Distressed Energy Assets:
Market Update and Key Considerations for Acquirers

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Roadmap

■ **Current Climate:** Discussion of the current restructuring environment

■ **Tactical Considerations:** The pros and cons of purchasing through bankruptcy and the differences between jurisdictions

■ **Process Questions:** Identification of potential targets and getting a seat at the table

■ **Legal Developments:** Changes in the legal landscape since the last downturn and after *Sabine*
Current Climate
What’s Going On?

- Upsurge in O&G-related bankruptcies in 2019 and more expected in 2020
- Current oil prices dramatically lower now
- Shale operators and OFS companies at greatest risk
Potential Reactions by E&P Companies

- Cut cap ex, and, in extreme cases, shut in wells to preserve for future production
- Delay plugging and abandonment activity where possible
- Cut expenses (i.e., employees, benefits)
Potential Reactions by E&P Companies (cont.)

- Cut shareholder dividends
- Limit merger and acquisition activity and any other non-critical spending
- Draw down revolvers prior to borrowing base redetermination
- Negotiate extensions of debt maturities
Predictions

- More covenant and payment defaults
- Difficulties in refinancing
- More contentious restructurings
- Second round of restructuring for some
- Forced liquidations
Acquisition and Divestiture Market

Upstream

- PE consolidating management teams
- Activity currently very sluggish but should pick up as more distressed assets come on the market
- Seeing more interest in gas assets as the supply/demand outlook for natural gas is improving
- Earn-outs becoming much more commonplace
- Midstream companies getting a seat at the table (or on the Zoom call)
  - Midstream issues (MVCs) often have to be addressed before a deal can be made
  - Complicates the transaction
  - Lengthens the negotiation process
Acquisition and Divestiture Market

Midstream

- PE consolidating management teams
- Activity also sluggish
- Critical to evaluate target’s midstream contracts
  - Credit/bankruptcy risk of counterparty
  - Risk of rejection in bankruptcy
  - Strength of dedication, release, assignment and other commercial provisions
Tactical Considerations
Pre-Filing Considerations

- Retention of advisors
- Source of DIP lending/exit financing
- Retention of a chief restructuring officer
- Restructuring v. liquidation
- Restructuring support agreement
Out of Court Sales

- Requires approval from board of directors/managing members
- Must properly exercise fiduciary duties
- Business judgment rule applies
- Lenders must agree to release liens
- Junior lienholder may refuse to release lien if proceeds insufficient to pay all
Bankruptcy Sales

- With court approval, can sell assets free and clear of all liens, claims and encumbrances

- Sale process governed by court order, usually including:
  - Ground rules for bids
  - Stalking horse bidder with bid protections
  - Auction
  - Hearing to approve winning bid
Bankruptcy Sales (cont.)

- Highest and best bid determined by debtor in consultation with stakeholders

- Difficult to challenge:
  - Disappointed bidder generally lacks standing in court
  - Quick closing moots appeal
  - Finding of good faith purchaser prevents unwinding sale after appeal
Process Questions
Purchasing through Bankruptcy

■ Strong bid = advantage to stalking horse
  ▪ Control the form of the asset purchase agreement and key terms
  ▪ Break-up fee and expense reimbursement
  ▪ Other bid protections

■ Looking for lower price = qualify and wait for auction
Purchasing through Bankruptcy
(cont.)

- Lenders can credit bid
- Potential advantages to purchasing existing claim
- Opportunities for taking assignment of contracts and leases
Legal Developments
Recent Bankruptcy Filings

- Whiting Petroleum Corporation
- Southland Royalty Company
- Alta Mesa Resources, Inc./ High Mesa, Inc.
- Sanchez Energy Corporation
Evolving Midstream Issues

- Within bankruptcy, courts have reached differing conclusions regarding whether midstream agreements can be rejected as executory contracts or are covenants running with the land and not subject to rejection.
- The SDNY has favored treating midstream agreements as executory contracts.
- The District of Colorado and Southern District of Texas have interpreted midstream agreements as covenants running with the land.
- These differing approaches can have a significant effect on a debtor’s options in a Chapter 11 case.
- Outside the bankruptcy context, there are increasing concerns regarding force majeure declarations and midstream contracts.
Decisions after *Sabine*


- *Alta Mesa Holdings, L.P. v. Kingfisher Midstream, LLC*, Bankruptcy Court for the Southern District of Texas, December 20, 2019 (applying Oklahoma law)