Opportunities and Alternatives for Distressed Energy Market Participants

Presented by Stephen M. Pezanosky  
Haynes and Boone, LLP

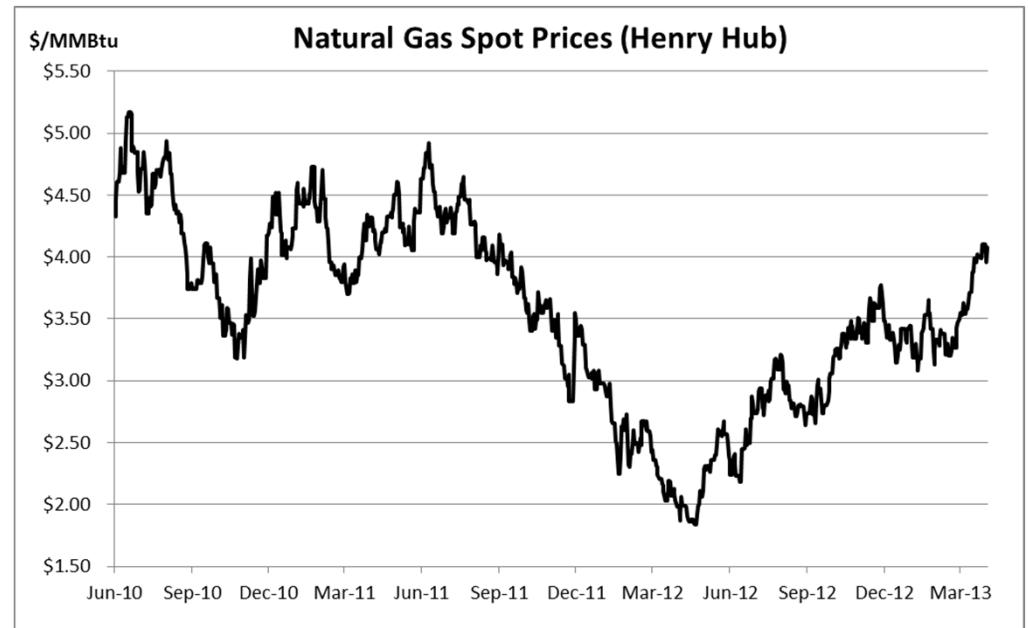


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# Opportunities in Distressed Natural Gas Acquisitions

## Increasing Liquidity Constraints for Operators

- Increased gas production due to advances in technology
- Historically low gas prices and lower reserve valuations for gas operators
- Reduced cash flow from lower priced production
- Continued exploration and production necessary to maintain lease positions



# Opportunities in Distressed Natural Gas Acquisitions

- Working Capital Facility Borrowing Base Adjustments
  - Working capital facility borrowing base predicated on reserve valuations
  - Borrowing base determinations in Spring and Fall
  - Lower gas prices may result in borrowing base adjustment below outstanding draws
  - Borrowings in excess of borrowing base will require a pay down – need for more liquidity.

# Opportunities in Distressed Natural Gas Acquisitions

- Acquisition and Investment Opportunities:
  - Acquire gas reserves at historically low valuations
  - Operators may need additional equity investment or mezzanine debt to address borrowing base limitations or pay downs
  - Operators may put themselves up for sale or for additional investment in a chapter 11 bankruptcy



# Opportunities in Distressed Natural Gas Acquisitions

- Typical Situation
  - Company (operator) faced with borrowing base adjustment or pressure from secured lender
  - Lower revenues due to declining gas prices
  - Inability to procure new leases or maintain existing leases
  - Company holds thousands of gas leases
  - Company is the operator under a number of JOAs, Rig Leases and Marketing Agreements

# Bankruptcy Sale and Auction Process

- Why Acquisition in Chapter 11?
  - Seller is in distress
  - Secured lender may require it
  - Purchaser may require it
  - Minimize challenges to the sale
  - Sale is free and clear
  - Easier to assign contracts
  - Resolve Title Issues



# Bankruptcy Sale and Auction Process

- Section 363 of Bankruptcy Code
  - Primary provision to implement acquisition
  - Sale of all or a portion of debtor's property
  - Sale free and clear of any interest in property
  - Sale free and clear, only if:
    - consent from entity with interest in property;  
or
    - without consent if the interest is a lien and price for property is greater than aggregate value of all liens

# Bankruptcy Sale Timeline

- Sale Timeline

- Investment bankers retained to market assets
- Data room established and due diligence materials prepared
- Prepare teaser and information memorandum
- Contact prospective buyers; distribute teaser
- Negotiate confidentiality agreements
- Distribute information memorandum
- Management presentations and due diligence
- Selection of stalking horse bid





## Bankruptcy Sale Timeline (cont'd)

- Sale Timeline
  - Negotiate stalking horse APA and bid procedures/protections
  - **File chapter 11**
  - Obtain Court approval of bid procedures/protections (including credit bid rights or limitations)
  - Market assets
  - Qualify bidders (deposits, blackline APA, no outs)
  - Deadline for submission of competing bids
  - Auction
  - Court approval of prevailing bidder

# Bankruptcy Stalking Horse Bid Protections

- Bid Procedures and Stalking Horse Protections
  - Established in Court Order
  - Break-up Fee
  - Expense reimbursement
  - Overbid requirement
  - Required bid increments
  - Credit bid the break-up fee
  - Consider Credit Bid Rights



# Bankruptcy Sale – Assignment of Contracts

- Bankruptcy Code Allows Contract Assignment
  - Leases and contracts may be assumed/assigned or rejected
  - Assignment can be implemented despite consent rights of counter-party to contract
  - Assignment requires curing past defaults and providing adequate assurance of future financial performance
  - Who pays cure (buyer or seller) is a negotiated point



# Bankruptcy Sale – Contract Assignment Issues

- Treatment of O&G Leases in Bankruptcy
  - Most jurisdictions treat oil and gas leases as interests in real property
  - May not be able to rely on Bankruptcy Code provisions that allow assumption and assignment of leases
  - Lessor consent provisions may be applicable



## Bankruptcy Sale – Contract Assignment Issues

- Treatment of JOAs in Bankruptcy
  - JOAs are executory contracts that may be assumed / assigned or rejected in an operator's bankruptcy
  - Purchaser can decide whether to take an assignment of JOA from Seller
  - Assignment requires payment of cure and adequate assurance of future performance

# Asset vs. Stock Acquisition

- May need to acquire new equity instead of assets
  - Avoids recording a multitude of lease assignments
  - Avoids obtaining any necessary consents to lease assignments
  - May not be a 363 sale process, but an 1129 plan process
  - Plan process may take longer than 363 sale process
  - Buyer may serve as plan sponsor
  - under plan of reorganization / liquidation
  - New equity is issued in seller that receives discharge under plan



## Due Diligence Issues

- Usually on a fast track
- May require substantial effort if number of oil and gas leases is large
- Environmental issues should be examined
- Buyer's lender may have more stringent requirements as to "materiality" Due diligence needs to take this into account
- If stalking horse, consider work fee

# Purchase Agreement Negotiation

- Competitive bidders should consider “going light” on markup to stalking horse bid
- Pay attention to adjustments due to changes in gas prices from effective date until closing
- Focus on working capital adjustments
- Agreement should indicate who is responsible for “cure obligations”
- Seller - consider limiting damages for breach to purchase deposit



## Post Acquisition Issues

- After the Closing:
  - Who is responsible for cure on assumed contracts?
  - Responsibility for claim resolution process
  - Consider effort in recording lease assignments
  - Consider effort in recording mortgage in each county from acquisition financing
  - Who receives tax refunds and who is responsible for doing work to receive them?



# Benefits of Chapter 11

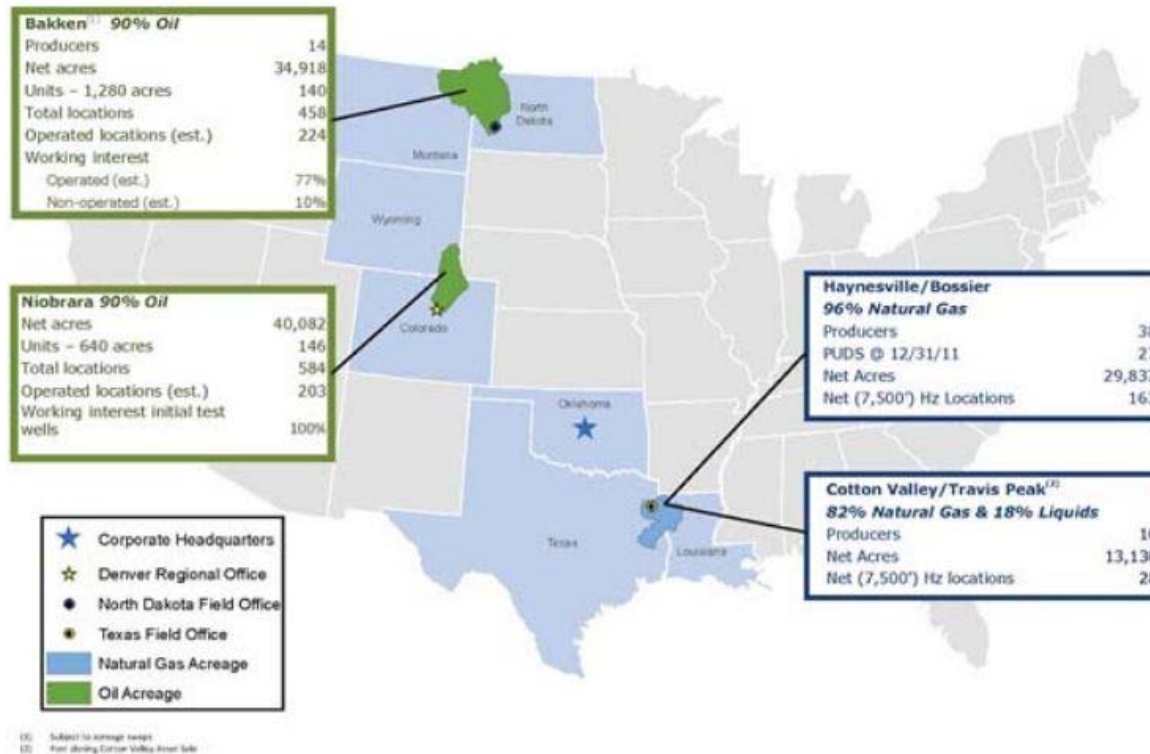
## Benefits of Chapter 11 Acquisitions

- Assets are free and clear of liens, claims and interests
- Resolution of Title and Environmental Issues
- Resolve Consent Issues
- Cherry Pick the Good Assets
- No fraudulent transfer risk
- Limited successor liability
- Court approved bid procedure
- Bid Protections
- Reimbursement and breakup fees
- Possibility of low purchase price
- Stalking horse may be DIP Lender

# Current Cases – GMX Resources, Inc.

Oil and gas exploration and production company

Chapter 11 filing in Western District of Oklahoma on April 1, 2013



## Current Cases – GMX Resources, Inc.

- Issues
  - Significant long term debt of \$ 427 million
  - Insufficient capital to fund debt service (interest on bond debt - \$43 million/year)
  - Insufficient capital to continue drilling program to develop proven undeveloped reserves
  - Company was unable to raise capital from debt/equity offerings in early 2013
    - Credit Suisse engaged but no investor interest
    - Jefferies engaged but no investor interest

## Current Cases – GMX Resources, Inc.

- Bankruptcy case proposed resolution
  - Basic liquidation in chapter 11
  - DIP financing provided by “Backstop Lenders” that hold about 80% of Senior Secured Notes.
  - Backstop Lenders will serve as a stalking horse for a 363 sale (credit bid amount to be determined).
  - Sale procedures
    - File sale motion within 20 days from petition date
    - Bid procedures approved within 30 days from filing sale motion
    - Order approving sale of assets entered within 75 days from filing sale motion

## Current Cases – ATP Oil & Gas

- Bankruptcy case overview
  - Case filed in Southern District of Texas (Houston) on August 17, 2012
  - Roll-up DIP loan, ATP has utilized majority of availability under DIP loan
  - ATP faced with numerous operational issues that have decreased revenue and increased expenses
  - This has required three court approved amendments to the DIP loan
  - ATP sought Bankruptcy Court approval to shut in Gomez field – NPIs, Overrides, perpetual royalties and expenses have made field unprofitable

## Current Cases – ATP Oil & Gas

- Asset Sale Procedures
  - Sale includes Shelf Assets and Deepwater Assets
  - Lenders allowed to credit bid
  - April 16, 2013 Bid Deadline
  - April 23, 2013 Auction
  - April 25, 2013 Sale hearing
  - May 9, 2013 Deadline to consummate sale; DIP financing and cash collateral use terminates
  - Deadlines subject to change

## Current Cases – ATP Oil & Gas

- ORRI/NPI Litigation
  - Pre-bankruptcy, ATP “sold” term ORRI/NPI interests for appx. \$500 million [ORRI/NPI interests relate to offshore wells]
  - Post-bankruptcy, ATP calls the term ORRI/NPI interests “disguised financing transactions” in order to bring the interests back into the bankruptcy estate
  - Certain ORRI/NPI holders sue in Bankruptcy Court seeking validation of transactions as true sales



## Current Cases – ATP Oil & Gas

- ORRI/NPI Litigation - Procedure
  - Bankruptcy Court will undertake two phase consideration:
    - Court will consider “financing issues” first – whether the ORRI/NPI interests constitute outright transfers of ownership or are disguised financings.
    - If the Court determines the ORRI/NPI interests are disguised financings and not true sales, the Court will determine the priority of the competing interests [the ORRI/NPI interests will be property of the bankruptcy estate and the court will determine who has claim to the assets]

## Current Cases – ATP Oil & Gas

- ORRI/NPI Litigation - Issues
  - What is the nature of a Federal, offshore oil and gas lease?
  - What is the nature of the ORRI/NPI interests? [real property production payment or contract right subject to rejection under 365 of Bankruptcy Code]
    - If real property production payment, ORRI/NPI holders retain the interest
    - If contract right subject to rejection, ATP can retain the interest
    - Or, recharacterize the transaction as a disguised financing and ATP can retain the interest

## Current Cases – ATP Oil & Gas

- ORRI/NPI Litigation - Issues
  - What law applies in making this determination?
    - Louisiana law – production payment is a real property interest.
    - Bankruptcy Code – production payment is not property of the estate
    - OCSLA choice of law issues – use state law unless conflict with Federal law.

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