HEDGING OIL & GAS PRODUCTION

Jesse S. Lotay
Jackson Walker L.L.P.

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Overview

I. Why Hedge Oil & Gas Production?
II. Over-the-Counter Transactions vs. Exchange-Traded Transactions
III. How are Over-the-Counter Transactions Documented?
IV. ISDA Overview
V. Drafting Tips for Negotiating the ISDA Master Agreement
VI. Bankruptcy Considerations
VII. Dodd-Frank Act

I. Why Hedge Oil & Gas Production?

Why Hedge?

- The primary benefit of hedging oil and gas production is the producer's ability to reduce the impact of unanticipated price declines—known as price risk—on its revenue.

Hedging Transactions

- Some transactions have the effect of *locking in the price* the producer will receive, but prevent it from benefiting if prices rise.
  - Swap Contracts
  - Fixed-Price Physical Contracts
  - Futures Contracts
- Other transactions, have the effect of *establishing the minimum price* the producer will receive, but require it to pay an upfront premium.
  - Put Option Contracts

Hedging Considerations

- The decision to hedge is made on a case-by-case basis depending on various considerations. These considerations may include:
  - Sensitivity of the producer's business plan and capital structure to revenue fluctuations
  - Appetite for risk
  - Lender or investor imposed restrictions or requirements
  - Confidence in engineering projections of future production

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