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Rice Energy Inc.
Form 10-Q
November 12, 2014

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

FORM 10-Q

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

For the quarterly period ended September 30, 2014

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: 001-36273

Rice Energy Inc.

(Exact name of registrant as specified in its charter)

Delaware

46-3785773

(State or other jurisdiction of incorporation or organization)

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

400 Woodcliff Drive

15317

Canonsburg, Pennsylvania

(Address of principal executive offices)

(Zip code)

(724) 746-6720

(Registrant's telephone number, including area code)

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 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 small reporting company. See the definitions of "large accelerated filer", "accelerated filer" and "smaller reporting company" in Rule 12b-2 of the Exchange Act. (Check one):

Large accelerated filer

Accelerated filer

Non-accelerated filer

Smaller reporting company

(Do not check 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

Number of shares of the registrant's common stock outstanding at November 10, 2014: 136,280,766 shares

RICE ENERGY INC.
QUARTERLY REPORT ON FORM 10-Q
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Cautionary Statement Regarding Forward-Looking Statements

This Quarterly Report on Form 10-Q (the “Quarterly Report”) contains “forward-looking statements” within the meaning of Section 27A of the Securities Act and Section 21E of the Securities Exchange Act of 1934, as amended (the “Exchange Act”). All statements, other than statements of historical fact included in this Quarterly Report, regarding our strategy, future operations, financial position, estimated revenues and income/losses, projected costs, prospects, plans and objectives of management are forward-looking statements. When used in this Quarterly Report, the words “could,” “believe,” “anticipate,” “intend,” “estimate,” “expect,” “project” and similar expressions are intended to identify forward-looking statements, although not all forward-looking statements contain such identifying words. These forward-looking statements are based on our current expectations and assumptions about future events and are based on currently available information as to the outcome and timing of future events. When considering forward-looking statements, you should keep in mind the risk factors and other cautionary statements described under the heading “Item 1A. Risk Factors” in (i) our Annual Report on Form 10-K (the “2013 Annual Report”) for the year ended December 31, 2013 and (ii) our Quarterly Report (the “June 30, 2014 Quarterly Report”) for the quarter ended June 30, 2014, each on file with the Securities and Exchange Commission (the “SEC”), and in “Item 1A. Risk Factors” of this Quarterly Report. Forward-looking statements may include statements about our:

- business strategy;
- reserves;
- financial strategy, liquidity and capital required for our development program;
- realized natural gas, natural gas liquid (“NGL”) and oil prices;
- timing and amount of future production of natural gas, NGLs and oil;
- hedging strategy and results;
- future drilling plans;
- competition and government regulations;
- pending legal or environmental matters;
- marketing of natural gas, NGLs and oil;
- leasehold or business acquisitions;
- costs of developing our properties and conducting our gathering and other midstream operations;
- general economic conditions;
- credit markets;
- uncertainty regarding our future operating results; and
- plans, objectives, expectations and intentions contained in this Quarterly Report that are not historical.

We caution you that these forward-looking statements are subject to all of the risks and uncertainties, most of which are difficult to predict and many of which are beyond our control, incident to the exploration for and development, production, gathering and sale of natural gas, NGLs and oil. These risks include, but are not limited to: commodity price volatility; inflation; lack of availability of drilling and production equipment and services; environmental risks; drilling and other operating risks; regulatory changes; the uncertainty inherent in estimating natural gas reserves and in projecting future rates of production, cash flow and access to capital; the timing of development expenditures; and the other risks described under the heading “Item 1A. Risk Factors” in our 2013 Annual Report, our June 30, 2014 Quarterly Report and this Quarterly Report.

Reserve engineering is a process of estimating underground accumulations of natural gas, NGLs and oil that cannot be measured in an exact way. The accuracy of any reserve estimate depends on the quality of available data, the interpretation of such data and price and cost assumptions made by reserve engineers. In addition, the results of drilling, testing and production activities may justify revisions of estimates that were made previously. If significant, such revisions could change the schedule of any further production and development drilling. Accordingly, reserve estimates may differ significantly from the quantities of natural gas, and NGLs and oil that are ultimately recovered. Should one or more of the risks or uncertainties described in this Quarterly Report occur, or should underlying assumptions prove incorrect, our actual results and plans could differ materially from those expressed in any forward-looking statements.

All forward-looking statements, expressed or implied, included in this Quarterly Report are expressly qualified in their entirety by this cautionary statement. This cautionary statement should also be considered in connection with any subsequent written or oral forward-looking statements that we or persons acting on our behalf may issue.

Except as otherwise required by applicable law, we disclaim any duty to update any forward-looking statements, all of which are expressly qualified by the statements in this section, to reflect events or circumstances after the date of this Quarterly Report.

Commonly Used Defined Terms

As used in the Quarterly Report, unless the context indicates or otherwise requires, the following terms have the following meanings:

- “Rice Energy,” the “Company,” “we,” “our,” “us” or like terms refer collectively to Rice Energy Inc. and its consolidated subsidiaries, including Rice Drilling B LLC;
- “Rice Drilling B” refers to Rice Drilling B LLC, our wholly-owned subsidiary;
- “Rice Partners” refers to Rice Energy Family Holdings, LP (formerly known as Rice Energy Limited Partners), an entity affiliated with members of the Rice family;
- “Rice Holdings” refers to Rice Energy Holdings LLC;
- “Rice Appalachia” refers to Rice Energy Appalachia, LLC, the parent company of Rice Drilling B prior to our initial public offering;
- “Alpha Holdings” refers to Foundation PA Coal Company, LLC, a wholly owned indirect subsidiary of Alpha Natural Resources, Inc.;
- “Marcellus joint venture” refers collectively to Alpha Shale Resources, LP and its general partner, Alpha Shale Holdings, LLC;
- “Natural Gas Partners” refers to a family of private equity investment funds organized to make direct equity investments in the energy industry, including the funds invested in us; and
- “NGP Holdings” refers to NGP Rice Holdings, LLC.

PART I - FINANCIAL INFORMATION

Item 1. Financial Statements

Introduction to the Condensed Consolidated Financial Statements

The unaudited condensed consolidated financial statements have been prepared on the basis that Rice Energy Inc. is a corporation under the Internal Revenue Code subject to federal income tax. The unaudited condensed consolidated financial statements should be read in conjunction with the notes accompanying such unaudited condensed consolidated financial statements as well as “Item 2. Management’s Discussion and Analysis of Financial Condition and Results of Operations,” each included elsewhere in this Quarterly Report. Please see “—Notes to Condensed Consolidated Financial Statements (Unaudited)—5. Acquisitions” for further details on the purchase price allocations and resulting impact on the corresponding condensed consolidated balance sheet and for the related pro forma information.

The unaudited condensed consolidated financial statements as of and for the three and nine months ended September 30, 2014 reflect the following transactions:

Initial Public Offering

On January 29, 2014, we completed our initial public offering (“IPO”) of 50,000,000 shares of our \$0.01 par value common stock, which included 30,000,000 shares sold by us, 14,000,000 shares sold by NGP Holdings, the selling stockholder in our IPO, and 6,000,000 shares sold subject to an option granted to the underwriters by the selling stockholder.

The net proceeds of our IPO, based on the public offering price of \$21.00 per share, were approximately \$992.6 million, which resulted in net proceeds to us of \$593.6 million after deducting expenses and underwriting discounts and commissions of approximately \$36.4 million and the net proceeds to the selling stockholder of approximately \$399.0 million after deducting expenses and underwriting discounts of approximately \$21.0 million. We did not receive any proceeds from the sale of the shares by the selling stockholder. A portion of the net proceeds from our IPO were used to repay all outstanding borrowings under the revolving credit facility of our Marcellus joint venture, to make a \$100.0 million payment to Alpha Holdings in partial consideration for the Marcellus JV Buy-In (as defined below) and to repay all outstanding borrowings under our Senior Secured Revolving Credit Facility (as defined below). We used the remainder of the net proceeds from our IPO to fund a portion of our capital expenditure plan.

Corporate Reorganization

A corporate reorganization occurred concurrently with the completion of our IPO on January 29, 2014. As a part of this corporate reorganization, we acquired all of the outstanding membership interests in Rice Appalachia and Rice Drilling B (other than those already held by Rice Appalachia) in exchange for shares of our common stock. Our business continues to be conducted through Rice Drilling B, now a wholly owned subsidiary. This reorganization constituted a common control transaction and the accompanying consolidated financial statements are presented as though this reorganization had occurred for the earliest period presented.

As of January 29, 2014, upon (a) the completion of the IPO, (b) the issuance of (i) 43,452,550 shares of common stock to NGP Holdings, (ii) 20,300,923 shares of common stock to Rice Holdings, (iii) 2,356,844 shares of common stock to Daniel J. Rice III, (iv) 20,000,000 shares of common stock to Rice Partners, (v) 160,831 shares of common stock to the persons holding incentive units representing interests in Rice Appalachia and (vi) 1,728,852 shares of common stock to the members of Rice Drilling B (other than Rice Appalachia), each of which were issued by us in connection with the closing of the IPO, and (c) the issuance of 9,523,810 shares of common stock to Alpha Holdings in connection with the completion of the Marcellus JV Buy-In, we had 127,523,810 shares of common stock outstanding.

Compensation Charge in Connection with the Reorganization

Rice Appalachia, as the parent company of Rice Drilling B, historically granted incentive units to certain members of management and other employees. The incentive units provided the holder with a performance bonus for fair value accretion of Rice Appalachia equity.

In connection with the IPO and the related corporate reorganization, the holders of incentive units in Rice Appalachia contributed their Rice Appalachia incentive units (except for those incentive units related to the incentive burden attributable to Mr. Daniel J. Rice III, which we acquired from the holder of such incentive units in exchange for the issuance of 160,831 shares of our common stock as described above) to Rice Holdings and NGP Holdings in return

for substantially similar incentive units in such entities. In the first quarter of 2014, certain incentive units granted by NGP Holdings to certain employees triggered the pre-determined payout criteria, resulting in a cash payment by NGP Holdings of \$4.4 million. No payments were made in respect of incentive units prior to the completion of the IPO. The exchange of incentive units and cash payment collectively resulted in non-cash compensation expense of \$7.8 million being recorded in the first quarter of 2014 by the Company. As a result of the IPO, the payment likelihood related to the incentive units was deemed probable, requiring the Company to recognize expense.

During the nine months ended September 30, 2014, we recognized approximately \$101.7 million of compensation expense relative to these incentive units. We expect to recognize approximately \$79.8 million of additional compensation expense over the remaining expected service periods related to the Rice Holdings interests. The NGP Holdings interests are considered a liability-based award and will be adjusted on a quarterly basis until all payments have been made. As of September 30, 2014, the unrecognized compensation expense related to the NGP Holdings units is approximately \$77.3 million, which will be recognized over the remaining expected service period. The compensation expense related to these interests is treated as additional paid in capital from Rice Holdings and NGP Holdings in our financial statements and is not deductible for federal or state income tax purposes. The compensation expense recognized is a non-cash charge, with the settlement obligation resting on NGP Holdings and Rice Holdings, and as such are not dilutive to Rice Energy Inc. As of September 30, 2014, approximately \$19.8 million had been paid on the incentive units.

In August 2014, the triggering event for the Rice Holdings incentive units was achieved. As a result, in August of 2015, 2016 and 2017, Rice Holdings will distribute one third, one half and all, respectively, of its then-remaining assets (consisting solely of shares of our common stock) to its members pursuant to the terms of its limited liability company agreement. As a result, over time, the shares of our common stock held by Rice Holdings will be transferred in their entirety to Rice Partners (or its successors) and the incentive unitholders.

Marcellus JV Buy-In

On January 29, 2014, in connection with the closing of the IPO and pursuant to the Transaction Agreement between us and Alpha Holdings dated as of December 6, 2013, we completed our acquisition of Alpha Holdings' 50% interest in our Marcellus joint venture in exchange for total consideration of \$322.0 million, consisting of \$100.0 million of cash and our issuance to Alpha Holdings of 9,523,810 shares of our common stock (the "Marcellus JV Buy-In"). This transaction resulted in a non-recurring gain of \$203.6 million in the first quarter of 2014 due to the remeasurement of our previously recorded equity investment at fair value.

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Rice Energy Inc.

Condensed Consolidated Balance Sheets

(Unaudited)

(in thousands)

	September 30, 2014	December 31, 2013
Assets		
Current assets:		
Cash	\$131,978	\$31,612
Restricted cash	—	8,268
Accounts receivable	136,560	31,765
Receivable from affiliate	222	2,244
Deposits	760	601
Prepaid expenses and other	2,374	262
Derivative assets	8,546	—
Total current assets	280,440	74,752
Investments in joint ventures	—	49,814
Gas collateral account	3,995	3,700
Proved natural gas properties, net	1,023,603	270,523
Unproved natural gas properties	1,158,483	457,836
Property and equipment, net	13,637	5,972
Deferred financing costs, net	20,452	12,292
Goodwill	338,036	—
Intangible assets, net	48,199	—
Other non-current assets	386	—
Derivative assets	8,555	4,921
Total assets	\$2,895,786	\$879,810
Liabilities and stockholders' equity		
Current liabilities:		
Current portion of long-term debt	\$1,006	\$20,120
Accounts payable	95,218	51,219
Royalties payable	28,906	9,393
Accrued interest	24,219	250
Accrued capital expenditures	176,087	16,753
Other accrued liabilities	19,378	8,283
Leasehold payable	24,940	18,606
Derivative liability	—	965
Payable to affiliate	—	6,148
Operated prepayment liability	1,886	1,201
Total current liabilities	371,640	132,938
Long-term liabilities:		
Long-term debt	900,000	406,822
Leasehold payable	3,330	1,675
Deferred tax liabilities	199,040	—
Restricted units	—	36,306
Other long-term liabilities	9,218	3,422
Total liabilities	1,483,228	581,163
Stockholders' equity	1,412,558	298,647

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Total liabilities and stockholders' equity	\$2,895,786	\$879,810
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The accompanying notes are an integral part of these Condensed Consolidated Financial Statements.

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Rice Energy Inc.
Condensed Consolidated Statements of Operations
(Unaudited)