REMAKING TOREADOR

With a new chief executive officer and new strategy, Toreador Resources has revamped its finances and is aiming at a Bakken shale look-alike in France.

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Few E&P companies have been so completely remade in recent months as has Toreador Resources Corp. The small-cap company that focuses on international plays has been going through tremendous change. Symbolic of this, corporate headquarters were moved from Dallas to Paris this year—and not nearby Paris, Texas, but la Belle France.

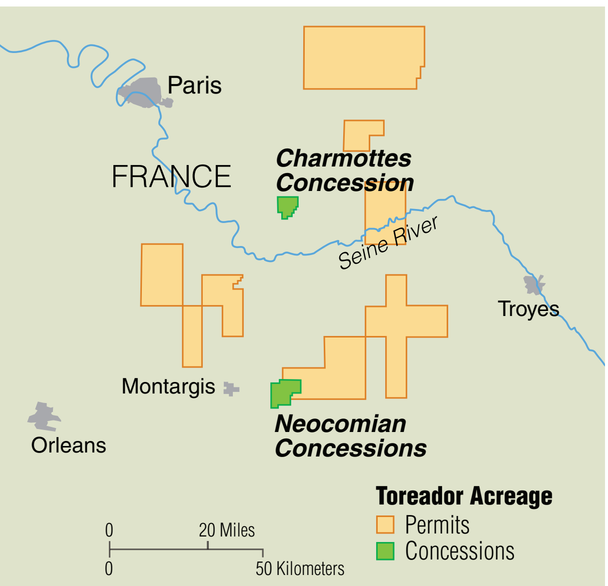
Last month, its key Turkish and Hungarian interests that once commanded most of the capital budget were sold, marking the company's exit from those countries. Debt is coming down. The staff has been reduced.

Toreador's new focus? Conventional and unconventional oil resources in the Paris Basin.

"I can't imagine another company in our peer group going through such fundamental change as we are," says Craig M. McKenzie, who this past March was named Toreador's new president and chief executive officer, after serving as interim president and CEO since late January.

"Our priority is to put the company on firm footing. I find that a lot of small E&Ps overextend themselves because they want to conquer a lot of geographies. We don't want to get smaller, per se, but to be more disciplined and focused."

Toreador's new strategy was formally unveiled in June. It involves growing its conventional oil reserves in France, where it produces about 900 barrels per day.



More exciting, however, Toreador hopes to create a first-mover advantage by bringing U.S. horizontal drilling and frac technology to bear on oil-shale assets in the Paris Basin south and east of Paris, where it estimates that its acreage could hold 30 billion barrels of oil shale in place.

"An unconventional wave is about to hit Europe and we think we'll be on the leading edge. We think we have a tremendous business case on our hands, but this is not going to be a walk in the park, either," McKenzie says. "We hope to condense the learning curve in the Bakken and tap into that expertise. We hope to spud three wells in 2010 and get some new cores."

In the Paris Basin, operators have drilled only a few horizontal wells and certainly, no multilaterals. Big fracture stimulations common in U.S. shale and tight-gas basins have not been done. The reserve potential on Toreador's acreage could be 400 million barrels of oil, versus its current asset base of about 10 million, he adds.

"Not only has the company reduced net debt from $105 million at the beginning of 2009 to $43 million currently through exiting Turkey, Romania and Hungary, it is now a pure play on France, where it has about 649,000 net acres in the Paris Basin, plus another 154,000 net acres granted pending formal approval," says an October report from Pritchard Capital Partners.

"An estimated 95 billion barrels of oil have been generated in the Paris Basin, but since less than 2% has been found, tremendous volumes remain in the source rock."

At press time the company was about to spud one conventional oil well on its La Garenne prospect, a 100%-owned license, that will drill into limestone formations. The well is expected to cost about $2.2 million.

Demand for change

Dr. Peter J. Hill, an old BP hand, is non-executive chairman of the board. He joined the company to effect these changes. McKenzie also worked at BP, and both have managed international E&P companies—often, companies that needed to restructure.

McKenzie has more than 23 years in the industry, mostly with BG and BP. Before Toreador, he served for about a year as CEO of Canadian Superior Energy Inc., the beleaguered Calgary E&P that is now emerging from bankruptcy, and which has huge gas reserves offshore Trinidad & Tobago.

He was president of BG Trinidad & Tobago from May 2004 to September 2007. From 1986

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to 2004, he held senior positions at Amoco and with BP.

Unrest at Toreador began percolating in 2008 when, even before the financial crisis hit the energy industry, the company reported a loss of $65.8 million in the second quarter. At that time it was still pursuing its exploration and production efforts offshore Turkey in the Black Sea, in the South Akcakoca Sub-basin. It had had some exploration success. (See "Turkey," *Oil and Gas Investor*, February 2008.)

McKenzie says the company's dramatic transformation is self-driven. "The bondholders did not press us. In January 2009 we simply walked in and did not like our balance sheet. Total debt was about $110 million at the time but the market cap was less than $40 million, so we set out to reduce debt and bring some discipline into the company."

From a high of around $40 at one time, the stock price had declined to as low as $12 per share, and then fell further to $1.96 after the global financial crisis hit.

"That is a lot of value erosion. If you look at the SEC filings, you'll see a lot of shareholder protest or displeasure even before the global meltdown," McKenzie says. "The shareholders thought management was not acting quickly enough or dramatically enough. Management was sort of 'steady as she goes,' but shareholders wanted something much more urgent."

The company had drilled 13 dry holes in two years, mostly in Hungary and Romania, and its Turkish drilling success was paid for with too much borrowed money, he says.

"A cardinal rule is you don't borrow to drill exploration wells. If you have a dry hole, you find yourself with a write-off and yet, you still have to pay the money back. A lot of the erosion in value was self-inflicted."

McKenzie and a new board of directors moved quickly. In March 2009, Toreador sold a 26.75% interest in its Black Sea assets offshore Turkey to Petrol Ofisi for $55 million, and in turn, paid off its loan from the International Finance Corp. In April, it repurchased $16.7 million face value of its 5% convertible senior notes, due 2025, at a discount of $12.7 million.

In September, Toreador Hungary Ltd. was sold to RAG (Rohol-Aufsuchungs AG), a private Austrian energy company, for $5.8 million, plus a contingent payment of $2.9 million, to be paid upon completion of agreements relating to certain Hungarian assets.

The company's final exit from Turkey culminated in the sale last month of Toreador Turkey Ltd. to Tiway Oil, a private Norwegian company. Toreador received $10.6 million at closing, but it will also be paid up to $40 million, plus contingent future-net-profit payments, based on exploration success. The deal resulted in a financial gain of about $21.2 million, recorded in third-quarter 2009.

Combined cash proceeds of both deals will be $16.4 million (not counting contingent future payments of up to $43 million). Toreador intends to continue repurchasing some of the $64 million of outstanding convertible notes that are putable to the company at par in October 2010. External financing will likely be needed in 2010 to pay for this cash call if bondholders choose to force repayment of the converts. A loan backed by the French reserves is plausible. In addition, the company is seeking a partner for its nascent shale campaign.

Early on, Toreador shareholders remade its board of directors. Along with Hill and McKenzie, they elected Julien Balkany, Adam Kroloff, Ian Vann, Herbert Williamson III, and in September 2009, Bernard de Combret. Each has extensive experience in E&P or finance. Kroloff and Vann, based in London, bring insights into European markets and underscore Toreador's goal "to create a leading pan-European and Mediterranean E&P company."

Balkany is managing director of Nanes Delorme Capital Management, a New York broker-dealer and investor in the company. Williamson, an investment banker, was a principal at Petrie Parkman & Co. in the early 1990s. Combret is former deputy chairman of the executive committee at Total.

Bonjour Bakken

Analysts at Thomas Weisel Partners initiated research coverage of the new Toreador in September with an overweight rating. Their report, titled "Bonjour Bakken," focuses on the emerging oil-shale play in France that Toreador intends to drill in 2010 with three pilot wells.

This shale appears geologically similar to North Dakota's Bakken play. Basin-wide subsurface modeling is ongoing with the help of consultant Beicip Franlab. Data so far show a favorable comparison to the Bakken shale in several respects, such as thermal oil content, often referred to as TOC.

"There are more than 1,000 penetrations in the Paris Basin and 600 confirm the presence of the oil shale," McKenzie says. "We think the resource potential has always been there, but it has not been explored with modern drilling techniques."

The last wave of drilling activity in France occurred in the early 1980s, well before the advent of recent completion techniques that have led to surging U.S. shale production. Toreador plans to drill its three wells vertically to the top of the shale zone, with core analysis to follow. The company needs further information on the porosity, permeability and nature of the naturally occurring fractures.

"Although the Lower Jurassic shales of the Paris Basin offer considerable potential, successful exploitation will likely require a degree of trial and error as optimal development techniques are identified. Toreador plans to bring in a strategic partner to provide funding and share some of the risk," the report says. □