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Unsecured Creditors*

**UNITED STATES BANKRUPTCY COURT
SOUTHERN DISTRICT OF NEW YORK**

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	:	
In re	:	
	:	Chapter 11
BREITBURN ENERGY	:	
PARTNERS LP, et al.,¹	:	Case No. 16-11390 (SMB)
	:	
Debtors.	:	(Jointly Administered)
	:	
	:	
-----	x	Re: Docket No. 85

**OBJECTION OF THE OFFICIAL COMMITTEE OF
UNSECURED CREDITORS TO THE DEBTORS' APPLICATION
TO RETAIN LAZARD FRÈRES & CO. LLC AS INVESTMENT BANKER**

¹ The Debtors in these chapter 11 cases, along with the last four digits of each Debtor's federal tax identification number, as applicable, are: Breitburn Energy Partners LP (9953); Breitburn GP LLC (9948); Breitburn Operating LP (5529); Breitburn Operating GP LLC (5525); Breitburn Management Company LLC (2858); Breitburn Finance Corporation (2548); Alamitos Company (9156); Beaver Creek Pipeline, L.L.C. (7887); Breitburn Florida LLC (7424); Breitburn Oklahoma LLC (4714); Breitburn Sawtelle LLC (7661); Breitburn Transpetco GP LLC (7222); Breitburn Transpetco LP LLC (7188); GTG Pipeline LLC (3760); Mercury Michigan Company, LLC (3380); Phoenix Production Company (1427); QR Energy, LP (3069); QRE GP, LLC (2855); QRE Operating, LLC (9097); Terra Energy Company LLC (9616); Terra Pipeline Company LLC (3146); and Transpetco Pipeline Company, L.P. (2620). The Debtors' mailing address is 707 Wilshire Boulevard, Suite 4600, Los Angeles, California 90017.

The official committee of unsecured creditors (the “Committee”) hereby submits this objection (the “Objection”) to the *Application of Debtors Pursuant to 11 U.S.C. §§ 327(a) and 328(a), Federal Rules of Bankruptcy Procedure 2014(a) and 2016(a), and Local Rules 2014-1 and 2016-1 for Authorization to Employ and Retain Lazard Frères & Co. LLC as Investment Banker to the Debtors Effective as of the Petition Date* [Docket No. 85] (the “Application”)² and in support thereof, respectfully states as follows:

Introduction

1. The Committee recognizes that the Debtors require a qualified investment banker to assist with their restructuring, and does not oppose the Debtors’ retention of Lazard for that role. Nevertheless, the proposed compensation for Lazard:

- is too high in light of the circumstances of the case and compared to investment banker fees approved in similar chapter 11 cases;
- would reward Lazard with above-market success fees, the amounts of which are untethered from the intensity, complexity, and amount of work that Lazard ultimately is required to perform; and
- does not appropriately incentivize Lazard to pursue all viable value-maximizing strategies.

2. Under the terms of Lazard’s engagement letter, Lazard would be entitled to a Monthly Fee of \$200,000, plus a \$17.5 million Restructuring Fee. Beyond this, Lazard’s proposed compensation includes a Financing Fee, payable upon completion of any financing transaction, even one involving only existing participants in the Debtors’ capital structure. And while the cap of \$23 million would apply to Lazard’s success fees (the Restructuring Fee and the Financing Fee), contrary to the Debtors’ representation in the Application (¶ 14(iv)), the cap would *not* limit Lazard’s Monthly Fees. Engagement Letter ¶ 3(d). Depending on the length of the cases, therefore, Lazard may earn well in excess of \$23 million.

² Capitalized terms not defined herein shall have the same meanings as in the Application.

3. While monthly fees and success fees may be common in cases such as these, the terms of Lazard's retention should reflect the realities and economics of these cases. As currently structured, they do not. The Debtors acknowledged at the first day hearing that these cases are not expected to involve a particularly complex restructuring. Rather, the Debtors view these cases "fundamentally as a balance sheet restructuring," given that the company is overleveraged but "operationally sound." Tr. of Hr'g, May 16, 2016, at 16:22-16:25; *see also* Jackson Decl. [D.I. 13] ¶ 33. Likewise, the Debtors' capital structure is straightforward – involving the "Second Liens, RBL Lenders, unsecured bonds . . . [and] quite little trade debt" – and all of the "major parties are already at the negotiating table." Tr. of Hr'g, May 16, 2016, at 16:25-17:2. Thus, these are not extraordinary cases justifying extraordinary compensation.

4. Yet, as discussed in more detail below, Lazard's fee structure is outside the range of fees approved in similarly sized chapter 11 cases, and the Application fails to provide a justification for the Debtors' agreement to pay above-market rates. Furthermore, the Debtors have not presented evidence demonstrating the process employed to select Lazard or the negotiation of the terms of Lazard's retention, further calling into question the reasonableness of the proposed fees. For example, the Application makes no mention of:

- what other investment bankers, if any, were interviewed by the Debtors;
- what fee structures were proposed by or discussed with other candidates;
- what, if any, negotiations took place with respect to Lazard's fee structure;
- who was involved in the decision to hire Lazard and agreed to the proposed fees; or
- what analysis the Debtors conducted to determine if Lazard's proposed fee structure reflects market terms, or whether a better rate could be obtained elsewhere.

5. In addition to being above market, the proposed fee structure does not compensate

Lazard proportionally to the amount of work actually to be performed. Lazard's total proposed compensation consists largely of the \$17.5 million Restructuring Fee, which would be payable *solely* as a result of the Debtors' emergence from chapter 11 – regardless of the nature or complexity of the restructuring transaction consummated, or the amount of time and effort actually required of Lazard. Likewise, the proposed retention terms would reward Lazard for the completion of a financing transaction, but not other types of transactions that might be in the best interests of the estates, including asset sales. The omission of a fee based on an asset sale *discourages* Lazard from pursuing such a transaction, and so risks unduly limiting the universe of potential resolutions of these cases.

6. As discussed below, the Committee believes it is possible to devise a fee structure that would enable Lazard to earn substantial amounts in these cases, consistent with market rates, but that also would serve the critical functions of rewarding Lazard commensurately with the amount of work performed and incentivizing Lazard to pursue all viable restructuring alternatives. The Committee respectfully submits, therefore, that the Application should not be approved unless Lazard's compensation is modified as discussed herein.

Objection

7. Section 328(a) of the Bankruptcy Code permits a debtor to obtain preapproval of compensation packages for its professionals, so long as the proposed retention is on "*reasonable terms and conditions.*" 11 U.S.C. § 328(a) (emphasis added); *see, e.g., Comm. of Equity Sec. Holders v. Official Comm. of Unsecured Creditors (In re Federal-Mogul Global Inc.)*, 348 F.3d 390, 397 (3d Cir. 2003) ("[T]he Court may approve the employment of a professional on any terms and conditions that the Court finds necessary to satisfy the requirement of reasonableness.").

8. The Court, “in its duties as a gatekeeper, must have a sufficiently strong record when deciding whether to approve a professional under § 328(a)” in order to determine that the proposed terms are reasonable. *In re Energy Partners, Ltd.*, 409 B.R. 211, 225 (Bankr. S.D. Tex. 2009). Thus, a debtor must demonstrate by a preponderance of the evidence, rather than by conclusory statements, that its proposed retention of a professional (i) reflects normal business terms in the marketplace, (ii) resulted from arm’s-length negotiations, and (iii) is in the best interests of the estate. *See id.* at 225-31 (Bankr. S.D. Tex. 2009) (denying application based on lack of evidence of these factors); *see also In re High Voltage Eng’g Corp.*, 311 B.R. 320, 333-35 (Bankr. D. Mass. 2004) (denying application based on lack of evidence that proposed compensation was reasonable).

9. Proposed fee structures for investment bankers containing success bonuses require “close scrutiny” to ensure that they meet the reasonableness requirement. *See In re Drexel Burnham Lambert Grp. Inc.*, 133 B.R. 13, 27 (Bankr. S.D.N.Y. 1991). The burden to prove reasonableness is high because “[o]nce a fee arrangement is approved under § 328, the ability of the bankruptcy court, as well as creditors and parties in interest, to review the amount of compensation payable to the professional is circumscribed.” *High Voltage Eng’g Corp.*, 311 B.R. at 332; *see also Riker v. Official Comm. of Unsecured Creditors (In re Smart World Techs., LLC)*, 552 F.3d 228, 233 (2d Cir. 2009) (“[T]here is no question that a bankruptcy court may not conduct a § 330 inquiry into the reasonableness of the fees and their benefit to the estate if the court already has approved the professional’s employment under 11 U.S.C. § 328.”) (internal quotation marks omitted). That is, a court may only revisit the reasonableness of a professional’s fees if the terms and conditions “prove to have been improvident in light of developments *not*

capable of being anticipated at the time of the fixing of such terms and conditions.” 11 U.S.C. § 328(a) (emphasis added).

10. Accordingly, a bankruptcy court must be especially vigilant in ensuring that the reasonableness requirement has been satisfied *before* approving retention terms under section 328; otherwise, the professional’s compensation will be especially difficult to challenge later. In this regard, in ruling on a section 328 application, “a Bankruptcy Court need not approve or reject an application as presented but may approve an application with modified terms that the Court finds necessary to render the proposed employment reasonable.” *Federal-Mogul Global, Inc.*, 348 F.3d at 398 (affirming bankruptcy court’s authority to reduce proposed monthly fees of financial advisor).

11. Here, the Committee does not object to Lazard serving as the Debtors’ financial advisor. Rather, the Committee contends that the proposed compensation package is unreasonably high under the circumstances of these cases – where the Debtors’ restructuring is not expected to be particularly complex – and should not be approved unless it is modified, as discussed herein.

12. The Application does not provide any evidentiary basis to support the reasonableness of Lazard’s proposed fee structure. In particular, the Debtors have provided no information regarding their process for selecting Lazard, any negotiations that took place regarding the fee structure, who was involved in the selection and negotiation process, and what efforts the Debtors undertook (if any) to seek a better rate or to determine whether Lazard’s fees were in line with the market. *See Drexel Burnham Lambert Grp. Inc.*, 133 B.R. at 27 (“[T]he party retaining the professional must describe the process by which the financial banker/advisor has been selected.”). Instead, the Application merely recites the conclusory statement that the

proposed fee structure “adequately reflects: (i) the nature of the services to be provided by Lazard and (ii) fee and expense structures . . . typically utilized by Lazard and other leading investment banking firms, which do not bill their time on an hourly basis and generally are compensated on a transactional basis.” *See* Application ¶ 32.

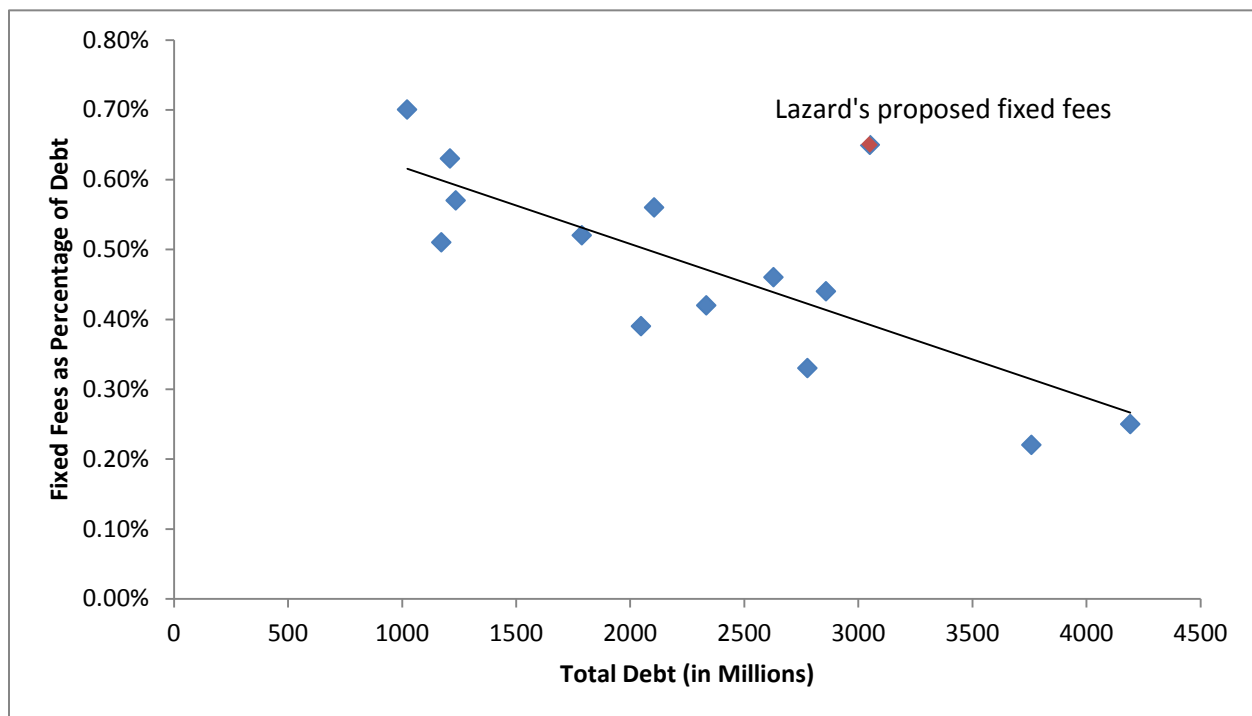
13. This conclusory assertion is not sufficient to carry the Debtors’ burden of proving reasonableness. It is also inaccurate. Contrary to the Debtors’ contention, the size of the requested fees does not comport with fees charged by investment banking firms for comparable engagements.

14. The table attached as Exhibit A hereto provides information about the fee structures of debtors’ investment bankers in comparable cases. This information is limited to chapter 11 cases involving oil-and-gas debtors in 2015 and 2016, where total debt exceeds \$1 billion. This data clearly demonstrates that the fees proposed here are above market: the average amount of fixed fees charged by debtors’ investment bankers (monthly fees plus restructuring fees), measured as a percentage of total prepetition debt, is 0.46%. When the analysis is further limited to those cases where total debt is between \$2 and \$4 billion – and thus the cases most closely analogous to this one in terms of size – the mean amount of fixed fees is even lower (0.40%). Lazard’s proposed fixed fees here, by contrast, would amount to 0.65% of the Debtors’ total pre-petition debt. This represents an approximately 60% premium above the mean in cases of similar size.

15. Other significant conclusions can be drawn from the data as well, including that there is not a linear relationship between the amount of total debt and the amount of fixed fees approved. Rather, it is the smallest cases that involve the highest fees, measured as a percentage

of debt.³ This indicates that there is a baseline fixed fee amount – and a minimum level of work required in all similar cases, regardless of size – and that premiums to this floor increase only modestly with the amount of debt. The total amount of debt involved in the Debtors’ cases (approximately \$3.05 billion) is not extraordinary, and the Debtors’ capital structure is not complex. Accordingly, these cases do not justify an above-market fixed fee.

16. The graph below charts the amount of fixed fees charged in the comparable cases against the amount of total debt in each case. It demonstrates that fixed fees, as a percentage of total debt, decrease as the size of the case increases. And it further illustrates that Lazard’s proposed fees here are above what is ordinary in the market for a case of this size.



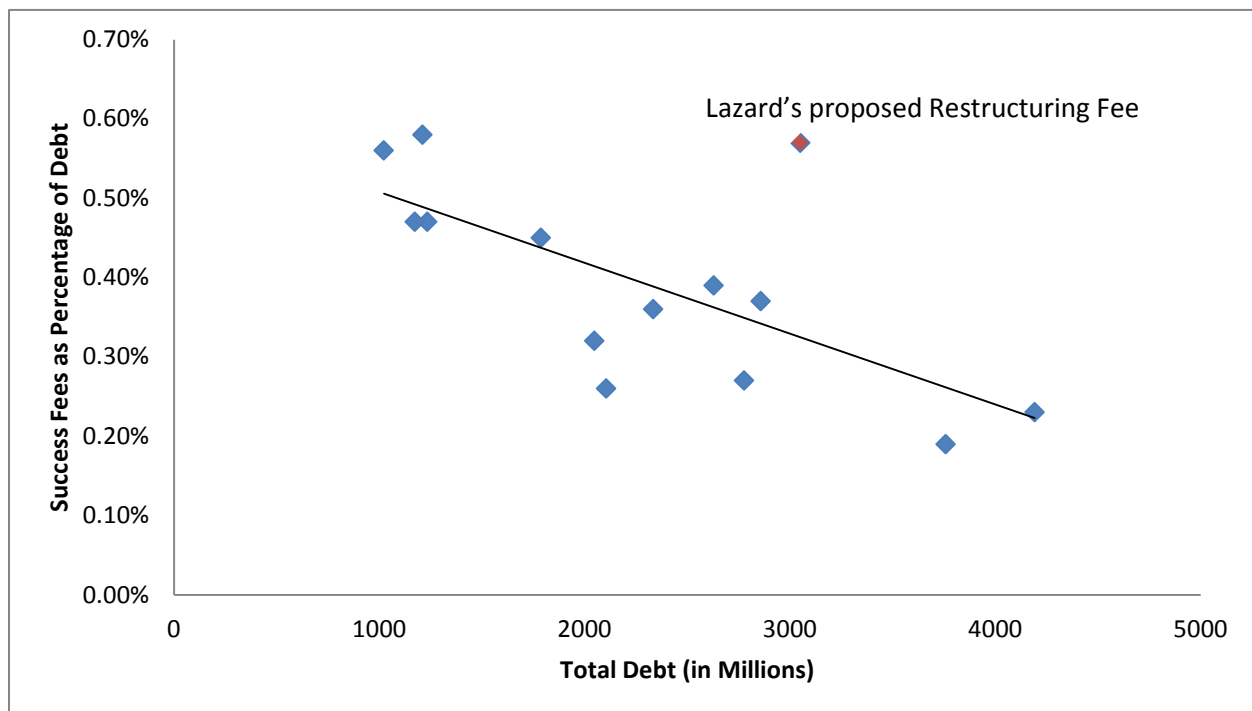
17. The data shows not only that Lazard’s total fixed fees are above market, but also that specific components of its fee structure, when viewed separately, are outside the norm. As

³ Compare, e.g., Magnum Hunter Resources (\$1.023 billion debt; fixed fees equal to 0.70%) and Hercules Offshore Inc. (\$1.211 billion debt; fixed fees equal to 0.63%), with Samson Resources (\$4,192 billion; fixed fees equal to 0.25%) and Ultra Petroleum (\$3.759 billion debt; fixed fees equal to 0.22%).

to the Restructuring Fee, there is not a single comparable case in which a success fee greater than \$10.6 million has been approved. Focusing solely on cases involving between \$2 and \$4 billion of total debt, the success fees range between \$6.5 million and \$10.5 million, with a midpoint of \$8.5 million. Lazard's proposed Restructuring Fee of \$17.5 million is far above this range.

18. Likewise, when reflected as a percentage of total debt, the Restructuring Fee proposed for Lazard is well above average: 0.57%, compared to a mean of 0.40%. Lazard itself, on numerous occasions, has agreed to a restructuring fee that is a far lower percentage of total debt.⁴

19. The graph below illustrates that Lazard's proposed Restructuring Fee, as a percentage of total debt, is above market given the size of the Debtors' cases:



20. The proposed monthly fee for Lazard is also at the high end of the market. As illustrated by Exhibit A, the average monthly fee charged by investment bankers in large oil-and-

⁴ See, e.g., Sabine Oil & Gas Corp. (0.27%), Paragon Offshore PLC (0.36%), RCS Capital Corp. (0.36%), and Swift Energy Co. (0.47%).

gas cases is \$161,000. Lazard's proposed monthly fee of \$200,000 reflects a nearly 25% premium to the mean.⁵

21. In addition, the Financing Fees proposed here are unreasonable in light of the amount of work likely to be required of Lazard to obtain financing, and Lazard should not be entitled to earn such fees with respect to financing transactions involving only existing stakeholders in the Debtors. An investment banker adds the most value to a financing transaction by locating potential providers of capital that are not already known to the Debtors, and running market tests and bidding processes. The Debtors should not pay top-market rates to an investment banker for a financing transaction involving only incumbent stakeholders – parties that “are already at the negotiating table.” Tr. of Hr'g, May 16, 2016, at 16:25-17:2.

22. Finally, the proposed fee structure does not reward Lazard proportionally to the level of work that may actually be required, and it fails adequately to incentivize Lazard to pursue all potential restructuring options. By entitling Lazard to a \$17.5 million Restructuring Fee *regardless* of what kind of transaction is consummated – or what level of work is actually performed – the proposed fee structure discourages Lazard from pursuing work-intensive alternatives. Especially notable is the fact that the proposed fees do not include any compensation that specifically rewards the consummation of asset sales, which may very well be a value-maximizing option for the Debtors.

23. The Committee therefore proposes an alternative fee structure that would include Monthly Fees of \$150,000, a Restructuring Fee of \$9 million (equal to 0.29% of total prepetition debt), and additional success fees that would reward Lazard for completing specific types of transactions: a debt financing fee equal to 0.25% of capital raised; an equity raise fee equal to

⁵ In the Chaparral case, the monthly fee was initially proposed to be \$200,000; but even in that case, the debtor's investment banker has since agreed (i) to reduce the monthly fee to \$175,000 beginning with the fourth month of that case and (ii) to credit half of the reduced monthly fee against any success fee.

0.25% of capital raised; and an asset sale fee equal to 1% of proceeds generated. The success fees would not be credited against the base Restructuring Fee; and Lazard's aggregate compensation would be capped at \$18 million. This structure, the Committee submits, would appropriately incentivize Lazard to explore *all* possible restructuring scenarios, including those involving asset sales, and would ensure that Lazard receives compensation reflecting the actual amount of work involved.

24. Taking an example of a potential restructuring scenario demonstrates that under the Committee's proposed structure, Lazard still would stand to receive significant sums for performing significant amounts of work. Assuming that a resolution of these cases involves raising \$200 million in equity, raising \$700 million in debt financing, and completing asset sales generating \$500 million in proceeds, and further assuming the cases last twelve months, Lazard would earn the \$18 million maximum.⁶ That is almost exactly the amount of the Restructuring Fee requested in the Application. The crucial difference, however, is that under the Committee's proposal, Lazard would earn this level of fees only as a result of completing several labor-intensive transactions.

25. The Committee therefore respectfully submits that its proposed fee structure, as described herein, would meet the reasonableness requirement of section 328(a); the fee structure proposed in the Application would not.

Conclusion

For the foregoing reasons, the Court should deny the relief requested in the Application as currently proposed, modify the terms of the proposed retention of Lazard as discussed herein,

⁶ The calculation is as follows: (\$9,000,000 Restructuring Fee) + (0.25% * \$200,000,000 = \$500,000 Equity Raise Fee) + (0.25% * \$700,000,000 = \$1,750,000 Debt Financing Fee) + (1% * \$500,000,000 = \$5,000,000 Asset Sale Fee) + (12 * \$150,000 = \$1,800,000 Monthly Fees) = \$18,050,000.

and grant such other relief as this Court deems just and proper.

Dated: June 13, 2016
New York, New York

/s/ Gregory A. Bray
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*Proposed Counsel for Official Committee of
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Exhibit A

Investment Banker Fee Summary

Oil and Gas Investment Banker Fee Summary (cases involving more than \$1 billion in total debt)

	Date Filed	Company	Jurisdiction	Advisor	Total Debt ¹	Monthly Fee	Success Fee	Total Fixed Fees ²	Success Fee as % of Debt	Total Fixed Fees as % of Debt	Exit Financing Fee			Sale Fee ³
											Senior Debt	Junior Debt	Equity	
1.	5/9/16	Chaparral Energy	D. Del.	Evercore	\$1,788	\$0.200	\$8.0	\$9.4	0.45%	0.52%	0.50%	1.25%	2.50%	1.00%
2.	4/30/16	Midstates Petroleum	S.D. Tex.	Evercore	\$2,048	\$0.175	\$6.5	\$8.1	0.32%	0.39%	N/A	N/A	N/A	N/A
3.	4/29/16	Ultra Petroleum	S.D. Tex.	Rothschild	\$3,759	\$0.120	\$7.2	\$8.2	0.19%	0.22%	0.60%	1.20%	2.40%	0.30%
4.	4/14/16	Energy XXI	S.D. Tex.	PJT	\$2,858	\$0.175	\$10.5	\$12.6	0.37%	0.44%	0.67%	2.01%	3.35%	1.00%
5.	2/14/16	Paragon Offshore plc	D. Del.	Lazard	\$2,334	\$0.175	\$8.5	\$9.9	0.36%	0.42%	0.63%	0.63%	0.63%	N/A
6.	12/31/15	Swift Energy Company	D. Del.	Lazard	\$1,235	\$0.150	\$5.8	\$7.1	0.47%	0.57%	1.00%	1.00%	2.00%	N/A
7.	12/15/15	Magnum Hunter Resources	D. Del.	PJT	\$1,023	\$0.155	\$5.8	\$7.1	0.56%	0.70%	1.00%	3.00%	5.00%	1.00%
8.	12/3/15	Vantage Drilling	D. Del.	Lazard	\$2,629	\$0.150	\$10.2	\$12.0	0.39%	0.46%	1.25%	1.25%	1.25%	N/A
9.	12/7/15	Energy & Exploration Partners	N.D. Tex.	Evercore	\$1,173	\$0.150	\$5.5	\$6.0	0.47%	0.51%	1.00%	1.00%	1.00%	N/A
10.	9/16/15	Samson Resources	D. Del.	Blackstone	\$4,192	\$0.175	\$9.5	\$10.6	0.23%	0.25%	1.00%	1.00%	5.00%	1.31%
11.	8/13/15	Hercules Offshore Inc.	D. Del.	Lazard	\$1,211	\$0.150	\$7.0	\$7.7	0.58%	0.63%	0.50%	0.50%	0.50%	N/A
12.	7/15/15	Sabine Oil & Gas	S.D.N.Y.	Lazard	\$2,777	\$0.150	\$7.5	\$9.3	0.27%	0.33%	1.50%	1.50%	3.00%	N/A
13.	3/17/15	Quicksilver Resources	D. Del.	Houlihan Lokey	\$2,105	\$0.150	\$10.6	\$11.8	0.50%	0.56%	0.75%	2.00%	5.00%	0.71%
					Mean	\$0.160	\$7.89	\$9.22	0.40%	0.46%	0.87%	1.36%	2.64%	0.89% ⁴
					Median	\$0.150	\$7.50	\$9.30	0.39%	0.46%	0.88%	1.23%	2.45%	1.00%
					Maximum	\$0.200	\$10.60	\$12.60	0.58%	0.70%	1.50%	3.0%	5.00%	1.31%
					Minimum	\$0.120	\$5.50	\$6.00	0.19%	0.22%	0.50%	0.5%	0.50%	0.30%
Breitburn					\$3,050	\$0.200	\$17.5	\$19.9	0.57%	0.65%	0.38%	0.38%	1.00%	0.0%

FINANCING FEE CREDITING

Crediting/Contingent Fee Based on Insider/Outsider Status

Crediting Based on Size of Restructuring Fee

Basic or No Crediting (If crediting, net fee shown)

¹ Total Debt excludes preferred equity.² Total Fixed Fees includes monthly fees plus success fee, and assumes a 12-month case, net of any crediting of monthly fees against the success fee.³ Sale Fee assumes sale at midpoint of fee tier structure and net of any crediting.⁴ Exit Financing Fee summary statistics only include blue shaded data.