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Cover Story

Houston bankruptcy law firms beef up to handle uptick of energy bankruptcies

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Charlie Beckham began his bankruptcy practice in the 1980s, where he represented several companies during the oil crash. In the 1990s, he advised bankruptcy clients such as El Paso Refinery and Circle K. Today, he stays busy as a partner in the bankruptcy practice of Haynes and Boone LLP, No. 4 on Houston Business Journal's 2016 Largest Bankruptcy Law Firms List.



SOURCE: HAYNES AND BOONE LLP

This cycle, however, has a different significance for him than those of the past.

“My son works in the oil and gas industry. He hasn’t been laid off yet, but it is something I talk to him about on a fairly frequent basis just to see what’s going on,” Beckham said.

Beckham recognizes that this is part of his profession — consulting energy companies on what to do during one of the more than 150 bankruptcies that have been filed by energy companies in North America since January 2015. A consolidation here, a capital reallocation there. It means the same thing.

“It personalizes it,” Beckham said. “It makes me realize that when a company is laying off employees and terminating contracts, it has a broader, more sweeping

effect. It affects human beings who go to work every day, work hard and because of factors beyond their control, helping one company survive may have an adverse impact upon some other business.”

Dozens of lawyers like Beckham are in their heyday right now in Houston. Since January 2015, the bankruptcies filed in North America by upstream and oil field services companies have collective debts valued at more than \$65.89 billion, and the pace continues to increase. The value and frequency of energy bankruptcy filings in the first half of 2016 compared to the same time last year is more than 10 times larger, and experts predict we have only reached the halfway point.

All of this creates a busy time for bankruptcy lawyers in Houston and around the country. Practices are beefing up their bankruptcy teams, either through new partner hires or pulling from other departments internally, and everyone is taking stock of their client list to make sure it's squared away.

Today's bankruptcy lawyers understand that a busy day in their job means a bad day in someone else's, but still, bankruptcy is a booming business in the Bayou City.

How we got here

When U.S. exploration and production companies began to ramp up land acquisitions in places like the Eagle Ford, Permian and Bakken, it was due in large part to revolutionary technology involving fracking. It opened the floodgates on what was once a relatively small supply of accessible oil and natural gas, creating a new opportunity for E&P players to unearth millions of barrels of oil and gas at attainable costs.

Following the Great Recession in 2009, the U.S. rig count rose from 876 rigs nationwide to its peak of 2,026 rigs in November 2011, according to the Baker Hughes rig data.

Then it all crashed.

Why the crash happened is subject to different theories, but on a high level, it's a simple case of supply and demand. The U.S. technological advancements with fracking created a glut beyond anyone's wildest dreams.

“Technology caught up to people so fast, they just couldn’t prepare for it,” said John Higgins, a Houston partner and leader of the bankruptcy practice at Houston-based Porter Hedges, which ranks No. 1 on HBJ’s Bankruptcy Law Firms List.

Companies valued the cost of oil in the ground between \$75 and \$100 a barrel, and they were getting money to drill at those prices. However, over time, the uptick in drilling led to a dramatic oversupply in the market. The domestic boom, coupled with geopolitical factors in the Middle East, and very rapidly there was a massive oversupply of oil. E&P companies began to significantly curtail their production through a reduced rig count. But as the price of oil continued its downward trend, it meant smaller and midsized companies were forced to make cuts. That includes a reduction of workforce, restriction of research and development budgets and contract restructuring.

Additionally, the maturity of the capital markets compared to the 1980s significantly increased the amount of capital in play in today’s energy industry, experts say. Interest rates on loans were significantly cheaper, and banks were willing to invest in an energy market that looked wildly optimistic. Companies continued to drill, service companies continued to manufacture parts and hire workers to handle the industry with no end in sight.

“You can see them tightening their belt, cutting fat. Now they’re cutting into muscle,” said Hugh Ray, a principal at McKool Smith and the head of the firm’s bankruptcy practice. McKool Smith ranks No. 2 on HBJ’s Bankruptcy Law Firms List. “They entertained the fantasy of being profitable at fairly low prices for a while, but as long as oil prices stay anywhere near where they are now, the fellas who made this country energy-independent with fracking are not going to be able to stay in business.”

Bankruptcies boom in Houston

Of all the energy bankruptcies filed in North America since January 2015, the Southern District of Texas, which includes Houston cases, has carried the lion’s share.

Texas bankruptcy courts have handled 82 of the 157 energy-related bankruptcies since the beginning of 2015, according to data from Haynes and Boone. That

equates to 52 percent of the \$65.89 billion worth of bankruptcies filed in this cycle.

The Southern District of Texas has handled 34 bankruptcies, which includes more than \$23 billion worth of debt. In comparison, the South District's 34 bankruptcy cases so far are more than Canada or any other individual state where an energy bankruptcy has been filed.

Bankruptcies are either filed where a company is incorporated, where a company is domiciled or where a company has its primary place of business. For a company in the energy industry, usually one of those three criteria mean Houston, or at the very least, Texas. In many cases, these companies choose to file here because of the knowledge base of the bench and track record of favorability, bankruptcy lawyers say.

"There are good judges everywhere, but Texas currently has good judges with a lot of experience in the oil and gas industry with more dexterity with respect to the oil and gas industry," said Beckham with Haynes and Boone.

And, coincidentally, a case with precedent was established when a Houston company chose to take its monumental bankruptcy elsewhere.

"Enron was filed in New York. The judge in that case said you can file for bankruptcy where you want," said McKool's Ray. "On that same rationale that Enron had its business in New York City, some of the companies headquartered around the country would come here because oil and gas is a specialized business and if you have judges familiar with the terminology, you're like to get a more fair and quicker result."

What happens next

What happens in the future is partially dependent on the price of oil in the near term, however, most believe the prolonged downturn has already caused damage beyond repair for many companies in E&P and oil field services.

Whether a company makes it out of this downturn whole is dependent on how they valued their assets during peak times. If a company borrowed from a bank saying its assets are worth \$100, it needs to meet that cost structure in order to repay the

loan on time. Stronger companies are able to take out second liens at harsher interest rates to try and weather the storm, but for many, bankruptcy is the only place to turn.

“(Some companies) were able to go out to the markets and find the expensive money again,” Beckham said. “Some companies have been able to do that, some have not. The ones that have not been able to buy additional time by getting expensive financing have tumbled, so far.”

The industry has essentially reached the halfway point, and that by the end of 2016, we’ll be looking at around 300 bankruptcies filed in the industry, said Buddy Clark, head of Haynes and Boone’s energy practice.

That said, many are looking at the fallout a bankrupt oil and gas industry can have on the larger Houston economy.

“Next year, we’ll see apartments and office space go in the tank. We’ll see some banks have some problems. It’s a trickle-up deal. Bankruptcies are a trailing indicator,” Ray said.

The grim outlook is in large part because low oil prices have already forced many of these companies to dive deeper into their pockets — or someone else’s — for additional operating capital. The ones that are able to go after harsher loans will do so, Beckham said, but for many, they’ve approached the end of the rope.

“Depending on the cost structure for production for these companies, the increase to say \$50 a barrel gives many companies the ability to pay their lease operations, pay general and administrative expenses, but still provides low levels to pay for cap expenditures,” Beckham said. “It doesn’t fix their balance sheet if its based on acquisitions that they did when oil was \$100.”

So if Chapter 11 occurs, what happens next is dependent on the assets a company has, the management team in control and the balance sheet. Private equity, institutional investors and other avenues of capital are still interested in the oil and gas industry, for the right price.

“A lot of folks who are debt holders are taking a long-term approach. They convert debt to equity and wait for commodity prices to return. That could mean shakeups

in management,” Beckham said.

And that seems to be an ongoing trend, where after a restructuring, debt holders are much more willing to stay involved with the company, believing that through the process the company was able to right size its balance sheet and can create an opportunity for a return on investment, Higgins said.

For others, however, it means the end of a business. Consolidations and liquidations could become more common for the companies that have a less-than-desirable asset portfolio and are overleveraged.

“And in 2019, 2020, the litigation starts over who is to blame for this, that and the other. That’ll drag on, and then there will be another downturn by the time that gets cleaned up,” Ray said.

Recruiting

With all of the action in bankruptcy court in recent months, the lawyers who specialize in the field are in high demand. Bankruptcy leaders and partners say they’re routinely fielding calls from headhunters and other firms looking to bolster a practice.

“We have one new lawyer who just started, and we’re looking for others,” Ray said. “We haven’t been busier since the 1980s.”

But while hiring more today is something firms are willing to do when the opportunity arises, for the most part, the market has been stable, partners say. That’s because this is the most exciting period in a bankruptcy lawyer’s career in terms of the level of workload, and the top firms are able to satiate their lawyers’ appetite with challenging and intriguing casework.

Other firms, in addition to adding bodies to their bankruptcy practice, pull from other departments in the law firm. Frequently, a bankruptcy trial needs expertise in energy, real estate, litigation and other departments, as well, said Shari Heyen, a bankruptcy shareholder at Greenberg Traurig, which ranked No. 10 on the HBJ's Bankruptcy Law Firms List.

“We’re able to successfully put together a team who can meet the issues of the case. We sit down in a round table fashion and talk in various ways to achieve a

result,” Heyen said.

North american energy cos. that have filed for bankruptcy in 2016

COVER STORY

NORTH AMERICAN ENERGY COS. THAT HAVE FILED FOR BANKRUPTCY IN 2016

In 2016, 76 North American energy companies have filed for bankruptcy, amounting to more than \$40 billion in debt, and experts expect that number to continue to climb. The largest bankruptcy of the year belongs to Houston-based Linn Energy LLC (Nasdaq: LINE) with more than \$5.9 billion in debt. However, when combined with its subsidiaries, Linn's debt is roughly \$8.28 billion, according to court filings. The company is expected to continue operations through its bankruptcy process and will continue to pay employee wages and health care.

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How many of the 75 North American energy bankruptcies filed in 2016 that include debts of \$1 billion or more.

FILING DATE	COURT	COMPANY	TOTAL
Jan. 11	Southern District Texas	Aurora Operating LLC	\$2.35 million
Jan. 18	Southern District Texas	MOG Producing LP	\$4.29 million
Jan. 19	New Mexico	Alliance Well Service LLC	\$4.5 million
Jan. 25	Northern District Texas	Antero Energy Partners LLC	\$25.45 million
Jan. 31	Delaware	Extreme Plastics Plus Inc.	\$69.9 million
Feb. 3	Northern District Texas	Emkey Resources LLC	\$22.35 million
Feb. 3	Western District Oklahoma	Osage Exploration and Development Inc.	\$39.46 million
Feb. 4	Southern District Texas	Ginger Oil Co.	\$6.47 million
Feb. 14	Delaware	Paragon Offshore PLC	\$2.4 billion
Feb. 17	Canada	Argent Energy Trust	\$153.4 million
Feb. 17	Southern District Texas	Argent Energy (U.S.) Holdings Inc.	\$51.9 million
Feb. 17	Southern District Texas	Primrose La Sara LLC	\$4.3 million
Feb. 19	Colorado	Craig Energy LLC	\$45.4 million
Feb. 26	Western District Texas	DRM Sales & Supply LLC	\$19.18 million
March 1	Colorado	D.J. Simmons Inc.	\$10.9 million
March 1	Northern District Texas	GreenHunter Resources Inc.	\$23.7 million
March 2	Northern District Texas	Universal Well Service Holdings Inc.	\$25.15 million
March 4	Southern District Texas	Wellhead Distributors International	\$31.7 million
March 4	Western District Louisiana	S-3 Pump Service Inc.	\$13.5 million
March 8	Northern District Texas	RMR Operating LLC	\$3.5 million
March 10	Southern District Texas	ESP Petrochemicals, Inc.	\$7.4 million
March 13	Northern District Texas	Wellflex Energy Solutions LLC	\$3.9 million
March 14	Northern District Texas	DJ Oilfield Seives LLC	\$3.01 million
March 15	Delaware	New Source Energy Partners LP	\$51.17 million
March 18	Delaware	Venoco Inc.	\$1.28 billion
March 22	Delaware	Emerald Oil Inc.	\$312 million
March 24	Eastern District Louisiana	Whistler Energy II LLC	\$155 million
March 25	Southern District Texas	East African Drilling Ltd.	\$45.35 million
March 28	Northern District Texas	Crossfire Manufacturing LLC	\$653,600
March 31	Northern District Texas	7711 Operating Company LLC	\$532,500
April 1	Western District Louisiana	Keithville Well Drilling & Services LLC	\$9.3 million
April 1	Western District Oklahoma	PostRock Energy Corp.	\$99.18 million
April 1	Western District Texas	ATK Oilfield Transportation Inc.	\$34.9 million
April 4	Western District Texas	Sanjel Inc.	\$1.1 billion
April 4	Western District Texas	Bluff Creek Production LLC	\$7.09 million
April 13	Southern District Texas	Hydrocarb Energy Corp.	\$12.5 million
April 13	Southern District Texas	Aztec Oil & Gas Inc.	\$1.5 million
April 14	Southern District Texas	Energy XXI Ltd.	\$2.75 billion

FILING DATE	COURT	COMPANY	TOTAL
April 15	Northern District Oklahoma	Sheehan Pipe Line Construction Co.	\$68.4 million
April 15	Northern District Texas	DiamoNorthern District Tank Rental Inc.	\$8.92 million
April 15	Southern District Texas	Goodrich Petroleum Corp.	\$444.2 million
April 21	Eastern District Texas	FPUSA LLC.	\$2.3 million
April 21	Northern District Texas	Paladin Energy Corp.	\$23.48 million
April 21	Western District Texas	Trinity River Resources LP	\$133.8 million
April 26	Western District Texas	West Texas Poly Pump LLC	\$3.7 million
April 29	Southern District New York	Pacific Exploration & Production Corp.	\$5.32 billion
April 29	Southern District Texas	Ultra Petroleum Corp.	\$3.9 billion
April 29	Utah	Energy Drilling LLC.	\$657,872
April 30	Southern District Texas	Midstates Petroleum Company Inc.	\$2.045 billion
May 2	Northern District Alabama	Calera Gas LLC	\$212,700
May 3	Alaska	Aurora Gas LLC	\$389,100
May 3	Western District Texas	CaNorthern Districtescent Well Service LLC	\$0
May 9	Delaware	Chaparral Energy Inc.	\$1.79 billion
May 11	Southern District Texas	Linn Energy LLC	\$5.962 billion
May 11	Southern District Texas	Berry Petroleum Company LLC	\$1.733 billion
May 11	Western District Texas	J P S Completion Fluids Inc.	\$4.49 million
May 12	Eastern District Virginia	Penn Virginia Corp.	\$1.18 billion
May 15	Southern District New York	Breitbart Operating LP	\$3.047 billion
May 16	Canada	Connacher Oil and Gas Ltd.	\$199.7 million
May 16	Southern District Texas	SandRidge Energy Inc.	\$4.19 billion
May 17	New Mexico	Hungry Horse LLC	\$5.4 million
May 17	Southern District Texas	Hawk Oilfield Service Inc.	\$1.2 million
May 17	Western District Texas	Tall City Well Service, LP	\$14.4 million
May 18	Pennsylvania	NuWeld Inc.	\$10.2 million
May 18	Western District Texas	Ricochet Energy Inc.	\$11.35 million
May 20	Delaware	Intervention Energy Holdings LLC	\$140 million
May 23	Southern District Texas	Armada Water Assets Inc./Wes-Tex Vacuum Service Inc.	\$24.9 million
May 24	Southern District Texas	Mark A. Martinez LLC	\$0
May 29	Southern District Texas	Linc USA GP	\$414.35 million
May 31	Colorado	Fort Drilling LLC	\$0
June 2	Southern District Texas	Warren Resources Inc.	\$486.3 million
June 3	Northern District Texas	Tauren Exploration Inc.	\$22 million
June 5	Delaware	Hercules Offshore Inc.	\$622 million
June 7	Delaware	Seventy Seven Energy Inc.	\$1.725 billion
June 17	Delaware	Maxus Energy Corp.	\$295.2 million
June 29	Delaware	Triangle USA Petroleum Corp.	\$691.8 million

NOTE: INCLUDES CHAPTER 7, CHAPTER 11, CHAPTER 15 AND CANADIAN CASES
SOURCE: HAYNES & BOONE