ABRAXAS PETROLEUM CORP
Form 10-K
March 15, 2019

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UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

**FORM 10-K**

(Mark One)

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

For the Fiscal Year Ended December 31, 2018

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

Commission File Number 001-16071

**ABRAXAS PETROLEUM CORPORATION**

(Exact name of Registrant as specified in its charter)

| | |
|---|---|
| **Nevada** | **74-2584033** |
| (State or Other Jurisdiction of Incorporation or Organization) | (I.R.S. Employer Identification Number) |

**18803 Meisner Drive**

**San Antonio, TX 78258**

(Address of principal executive offices)

**(210) 490-4788**

Registrant's telephone number, including area code

SECURITIES REGISTERED PURSUANT TO SECTION 12(b) OF THE ACT:

| **Title of each class:** | **Name of each exchange on which registered:** |
|---|---|
| Common Stock, par value $.01 per share | The NASDAQ Stock Market, LLC |

SECURITIES REGISTERED PURSUANT TO SECTION 12(g) OF THE ACT:

**None**

Indicate by check mark if the registrant is a well-known seasoned issuer as defined in Rule 405 of the Securities Act. Yes No

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Exchange Act.

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 if 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 if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K.

Yes No

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Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, or a non-accelerated filer or a smaller reporting company. See definition 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 | (Do not check if a smaller reporting company) | Smaller reporting company |
| | | Emerging Growth Company |

If an emerging growth company, indicate by check mark if the registrant has elected not to use the extended transition period for complying with any new or revised financial accounting standards provided pursuant to Section 13(a) of the Exchange Act.

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

As of June 30, 2018, the last day of the registrant's most recently completed second fiscal quarter, the aggregate market value of the common stock held by non-affiliates of the registrant was $470,774,656 based on the closing sale price as reported on The NASDAQ Stock Market.

As of March 8, 2019, there were 166,934,860 shares of common stock outstanding.

Documents Incorporated by Reference:

| Document | Parts Into Which Incorporated |
|---|---|
| Portions of the registrant's Proxy Statement relating to the 2019 Annual Meeting of Stockholders to be held on May 7, 2019. | Part III |

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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 “Business,” “Properties,” “Risk Factors” and “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;
- the availability of capital including under our credit facility;
- our success in development, exploitation and exploration activities;
- declines in our production of oil and gas;
- our indebtedness and the significant amount of cash required to service our indebtedness,
- the proximity, capacity, cost and availability of pipelines and other transportation facilities,
- limits on our growth and our ability to finance our operations, fund our capital needs and respond to changing conditions imposed by our credit facility and restrictive debt covenants;
- our ability to make planned capital expenditures;
- ceiling test write-downs resulting, and that could result in the future, from lower oil and gas prices;
- political and economic conditions in oil producing countries, especially those in the Middle East;
- price and availability of alternative fuels;
- our ability to procure services and equipment for our drilling and completion activities;

- our acquisition and divestiture activities;
- weather conditions and events; and
- other factors discussed elsewhere in this report.

Initial production, or IP, rates, for both our wells and for those wells that are located near our properties, are limited data points in each well's productive history. These rates are sometimes actual rates and sometimes extrapolated or normalized rates. As such, the rates for a particular well may change as additional data becomes available. Peak production rates are not necessarily indicative or predictive of future production rates, expected ultimate recovery, or EUR, or economic rates of return from such wells and should not be relied upon for such purposes. Equally, the way we calculate and report peak IP rates and the methodologies employed by others may not be consistent, and thus the values reported may not be directly and meaningfully comparable. Lateral lengths described are indicative only. Actual completed lateral lengths depend on various considerations such as lease-line offsets. Abraxas standard length laterals, sometimes referred to as 5,000 foot laterals, are laterals with completed length generally between 4,000 feet and 5,500 feet. Mid-length laterals, sometimes referred to as 7,500 foot laterals, are laterals with completed length generally between 6,500 feet and 8,000 feet. Long laterals, sometimes referred to as 10,000 foot laterals, are laterals with completed length generally longer than 8,000 feet.

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**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.

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.

“***Boepd*****"** - barrels of oil equivalents per day.

“***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.

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"***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:**

"***Developed oil and gas reserves****" Developed oil and gas reserves are reserves of any category that can be expected to be recovered:

(i) Through existing wells with existing equipment and operating methods or in which the cost of the required equipment is relatively minor compared to the cost of a new well; and

(ii) Through installed extraction equipment and infrastructure operational at the time of the reserves estimate if the extraction is by means not involving a well.

***"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 developed reserves***"* Reserves that can be expected to be recovered through existing wells with existing equipment and operating methods.

"***Proved reserves****" Reserves that geological and engineering data demonstrate with reasonable certainty to be recoverable in future years from known reservoirs under existing economic and operating conditions.

***"Proved undeveloped reserves"*** *or* ***"PUDs*"*** Reserves that are expected to be recovered from new wells on undrilled acreage or from existing wells, in each case where a relatively major expenditure is required.

"***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"). PV-10 is considered a non-GAAP financial measure under SEC regulations because it does not include the effects of future income taxes, as is required in computing the standardized measure of discounted future net cash flows. We believe that PV-10 is an important measure that can be used to evaluate the relative significance of our oil and gas properties and that PV-10 is widely used by securities analysts and investors when evaluating oil and gas companies. Because many factors that are unique to each individual company impact the amount of future income taxes to be paid, the use of a pre-tax measure provides greater comparability of assets when evaluating companies. We believe that most other companies in the oil and gas industry calculate PV-10 on the same basis. PV-10 is computed on the same basis as the standardized measure of discounted future net cash flows but without deducting income taxes.

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"***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."

***"Undeveloped oil and gas reserves***"*" Undeveloped oil and gas reserves are reserves of any category that are expected to be recovered from new wells on undrilled acreage, or from existing wells where a relatively major expenditure is required for recompletion.

* This definition is an abbreviated version of the complete definition set forth in Rule 4-10(a) of Regulation S-X. For the complete definition, see: http://www.ecfr.gov/cgi-bin/retrieveECFR?gp=1&SID=7aa25d3cede06103c0ecec861362497d&ty=HTML&h=L&n=pt17.3.21

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**Part I**

*Information contained in this report represents the consolidated operations of Abraxas Petroleum Corporation. The terms “Abraxas,” “we,” “us,” “our,” or the “Company,” refer to Abraxas Petroleum Corporation, together with its consolidated subsidiaries including Raven Drilling, LLC which is a wholly owned subsidiary that owns a drilling rig. Unless otherwise noted, all disclosures are for Continuing Operations.*

## Item 1. Business

### General

We are an independent energy company primarily engaged in the acquisition, exploration, development and production of oil and gas. At December 31, 2018, our estimated net proved reserves were 67.2 MMBoe, of which 37% were classified as proved developed, 63% were oil and 96% of which (on a Boe basis) were operated by us. Our daily net production for the year ended December 31, 2018 was 9,809 Boepd, of which 64% was oil. Abraxas Petroleum Corporation was incorporated in Nevada in 1990. Our address is 18803 Meisner Drive, San Antonio, Texas 78258 and our phone number is (210) 490-4788.

Our oil and gas assets are located in three operating regions, the Permian/Delaware Basin, the Rocky Mountain, and South Texas. The following table sets forth certain information related to our properties as of and for the year ended December 31, 2018:

| | | | | Estimated Net Proved Reserves | | Net Production | |
|---|---|---|---|---|---|---|---|
| | Gross Producing Wells | Average Working Interest | Total Net Acres | (Mboe) | % Oil | (Mboe) | % Oil |
| Permian/Delaware Basin | 115 | 74.44 % | 23,617 | 41,058 | 61 % | 1,328 | 64 % |
| Rocky Mountain | 539 | 13.80 % | 20,616 | 24,331 | 68 % | 2,040 | 66 % |
| South Texas | 24 | 96.88 % | 12,959 | 1,839 | 27 % | 212 | 57 % |
| Total United States | 678 | 28.08 % | 57,192 | 67,228 | 63 % | 3,580 | 58 % |

Our properties in the Permian/Delaware Basin region are primarily located in Ward and Winkler Counties, Texas and produce oil and gas primarily from the Bone Spring and Wolfcamp formations.

Our properties in the Rocky Mountain region are primarily located in the Williston Basin of North Dakota and Montana.  In this region, our wells produce oil and gas from various reservoirs, primarily the Bakken, Three Forks and Red River formations.

Our properties in the South Texas region are located along the Edwards trend in DeWitt and Lavaca Counties, Texas and the Eagle Ford shale and the Austin Chalk in Atascosa County, Texas.  In the Edwards trend, our wells produce gas from the Edwards formation.

**Strategy**

Our business strategy is to focus our capital and resources on our core operated basins, improve financial flexibility and profitably grow production and reserves.  Key elements of our business strategy include:

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*Focus our capital and resources on our core operated basins.* Our core basins consist of the Permian/Delaware Basin (Bone Spring and Wolfcamp) and Williston Basin (Bakken and Three Forks). Given the disparity which has existed during the past several years and which continues currently between oil and gas prices, the economics of drilling oil wells is far superior to drilling gas wells. We anticipate making capital expenditures in 2019 of approximately $94.5 million, of which approximately $46.2 million is allocated to acquiring additional acreage and developing our Bone Spring/Wolfcamp properties in the Permian/Delaware Basin. The 2019 budget also allocates approximately $38.3 million for developing our Williston Basin/Bakken/Three Forks play in North Dakota, with the remaining amount allocated to acquisitions, facilities and general corporate purposes. As part of our efforts to focus our property portfolio, we also seek to sell assets we have deemed non-core. These include assets with a low working interest that are non-operated and/or that fall outside of our three core basins. Any proceeds from these asset sales have been and will continue to be used to reduce our indebtedness and/or be redeployed into our core operating basins. We are currently actively working to monetize our remaining Eagle Ford assets in South Texas.

*Improve financial flexibility*. Our primary sources of capital are availability under our credit facility and cash flows from operations. Availability under our credit facility is subject to a borrowing base which is determined semi-annually by our lenders. The next redetermination is scheduled for April 2019. As of December 31, 2018, we had $180.0 million outstanding on our credit facility and availability of $20.0 million, and we generated approximately $80.0 million of cash flows from operations.

We have also sold producing properties from time to time in order to provide us with financial flexibility. In December 2018 and January 2019, we sold various Eagle Ford assets in our South Texas region for approximately $1.6 million and are currently marketing our remaining Eagle Ford assets. In January 2019, we announced that we had engaged Petrie Partners to assist us in identifying and assessing our options for our Bakken properties. We are still early in this process and do not know the ultimate outcome. In the event that this process were to result in the sale of our Bakken properties, we believe that the proceeds would be used to significantly pay down or fully retire our debt, support our Raven No. 1 rig in the Delaware Basin until it achieves free cash flow and possibly buy back stock.

We seek to reduce the volatility of our cash flows from operations by hedging a portion of our production. As of December 31, 2018, we had NYMEX-based fixed price commodity swap arrangements, on approximately 51% of the oil production from our estimated net proved developed producing reserves (as of December 31, 2018) through December 31, 2019, 62% for 2020 and 66% for 2021. Subsequent to December 31, 2018, in connection with the redetermination of our credit facility, we have entered into additional fixed price commodity swaps. Taking these additional contracts into consideration, we have entered into fixed price commodity swap arrangements on approximately 61% of the oil production of our estimated net proved developed producing reserves (as of December 31, 2018) through December 31, 2019, 80% for 2020 and 75% for 2021.

During 2018, we had originally established a capital budget of $140.0 million. Capital spending for 2018 was $174.0 million. We exceeded our 2018 capital budget as a result of successfully acquiring more acreage in the Delaware Basin than we had originally budgeted which resulted in increased spending for acquisitions as well as for drilling and completing wells in this area as a result of our higher ownership interests.

We intend to maintain our liquidity and our balance sheet during 2019 by adjusting our capital budget as necessary, seeking to reduce expenses and by funding our capital budget primarily with cash flow from operations.

*Profitably grow production and reserves*. We have a substantial low-decline legacy production base as evidenced by our approximate 21-year average reserve life as of year-end 2018. Our capital is currently being deployed largely into unconventional oil assets with relatively predictable production profiles, yet steep initial decline rates. Therefore, the economics of these oil wells are highly dependent on both near term commodity prices and strong operational cost control. Cost savings achieved through efficiencies of using our own rig in the Williston Basin, and heightened focus on cost control in all of our operated positions both contribute to our historical success in adding low cost barrels to our production base.

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**2019 Budget and Drilling Activities**

Our capital expenditure budget for 2019 is approximately $94.5 million of which approximately $46.2 million is allocated to acquiring additional acreage and developing the Company's Bone Spring/Wolfcamp acreage in the Permian/Delaware Basin. The budget also allocates approximately $38.3 million to developing our Williston Basin Bakken/Three Forks play in North Dakota, with the remaining amount allocated to acquisitions, facilities and general corporate purposes. The 2019 capital expenditure budget is subject to change depending upon a number of factors, including the availability of sufficient capital resources including under our credit facility, the availability and costs of drilling and service equipment and crews, economic and industry conditions at the time of drilling, prevailing and anticipated prices for oil and gas, the results of our exploitation efforts, our financial results and our ability to obtain permits for drilling locations.

**Markets and Customers**

The revenue generated by our operations is highly dependent upon the prices we receive for our oil and gas. Historically, the markets for oil and gas have been volatile and are likely to continue to be volatile in the future. The prices we receive for our oil and gas production are subject to wide fluctuations and depend on numerous factors beyond our control including seasonality, the condition of the world wide economy (particularly the manufacturing sector), foreign imports, political conditions in other petroleum producing countries, the actions of the Organization of Petroleum Exporting Countries, domestic regulation, legislation and policies. Decreases in the prices we receive for our oil and gas have had, and could have in the future, an adverse effect on the carrying value of our proved reserves, our revenue, profitability and cash flow from operations. Refer to "Risk Factors – Risks Related to Our Industry — Market conditions for oil and gas and particularly volatility of prices for oil and gas, could adversely affect our revenue, cash flows from operations, profitability and growth" and "Management's Discussion and Analysis of Financial Condition and Results of Operations – Critical Accounting Policies" for more information relating to the effects that decreases in oil and gas prices have on us. To help mitigate the impact of commodity price volatility, we hedge a portion of our production through the use of fixed price swaps and basis differential swap contracts. See "Management's Discussion and Analysis of Financial Condition and Results of Operations – General – Commodity Prices and Hedging Arrangements" and Note 11 of the notes to our consolidated financial statements for more information regarding our derivative activities.

Substantially all of our oil and gas is sold at current market prices under short-term arrangements, as is customary in the industry. During the year ended December 31, 2018, two purchasers of production accounted for approximately 57% of our oil and gas sales. During the year ended December 31, 2017, three purchasers of production accounted for approximately 69% of our oil and gas sales and in 2016, two purchasers accounted for approximately 71% of our oil and gas sales. We believe that there are numerous other purchasers available to buy our oil and gas and that the loss of any of these purchasers would not materially affect our ability to sell our oil and gas. Furthermore, the largest purchasers of our oil and gas have changed from year to year from 2016 to 2018.

**Regulation of Oil and Gas Activities**

The exploration, production and transportation of all types of hydrocarbons are subject to significant governmental regulations. Our properties are affected from time to time in varying degrees by political developments and federal, state and local laws and regulations. In particular, oil and gas production operations and economics are, or in the past have been, affected by industry specific price controls, taxes, conservation, safety, environmental and other laws relating to the petroleum industry, and by changes in such laws and by periodically changing administrative regulations.

Federal, state and local laws and regulations govern oil and gas activities. Operators of oil and gas properties are required to have a number of permits in order to operate such properties, including operator permits and permits to dispose of salt water. In addition, under federal law, operators of oil and gas properties are required to possess certain certificates and permits in order to operate such properties. We possess all material requisite permits required by Federal,  state and other local authorities in which we operate properties.

***De***