802.2
802.3

[redacted]

[redacted]

July 25, 2006

Michael Verne, Esq.
Premerger Notification Office
Bureau of Competition
Federal Trade Commission
600 Pennsylvania Ave., NW
Washington, DC 20580

Dear Mr. Verne:

This letter summarizes the factual situation described to you in our conference call on Monday, July 24, 2006, during which you confirmed our conclusion that the below-described transaction would not be Hart-Scott-Rodino reportable. I would appreciate your confirming your concurrence with our conclusion to me by return email.

As described to you in our telephone call, Company A proposes to acquire an interest in off-shore oil and gas leases from Company B. Specifically, the transaction involves three agreements: (1) an Acquisition Agreement under which Company A will assume a one-third undivided interest in a block of approximately 80–90 leases in the Gulf of Mexico (the "leases"); (2) a Joint Operating Agreement under which Company B agrees to conduct all operations on the leases subject to Company A's right to approve certain expenditures; and (3) an Area of Mutual Interest Agreement under which the parties will agree that any further interest acquired by either party within the range of a certain geographic area surrounding the above-mentioned leases will be subject to the one-third (Company A) / two-third (Company B) ownership interest contemplated in the Acquisition Agreement. The hydrocarbon reserves subject to the leases are currently not drilled and are, therefore, currently not producing.

The total value of the one-third interest in the leases subject to the Acquisition Agreement is estimated to be in the range of $100–150 million. This value will be paid in the form of a "promote" in the drilling of three exploratory wells. In addition, Company A will reimburse Company B up to $16.5 million for sunk costs already incurred. All other expenses incurred under the terms of the Operating Agreement will be shared on a one-third (Company A) / two-third (Company B) basis.

I. Acquisition Agreement:

We have concluded that the acquisition of the one-third interest in the Company B lease holdings would not trigger an HSR reporting obligation. Because this is an acquisition of leases related to carbon-based mineral reserves, the acquisition must be analyzed under 16 C.F.R. § 802.3. Section 802.3 exempts "[a]n acquisition of reserves of oil, natural gas, shale or tar sands, or rights to reserves of oil, natural gas, shale or tar sands together with associated exploration or production assets" but only if their value does not exceed $500 million (the "Oil and Gas Exemption"). Although not specifically stated in § 802.3, we understand that it is the Premerger Notification Office's position that if an asset would qualify for an exemption if purchased outright, the purchase of a lease is similarly exempt. *See ABA Premerger Notification Practice Manual* Interpretation 3. The leases subject to the Acquisition Agreement involve the rights to reserves of oil and gas; in addition, the value of the leases is less than $500 million. Thus, under § 802.3, the acquisition of the one-third interest in the leases would not trigger an HSR reporting obligation.

In addition, to the extent that certain properties (oil and reserves) encumbered by portions of the leases have not yet generated any revenues, such properties will be treated as falling under the "Unproductive Real Property Exemption" set forth in 16 CFR § 802.2(c). As a result, any such properties would not count towards the $500 million Oil and Gas Exemption value threshold. In applying the Unproductive Real Property Exemption to any non-producing properties subject to the leases, it is not necessary to determine whether, for purposes of 16 CFR § 802.2(c)(2)(iii), such properties are or are not "adjacent to or used in conjunction with real property that is not unproductive real property" as long as any other such adjacent properties are otherwise exempt under the Oil and Gas Exemption. That is, if certain unproductive real properties subject to the leases are adjacent to productive real properties, which are part of the transaction but qualify for the Oil and Gas Exemption, the unproductive real properties still qualify for the Unproductive Real Property Exemption. Thus, because the properties subject to the leases are currently not producing, their value will not be applied toward the $500 million Oil and Gas Exemption limit.

II. Joint Operating Agreement:

We have also concluded that the formation of the venture contemplated by the Joint Operating Agreement also would not trigger an HSR reporting obligation. Because the Operating Agreement involves the formation of a venture to operate and maintain the leases subject to the Acquisition Agreement, the transaction must be examined under 16 C.F.R. § 801.40. Under § 801.40 the Size-of-Transaction test set out in 16 C.F.R. § 801.1(h) is first examined. The formation of the joint venture would not meet the Size-of-Transaction test as specified in § 801.1(h). The joint venture contemplated by the Operating Agreement does not involve the issuance of voting securities; it is strictly an agreement regarding the sharing of costs incurred in connection with operating and maintaining the leases. Thus, at the time of formation, no investor in the operating venture will hold voting securities in the venture valued in excess of $50 million ($56.7 million, as adjusted). In addition, no investor will hold more than 50% of the voting

securities of the venture at the time of formation. Thus, under § 801.1(h), the Size-of-Transaction test is not met and the formation of the venture contemplated in the joint operating agreement would not trigger an HSR reporting obligation.

III. Area of Mutual Interest Agreement:

In addition, we have concluded that execution of the Area of Mutual Interest Agreement would not trigger an HSR reporting obligation because it does not involve the present acquisition of assets or voting securities meeting the criteria of 15 U.S.C. 18(a).

Please call if you have any questions regarding the foregoing.

[redacted]

Agree
[redacted]
7/25/06