

## Special Report

### HELP ENERGY CLIENTS SURVIVE TOUGH TIMES

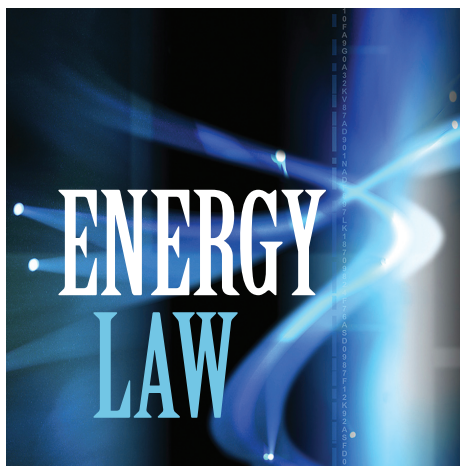
by SYLVIA ANN MAYER  
and RENÉE D. WELLS

A perfect storm has been brewing in the energy sector: a weak economy, low energy prices, the offshore drilling moratorium followed by stricter offshore drilling rules, and new regulations governing energy derivatives and trading. During this time of economic crisis, there are a number of ways in which outside and in-house counsel can help energy clients reassess their business functions to meet these challenges and obtain value in today's economic environment.

- *Act sooner rather than later.* This is the most important point for attorneys seeking to add value for their clients. The sooner a business identifies financial, legal, operational or other issues, the better. Attorneys must encourage their clients to plan for and think through potential problems. Advance warning allows more time to address the issue and avoid or minimize the impact of a crisis.

- *Understand and comply with regulatory changes.* From the Dodd-Frank Wall Street Reform and Consumer Protection Act to new offshore drilling requirements, energy companies face a variety of new rules and regulations that impact their businesses. Counsel must ensure that relevant employees and the company understand and comply with these rules and regulations. Once the company adopts procedures, it also should put systems in place to monitor compliance routinely.

- *Review debt and contract compli-*



ance. Attorneys should encourage their energy clients to implement debt and contract compliance monitoring systems. An early-warning system can identify compliance issues for management and the board, which attorneys and their clients then can address with lenders and other contract counterparties before the situation becomes dire.

- *Audit debt and contract records.* Attorneys should ensure that their clients' records are complete and should review all credit agreements and amendments for signatures and authorizations. The same is true for contracts, particularly critical contracts. Learning post-default that a critical amendment remains unsigned only exacerbates the problem.

- *Examine policies and procedures for customer and supplier relations.* Attorneys should encourage clients to monitor payment cycles, contract modifications and compliance. A slow-paying customer could be in tough economic straits. A

supplier who constantly requires contract modifications may be equally in crisis. Counsel should evaluate clients' customer and supplier policies and procedures to ensure that early-warning and response systems are in place to address any issues detected.

- *Consider exit options.* Attorneys should consider whether clients ought to exit an existing relationship to alleviate the identified problems. They can guide clients in determining whether the company should repay or refinance debt; can or should terminate vendor, supplier, customer or other contracts; or should breach obligations.

While the last option — a calculated breach — may come as a shock to clients, in some instances, it may be the best means to maximize value. Often, a company facing a crisis will continue performing under onerous contracts without evaluating the costs of a breach. Because contract law generally compels compensation rather than performance, it may be prudent to determine if breach is preferable to performance.

- *Review the directors-and-officers policy.* Lawyers periodically should review the D&O policy and consider the gamut of issues, from types of claims covered to the amount of coverage available. This is even more critical if counsel was not involved in negotiating or obtaining the policy. It is much easier and cheaper to get appropriate coverage pre-crisis than post-crisis.

- *Look at risk management policies and procedures.* Attorneys should re-examine, update and test risk manage-

ment policies and procedures regularly. They can help clients develop strategic risk management plans to avoid unnecessary costs and reduce potential legal and other exposure. As part of this process, clients should reassess their business goals and evaluate potential legal and financial risks associated with, among others, customers, creditors, employees and other third parties.

- *Identify, contain and reduce costs.* Lawyers can help clients avoid reactive decisions by identifying and analyzing business stressors, including discretionary spending. Clients should, among other things, review contracts and debt requirements to determine cost-cutting avenues, monitor cash flow, determine cash drains, and analyze working capital and overhead costs.

Once clients identify cost-cutting initiatives, counsel can help develop appropriate procedures and conduct a legal review. For example, if a reduction in force is necessary, counsel can analyze employment agreements and applicable labor and employment laws to determine the true economic savings of any such RIF.

- *Implement mechanisms to survive a counterparty crisis.* Now more than ever,

businesses must be prepared in case a customer or supplier seeks bankruptcy protection. Because of the risk that the debtor may claw back receivables and other transfers under preference or fraudulent-conveyance laws, a counterparty bankruptcy could significantly impact a company's finances.


In contrast, the Bankruptcy Code affords certain protections for swaps and forward contracts. Counsel should advise their clients regarding avoidance-action risks, safe-harbor protections and other rights available under the Bankruptcy Code, as well as the affirmative steps required to receive such protections.

For example, Bankruptcy Code §503(b)(9) grants special status to claims for payment of goods received within 20 days prior to filing bankruptcy; however, the creditor must assert this right in a timely manner or risk losing it. Knowledge of these potential issues permits clients to safeguard their businesses.

- *Recognize that cash is king.* In any crisis, and particularly a financial crisis, cash is critical. Lack of liquidity limits options, including the viability of an out-of-court or in-court restructuring or reorganization. Chapter 11 reorganiza-

tions and out-of-court restructurings require funding (cash) to succeed. In times of crisis, counsel should work closely with management to explore cash management options.

- *Get expert advice.* Enlist the services of experienced turnaround professionals. Hiring restructuring advisers does not mean a company is bankrupt. Instead, it means the company proactively is seeking expert advice to address its problems.

In a crisis situation, resources are limited and strategic alternatives may be non-existent. Attorneys play a critical role in helping their energy clients move through difficult times. 

*Sylvia Ann Mayer is a partner in Weil, Gotshal & Manges. She focuses on business reorganization and restructuring and has represented clients in a variety of industries, including the energy sector.*

*Reneé D. Wells, a senior associate with the firm's business finance and restructuring group, has represented businesses in the energy industry.*

*Both are in Houston.*