

ABRAXAS PETROLEUM CORP

Form 10-Q

May 09, 2014

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

(Mark One)

☒ QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934 FOR THE QUARTERLY PERIOD ENDED MARCH 31, 2014

☐ TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934 FOR THE TRANSITION PERIOD FROM _____ TO _____

COMMISSION FILE NUMBER: 001-16071

ABRAXAS PETROLEUM CORPORATION

(Exact name of registrant as specified in its charter)

Nevada

(State of Incorporation)

18803 Meisner Drive, San Antonio, TX 78258

(Address of principal executive offices) (Zip Code)

210-490-4788

(Registrant's telephone number, including area code)

74-2584033

(I.R.S. Employer Identification
No.)

Not Applicable

(Former name, former address and former fiscal year, if changed since last report)

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to the filing requirements for the past 90 days. Yes ☒ No ☐

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§ 232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes ☒ No ☐

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer or a smaller reporting company. See definition of "large accelerated filer," "accelerated filer" and "smaller reporting company"

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in Rule 12b-2 of the Exchange Act. (Check One)

Large accelerated filer ☐

Accelerated filer ☒

Non-accelerated filer ☐

Smaller reporting company ☐

(Do not mark if a smaller reporting company)

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). Yes ☐ No ☒

The number of shares of the issuer's common stock outstanding as of May 8, 2014 was 93,796,854.

Forward-Looking Information

We make forward-looking statements throughout this report. Whenever you read a statement that is not simply a statement of historical fact (such as statements including words like “believe,” “expect,” “anticipate,” “intend,” “will,” “plan,” “may,” “estimate,” “could,” “potentially” or similar expressions), you must remember that these are forward-looking statements, and that our expectations may not be correct, even though we believe they are reasonable. The forward-looking information contained in this report is generally located in the material set forth under the headings “Management’s Discussion and Analysis of Financial Condition and Results of Operations” but may be found in other locations as well. These forward-looking statements generally relate to our plans and objectives for future operations and are based upon our management’s reasonable estimates of future results or trends. The factors that may affect our expectations regarding our operations include, among others, the following:

- the prices we receive for our production and the effectiveness of our hedging activities;
- our success in development, exploitation and exploration activities;
- the availability of capital;
- our ability to make planned capital expenditures;
- declines in our production of oil and gas;
- our ability to procure services and equipment for our drilling and completion activities;
- our restrictive debt covenants;
- political and economic conditions in oil producing countries, especially those in the Middle East;
- price and availability of alternative fuels;
- our acquisition and divestiture activities;
- weather conditions and events;
- the proximity, capacity, cost and availability of pipelines and other transportation facilities; and
- other factors discussed elsewhere in this report.

GLOSSARY OF TERMS

Unless otherwise indicated in this report, gas volumes are stated at the legal pressure base of the State or area in which the reserves are located at 60 degrees Fahrenheit. Oil and gas equivalents are determined using the ratio of six Mcf of gas to one barrel of oil, condensate or natural gas liquids.

The following definitions shall apply to the technical terms used in this report.

Terms used to describe quantities of oil and gas:

“Bbl” – barrel or barrels.

“Bcf” – billion cubic feet of gas.

“Bcfe” – billion cubic feet of gas equivalent.

“Boe” – barrels of oil equivalent.

“MBbl” – thousand barrels.

“MBoe” – thousand barrels of oil equivalent.

“Mcf” – thousand cubic feet of gas.

“Mcfe” – thousand cubic feet of gas equivalent.

“MMBbl” – million barrels.

“MMBoe” – million barrels of oil equivalent.

“MMBtu” – million British Thermal Units of gas.

“MMcf” – million cubic feet of gas.

“MMcfe” – million cubic feet of gas equivalent.

“NGL” – natural gas liquids measured in barrels.

Terms used to describe our interests in wells and acreage:

“Developed acreage” means acreage which consists of leased acres spaced or assignable to productive wells.

“Development well” is a well drilled within the proved area of an oil or gas reservoir to the depth or stratigraphic horizon (rock layer or formation) noted to be productive for the purpose of extracting reserves.

“Dry hole” is an exploratory or development well found to be incapable of producing either oil or gas in sufficient quantities to justify completion.

“Exploratory well” is a well drilled to find and produce oil or gas in an unproved area, to find a new reservoir in a field previously found to be producing in another reservoir, or to extend a known reservoir.

“Gross acres” are the number of acres in which we own a working interest.

“Gross well” is a well in which we own an interest.

“Net acres” are the sum of fractional ownership working interests in gross acres (e.g., a 50% working interest in a lease covering 320 gross acres is equivalent to 160 net acres).

“Net well” is the sum of fractional ownership working interests in gross wells.

“Productive well” is an exploratory or a development well that is not a dry hole.

“Undeveloped acreage” means those leased acres on which wells have not been drilled or completed to a point that would permit the production of economic quantities of oil and gas, regardless of whether or not such acreage contains proved reserves.

Terms used to assign a present value to or to classify our reserves:

“Proved reserves” are those quantities of oil and gas reserves, which, by analysis of geoscience and engineering data, can be estimated with reasonable certainty to be commercially recoverable - from a given date forward, from known

reservoirs, and under defined economic conditions, operating methods, and government regulations.

“Proved developed reserves” are those quantities of oil and gas reserves that can be expected to be recovered through existing wells with existing equipment and operating methods. Additional reserves expected to be obtained through the application of fluid injection or other improved recovery techniques for supplementing the natural forces and mechanisms of primary recovery are included in “proved developed reserves” only after testing by a pilot project or after the operation of an installed program has confirmed through production response that increased recovery will be achieved.

“Proved developed non-producing reserves” are those quantities of oil and gas reserves that are developed behind pipe in an existing well bore, from a shut-in well bore or that can be recovered through improved recovery only after the necessary equipment has been installed, or when the costs to do so are relatively minor. Shut-in reserves are expected to be recovered from (1) completion intervals which are open at the time of the estimate but which have not started producing, (2) wells that were shut-in for market conditions or pipeline connections, or (3) wells not capable of production for mechanical reasons. Behind-pipe reserves are expected to be recovered from zones in existing wells that will require additional completion work or future recompletion prior to the start of production.

“Proved undeveloped reserves” or “PUDs” are those quantities of oil and gas reserves that are expected to be recovered from new wells on undrilled acreage or from existing wells where a relatively major expenditure is required for development. Reserves on undrilled acreage are limited to those drilling units offsetting productive units that are reasonably certain of production when drilled. Proved reserves for other undrilled units are claimed only where it can be demonstrated with reasonable certainty that there is continuity of production from the existing productive formation. Estimates for proved undeveloped reserves are not attributed to any acreage for which an application of fluid injection or other improved recovery technique is contemplated, unless such techniques have been proven effective by actual tests in the area and in the same reservoir.

“Probable reserves” are those additional reserves which analysis of geoscience and engineering data indicate are less likely to be recovered than proved reserves but more certain to be recovered than possible reserves.

“Possible reserves” are those additional reserves which analysis of geoscience and engineering data suggest are less likely to be recoverable than probable reserves.

“PV-10” means estimated future net revenue, discounted at a rate of 10% per annum, before income taxes and with no price or cost escalation or de-escalation, calculated in accordance with guidelines promulgated by the Securities and Exchange Commission (“SEC”).

“Standardized Measure” means estimated future net revenue, discounted at a rate of 10% per annum, after income taxes and with no price or cost escalation or de-escalation, calculated in accordance with Accounting Standards Codification (“ASC”) 932, “Disclosures About Oil and Gas Producing Activities.”

ABRAXAS PETROLEUM CORPORATION
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PART I
FINANCIAL INFORMATION

Item 1. Financial Statements

Abraxas Petroleum Corporation
Condensed Consolidated Balance Sheets
(in thousands)

	March 31, 2014 (Unaudited)	December 31, 2013
Assets		
Current assets:		
Cash and cash equivalents	\$349	\$5,205
Accounts receivable, net:		
Joint owners	7,710	15,493
Oil and gas production	19,013	16,625
Other	75	1,497
	26,798	33,615
Derivative asset – current	218	85
Other current assets	529	644
Total current assets	27,894	39,549
Property and equipment:		
Oil and gas properties, full cost method of accounting:		
Proved	597,615	564,755
Other property and equipment	38,684	38,959
Total	636,299	603,714
Less accumulated depreciation, depletion, and amortization	(429,408)	(423,069)
Total property and equipment – net	206,891	180,645
Deferred financing fees, net	1,791	2,140
Derivative asset – long-term	547	925
Other assets	391	391
Total assets	\$237,514	\$223,650

See accompanying notes to condensed consolidated financial statements (unaudited).

Abraxas Petroleum Corporation
Condensed Consolidated Balance Sheets (continued)
(in thousands, except share data)

	March 31, 2014 (Unaudited)	December 31, 2013
Liabilities and Stockholders' Equity		
Current liabilities:		
Accounts payable	\$40,904	\$52,793
Oil and gas production payable	16,961	23,810
Accrued interest	65	31
Other accrued expenses	1,716	1,231
Derivative liability – current	2,860	2,728
Current maturities of long-term debt	2,158	2,142
Total current liabilities	64,664	82,735
Long-term debt, excluding current maturities	68,404	41,790
Other liabilities	57	57
Derivative liability – long-term	2,510	2,274
Future site restoration	9,846	9,888
Total liabilities	145,481	136,744
Stockholders' Equity		
Preferred stock, par value \$0.01 per share, authorized 1,000,000 shares; -0- issued and outstanding	—	—
Common stock, par value \$0.01 per share, authorized 200,000,000 shares; 93,676,095 and 92,906,049 issued and outstanding, respectively	937	929
Additional paid-in capital	253,670	253,193
Accumulated deficit	(161,905)	(166,609)
Accumulated other comprehensive (loss) income	(669)	(607)
Total stockholders' equity	92,033	86,906
Total liabilities and stockholders' equity	\$237,514	\$223,650

See accompanying notes to condensed consolidated financial statements (unaudited).

Abraxas Petroleum Corporation
Condensed Consolidated Statements of Operations
(Unaudited)
(in thousands except per share data)

	Three Months Ended March 31,	
	2014	2013
Revenue:		
Oil and gas production revenues	\$25,850	\$21,163
Other	43	33
	25,893	21,196
Operating costs and expenses:		
Lease operating expenses	5,892	6,462
Production taxes	2,204	1,927
Depreciation, depletion, and amortization	7,635	6,509
General and administrative (including stock-based compensation of \$439 and \$474 respectively)	2,823	2,530
	18,554	17,428
Operating income	7,339	3,768
Other (income) expense:		
Interest income	—	(1)
Interest expense	608	1,208
Amortization of deferred financing fees	348	333
Loss on derivative contracts - Realized	734	925
Loss on derivative contracts - Unrealized	945	621
Other	—	87
	2,635	3,173
Net income before income tax expense	4,704	595
Income tax expense	—	—
Net income	\$4,704	\$595
Net income per common share – basic	\$0.05	\$0.01
Net income per common share – diluted	\$0.05	\$0.01
Weighted average shares outstanding:		
Basic	92,566	92,290
Diluted	94,321	93,264

See accompanying notes to condensed consolidated financial statements (unaudited).

Abraxas Petroleum Corporation
Condensed Consolidated Statements of
Other Comprehensive Income (Loss)
(Unaudited)
(in thousands)

	Three Months Ended March 31,	
	2014	2013
Consolidated net income	\$4,704	\$595
Other comprehensive income (loss):		
Change in unrealized value of investments	—	(7)
Foreign currency translation adjustment	(62)	(131)
Other comprehensive income (loss)	(62)	(138)
Comprehensive income	\$4,642	\$457

See accompanying notes to condensed consolidated financial statements (unaudited).

Abraxas Petroleum Corporation
Condensed Consolidated Statements of Cash Flows
(Unaudited)
(in thousands)

	Three Months Ended March 31,	
	2014	2013
Operating Activities		
Net income	\$4,704	\$595
Adjustments to reconcile net income to net cash provided by operating activities:		
Change in derivative fair value	613	592
Depreciation, depletion, and amortization	7,635	6,509
Amortization of deferred financing fees	348	333
Accretion of future site restoration	144	172
Stock-based compensation	439	474
Changes in operating assets and liabilities:		
Accounts receivable	6,812	(8,804)
Other	113	(69)
Accounts payable and accrued expenses	(18,384)	) 10,111
Net cash provided by operating activities	2,424	9,913
Investing Activities		
Capital expenditures, including purchases and development of properties	(36,719)	) (17,773)
Proceeds from sale of oil and gas properties	2,782	—
Net cash used in investing activities	(33,937)	) (17,773)
Financing Activities		
Proceeds from long-term borrowings	27,000	12,000
Payments on long-term borrowings	(370)	) (6,047)
Exercise of stock options	46	—
Other	(20)) —
Net cash provided by financing activities	26,656	5,953
Effect of exchange rate changes on cash	1	—
Decrease in cash	(4,856)	) (1,907)
Cash and equivalents, at beginning of period	\$5,205	\$2,061
Cash and equivalents, at end of period	\$349	\$154
Supplemental disclosure of cash flow information:		
Interest paid	\$430	\$1,016

See accompanying notes to condensed consolidated financial statements (unaudited).

Abraxas Petroleum Corporation
Notes to Condensed Consolidated Financial Statements
(Unaudited)
(tabular amounts in thousands, except per unit data)

Note 1. Basis of Presentation

The accounting policies followed by Abraxas Petroleum Corporation and its subsidiaries (the “Company”) are set forth in the notes to the Company’s audited consolidated financial statements in the Annual Report on Form 10-K for the year ended December 31, 2013 filed with the SEC on March 17, 2014. Such policies have been continued without change. Also, refer to the notes to those financial statements for additional details of the Company’s financial condition, results of operations, and cash flows. All material items included in those notes have not changed except as a result of normal transactions in the interim, or as disclosed within this report. The accompanying interim condensed consolidated financial statements have not been audited by our independent registered public accountants, but in the opinion of management, reflect all adjustments necessary for a fair presentation of the financial position and results of operations. Any and all adjustments are of a normal and recurring nature. Although management believes the unaudited interim related disclosures in these condensed consolidated financial statements are adequate to make the information presented not misleading, certain information and footnote disclosures normally included in annual audited consolidated financial statements prepared in accordance with accounting principles generally accepted in the United States of America have been condensed or omitted pursuant to the rules and regulations of the SEC. The results of operations and the cash flows for the period ended March 31, 2014 are not necessarily indicative of the results to be expected for the full year. The condensed consolidated financial statements included herein should be read in conjunction with the consolidated audited financial statements and the notes thereto included in the Company’s Annual Report on Form 10-K for the year ended December 31, 2013.

Consolidation Principles

The terms “Abraxas,” “Abraxas Petroleum,” “we,” “us,” “our” or the “Company” refer to Abraxas Petroleum Corporation and of its subsidiaries, including Raven Drilling, LLC (“Raven Drilling”) and a wholly-owned foreign subsidiary, Canadian Abraxas Petroleum, ULC (“Canadian Abraxas”).

Canadian Abraxas’ assets and liabilities are translated to U.S. dollars at period-end exchange rates. Income and expense items are translated at average rates of exchange prevailing during the period. Translation adjustments are accumulated as a separate component of stockholders’ equity.

Rig Accounting

In accordance with SEC Regulation S-X, no income is to be recognized in connection with contractual drilling services performed in connection with properties in which the Company or its affiliates holds an ownership, or other economic interest. Any income not recognized as a result of this limitation is to be credited to the full cost pool and recognized through lower amortization as reserves are produced.

Use of Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities as of the date of the financial statements and reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

Stock-Based Compensation and Option Plans

Stock Options

The Company currently utilizes a standard option-pricing model (i.e., Black-Scholes) to measure the fair value of stock options granted to employees and directors.

The following table summarizes the Company's stock-based compensation expense related to stock options for the periods presented:

Three Months Ended March 31,	
2014	2013
\$ 306	\$ 362

The following table summarizes the Company's stock option activity for the three months ended March 31, 2014:

	Number of Shares	Weighted Average Option Exercise Price Per Share	Weighted Average Grant Date Fair Value Per Share
Outstanding, December 31, 2013	5,400	\$2.77	\$1.98
Granted	923	3.15	2.28
Exercised	(59)	) 2.07	1.31
Canceled	(29)	) 3.23	2.30
Outstanding, March 31, 2014	6,235	\$2.83	\$1.99

Additional information related to stock options at March 31, 2014 and December 31, 2013 is as follows:

	March 31, 2014	December 31, 2013
Options exercisable	4,112	3,828

As of March 31, 2014, there was approximately \$2.1 million of unamortized compensation expense related to outstanding stock options that will be recognized in 2014 through 2018.

Restricted Stock Awards

Restricted stock awards are awards of common stock that are subject to restrictions on transfer and to a risk of forfeiture if the awardee terminates employment with the Company prior to the lapse of the restrictions. The fair value of such stock was determined using the closing price on the grant date and compensation expense is recorded over the applicable vesting periods.

The following table summarizes the Company's restricted stock activity for the three months ended March 31, 2014:

	Number of Shares	Weighted Average Grant Date Fair Value Per Share
Unvested, December 31, 2013	355	\$3.24
Granted	741	3.15
Vested/Released	—	4.88
Forfeited	(8)	) 3.44
Unvested, March 31, 2014	1,088	\$3.18

The following table summarizes the Company's stock-based compensation expense related to restricted stock for the periods presented:

Three Months Ended March 31,

2014

2013

\$133

\$112

12

As of March 31, 2014, there was approximately \$2.6 million of unamortized compensation expense relating to outstanding restricted shares that will be recognized in 2014 through 2018.

Oil and Gas Properties

The Company follows the full cost method of accounting for oil and gas properties. Under this method, all direct costs and certain indirect costs associated with the acquisition of properties and successful, as well as unsuccessful, exploration and development activities are capitalized. Depreciation, depletion, and amortization of capitalized oil and gas properties and estimated future development costs, excluding unproved properties, are based on the unit-of-production method based on proved reserves. Net capitalized costs of oil and gas properties, less related deferred taxes, are limited by country, to the lower of the unamortized capitalized cost or the cost ceiling. The ceiling cost is calculated as PV-10, plus the cost of properties not being amortized, if any, plus the lower of cost or estimated fair value of unproved properties included in the costs being amortized, if any, less related income taxes. We calculate the projected income tax effect using the "short-cut" method for the cost ceiling test calculation. Costs in excess of the cost ceiling are charged to proved property impairment expense. No gain or loss is recognized upon sale or disposition of oil and gas properties, except where the sale or disposition causes a significant change in the relationship between capitalized cost and the estimated quantity of proved reserves. We apply the full cost ceiling test on a quarterly basis on the date of the latest balance sheet presented. At March 31, 2014, our net capitalized costs of oil and gas properties in the United States and Canada did not exceed the cost ceiling of our estimated proved reserves.

Restoration, Removal and Environmental Liabilities

The Company is subject to extensive Federal, provincial, state and local environmental laws and regulations. These laws regulate the discharge of materials into the environment and may require the Company to remove or mitigate the environmental effects of the disposal or release of petroleum substances at various sites. Environmental expenditures are expensed or capitalized depending on their future economic benefit. Expenditures that relate to an existing condition caused by past operations and that have no future economic benefit are expensed.

Liabilities for expenditures of a non-capital nature are recorded when environmental assessments and/or remediation is probable, and the costs can be reasonably estimated. Such liabilities are generally undiscounted unless the timing of cash payments for the liability or component are fixed or reliably determinable.

The Company accounts for asset retirement obligations based on the guidance of ASC 410 which addresses accounting and reporting for obligations associated with the retirement of tangible long-lived assets and the associated asset retirement costs. ASC 410 requires that the fair value of a liability for an asset's retirement obligation be recorded in the period in which it is incurred and the corresponding cost capitalized by increasing the carrying amount of the related long-lived asset. The liability is accreted to its then present value each period, and the capitalized cost is depreciated over the estimated useful life of the related asset. For all periods presented, we have included estimated future costs of abandonment and dismantlement in our full cost amortization base and amortize these costs as a component of our depletion expense in the accompanying condensed consolidated financial statements.

The following table summarizes the Company's asset retirement obligation transactions for the three months ended March 31, 2014 and the year ended December 31, 2013: