PDC ENERGY, INC.
Form 10-Q
May 06, 2016
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UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

FORM 10-Q

T QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the quarterly period ended March 31, 2016

or

£ 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 001-37419
PDC ENERGY, INC.
(Exact name of registrant as specified in its charter)

Delaware	95-2636730
(State of incorporation)	(I.R.S. Employer Identification No.)

1775 Sherman Street, Suite 3000
Denver, Colorado 80203
(Address of principal executive offices) (Zip code)

Registrant's telephone number, including area code: (303) 860-5800

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 such filing requirements for the past 90 days. Yes x No o

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Website, 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 x No o

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 definitions of "large accelerated filer," "accelerated filer" and "smaller reporting company" in Rule 12b-2 of the Exchange Act.

Large accelerated filer x	Accelerated filer o

Non-accelerated filer o (Do not check if a smaller reporting company)	Smaller reporting company o

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

Indicate the number of shares outstanding of each of the issuer's classes of common stock, as of the latest practicable date: 46,318,394 shares of the Company's Common Stock ($0.01 par value) were outstanding as of April 18, 2016.

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SPECIAL NOTE REGARDING FORWARD-LOOKING STATEMENTS

This Quarterly Report on Form 10-Q contains forward-looking statements within the meaning of Section 27A of the Securities Act of 1933 ("Securities Act") and Section 21E of the Securities Exchange Act of 1934 ("Exchange Act") regarding our business, financial condition, results of operations and prospects. All statements other than statements of historical facts included in and incorporated by reference into this report are "forward-looking statements" within the meaning of the safe harbor provisions of the United States ("U.S.") Private Securities Litigation Reform Act of 1995. Words such as expects, anticipates, intends, plans, believes, seeks, estimates and similar expressions or variations of such words are intended to identify forward-looking statements herein. These statements relate to, among other things: estimated future production (including the components of such production), sales, expenses, cash flows, liquidity and balance sheet attributes; estimated crude oil, natural gas and natural gas liquids (“NGLs”) reserves; the impact of prolonged depressed commodity prices including potentially reduced production and associated cash flow; anticipated capital projects, expenditures and opportunities, including our expectation that 2016 cash flows from operations will approximate cash flows from investing activities; expected capital budget allocations; our operational flexibility and ability to revise our development plan, either upward or downward; availability of sufficient funding and liquidity for our capital program and sources of that funding; that we do not expect a material change in the borrowing base of our revolving credit facility as a result of the May 2016 semi-annual redetermination; that we expect quarter-over-quarter production growth; expected losses of Riley Natural Gas ("RNG") through 2022 and expected discontinuation of RNG's business; future exploration, drilling and development activities, including non-operated activity, the number of drilling rigs we expect to run, number of locations and lateral lengths; expected 2016 production and cash flow ranges; our evaluation method of our customers' and derivative counterparties' credit risk; effectiveness of our derivative program in providing a degree of price stability; potential for future impairments; expected sustained relief of gathering system pressure; compliance with debt and senior notes covenants; expected funding sources for payment of our 3.25% convertible senior notes due May 2016; impact of litigation on our results of operations and financial position; that we do not expect to pay dividends in the foreseeable future; and our future strategies, plans and objectives.

The above statements are not the exclusive means of identifying forward-looking statements herein. Although forward-looking statements contained in this report reflect our good faith judgment, such statements can only be based on facts and factors currently known to us. Forward-looking statements are always subject to risks and uncertainties, and become subject to greater levels of risk and uncertainty as they address matters further into the future. Throughout this report or accompanying materials, we may use the terms “projection” or similar terms or expressions, or indicate that we have “modeled” certain future scenarios. We typically use these terms to indicate our current thoughts on possible outcomes relating to our business or the industry in periods beyond the current fiscal year. Because such statements relate to events or conditions further in the future, they are subject to increased levels of uncertainty.

Important factors that could cause actual results to differ materially from the forward-looking statements include, but are not limited to:

- changes in worldwide production volumes and demand, including economic conditions that might impact demand;
- volatility of commodity prices for crude oil, natural gas and NGLs and the risk of an extended period of depressed prices;
- reductions in the borrowing base under our revolving credit facility;
- impact of governmental policies and/or regulations, including changes in environmental and other laws, the interpretation and enforcement related to those laws and regulations, liabilities arising thereunder and the costs to comply with those laws and regulations;
- declines in the value of our crude oil, natural gas and NGLs properties resulting in further impairments;

- changes in estimates of proved reserves;
- inaccuracy of reserve estimates and expected production rates;
- potential for production decline rates from our wells being greater than expected;
- timing and extent of our success in discovering, acquiring, developing and producing reserves;
- availability of sufficient pipeline, gathering and other transportation facilities and related infrastructure to process and transport our production and the impact of these facilities and regional capacity on the prices we receive for our production;
- timing and receipt of necessary regulatory permits;
- risks incidental to the drilling and operation of crude oil and natural gas wells;
- future cash flows, liquidity and financial condition;
- competition within the oil and gas industry;
- availability and cost of capital;
- our success in marketing crude oil, natural gas and NGLs;
- effect of crude oil and natural gas derivatives activities;
- impact of environmental events, governmental and other third-party responses to such events, and our ability to insure adequately against such events;
- cost of pending or future litigation;
- effect that acquisitions we may pursue have on our capital expenditures;
- our ability to retain or attract senior management and key technical employees; and
- success of strategic plans, expectations and objectives for our future operations.

Further, we urge you to carefully review and consider the cautionary statements and disclosures, specifically those under the heading "Risk Factors," made in this Quarterly Report on Form 10-Q, our Annual Report on Form 10-K for the year ended December 31, 2015 (the "2015 Form 10-K"), filed with the U.S. Securities and Exchange Commission ("SEC") on February 22, 2016, and our other filings with the SEC for further information on risks and uncertainties that could affect our business, financial condition, results of operations and prospects, which are incorporated by this reference as though fully set forth herein. We caution you not to place undue reliance on the forward-looking statements, which speak only as of the date of this report. We undertake no obligation to update any forward-looking statements in order to reflect any event or circumstance occurring after the date of this report or currently unknown facts or conditions or the occurrence of unanticipated events. All forward-looking statements are qualified in their entirety by this cautionary statement.

REFERENCES

Unless the context otherwise requires, references in this report to "PDC Energy," "PDC," "the Company," "we," "us," "our" or "ours" refer to the registrant, PDC Energy, Inc. and all subsidiaries consolidated for the purposes of its financial statements, including our proportionate share of the financial position, results of operations, cash flows and operating activities of our affiliated partnerships. See Note 1, Nature of Operations and Basis of Presentation, to our condensed consolidated financial statements included elsewhere in this report for a description of our consolidated subsidiaries.

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PART I - FINANCIAL INFORMATION
ITEM 1. FINANCIAL STATEMENTS

PDC ENERGY, INC.
Condensed Consolidated Balance Sheets
(unaudited; in thousands, except share and per share data)

	March 31, 2016	December 31, 2015
Assets		
Current assets:		
Cash and cash equivalents	$238,545	$850
Accounts receivable, net	100,053	104,274
Fair value of derivatives	183,484	221,659
Prepaid expenses and other current assets	5,970	5,266
Total current assets	528,052	332,049
Properties and equipment, net	1,942,498	1,940,552
Fair value of derivatives	35,641	44,387
Other assets	9,206	53,555
Total Assets	$2,515,397	$2,370,543
Liabilities and Shareholders' Equity		
Liabilities		
Current liabilities:		
Accounts payable	$73,898	$92,613
Production tax liability	26,541	26,524
Fair value of derivatives	5,173	1,595
Funds held for distribution	28,008	29,894
Current portion of long-term debt	114,183	112,940
Accrued interest payable	19,758	9,057
Other accrued expenses	20,610	28,709
Total current liabilities	288,171	301,332
Long-term debt	492,717	529,437
Deferred income taxes	100,080	143,452
Asset retirement obligation	82,703	84,032
Fair value of derivatives	5,966	695
Other liabilities	29,311	24,398
Total liabilities	998,948	1,083,346
Commitments and contingent liabilities		
Shareholders' equity		
Preferred shares - par value $0.01 per share, 50,000,000 shares authorized, none issued	—	—
Common shares - par value $0.01 per share, 150,000,000 authorized, 46,210,022 and 40,174,776 issued as of March 31, 2016 and December 31, 2015, respectively	462	402
Additional paid-in capital	1,208,117	907,382
Retained earnings	308,892	380,422
Treasury shares - at cost, 20,836 and 20,220 as of March 31, 2016 and December 31, 2015, respectively	(1,022)	(1,009)

Total shareholders' equity	1,516,449	1,287,197
Total Liabilities and Shareholders' Equity	$2,515,397	$2,370,543

See accompanying Notes to Condensed Consolidated Financial Statements
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PDC ENERGY, INC.
Condensed Consolidated Statements of Operations
(unaudited; in thousands, except per share data)

	Three Months Ended March 31,	
	2016	2015
Revenues		
Crude oil, natural gas and NGLs sales	$75,367	$74,109
Sales from natural gas marketing	2,171	3,233
Commodity price risk management gain, net	11,056	66,662
Well operations, pipeline income and other	2,237	628
Total revenues	90,831	144,632
Costs, expenses and other		
Lease operating expenses	15,330	16,285
Production taxes	4,071	3,893
Transportation, gathering and processing expenses	4,041	1,338
Cost of natural gas marketing	2,578	3,258
Exploration expense	210	285
Impairment of crude oil and natural gas properties	1,001	2,772
General and administrative expense	22,779	21,045
Depreciation, depletion and amortization	97,388	55,820
Provision for uncollectible notes receivable	44,738	—
Accretion of asset retirement obligations	1,812	1,560
Gain on sale of properties and equipment	(84)	(21)
Total cost, expenses and other	193,864	106,235
Income (loss) from operations	(103,033)	38,397
Interest expense	(11,894)	(11,725)
Interest income	1,558	1,113
Income (loss) from before income taxes	(113,369)	27,785
Provision for income taxes	41,839	(10,723)
Net income (loss)	$(71,530)	$17,062
Earnings per share:		
Basic	$(1.72)	$0.47
Diluted	$(1.72)	$0.46
Weighted-average common shares outstanding:		
Basic	41,608	36,349
Diluted	41,608	36,981

See accompanying Notes to Condensed Consolidated Financial Statements

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PDC ENERGY, INC.
Condensed Consolidated Statements of Cash Flows
(unaudited; in thousands)

	Three Months Ended March 31,	
	2016	2015
Cash flows from operating activities:		
Net income (loss)	$(71,530)	$17,062
Adjustments to net income (loss) to reconcile to net cash from operating activities:		
Net change in fair value of unsettled derivatives	55,770	(16,230)
Depreciation, depletion and amortization	97,388	55,820
Provision for uncollectible notes receivable	44,738	—
Impairment of crude oil and natural gas properties	1,001	2,772
Accretion of asset retirement obligation	1,812	1,560
Stock-based compensation	4,682	4,368
Gain on sale of properties and equipment	(84)	(21)
Amortization of debt discount and issuance costs	1,754	1,751
Deferred income taxes	(43,372)	8,534
Non-cash interest income	(1,194)	(1,112)
Other	(8)	(568)
Changes in assets and liabilities	10,193	7,941
Net cash from operating activities	101,150	81,877
Cash flows from investing activities:		
Capital expenditures	(122,759)	(176,111)
Proceeds from sale of properties and equipment	90	24
Net cash from investing activities	(122,669)	(176,087)
Cash flows from financing activities:		
Proceeds from sale of common stock, net of issuance costs	296,578	202,851
Proceeds from revolving credit facility	85,000	165,000
Repayment of revolving credit facility	(122,000)	(221,000)
Other	(364)	(1,213)
Net cash from financing activities	259,214	145,638
Net change in cash and cash equivalents	237,695	51,428
Cash and cash equivalents, beginning of period	850	16,066
Cash and cash equivalents, end of period	$238,545	$67,494
Supplemental cash flow information:		
Cash payments for:		
Interest, net of capitalized interest	$599	$569
Income taxes	—	8,088
Non-cash investing and financing activities:		
Change in accounts payable related to purchases of properties and equipment	$(23,544)	$(35,836)
Change in asset retirement obligation, with a corresponding change to crude oil and natural gas properties, net of disposals	404	302
Purchase of properties and equipment under capital leases	635	472

See accompanying Notes to Condensed Consolidated Financial Statements

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PDC ENERGY, INC.
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
March 31, 2015
(Unaudited)

NOTE 1 - NATURE OF OPERATIONS AND BASIS OF PRESENTATION

PDC Energy, Inc. (the "Company," "we," "us," or "our") is a domestic independent exploration and production company that produces, develops, acquires and explores for crude oil, natural gas and NGLs, with primary operations in the Wattenberg Field in Colorado and the Utica Shale in southeastern Ohio. Our operations in the Wattenberg Field are focused in the horizontal Niobrara and Codell plays and our Ohio operations are focused in the Utica Shale play. As of March 31, 2016, we owned an interest in approximately 3,000 gross wells. We are engaged in two business segments: Oil and Gas Exploration and Production and Gas Marketing.

The accompanying unaudited condensed consolidated financial statements include the accounts of PDC, our wholly-owned subsidiary Riley Natural Gas ("RNG") and our proportionate share of our four affiliated partnerships. Pursuant to the proportionate consolidation method, our accompanying condensed consolidated financial statements include our pro rata share of assets, liabilities, revenues and expenses of the entities which we proportionately consolidate. All material intercompany accounts and transactions have been eliminated in consolidation.

In our opinion, the accompanying condensed consolidated financial statements contain all adjustments (consisting of only normal recurring adjustments) necessary for a fair presentation of our financial statements for interim periods in accordance with accounting principles generally accepted in the United States of America ("U.S. GAAP") and with the instructions to Form 10-Q and Article 10 of Regulation S-X of the SEC. Accordingly, pursuant to such rules and regulations, certain notes and other financial information included in audited financial statements have been condensed or omitted. The December 31, 2015 condensed consolidated balance sheet data was derived from audited statements, but does not include disclosures required by U.S. GAAP. The information presented in this Quarterly Report on Form 10-Q should be read in conjunction with our audited consolidated financial statements and notes thereto included in our 2015 Form 10-K. Our results of operations and cash flows for the three months ended March 31, 2016 are not necessarily indicative of the results to be expected for the full year or any other future period.

NOTE 2 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Recently Issued Accounting Standards

In May 2014, the Financial Accounting Standards Board ("FASB") and the International Accounting Standards Board issued their converged standard on revenue recognition that provides a single, comprehensive model that entities will apply to determine the measurement of revenue and timing of when it is recognized. The underlying principle is that an entity will recognize revenue to depict the transfer of goods or services to customers at an amount that the entity expects to be entitled to in exchange for those goods or services. The standard outlines a five-step approach to apply the underlying principle: (1) identify the contract with the customer, (2) identify the separate performance obligations in the contract, (3) determine the transaction price, (4) allocate the transaction price to separate performance obligations and (5) recognize revenue when (or as) each performance obligation is satisfied. In March 2016, the FASB issued an update to the standard intended to improve the operability and understandability of the implementation guidance on principal versus agent considerations when recognizing revenue. The revenue standard is effective for annual reporting periods beginning after December 15, 2017, including interim periods within that reporting period. The revenue standard can be adopted under the full retrospective method or simplified transition method. Entities are permitted to adopt the revenue standard early, beginning with annual reporting periods after December 15, 2016. We are currently evaluating the impact these changes may have on our condensed consolidated financial statements.

In August 2014, the FASB issued a new standard related to the disclosure of uncertainties about an entity's ability to continue as a going concern. The new standard requires management to assess an entity's ability to continue as a going concern at the end of every reporting period and to provide related footnote disclosures in certain circumstances. The new standard will be effective for all entities in the first annual period ending after December 15, 2016, with early adoption permitted. We expect to adopt this standard in the fourth quarter of 2016. Adoption of this standard is not expected to have a significant impact on our condensed consolidated financial statements.

In February 2016, the FASB issued an accounting update aimed at increasing the transparency and comparability among organizations by recognizing lease assets and liabilities on the balance sheet and disclosing key information about related leasing arrangements. For leases with terms of more than twelve months, the accounting update requires lessees to recognize an asset for its right to use the underlying asset and a lease liability for the corresponding lease obligation. Both the lease asset and liability will initially be measured at the present value of the future minimum lease payments over the lease term. Subsequent measurement, including the presentation of expenses and cash flows, will depend upon the classification of the lease as either a finance or operating lease. The guidance is effective for fiscal years beginning after December 15, 2018, and interim periods within those years, with early adoption permitted, and is to be applied as of the beginning of the earliest period presented using a modified retrospective approach. We are currently evaluating the impact these changes may have on our condensed consolidated financial statements.

In March 2016, the FASB issued an accounting update on stock-based compensation intended to simplify several aspects of the accounting for employee share-based payment award transactions. Areas of simplification include income tax consequences, classification of the awards as either equity or liabilities and the classification on the statement of cash flows. The guidance is effective for fiscal years beginning after December 15, 2016, and interim periods within those years, with early adoption permitted. We are currently evaluating the impact these changes may have on our condensed consolidated financial statements.

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