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Bankruptcy Update

Expert Analysis

Bankruptcy Filings In Oilfield Services Sector

By **Edward E. Neiger**

This article focuses on bankruptcy filings in the oilfield services sector as the industry reacts to capital expenditure cuts by upstream energy companies and a reduction in drilling activity. The column delves into the bankruptcy proceedings of Hercules Offshore Inc., Seventy Seven Energy Inc., Paragon Offshore plc and C&J Energy Services Ltd.

Offshore Drilling Vessels

On June 5, 2016, a mere six months after emerging from its last bankruptcy proceeding, Hercules Offshore Inc. and its affiliates filed voluntary petitions for relief under Chapter 11 of the Bankruptcy Code in the U.S. Bankruptcy Court for the District of Delaware.

Hercules' last bankruptcy case was a speedy reorganization whereby the debtors converted $1.2 billion in senior notes to equity in the reorganized company. Upon emergence, the debtors found the market for their services—providing vessels for shallow-water offshore drilling operations—remained weak as the oilfield services sector decline continued. As a result, only seven of the debtors' 25 rigs were in operation upon their filing date.

Back in bankruptcy court, the debtors came armed with a pre-packaged bankruptcy plan supported by 99.7 percent of its lenders. The plan proposed to pay unsecured creditors in full and provide some recoveries to equity holders contingent on garnering their support. This would be accomplished through the creation of a wind-down entity charged with liquidating and monetizing the company's assets.

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The debtors looked to set a fast confirmation timetable, seeking a July 11 confirmation date. However, the fast track case hit a speed bump as major shareholder Centerbridge Partners LP objected and called for the formation of an equity committee. An equity committee was formed in response to Centerbridge's request, and the confirmation hearing was adjourned to Aug. 10 to provide the newly formed equity committee with time to investigate the company's finances.

With a contested confirmation hearing looming, the debtors announced in early August that they will enter mediation to attempt to resolve their disputes with the equity committee as well as the Office of the United States Trustee and the Securities and Exchange Commission which raised issues with the plan and proposed releases for parties that may have contributed to the repeat bankruptcy filing. In light of the mediation, the confirmation hearing is now set to begin on Sept. 22.

Hercules Offshore (Bankr. D. Del. Case No. 16-11385)

Onshore Operations

On June 7, 2016, Seventy Seven Energy Inc. and affiliates filed petitions for relief under Chapter 11 of the Bankruptcy Code in the U.S. Bankruptcy Court in Delaware.

The company—a spinoff from Chesapeake Energy Corporation—operates onshore, primarily in the Anadarko and Permian Basins and Eagle Ford, Haynesville, Marcellus, Niobara and Utica shales. The debtors' operations consist of drilling, hydraulic fracturing and oil field rentals.

The debtors listed more than $1.7 billion in total debt and almost $1.8 billion

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in assets. The company commenced creditor vote solicitation on May 9 and arrived in bankruptcy court with a pre-packaged Chapter 11 plan enjoying significant creditor support.

The debtors' plan of reorganization was premised on the conversion of two tranches of unsecured notes—$650 million in notes set to mature in 2019 and $450 million in notes set to mature in 2022—into equity in the reorganized entity. In turn, unsecured trade creditors will be paid in full in the ordinary course of the debtors' business. Term lenders, owed approximately $500 million, are expected to recover the full value of their debt with only certain loan terms subject to modification.

To finance their operations under Chapter 11, the debtors secured a $100 million financing facility administered by Wells Fargo. The debtors faced some controversy when the Office of the United States Trustee objected to the debtors' request to seal the terms of the financing, but the debtors were ultimately successful in keeping the terms confidential.

The debtors won confirmation of their plan on July 13, in one of the fastest successful trips through bankruptcy in recent years.

Seventy Seven Energy (Bankr. D. Del. Case No. 16-11409)

Offshore Drilling Rigs

On Feb. 14, 2016, Paragon Offshore plc and its affiliates filed voluntary petitions for relief under Chapter 11 of the Bankruptcy Code in the U.S. Bankruptcy Court in Delaware.

As discussed in a prior column, the debtors provide offshore drilling rigs used to conduct oil and gas drilling for exploration and production. They encountered financial distress in the wake of the global decline in oil and gas prices and commenced their Chapter 11 cases with a prearranged Chapter 11 plan. Under the original proposed plan, bondholders would have exchanged $984 million in senior unsecured notes for $345 million in cash plus 35 percent of equity, and existing equity holders would retain 65 percent of equity. Critically, the plan did not have the support of the term lenders, owed approximately $650 million.

The term lenders interposed objections to both the adequacy of the debtors' disclosure statement describing its plan of reorganization and the viability of the debtors' plan. In response, in April, the debtors revised their company valuation estimate by approximately $150 million to account for continued market weakness.

With the term lenders' objections unresolved, a confirmation trial commenced on June 21. At the trial, the debtors argued that the debt-for-equity swap contemplated by the plan together with some cash payments will lead the company to recovery. The term lenders countered that the debtors' fleet of offshore drilling rigs is dated and unable to compete in an already strained industry. Following the trial, a decision on confirmation was reserved pending the resolution of a discovery dispute among the parties.

Subsequently, on Aug. 16, the debtors filed an amended plan and disclosure statement, rendering the pending confirmation decision moot. The amended plan relies on the debtors' actual financial performance through June 30 which surpassed projections but includes a downward projection through 2018 on the assumption that the industry will experience a prolonged downturn. A second confirmation trial is set to commence on Sept. 26.

Paragon Offshore plc (Bankr. D. Del. Case No. 16-10386)

Oilfield Services

On July 20, 2016, C&J Energy Services Ltd. and affiliates filed petitions for relief under Chapter 11 of the Bankruptcy Code in the U.S. Bankruptcy Court for the Southern District of Texas.

The debtors provide well construction, well completion, well support and other complementary oilfield services to oil and gas exploration and production companies. One of the largest completion and production services companies in North America, C&J Energy has operations in most major oil and natural gas regions producing regions across the continental United States and Canada.

Prior to the commencement of their Chapter 11 cases, the debtors reached a restructuring support agreement with holders of approximately 83 percent of the prepetition secured debt. The plan contemplated by the restructuring support agreement is centered on a debt-for-equity swap engineered to deleverage the debtors' balance sheet and would include a $200 million rights offering aimed to add liquidity. The restructuring support agreement leaves open plan treatment of general unsecured creditors, and the plan may ultimately face opposition from the official committee of unsecured creditors if a consensual deal cannot be reached.

The supporting lenders also agreed to provide the debtors with a $100 million DIP financing facility to finance their operations under Chapter 11. The debtors have secured interim authority to access the DIP financing facility.

C&J Holding Co. (Bankr. S.D. Tex., Case No. 16-33590)