



Locke Lord's High Noon Knowledge Series

Distressed Energy Assets:

Market Update and Key Considerations for Acquirers

Philip Eisenberg
Bankruptcy,
Restructuring &
Insolvency Practice

Elizabeth Guffy
Bankruptcy,
Restructuring &
Insolvency Practice

Terry Radney
Co-Chair
Energy Practice

April 23, 2020

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*

- ***Monarch Midstream v. Badlands Production Company***, Bankruptcy Court for the District of Colorado, September 30, 2019 (applying Utah law)
- ***Alta Mesa Holdings, L.P. v. Kingfisher Midstream, LLC***, Bankruptcy Court for the Southern District of Texas, December 20, 2019 (applying Oklahoma law)

Q&A



Philip Eisenberg
T: 713-226-1304
peisenberg@lockelord.com



Terry Radney
T: 713-226-1384
tradney@lockelord.com



Elizabeth Guffy
T: 713-226-1328
eguffy@lockelord.com

Atlanta | Austin | Boston | Brussels | Chicago | Cincinnati | Dallas | Hartford | Hong Kong | Houston | London | Los Angeles
Miami | New Orleans | New York | Princeton | Providence | San Francisco | Stamford | Washington DC | West Palm Beach

ATTORNEY ADVERTISING. Locke Lord LLP disclaims all liability whatsoever in relation to any materials or information provided. This presentation is provided solely for educational and informational purposes. It is not intended to constitute legal advice or to create an attorney-client relationship. If you wish to secure legal advice specific to your enterprise and circumstances in connection with any of the topics addressed, we encourage you to engage counsel of your choice. © 2020 Locke Lord LLP