

REVISITING SECURITY RIGHTS UNDER OFFSHORE OPERATING AGREEMENTS

PLANO

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OPERATOR & NON-OPERATOR CONCERNS

- Impacts of early 2020 global price war, COVID-19 and new Presidential Administration actions
- Many operators and non-operators sought bankruptcy protection in 2020, which will likely continue in 2021
- Increased concern about risk of counterparty default of payment and performance obligations under Offshore Operating Agreement due to financial difficulties

OOA PROTECTIONS & REMEDIES

- Non-paying participants not a new issue
- Offshore Operating Agreements (OOAs) provide the parties with certain protections and remedies to reduce the risk and impact of a non-paying participant on other OOA parties/participants and ongoing and future operations
 - Advance Payments; Cash Calls; Suspension of Rights; Non-Consent Penalties

OOA PROTECTIONS & REMEDIES

- Most OOAs provide for reciprocal grants of security rights by the Operator and the Non-Operator in favor of their respective counterparty
- Secures the parties proportionate share of their respective obligations under the OOA
 - Including the payment of JIB/expenses
- Secured by the parties' respective interests in the joint property

OOA PROTECTIONS & REMEDIES

Purpose of security rights provisions:

- To create non-possessory rights over specific property of another party
- Includes the right to seize and sell that property and be paid by preference from the proceeds of that sale

NAVIGATING THE OOA SECURITY RIGHTS PROVISIONS

TYPICAL COMPONENTS OF OOA SECURITY RIGHTS PROVISIONS

CREATION OF SECURITY RIGHTS

- **Mortgage (real/immovable property)**
- **Security Interest (personal/movable property)**

PERFECTION OF SECURITY RIGHTS

- **Memorandum of OOA**
- **UCC-1 Financing Statement**

TYPICAL COMPONENTS OF OOA SECURITY RIGHTS PROVISIONS

Confirm existence, validity and reciprocity of the security rights provisions

TYPICAL COMPONENTS OF OOA SECURITY RIGHTS PROVISIONS

Two distinct and reciprocal grants of security rights should be included:

- (1) a mortgage upon real/immovable property
- (2) a security interest in personal/movable property, including fixtures.

TYPICAL COMPONENTS OF OOA SECURITY RIGHTS PROVISIONS

- Each Non-Operator grants to the Operator:
 - (i) a mortgage over its real (immovable) property interests located within the “Contract Area,” and
 - (ii) a security interest over its personal (movable) property interests (includes fixtures and as-extracted collateral)
- The Operator grants a like mortgage and security interest to the Non-Operator

TYPICAL COMPONENTS OF OOA SECURITY RIGHTS PROVISIONS

Determine what property is covered by
the mortgage and security interests
involved

TYPICAL COMPONENTS OF OOA SECURITY RIGHTS PROVISIONS

WHERE CAN YOU FIND THE PROVISIONS?

1. Body of the OOA
2. Exhibit(s) to the OOA
3. Combination of both
4. No provisions

LOUISIANA MORTGAGE

Nonpossessory right created over immovable (real) property, including a mineral lease, to secure the performance of an obligation

LOUISIANA MORTGAGE

Upon the mortgagor's default of an obligation secured by the mortgage:

- The mortgagee has the right to seize and sell the property
- Have the proceeds applied toward the satisfaction of the obligation in preference to claims of others

LOUISIANA MORTGAGE

- Must be in writing
- Must have a grant of mortgage
- Must be signed by the mortgagor
- Must state the amount (or maximum amount) secured by the mortgage
- Must describe the mortgaged property

LOUISIANA MORTGAGE

- The security rights provisions contained in many “base forms” of OOAs are usually not sufficient to establish a valid Louisiana mortgage
- Must be amended

SECURITY INTERESTS

- Created pursuant to Article 9 of the Uniform Commercial Code (UCC)
- Article 9 has been adopted by Louisiana, with modifications
- Article 9 in Louisiana is referred to as Chapter 9

LOUISIANA SECURITY INTERESTS

- A security interest is an interest in movable (personal) property or fixtures
- Created by contract
- Secures the payment of performance of an obligation

LOUISIANA SECURITY INTERESTS

Security interests “attach” to collateral and are enforceable against a debtor only when the last of 3 requirements has been met:

1. The debtor authenticates (or signs) a security agreement containing a description of the collateral
2. That value be given
3. That the debtor has rights in the collateral

PERFECTION

PROTECT AND PRESERVE
SECURITY RIGHTS

PERFECTION

- Perfecting security rights requires affirmative steps to be taken by the secured party
- Perfection must be done in accordance with applicable state law
- An unperfected security right is subordinate to the interests of perfected creditors
- Timing matters – “First in Time, First in Right”

LOUISIANA PUBLIC RECORDS DOCTRINE

- In Louisiana, actual or constructive of rights affecting real (immovable) property does NOT bind third persons
- Certain rights must be properly recorded in the applicable parish records to be effective against third persons (*i.e.*, real rights, mortgages, mineral rights, mineral leases, and leases of immovable property)

LOUISIANA PUBLIC RECORDS DOCTRINE

- Louisiana Clerks of Court maintain separate conveyance, mortgage and UCC records
- Documents must be recorded in the proper records to be effective
 - Example: A filing required to be in the mortgage records that is improperly filed in the conveyance records is ineffective against third persons

PERFECTION OF MORTGAGES

- Original of mortgage must be recorded in the mortgage records in parish where the property is located
- Or, for OCS leases, the coastal parish(es) adjacent to the offshore lease(s)

PERFECTION OF MORTGAGES

- Perfection of the mortgage granted in OOA requires the mortgage instrument be recorded in the appropriate parish mortgage records
- Not practical to record entire OOA
- Custom is to record a legally sufficient recording supplement instead, containing the statutory mortgage requirements
- Typically attached as an exhibit to an OOA

PERFECTION OF MORTGAGES

- As a mortgage, the recording supplement must contain an actual, complete grant of mortgage
 - Cannot simply refer to a grant of security made in the OOA
- It must be signed by each mortgagor
 - The Operator cannot sign on behalf of all parties

PERFECTION OF SECURITY INTERESTS

- Perfection of a security interest puts third parties on notice of the security interest
- Allows a party to prevail over a creditor using judicial process to obtain a lien on the collateral, including a trustee in bankruptcy

PERFECTION OF SECURITY INTERESTS

Perfection may be accomplished by:

- (i) Possession
- (ii) Control
- (iii) Filing (UCC Financing Statement)

PERFECTION OF SECURITY INTERESTS

- Use UCC-1 Form whenever possible
- Louisiana has own UCC-1 form
- Non-standard form is acceptable, but must include all statutorily required information (i.e., contained in state's UCC-1 form)

PERFECTION OF SECURITY INTERESTS

UCC FINANCING STATEMENT CONTENTS

- **Identify the debtor's name**
- Identify the debtor's business form
- Identify the debtor's jurisdiction of organization
- Identify the secured party's name
- Identify the parties' respective addresses

PERFECTION OF SECURITY INTERESTS

UCC FINANCING STATEMENT CONTENTS

- Identify the collateral covered - Usually tracks the description in the security agreement
- Typically attach the recording supplement to the UCC-1 Form

PERFECTION OF SECURITY INTERESTS

UCC FINANCING STATEMENT CONTENTS

AS-EXTRACTED COLLATERAL AND FIXTURES

- Must indicate that it covers both of these types of collateral
- Must include a description of the real/immovable property associated with these types of collateral

PERFECTION OF SECURITY INTERESTS

UCC FINANCING STATEMENT CONTENTS

AUTHORIZATION

- Debtor signatures not required
- But, UCC filings must be authorized by the debtor in an authenticated record
- In most cases, the debtor's execution of the security agreement suffices (*i.e.*, OOA and recording supplement)

PERFECTION OF SECURITY INTERESTS

FILING UCC FINANCING STATEMENTS

WHERE TO FILE

- UCC Financing Statements must be filed in all appropriate jurisdictions
- Varies depending on type of collateral and state of debtor's "location"

PERFECTION OF SECURITY INTERESTS

FILING UCC FINANCING STATEMENTS

WHERE TO FILE

Fixtures and As-Extracted Collateral

- UCC Records of any 1 Louisiana Parish
- Not real/immovable property specific
- Only 1 filing is required
- Filed mortgage does not serve as financing statement in Louisiana

PERFECTION OF SECURITY INTERESTS

FILING UCC FINANCING STATEMENTS

WHERE TO FILE

Most Other Collateral

- UCC Records of jurisdiction where the debtor is “located” (*i.e.*, incorporated or formed)
- Usually with Secretary of State in most other states

FILINGS WITH BOEM

- Recording Supplements and UCC Financing Statements should also be filed in BOEM's Non-Required Lease File for each affected lease
- Nothing under applicable federal law expressly requires instruments creating or evidencing a mortgage or security interest be filed with or approved by BOEM
- But, current federal regulations do provide that “economic interests” created by the working interest owners of OCS leases must be filed in BOEM's Non-Required Lease files

FILINGS WITH BOEM

- “Economic interest” is defined as “any right to, or any right dependent upon, production of crude oil, natural gas, or natural gas liquids and includes, but is not limited to:
 - a royalty interest
 - an overriding royalty interest, whether payable in cash or in kind
 - a working interest that does not include a record title interest or an operating rights interest
 - a carried working interest
 - a net profits interest
 - a production payment

SUBSEQUENT FILINGS

ENSURE SECURITY RIGHTS
CONTINUE TO RECEIVE
HIGHEST PRIORITY POSSIBLE

MORTGAGE REINSCRIPTION

- General rule is that a mortgage is effective on the records for 10 years from the date of the document
- A Notice of Reinscription must be filed in the mortgage records where original mortgage was recorded
 - Within ten (10) years from the date of the instrument
 - Within each following ten (10) year period from the date of filing of the previously filed reinscription

MORTGAGE REINSCRIPTION

Reinscription is accomplished by filing a signed “notice of reinscription”

Must contain:

- Name of the mortgagor
- Recordation information of the document being reinscribed
- Declares the instrument reinscribed

UCC CONTINUATION STATEMENTS

- A UCC Financing Statement is effective for 5 years
- A UCC Continuation Statement must be filed within the six-month period before the end of the 5-year term
- Otherwise UCC filing will terminate

UCC CONTINUATION STATEMENTS

- Each Secured Party of Record must authorize a Continuation Statement
- A Continuation Statement authorized by one secured party of record, will not be effective to continue a UCC Financing Statement as to any other secured party or record

OTHER SUBSEQUENT FILINGS

- Other filings may be required to evidence changes to the original information provided in a mortgage or UCC Financing Statement
- Depends on the types of change and what state law governs the change
- Examples include:
 - Mergers and name changes
 - Adding and removing parties
 - Enlargement or contraction of the Contract Area
 - Adding or removing collateral or other changes in collateral

RECORDING SUPPLEMENT AS NOTICE OF OOA

In addition to serving as a mortgage and UCC security agreement, a recording supplement can also serve to provide notice to third persons of the existence of the OOA itself.

RECORDING SUPPLEMENT AS NOTICE OF OOA

- By special statute, the recording supplement does not have to include all OOA provisions
- But, must contain:
 1. Description of real/immovable property subject to the OOA
 2. State in general terms the nature of the OOA, including any provisions which a third-party is required to have notice under Louisiana law
 3. State where the complete agreement may be found – usually the address of the operator

RECORDING SUPPLEMENT AS NOTICE OF OOA

- Must be filed in the *conveyance* records of any parish where real/immovable property located
- Or, adjacent parish in the case of OCS Leases

QUESTIONS?

Thank you

FOR YOUR TIME AND CONSIDERATION

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