

HEDGING OIL & GAS PRODUCTION

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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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