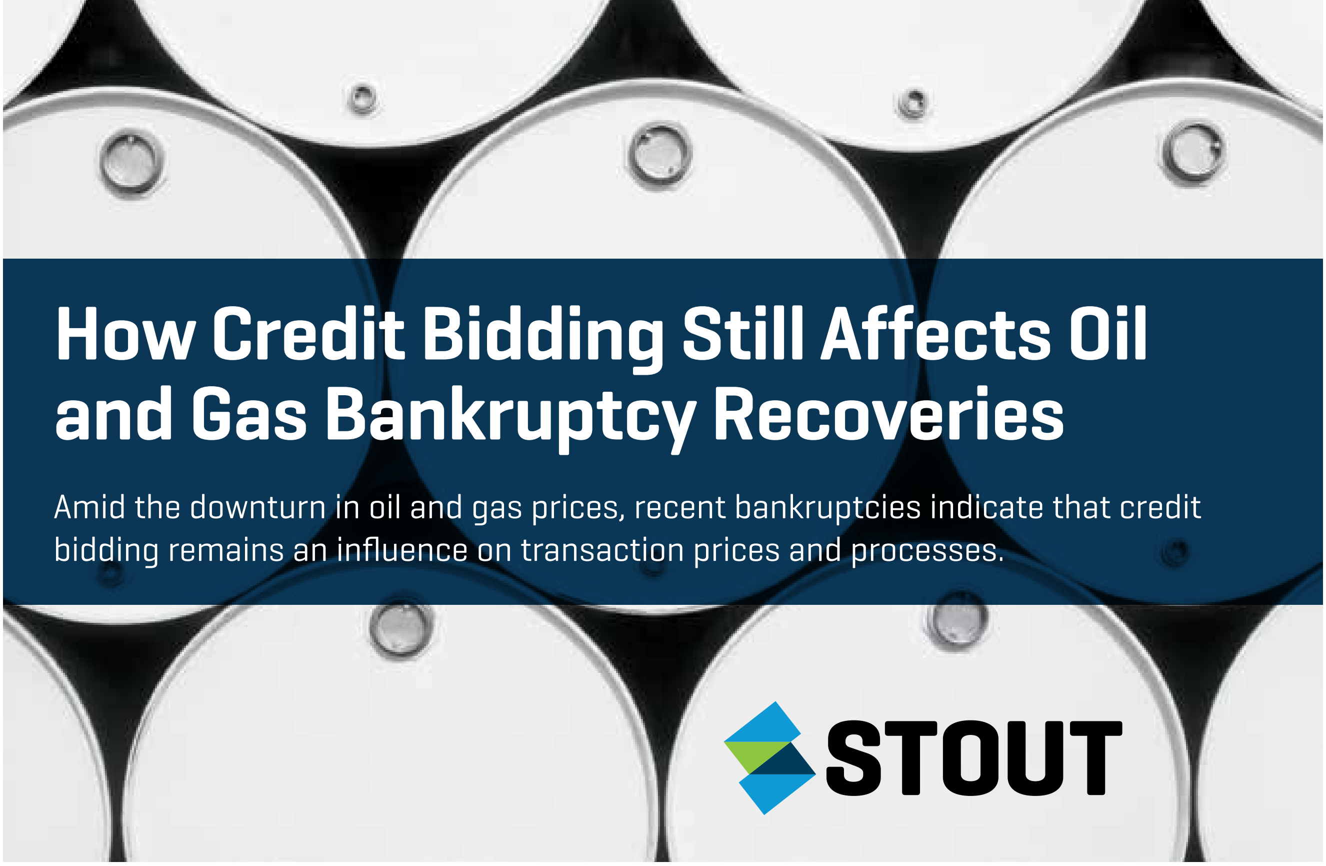
How Credit Bidding Still Affects Oil and Gas Bankruptcy Recoveries

Amid the downturn in oil and gas prices, recent bankruptcies indicate that credit bidding remains an influence on transaction prices and processes.

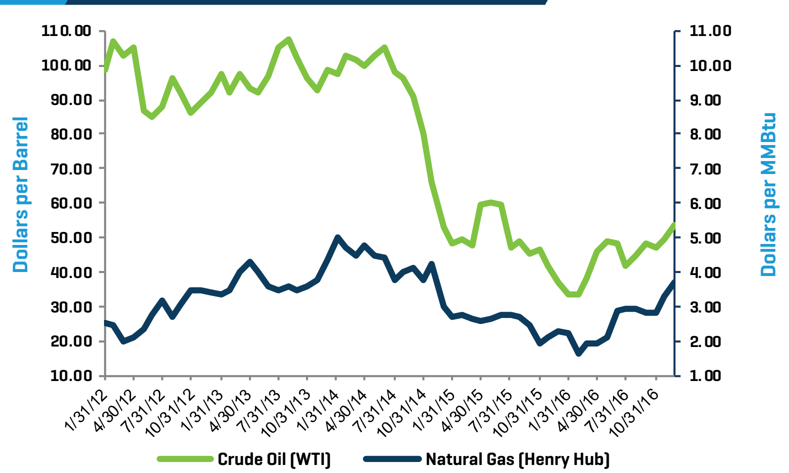


In 2014, while reporting on credit bidding during oil and gas bankruptcies,[1] we found that in instances where credit bidding was a factor, the estate secured a value that was distinctly lower than the average market price of comparable transactions. Since then, the price of oil has fluctuated a great deal, first falling significantly, then rebounding slightly, and finally starting to recover (Figure 1).

We revisit the topic of credit bidding and examine information related to the recent oil and gas downturn. At question is whether these events have resulted in different findings nearly three years later.

From January 1, 2014, through December 1, 2016, 114 oil and gas companies sought bankruptcy protection.[2] Of these companies, 23 were publicly listed in the U.S. at the time of filing. The UCLA-LoPucki Bankruptcy Research Database (BRD), which covers public companies, is useful in analyzing these restructurings. According to the BRD, the restructuring transactions fell into five categories, as shown in Figure 2.

FIGURE 1 5-YEAR HISTORICAL OIL AND GAS PRICES AS OF JAN 5, 2017



Source: Bloomberg

FIGURE 2 RESTRUCTURING TRANSACTIONS OF PUBLIC OIL AND GAS COMPANIES

Transaction Type	# of Transactions
Credit bid	4
Sale	4
Debt for equity exchange	12
Quasi-sale	1
Ongoing	2
Total	**23**

Source:
UCLA-LoPucki Bankruptcy Research Database
Data: January 1, 2014-December 1, 2016

[1] "How Credit Bidding Is Impacting Oil and Gas Bankruptcy Recoveries," Stout Journal, Fall 2014.
[2] Haynes and Boone LLP Oil Patch Bankruptcy Monitor, updated December 14, 2016.

Four of the 23 public company restructuring transactions involved credit bidding by secured lenders. One transaction involved an equity sponsor and senior lender funding a separate company that acquired the bankrupt company's assets in exchange for assuming certain liabilities. The other cases were negotiated asset sales (four), debt for equity exchanges (12), or still ongoing as of January 2017 (two). So it is clear that during the downturn, debt for equity exchanges were more popular than sales processes where the lender was interested in credit bidding – even though both methods often end with the creditors as the new equity owners.

We evaluated the four credit bidding cases to determine whether the prices obtained at auction were comparable with those realized in similar transactions during the same time period. For this analysis, we used transactions reported by IHS Herold. It should be noted, however, that each case is unique, and in some cases multiple issues can impact the value obtained.

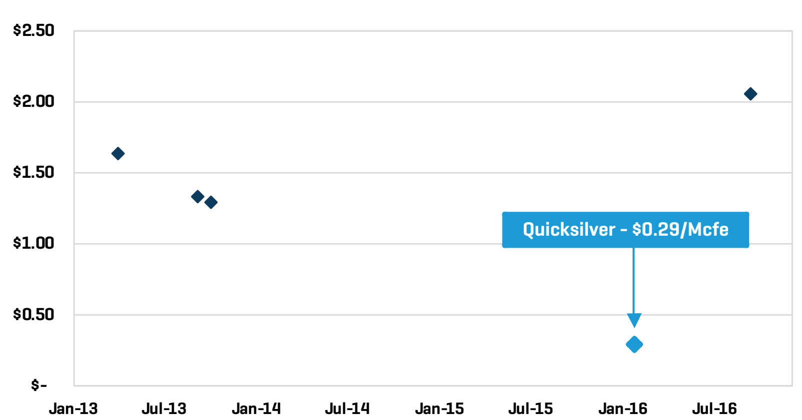
The following is a brief recap of each of the credit bidding cases.

Quicksilver Resources

Quicksilver Resources filed for Chapter 11 bankruptcy protection in the state of Delaware on March 17, 2015. The firm's oil and natural gas properties in the U.S. were principally located in the Barnett Shale in north-central Texas and the Delaware Basin in western Texas. Quicksilver's Canadian subsidiaries were not included in the bankruptcy. As of December 31, 2014, Quicksilver had reported owning approximately 89,000 net acres in the Barnett Shale, with proven reserves of approximately 0.8 trillion cubic feet equivalents. The Delaware Basin properties were largely development-stage investments and had few reserves.

After months of marketing Quicksilver's assets, an auction was held January 20-21, 2016. Quicksilver declared the all-cash bid for the oil and gas assets from BlueStone Natural Resources II, LLC in the amount of $245 million the highest or otherwise best bid. On January 22, 2016, Quicksilver and BlueStone executed the asset purchase agreement for this sale, with an implied transaction value of $0.29/million cubic feet equivalents (Mcfe), as shown in Figure 3. The backup buyer was a lender group with an offer of $250 million, composed of $93 million in cash and a $157 million credit bid.

FIGURE 3 QUICKSILVER AND RELATED BARNETT SHALE TRANSACTIONS (US$/MCFE)



Source: IHS Herold

Emerald Oil

Emerald Oil and its affiliates filed for Chapter 11 bankruptcy protection in Delaware on March 22, 2015. The company's assets consisted of approximately 76,000 net acres in the Williston Basin in North Dakota. The debtors estimated that their holdings as of December 31, 2014, included approximately 14.0 million barrels of proven, developed oil reserves and approximately 11.0 billion cubic feet of proven, developed natural gas reserves, for total reserves of 15.9 million barrels of oil equivalent (MMBoe).

In the months leading up to the petition date, the debtors negotiated with various parties concerning a potential sale of a material portion or substantially all of the debtors' assets. Emerald Oil then entered into a stalking horse asset purchase agreement with a buyer formed and owned by CL Energy Opportunity Fund, L.P., and SSC Emerald LP, with the initial bid of $73 million later increasing to $110 million. An auction was scheduled to take place on September 29, 2016. Pre-auction, New Emerald Energy, a company formed by a slightly different lender group, also submitted a qualified bid. When the stalking horse bidder indicated that it had decided not to participate in the auction, the debtors designated New Emerald Energy's $110.5 million bid as the successful bid.

New Emerald Energy is jointly owned by Cortland Capital Markets, LLC; CL Energy Opportunity Fund, L.P.; and affiliates of Fir Tree Partners.

New Emerald Energy's investors were prepetition secured creditors who credit bid most of the $110 million outstanding on the prepetition secured credit facility and the debtor-in-possession package provided to Emerald. New Emerald Energy's winning offer comprised a $94.5 million credit bid, $16 million cash, and the assumption of certain obligations. The implied transaction value was $6.95/barrel of oil equivalent ($6.95/Boe), as shown in Figure 4.

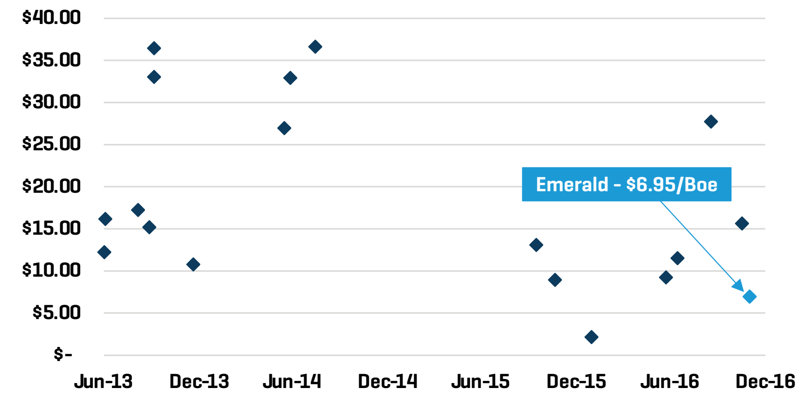
RAAM Global Energy

RAAM Global Energy and its affiliates filed for Chapter 11 bankruptcy protection in Houston on October 26, 2015. The company's producing assets were located offshore in the Gulf of Mexico and onshore in Louisiana, Texas, Oklahoma, and California. As of September 30, 2015, the debtors had estimated total proven oil and natural gas reserves of 8.57 MMBoe. Of the reserves, 47% were in the shallow waters off the Louisiana shore and 53% were onshore.

In the months prior to filing for bankruptcy, RAAM sought to restructure its debt by proposing to its noteholders an exchange for a share of $50 million in new notes and 1.17 million shares of RAAM common stock. However, RAAM failed to attain the 99% minimum required by the exchange offer conditions, with only 94.77% of the outstanding noteholders tendering their notes for exchange. In response, the debtors and their investment bankers undertook a thorough marketing process seeking third-party stalking horse bidders. Despite coming close to finalizing a purchase agreement with a stalking horse bidder for a portion of RAAM's assets, the debtors saw the potential agreement fall through due to changing market conditions.

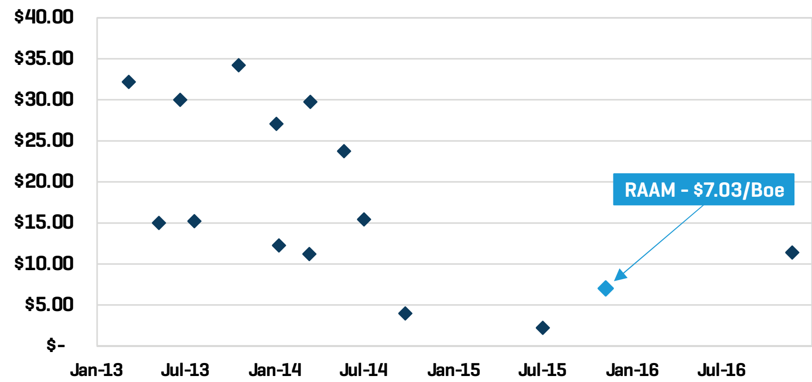
A private equity fund then acquired the first lien debt, which was secured by a first lien on substantially all of the debtors' real and personal property, and entered into a stalking horse agreement

FIGURE 4 EMERALD AND RELATED BAKKEN SHALE/WILLISTON TRANSACTIONS (US$/BOE)



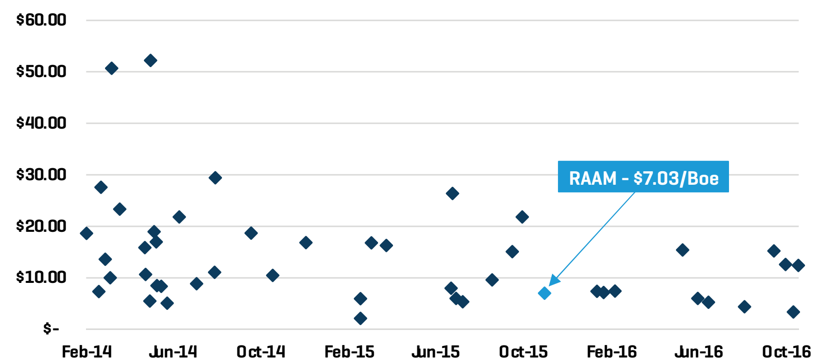
Source: IHS Herold

FIGURE 5 RAAM AND RELATED GULF OF MEXICO TRANSACTIONS (US$/BOE)



Source: IHS Herold

FIGURE 6 RAAM AND RELATED GULF COAST ONSHORE TRANSACTIONS (US$/BOE)



Source: IHS Herold

with the company. The fund submitted an offer that included a $58.8 million credit bid, $2.5 million cash, and the assumption of certain obligations. No other buyers participated in the auction. The implied transaction value was $7.03/Boe. Although the public sale documents do not provide an allocation of the purchase price to the onshore or offshore assets, Figures 5 and 6 assume that the purchase price was split 47% offshore and 53% onshore.

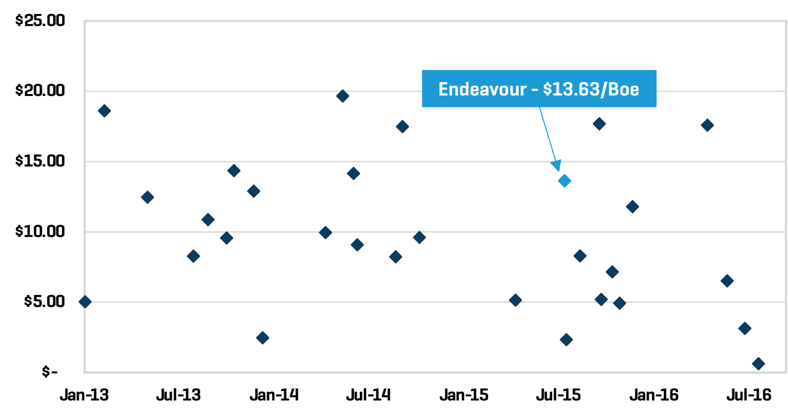
Endeavour International

Endeavour International and certain affiliates filed for Chapter 11 protection on October 10, 2014. The company held working interests in oil and gas leases in the U.S. as well as North Sea oil and gas licenses in the U.K. Endeavour's U.K. assets composed approximately 82% of its proven reserves, and its U.S. assets rounded out the remaining 18%. As of December 31, 2014, Endeavour reported total proven reserves of 12.2 MMBoe.

After a contentious process, on August 3, 2015, Endeavour reached an agreement with its unsecured creditors and secured lenders. The offer comprised a $398 million credit bid for equity in the U.K. holding company, an intercompany note from the U.K. entities, and a commitment to pay administrative expenses and to wind down the U.S. operations. As of December 31, 2014, the U.K. proven and probable (2P) assets totaled 29.2 MMBoe, for an implied transaction value of $13.63/Boe (Figure 7).

On August 11, 2015, Endeavour sold its U.S. assets in Colorado and in the Marcellus and Haynesville basins in the northeast and the southwest U.S., respectively. Augustus Energy Partners II LLC bought the Colorado assets with a cash offer of $7.85 million. Energy Reserves Group LLC won the auction for the Marcellus and Haynesville shale assets with a cash bid of $1.46 million.

FIGURE 7 ENDEAVOUR AND RELATED NORTH SEA TRANSACTIONS (US$/BOE)



Source: IHS Herold

FIGURE 8 ANALYSIS OF CERTAIN ASPECTS OF THE SALES PROCESS

Company	Time for Auction Process	Title, Ownership, or Reserve Report Issues	Number of Bidders	Credit Bidding	Sales Price Achieved	Market Comparable Prices
GMX	21 weeks	No material Issues	2	Yes	$1.58 per Mcfe	$2.73 per Mcfe
Delta	20 weeks plus time prior to filing	No material Issues	9	Yes	$0.28 per Mcfe	$2.33 per Mcfe
ATP	16 weeks	No material Issues	5	Yes	$3.60 per Boe	$21.72 per Boe
TXCO	16 weeks	No material Issues	2+	No	$22.79 per Boe	$19.12 per Boe
Edge Petroleum	8 weeks plus time prior to filing	No material Issues	2	No	$2.84 per Mcfe	$1.86 per Mcfe
Transmeridian Exploration	13 weeks	No material Issues	3	Yes	N/A	N/A

Source: IHS Herold

FIGURE 9 ANALYSIS OF CERTAIN ASPECTS OF THE SALES PROCESS

Company	Time for Auction Process	Title, Ownership, or Reserve Report Issues	Number of Bidders	Credit Bidding	Sales Price Achieved	Market Comparable Prices
Quicksilver Resources Inc.	15 weeks	No material Issues	2	Yes (Back up Bidder)	$0.29 per Mcfe	$1.58 per Mcfe
Emerald Oil, Inc.	4 weeks plus time prior to filing	No material Issues	2	Yes	$6.95 per Boe	$19.18 per Boe
RAAM Global Energy Company	5 weeks plus time prior to filing	No material Issues	1	Yes	$7.15 per Boe	$18.85 per Boe (offshore) $14.28 per Boe (onshore)
Endeavour International Corporation	11 weeks	No material Issues	1	Yes	$13.63 per Boe	$9.76 per Boe

Source: IHS Herold

Analysis and Comparison – 2014 vs. Recent Transactions

In our 2014 article, we examined six transactions for the effect of credit bidding. Figure 8, taken from that article, presents a summary of the cases that were studied.

Our more recent analysis of four transactions that involved credit bidding revealed that in two cases the value realized by the estate was below market value, while the other two were consistent with contemporaneous sales (Figure 9).

Reviewed alongside four comparable sales, the Quicksilver sale realized the lowest transaction price per Mcfe. The Emerald sale, measured against seven comparable transactions during 2015 and 2016, realized the second-lowest transaction price per Mcfe. Analysis of the RAAM transaction was more complex because the debtor did not report an allocation of value to onshore or offshore assets, and yet the 2015 and 2016 onshore and offshore comparable transactions show that the sale price was consistent with the market. The Endeavour sale of North Sea assets realized a transaction price that was also consistent with the market.

The Effect of Credit Bidding

Our recent study revealed that in the current wave of oil and gas bankruptcies, the time to auction is significantly faster compared with findings in the 2014 analysis. Meanwhile, the number of bidders participating in the auctions is significantly lower.

With the support of this evidence, we continue to believe credit bidding can have a negative effect on transaction prices due to other bidders being discouraged from participating when the lender is also a potential buyer. To minimize this negative effect, debtors and other interested parties should negotiate terms during the marketing process to ensure that all bidders have a fair opportunity to participate.

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