

Transactions Best Practice,
Commercial Managers Forum

Technical Notes

Issue 1
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Acknowledgments

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1 Introduction

Over recent years there has been a significant evolution in the make-up of the companies operating and owning equity in the UK Continental Shelf (UKCS). Investment by private equity-backed companies has increased and many utilities have divested or consolidated interests into new operators (e.g. Centrica and Bayerngas who combined to form Spirit Energy in 2017), while the proportion of production held by major operators has fallen from around 60 percent in 2000 to less than 50 percent in 2018. As a result, the stakeholders involved in an M&A transaction typically represent a more diverse “corporate landscape” than in the past when assets were more typically transferred between established E&P companies. Deals are also becoming increasingly innovative to allow successful transfer of interests.

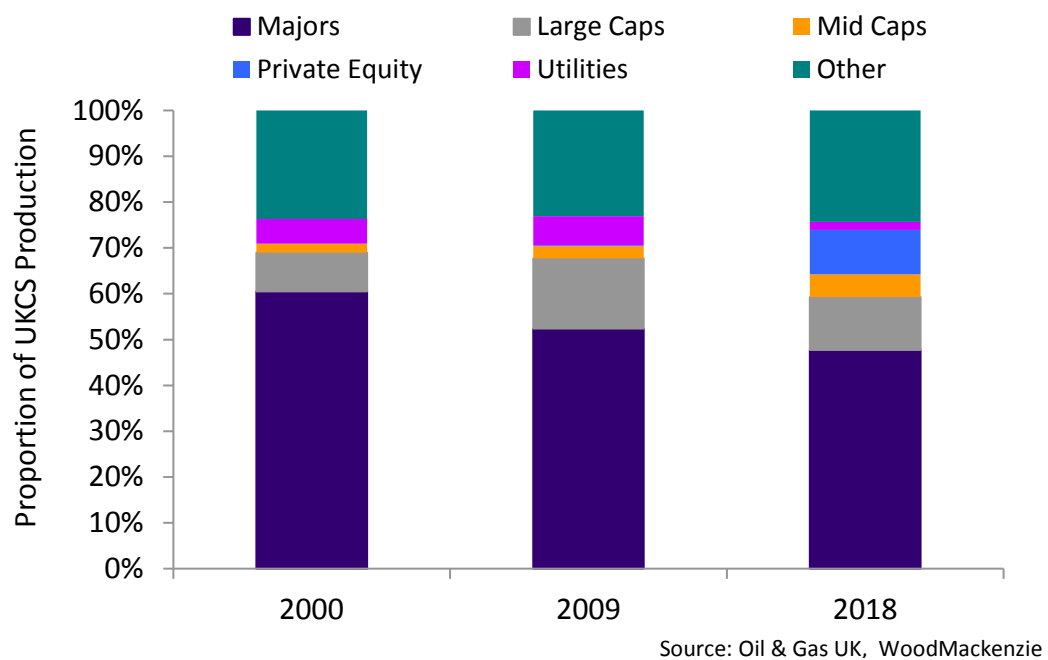


Figure 1 - change in equity production mix since 2000

In October 2017, subsequent to an 18-month period when a number of UKCS transactions had been completed or were still progressing, the Oil and Gas Authority (OGA) expressed its concern about the time it was taking to secure partner approvals to some licence and infrastructure transfers and indeed the efficiency of the commercial process.

In response, the UK Commercial Managers Forum conducted several discussions with buyers, sellers and other stakeholders to identify common themes contributing either to the success of, or delay to, such transactions. Discussions centred around:

- (i) the understanding of MER UK aspects to transactions and regulatory approvals;
- (ii) best practice around planning and preparation;
- (iii) relationship and communication aspects; and
- (iv) behaviours that were viewed as helpful or hindering to timely completion.

These discussions, referred to as “fieldwork” throughout this document, form the basis of this guidance note.

An overarching diagram of the transaction process is provided in Appendix 2 for reference.

This voluntary best practice guide has been developed by a cross section of industry commercial and legal practitioners. It envisages a transaction involving an upstream asset, however the principles apply equally to other types of transactions e.g. involving infrastructure.

2 Executive Summary

There is a need to maintain the pace of deal flow to attract companies with the financial means and motivation to invest, to provide new capital for exploration, development and re-development projects and who can introduce new ways of working to the UKCS. In several cases securing partner approvals to licence and infrastructure transfers could be achieved on a more efficient and timelier basis.

Since Q4, 2017 a group of commercial managers have reviewed a number of deals on the UKCS, under the oversight of the Commercial Managers Forum, to identify where there may be opportunities for improvement in the way transactions are carried out on the UKCS in response to the increasing diversity of licensees and the challenges of working in a mature basin.

Whilst the key points identified are summarised below, it is recommended that this report is read in full:

- (i) All parties should be aware of their obligations to achieve MER UK and aligned to deliver them.
- (ii) Take time to understand the requirements of the Department for Business, Energy and Industry (BEIS), the Offshore Petroleum Regulator for Environment and Decommissioning (OPRED) and the Health and Safety Executive (HSE) as well as those of the OGA;
- (iii) Good deals benefit from careful upfront planning and preparation, allocate appropriate time and resources to do so;
- (iv) A realistic timetable to completion of the deal should be agreed at the start by all parties. All risks and uncertainties that could derail the timetable should be identified and addressed as early as possible in an open and timely manner. Legitimate requirements of approving stakeholders must be both reasonable and raised/sought in a timely fashion consistent with the Commercial Code of Practice (CCOP) and the Negotiations Best Practice guidance;
- (v) Keep the OGA apprised on the intent of the deal. The timetable, progress and emerging issues should be shared with the OGA without necessarily seeking regulatory intervention;
- (vi) Where financial competency may be an issue, it should be addressed openly and early both by the parties to the deal and their Joint Venture (JV) partners. Companies should establish and articulate their criteria regarding financial competency once all documents have been provided rather than waiting until the deal is near completion;
- (vii) Decommissioning liabilities are often the biggest issue facing new entrants. The transacting party should give appropriate focus to decommissioning security arrangements prior to commencing any substantive transaction, with consideration already given to how liabilities will be addressed within the JV and with a new entrant;
- (viii) Good behaviours and relationships and effective communication with key stakeholders are a critical factor in successful deals; and

- (ix) All parties within the transaction should be aware of the requirements of the Commercial Code of Practice and ideally be signatories to the code or commit to undertake activities consistent with the requirements of the code.

3 MER UK and regulatory approvals

Upfront discussions within and between the buyer and seller organisations to ensure there is good understanding by the respective teams of how the transaction in question contributes to MER UK is helpful. Additionally, where either party has a parent company, or requires approvals from, outside the UK they should be made properly aware of the intent of MER UK and reminded that UKCS participants are legally bound to support MER UK.

4 Early engagement with the OGA and other bodies such as the HSE and OPRED is encouraged both to understand their consent processes and to seek clarity, if necessary, around their requirements. Upfront planning and preparation

In addition to regulatory approvals, there are often multiple stakeholders (JV partners, service providers and other parties to contracts) involved in providing consents and novating contracts and agreements (collectively referred to as the “consents process” in this document). Upfront planning by the buyer and seller in the following areas is suggested:

- (i) Early identification of all stakeholders to the transaction, especially those that will be involved in the consents process. Particular consideration should be given to those where there is not normally day-to-day engagement e.g. landowners including Crown Estate.
- (ii) Early identification and consideration of stakeholder requirements and expectations that may arise during the consents process, and the likely reaction from others who are party to the transaction. This should include reviewing the relevant Joint Operating Agreement (JOA) to ensure a good awareness of all rights and obligations and understanding of any unusual clauses or requirements related to assignment or sale of an interest. This can commence when there is reasonable certainty around the deal i.e. before it is announced and indeed may influence how the deal is structured.
- (iii) Ensure proper consideration is given to business/commercial issues (e.g. outstanding audit points) and future scenarios that are important to stakeholders. All of these issues should be disclosed to the buyer by the seller and together they should assess the impact of these issues (including on the terms of their deal), their potential consequences over time for all stakeholders and possible solutions to resolve such issues. However, whereas understanding, openness and engagement is key, this does not necessarily mean that a seller is obliged to resolve all pre-existing business issues prior to divestment or that other stakeholders may not impose satisfaction of such issues as a condition to their consent to transfer. All stakeholders need to consider the extent to which proposed conditions could hamper the completion of any proposed deal or fetter a legal right to transfer under the JOA.
- (iv) Ensure adequate business, commercial and legal resources are dedicated to the transaction and have knowledge of the assets/business. This should cover a broad range of disciplines appropriate to the transaction. Ensure legal resources have the relevant level of upstream experience, combined with a pragmatic behavioural style and approach to resolving issues. Where transfers of operatorship are involved, this may take the form of “transition teams” within the buyer and seller organisations (see Appendix 1). Those involved should have clear authority and mandate and be empowered to make decisions. Adequate resource should of course continue to be available to maintain good stewardship of the asset during the transaction. Transacting parties should also carefully consider the resource implications for all stakeholders whose approval is required to complete the transaction.
- (v) Buyer and seller transition teams investing time upfront in getting to know each other is seen to be helpful and continuity of key players is recommended to avoid a pause if people change out. It is important that the buyer and seller workstream representatives in the transition team also understand the scope of the transaction and the underpinning commercial agreements

and behave in accordance with them. Also consider inviting JV partners to a transition workstream discussion at an early stage to ensure all relevant parties understand the transition process.

- (vi) Taking all of the above into consideration, the buyer and seller should set a realistic timeline and appropriate “route map” for stakeholder engagement and communicate this with the OGA, JV partners and any other key stakeholders at the outset. Seller and buyer must communicate to, and carefully consider the realistic and reasonable requirements (including approval time-frames) of, all stakeholders whose consent is required to deliver the deal, including the Master Deed process.

Delivery against the agreed timeline should be monitored on a frequent and timely basis. Areas falling behind or deviating from the plan will be identified and any appropriate interventions made on a timely basis at the right level within organisations and if appropriate, with the OGA.

Consideration should be given to communication of key information (e.g. financial and technical capability packs) to senior management in the organisations that need to consent to the transfer of equity.

5 Relationships and communications

As noted above there may be multiple stakeholders impacted in some way by the transaction therefore initial, and ongoing, communication to all stakeholders is important.

- (i) Engage early with the identified stakeholders, including regulatory bodies, to outline the planned timeline including the timing of requests for novations etc. This is particularly important since parties outside of the buyer and seller will need to identify resources.
- (ii) Financial and technical operating capability should be addressed early on. It is a key feature of the consents process so upfront preparation in this area, ideally prior to deal announcement, with the seller putting themselves in the shoes of a buyer and those giving consent to the transaction, means communication of buyer capability can start immediately after announcement of the transaction (see “Financial capability” below)
- (iii) Stakeholder issues and concerns should be identified and addressed. Where stakeholders have legitimate concerns (e.g. regarding financial, technical / operational capability of the buyer) and are not forthcoming with consents, they should be clear at the outset on exactly what the issues are and whether or not they see a path to resolution. Stakeholders should provide timely and clear feedback on whether the action being taken by the buyer or seller to find a solution is appropriate given time and potentially money is being invested in a solution. Lack of clarity and feedback in these areas was cited as an impediment during the fieldwork.
- (iv) In a similar vein, where applicable and appropriate, legitimate packaging of issues, including historical unresolved commercial issues, should be established at the outset. Careful consideration of this is required by the buyer and seller as part of early engagement and planning. The non-transferring owners bringing in such issues at a late stage is not acceptable. It should also be noted that using a sale/purchase process as a means to resolve all such historical issues may not be legally acceptable (see comment above regarding fettering of JOA rights).
- (v) Likewise, all stakeholders should engage in early dialogue to clarify the relevance of “technical capability” aspects where these are not part of the JOA rights of non-transferring parties, and the transaction does not involve a transfer of operatorship.
- (vi) Regular status updates to all parties to the transaction should take place, even if only to say nothing has changed, so that stakeholders are not wondering what is happening (and potentially de-prioritising activity related to the transaction).
- (vii) Progress against the timeline should be communicated in the regular status updates to help stakeholders other than the buyer and seller determine resource requirements e.g. for review of documents and novations. Consideration should be given to timing of face-to-face meetings with stakeholders.

6 Financial capability

When a transaction is announced, early engagement with existing equity owners should take place and consideration given to providing useful information on the following areas upfront. This list is not meant to be prescriptive or exhaustive, but an indication of the areas where information could be helpful. This will vary transaction by transaction and company by company e.g. for a listed company a link to Annual Report may be sufficient.

Where financial capability information is provided in a timely manner and is sufficient to demonstrate requisite financial capability, taking account of all stakeholders' reasonable requests, stakeholders required to consent to the transfer should not make additional unreasonable demands on either the buyer or seller.

Typically, the following should be considered:

- Key information on the buyer/buyer group e.g. transparency on group structure, net assets, financial backing, group credit rating (where available, recognising this may not exist in some cases) etc;
- Published financial data e.g. annual report and accounts;
- Where published financial data is not up-to-date or does not exist, provide appropriate alternative information e.g. previous 3 years plus forecast 3 years including balance sheet, cash flow and assumptions on oil and gas prices;
- Where appropriate, the buyer should demonstrate how it will meet ongoing operating/capital costs if, for example, outages in production occur;
- To the extent decommissioning is not an entirely bilateral issue between the buyer and seller (and therefore potentially confidential), a clear position on decommissioning liabilities between seller and buyer should be set out. Seller to consider impact on existing owners of the proposed structure and any change in risks to facilitate discussion of key issues. If the transaction involves changes to existing agreements, for example a Decommissioning Security Agreement, consider timing and engagement with second-tier participants;
- See Appendix 3 for suggested format and considerations.

Face-to-face meeting with all owners should take place once information has been shared to discuss issues and agree a timeline to resolve.

Existing owners should be clear on issues and company positions with clear mandates for approval and resolution of issues, so the buyer and seller understand concerns and can address them on a timely basis.

The OGA should be kept updated on progress with financial capability discussions and concerns raised to understand the position of the seller/buyer but also the existing owner's concerns.

7 Behaviours

Commercial behaviours are often cited as a cause of delay in negotiations or transactions and hence were discussed during the fieldwork. The following were identified as “helpful” or “hindering”:

7.1 *Helpful behaviours*

- Transparency, openness and clarity from all stakeholders around key issues and corporate process/timelines;
- Understanding of ongoing relevant commercial issues and raising early;
- Approaching problems with a solution mindset – being pragmatic/flexible;
- Listening and seeking to appreciate other stakeholders’ positions;
- Hard focus on the issues not the personalities (recognising that personality clashes may occur); and
- Senior management support and engagement.

7.2 *Hindering behaviours*

- Linkage to unrelated issues and re-opening historical issues, particularly at the last minute, and making resolution of these a pre-condition to the transfer proceeding (unless agreed at the outset);
- Providing that a realistic timetable has been discussed/established at the outset by stakeholders, hiding behind corporate process or lack of clarity on what corporate functional approval processes need to take place (which may be delay tactics or using time as commercial leverage to run down the clock);
- Lack of ownership within an organisation, leading to drag on approvals and issue resolution;
- Aggressive assertion of rights by a party; and
- Unnecessary or premature escalation to senior management.

8 End of process review and self-assessment

A simple post completion review should occur within 1 month, covering the self-assessment of each other's performance against this guidance or other agreed process. This assessment will be shared and used for a formal feedback or lessons learned review and will be shared with the OGA if requested. In addition, a survey tool has been developed to capture and track factual elements, which will facilitate measurement of industry performance. Oil and Gas UK will host, administer and collate the survey results. The live survey link to use is: <https://www.surveymonkey.co.uk/r/CMF-CCOP>

9 Appendix

A Appendix 1 – Transition Workstreams

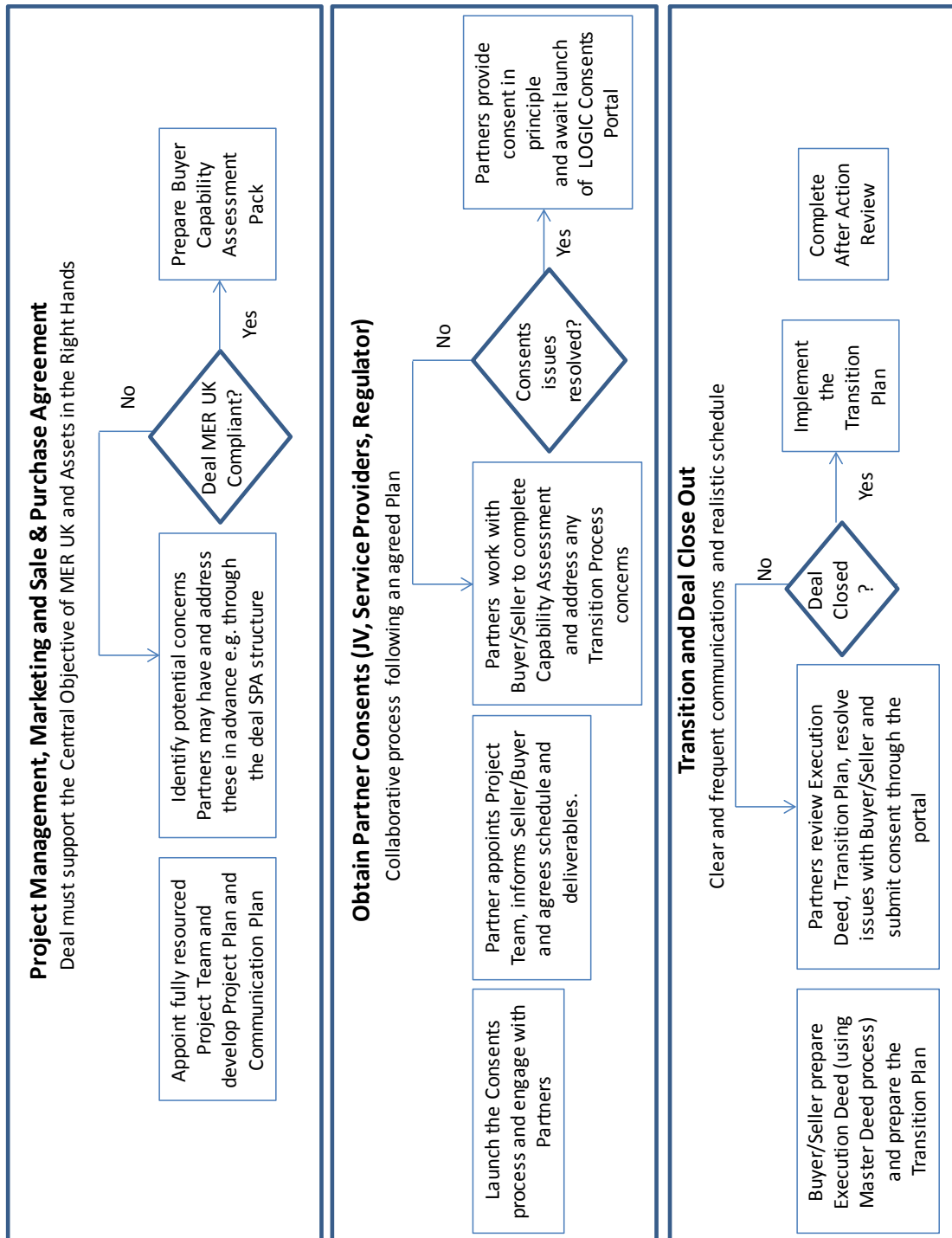
While not the focus of fieldwork underpinning this document, it was recognised that issues relating to the transfer of operatorship outside the commercial arena can contribute to delay in completion, in particular the transition of IT systems. Resourcing for the Transition Period (from deal announcement to completion) is critical.

Appointing a Transition Manager in each of the buyer and seller organisations prior to deal announcement, so that they can initiate planning for the Transition Period, is helpful. A transition project is likely to involve around 10-12 workstreams, depending on the size of the transaction and organisations. Typical workstreams are as follows:

- HR/People
- Information Technology and Systems
- Health, Safety, Security and Environment
- Procurement and Supply Chain
- Finance (accounting)
- Legal/commercial (including decommissioning)
- Transition Operations (site transition)
- Engineering
- Wells and Subsurface
- Communications
- Projects

Mirroring the workstreams above in each of the buyer and seller organisations, together with an agreed governance structure, has been found to be helpful.

B Appendix 2 – Transaction Process Diagram



1. In each box read from left to right.
2. The industry standard Execution/Master Deed process should be used wherever practicable. Where the buyer and seller believe it is more practicable to use standalone Novation Deeds these should follow the terms of the industry standard as closely as possible.

C Appendix 3 – Financial Capability (a suggested format)

Field: XX

Parties : YY (seller) and ZZ (buyer)

Transaction Announced: Date

The intent of this table is to highlight areas on which it might be helpful for the buyer in a transaction to provide information to JV Owners on the buyer’s technical and financial capability. It is not intended to be exhaustive nor to create an obligation for all information to be provided for every transaction. The scope of the information provided is likely to be different in the cases where the buyer is an established party in the UKCS and where the buyer is a new entrant to the basin.

		Date Provided	Comments
Seller:			
Buyer:			
Outline of buyer technical and operational capability			
Outline of buyer historical operational performance			
Is seller selling shares in a company or transferring interest in field	Shares/transfer of interest		
Has notice been given by seller to other owners under the JOA	Y/N		
Buyer Credit rating: Std & Poors, Moody’s (where available)			
Buyer parent company structure included	Y/N		
Brief outline of any significant shareholders in buyer company			
Brief outline of buyer funding (where appropriate) i.e. equity, debt, bonds – refer to publicly available information			

Is seller retaining decommission liability?	Y/N		
If seller retaining decom liability are changes required to existing DSA/JOA?	Y/N		
If seller transferring decom liability, adequate arrangements should be in place regarding security	Y/N		
High level financial information on buyer (historic and projected) – reference to publicly available information			
Buyer financial statements for last 3 years included	Y/N		
Buyer projected cash flow for next 3 years with assumptions made	Y/N		
Buyer cash flow under high mid, low-price scenarios	Y/N		



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Technical Notes

Technical Notes form part of the suite of industry-leading guidelines produced by Oil & Gas UK in collaboration with member companies. Drawing on a wealth of specialist resources and technical expertise, these notes are continually reviewed to improve the performance of all offshore operations.

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