Sanchez Energy Corp
Form 10-Q
November 10, 2014

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UNITED STATES
SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

Form 10-Q

ý **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

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

Commission file number: 1-35372

Sanchez Energy Corporation

(Exact name of registrant as specified in its charter)

Delaware (State or other jurisdiction of incorporation or organization)	**45-3090102** (I.R.S. Employer Identification No.)
1111 Bagby Street, Suite 1800 **Houston, Texas** (Address of principal executive offices)	**77002** (Zip Code)

(713) 783-8000
(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 ý No o

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

Large accelerated filer o	Accelerated filer ý	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 ý

Number of shares of registrant's common stock, par value $0.01 per share, outstanding as of November 5, 2014: 58,597,837.

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We were previously considered an "emerging growth company" as defined under the Jumpstart Our Business Startups Act of 2012, commonly referred to as the "JOBS Act." The JOBS Act permits a company to be classified as an "emerging growth company" for up to five years from the date of the completion of its initial public offering or until the earlier of (1) the last day of the fiscal year in which its total annual gross revenues exceed $1 billion, (2) the date that it becomes a "large accelerated filer" as defined in Rule 12b-2 under the Securities Exchange Act of 1934, as amended (the "Exchange Act"), which would occur if the market value of its common equity that is held by non-affiliates is $700 million or more as of the last business day of its most recently completed second fiscal quarter or (3) the date on which it has issued more than $1 billion in non-convertible debt during the preceding three year period. However, during the second quarter of 2014, the Company issued non-convertible debt such that we have now issued more than $1 billion in non-convertible debt during the preceding three year period. As such, we are no longer considered an "emerging growth company" under the JOBS Act.

Further, as of June 30, 2014, the market value of our common equity held by non-affiliates was greater than $700 million. As such, the Company will become a large accelerated filer as defined in Rule 12b-2 under the Exchange Act on December 31, 2014.

CAUTIONARY NOTE REGARDING FORWARD-LOOKING STATEMENTS

This Quarterly Report on Form 10-Q contains "forward-looking statements" within the meaning of the safe harbor provisions of the Private Securities Litigation Reform Act of 1995. All statements, other than statements of historical facts, included in this Quarterly Report on Form 10-Q that address activities, events or developments that we expect, believe or anticipate will or may occur in the future are forward-looking statements. These statements are based on certain assumptions we made based on management's experience, perception of historical trends and technical analyses, current conditions, anticipated future developments and other factors believed to be appropriate and reasonable by management. When used in this Quarterly Report on Form 10-Q, words such as "will," "potential," "believe," "estimate," "intend," "expect," "may," "should," "anticipate," "could," "plan," "predict," "project," "profile," "model," "strategy," "future" or their negatives or the statements that include these words or other words that convey the uncertainty of future events or outcomes, are intended to identify forward-looking statements, although not all forward-looking statements contain such identifying words. In particular, statements, express or implied, concerning our future operating results and returns or our ability to replace or increase reserves, increase production, or generate income or cash flows are forward-looking statements. Forward-looking statements are not guarantees of performance. Such statements are subject to a number of assumptions, risks and uncertainties, many of which are beyond our control. Although we believe that the expectations reflected in our forward-looking statements are reasonable and are based on reasonable assumptions, no assurance can be given that these assumptions are accurate or that any of these expectations will be achieved (in full or at all) or will prove to have been correct. Important factors that could cause our actual results to differ materially from the expectations reflected in the forward-looking statements include, among others:

- our ability to successfully execute our business and financial strategies;
- our ability to replace the reserves we produce through drilling and property acquisitions;
- the realized benefits of the acreage acquired in our various acquisitions and other assets and liabilities assumed in connection therewith;
- the extent to which our drilling plans are successful in economically developing our acreage in, and to produce reserves and achieve anticipated production levels from, our existing and future projects;

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the accuracy of reserve estimates, which by their nature involve the exercise of professional judgment and may therefore be imprecise;

the extent to which we can optimize reserve recovery and economically develop our plays utilizing horizontal and vertical drilling, advanced completion technologies and hydraulic fracturing;

our ability to successfully execute our hedging strategy and the resulting realized prices therefrom;

competition in the oil and natural gas exploration and production industry for employees and other personnel, equipment, materials and services and, related thereto, the availability and cost of employees and other personnel, equipment, materials and services;

our ability to access the credit and capital markets to obtain financing on terms we deem acceptable, if at all, and to otherwise satisfy our capital expenditure requirements;

the availability, proximity and capacity of, and costs associated with, gathering, processing, compression and transportation facilities;

the timing and extent of changes in prices for, and demand for, crude oil and condensate, natural gas liquids ("NGLs"), natural gas and related commodities;

our ability to compete with other companies in the oil and natural gas industry;

the impact of, and changes in, government policies, laws and regulations, including tax laws and regulations, environmental laws and regulations relating to air emissions, waste disposal, hydraulic fracturing and access to and use of water, laws and regulations imposing conditions and restrictions on drilling and completion operations and laws and regulations with respect to derivatives and hedging activities;

developments in oil-producing and natural gas-producing countries;

our ability to effectively integrate acquired crude oil and natural gas properties into our operations, fully identify existing and potential problems with respect to such properties and accurately estimate reserves, production and costs with respect to such properties;

the extent to which our crude oil and natural gas properties operated by others are operated successfully and economically;

the use of competing energy sources and the development of alternative energy sources;

unexpected results of litigation filed against us;

the extent to which we incur uninsured losses and liabilities or losses and liabilities in excess of our insurance coverage; and the other factors described under "Part I, Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations," "Part II, Item 1A. Risk Factors" and elsewhere in this Quarterly Report on Form 10-Q and in our other public filings with the Securities and Exchange Commission (the "SEC").

In light of these risks, uncertainties and assumptions, the events anticipated by our forward-looking statements may not occur, and, if any of such events do, we may not have correctly anticipated the timing of their occurrence or the extent of their impact on our actual results. Accordingly, you should not place any undue reliance on any of our forward-looking statements. Any forward-looking statement speaks only as of the date on which such statement is made, and we undertake no obligation to correct or update any forward-looking statement, whether as a result of new information, future events or otherwise, except as required by applicable law.

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Form 10-Q
For the Quarterly Period Ended September 30, 2014

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PART I FINANCIAL INFORMATION

Item 1. Unaudited Financial Statements

Sanchez Energy Corporation

Condensed Consolidated Balance Sheets (Unaudited)

(in thousands, except share amounts)

	September 30, 2014	December 31, 2013
ASSETS		
Current assets:		
Cash and cash equivalents	$ 596,272	$ 153,531
Oil and natural gas receivables	93,865	51,960
Joint interest billings receivables	16,855	5,803
Fair value of derivative instruments	9,748	
Deferred tax asset	4,717	6,882
Other current assets	12,103	1,386
Total current assets	733,560	219,562
Oil and natural gas properties, at cost, using the full cost method:		
Unproved oil and natural gas properties	378,323	244,570
Proved oil and natural gas properties	2,305,583	1,297,961
Total oil and natural gas properties	2,683,906	1,542,531
Less: Accumulated depreciation, depletion, amortization and impairment	(381,007)	(157,043)
Total oil and natural gas properties, net	2,302,899	1,385,488
Other assets:		
Debt issuance costs, net	50,003	19,806
Fair value of derivative instruments	3,075	1,304
Other assets	14,813	2,993
Total assets	$ 3,104,350	$ 1,629,153
LIABILITIES AND STOCKHOLDERS' EQUITY		
Current liabilities:		
Accounts payable	$ 17,306	$ 46,900
Accounts payable related entities	1,218	961
Other payables	4,708	2,963

Accrued liabilities		196,108		102,455
Deferred premium liability		4,017		717
Fair value of derivative instruments		38		4,623
Total current liabilities		223,395		158,619
Long term debt, net of premium (discount)		1,746,162		593,258
Asset retirement obligations		24,048		4,130
Deferred tax liability		30,649		10,868
Deferred premium liability		1,233		4,891
Fair value of derivative instruments		131		78
Total liabilities		2,025,618		771,844
Commitments and Contingencies (Note 15)				
Stockholders' equity:				
Preferred stock ($0.01 par value, 15,000,000 shares authorized; 1,838,985 and 3,000,000 shares issued and outstanding as of September 30, 2014 and December 31, 2013 of 4.875% Convertible Perpetual Preferred Stock, Series A, respectively; 3,532,330 and 4,500,000 shares issued and outstanding as of September 30, 2014 and December 31, 2013 of 6.500% Convertible Perpetual Preferred Stock, Series B, respectively)		53		75
Common stock ($0.01 par value, 150,000,000 shares authorized; 58,560,817 and 46,368,713 shares issued and outstanding as of September 30, 2014 and December 31, 2013, respectively)		586		464
Additional paid-in capital		1,077,712		867,108
Retained earnings (Accumulated deficit)		381		(10,338)
Total stockholders' equity		1,078,732		857,309
Total liabilities and stockholders' equity	$	3,104,350	$	1,629,153

The accompanying notes are an integral part of these condensed consolidated financial statements.

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Sanchez Energy Corporation

Condensed Consolidated Statements of Operations (Unaudited)

(in thousands, except per share amounts)

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2014	**2013**	**2014**	**2013**
REVENUES:				
Oil sales	$ 157,907	$ 87,436	$ 414,484	$ 171,635
Natural gas liquid sales	27,309	3,190	43,918	6,166
Natural gas sales	22,134	3,574	35,171	6,520
Total revenues	207,350	94,200	493,573	184,321
OPERATING COSTS AND EXPENSES:				
Oil and natural gas production expenses	34,380	11,026	64,203	21,098
Production and ad valorem taxes	10,916	5,531	29,161	10,942
Depreciation, depletion, amortization and accretion	93,463	38,372	225,297	76,368
General and administrative (inclusive of stock-based compensation expense of $10 and $6,657, respectively, for the three months ended September 30, 2014 and 2013, and $25,888 and $14,369, respectively, for the nine months ended September 30, 2014 and 2013)	12,821	15,195	60,999	35,564
Total operating costs and expenses	151,580	70,124	379,660	143,972
Operating income	55,770	24,076	113,913	40,349
Other income (expense):				
Interest and other income	82	32	97	104
Interest expense	(27,612)	(9,460)	(58,145)	(17,613)
Net gains (losses) on commodity derivatives	47,416	(14,436)	6,399	(13,812)
Total other income (expense)	19,886	(23,864)	(51,649)	(31,321)
Income before income taxes	75,656	212	62,264	9,028
Income tax expense (benefit)	26,625	(3,668)	21,946	(3,668)
Net income	49,031	3,880	40,318	12,696
Less:				
Preferred stock dividends	(4,274)	(5,485)	(29,599)	(13,041)
Net income allocable to participating securities	(2,068)		(495)	

Net income (loss) attributable to common stockholders	$	42,689	$	(1,605)	$	10,224	$	(345)
Net income (loss) per common share basic	$	0.77	$	(0.05)	$	0.20	$	(0.01)
Weighted average number of shares used to calculate net income (loss) attributable to common stockholders basic		55,732		34,737		51,153		33,651
Net income (loss) per common share diluted	$	0.69	$	(0.05)	$	0.20	$	(0.01)
Weighted average number of shares used to calculate net income (loss) attributable to common stockholders diluted		68,340		34,737		51,153		33,651

The accompanying notes are an integral part of these condensed consolidated financial statements.

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Sanchez Energy Corporation

Condensed Consolidated Statement of Stockholders' Equity for the Nine Months Ended September 30, 2014

(Unaudited)

(in thousands)

	Series A Preferred Stock		Series B Preferred Stock		Common Stock		Additional Paid-in Capital	Retained Earnings (Accumulated Deficit)	Total Stockholders' Equity
	Shares	Amount	Shares	Amount	Shares	Amount			
BALANCE, December 31, 2013	3,000	$ 30	4,500	$ 45	46,369	$ 464	$ 867,108	$ (10,338)	$ 857,309
Common shares issued					5,000	50	167,469		167,519
Preferred stock dividends								(12,302)	(12,302)
Restricted stock awards, net of forfeitures					1,653	17	(17)		
Exchange of preferred stock for common stock	(1,161)	(12)	(968)	(10)	5,539	55	17,264	(17,297)	
Stock-based compensation							25,888		25,888
Net income								40,318	40,318
BALANCE, September 30, 2014	1,839	$ 18	3,532	$ 35	58,561	$ 586	$ 1,077,712	$ 381	$ 1,078,732

The accompanying notes are an integral part of these condensed consolidated financial statements.

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Sanchez Energy Corporation

Condensed Consolidated Statements of Cash Flows (Unaudited)

(in thousands)

	Nine Months Ended September 30, 2014	Nine Months Ended September 30, 2013
CASH FLOWS FROM OPERATING ACTIVITIES:		
Net income	$ 40,318	$ 12,696
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation, depletion, amortization and accretion	225,297	76,368
Stock-based compensation expense	25,888	14,369
Net (gains) losses on commodity derivative contracts	(6,399)	13,812
Net cash settlement paid on commodity derivative contracts	(9,652)	(3,083)
Premiums paid on derivative contracts	(241)	(528)
Amortization of debt issuance costs	7,215	5,830
Accretion of debt discount (premium)	654	32
Deferred taxes	21,946	(3,668)
Changes in operating assets and liabilities:		
Accounts receivable	(52,957)	(29,903)
Other current assets	(10,734)	(301)
Accounts payable	(29,594)	8,427
Accounts payable related entities	257	(12,672)
Other payables	1,818	932
Accrued liabilities	58,864	26,413
Net cash provided by operating activities	272,680	108,724
CASH FLOWS FROM INVESTING ACTIVITIES:		
Payments for oil and natural gas properties	(532,300)	(295,670)
Payments for other property and equipment	(9,581)	(1,665)
Acquisitions of oil and natural gas properties	(558,113)	(402,669)
Purchases of investments		(10,000)
Sale of investments		11,591
Net cash used in investing activities	(1,099,994)	(698,413)
CASH FLOWS FROM FINANCING ACTIVITIES:		
Proceeds from borrowings	100,000	236,000
Repayment of borrowings	(100,000)	(236,000)
Issuance of senior notes, net of premium (discount)	1,152,250	593,000
Issuance of common stock	176,250	253,920
Issuance of preferred stock		225,000
Payments for offering costs	(8,731)	(20,861)
Financing costs	(37,412)	(23,104)
Preferred dividends paid	(12,302)	(7,556)
Purchase of common stock		(1,058)
Net cash provided by financing activities	1,270,055	1,019,341

Increase in cash and cash equivalents		442,741		429,652
Cash and cash equivalents, beginning of period		153,531		50,347
Cash and cash equivalents, end of period	$	596,272	$	479,999

NON-CASH INVESTING AND FINANCING ACTIVITIES:				
Asset retirement obligations	$	19,236	$	2,833
Change in accrued capital expenditures		34,789		38,842
Capital expenditures in accounts payable				18,352
Purchase of oil and natural gas properties in exchange for common stock				7,520
Accrued preferred stock dividends				5,485
Common stock issued in exchange for preferred stock		123,731		
SUPPLEMENTAL DISCLOSURE:				
Cash paid for interest	$	24,527	$	2,020

The accompanying notes are an integral part of these condensed consolidated financial statements.

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Sanchez Energy Corporation

Notes to the Condensed Consolidated Financial Statements

(Unaudited)

Note 1. Organization

Sanchez Energy Corporation (together with our consolidated subsidiaries, the "Company," "we," "our," "us" or similar terms) is an independent exploration and production company, formed in August 2011 as a Delaware corporation, focused on the exploration, acquisition and development of unconventional oil and natural gas resources in the onshore U.S. Gulf Coast, with a current focus on the Eagle Ford Shale in South Texas and the Tuscaloosa Marine Shale ("TMS") in Mississippi and Louisiana. We have accumulated net leasehold acreage in the oil and condensate, or black oil and volatile oil, windows of the Eagle Ford Shale and in what we believe to be the core of the TMS. We are currently focused on the horizontal development of significant resource potential from the Eagle Ford Shale.

Note 2. Basis of Presentation and Summary of Significant Accounting Policies

The accompanying condensed consolidated financial statements are unaudited and were prepared from the Company's records. The condensed consolidated financial statements were prepared in accordance with accounting principles generally accepted in the United States of America ("GAAP" or "U.S. GAAP") for interim financial information and with the instructions to Form 10-Q and Article 10 of Regulation S-X. The Company derived the condensed consolidated balance sheet as of December 31, 2013 from the audited financial statements filed in its Annual Report on Form 10-K for the fiscal year ended December 31, 2013 (the "2013 Annual Report"). Because this is an interim period filing presented using a condensed format, it does not include all of the disclosures required by U.S. GAAP. These condensed consolidated financial statements should be read in connection with the consolidated financial statements and notes thereto included in the 2013 Annual Report, which contains a summary of the Company's significant accounting policies and other disclosures. In the opinion of management, these financial statements include the adjustments and accruals, all of which are of a normal recurring nature, which are necessary for a fair presentation of the results for the interim periods. These interim results are not necessarily indicative of results to be expected for the entire year.

As of September 30, 2014, the Company's significant accounting policies are consistent with those discussed in Note 2 in the notes to the Company's consolidated financial statements contained in its 2013 Annual Report.

Use of Estimates

The condensed consolidated financial statements are prepared in conformity with U.S. GAAP, which requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. The most significant estimates pertain to proved oil and natural gas reserves and related cash flow estimates used in the calculation of depletion and impairment of oil and natural gas properties, fair value accounting for acquisitions, the evaluation of unproved properties for impairment, the fair value of commodity derivative contracts and asset retirement obligations, accrued oil and natural gas revenues and expenses and the allocation of general and administrative expenses. Actual results could differ materially from those estimates.

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Sanchez Energy Corporation

Notes to the Condensed Consolidated Financial Statements (Continued)

(Unaudited)

Note 2. Basis of Presentation and Summary of Significant Accounting Policies (Continued)

Recent Accounting Pronouncements

In May 2014, the Financial Accounting Standards Board ("FASB") issued Accounting Standards Update No. 2014-09, *Revenue from Contracts with Customers* ("ASU 2014-09"), which supersedes nearly all existing revenue recognition guidance under U.S. GAAP. The core principle of ASU 2014-09 is to recognize revenues when promised goods or services are transferred to customers in an amount that reflects the consideration to which an entity expects to be entitled for those goods or services. ASU 2014-09 defines a five step process to achieve this core principle and, in doing so, more judgment and estimates may be required within the revenue recognition process than are required under existing U.S. GAAP.

The standard is effective for annual periods beginning after December 15, 2016, and interim periods therein, using either of the following transition methods: (i) a full retrospective approach reflecting the application of the standard in each prior reporting period with the option to elect certain practical expedients, or (ii) a retrospective approach with the cumulative effect of initially adopting ASU 2014-09 recognized at the date of adoption (which includes additional footnote disclosures). We are currently evaluating the impact of our pending adoption of ASU 2014-09 on our consolidated financial statements and have not yet determined the method by which we will adopt the standard in 2017.

Note 3. Acquisitions

Our acquisitions are accounted for under the acquisition method of accounting in accordance with Accounting Standards Codification, or ASC, Topic 805, "Business Combinations." A business combination may result in the recognition of a gain or goodwill based on the measurement of the fair value of the assets acquired at the acquisition date as compared to the fair value of consideration transferred, adjusted for purchase price adjustments. The initial accounting for acquisitions may not be complete and adjustments to provisional amounts, or recognition of additional assets acquired or liabilities assumed, may occur as more detailed analyses are completed and additional information is obtained about the facts and circumstances that existed as of the acquisition dates. The results of operations of the properties acquired in our acquisitions have been included in the condensed consolidated financial statements since the closing dates of the acquisitions.

Catarina Acquisition

On June 30, 2014, we completed our acquisition of the Catarina properties (the "Catarina acquisition") for an aggregate adjusted purchase price of $559.3 million. The effective date of the transaction was January 1, 2014. The purchase price was funded with a portion of the proceeds from the issuance of the $850 million senior unsecured 6.125% notes due 2023 (the "Original 6.125% Notes") and cash on hand. The purchase price allocation for the Catarina acquisition is preliminary and is subject to further adjustments and the settlement of certain post-closing adjustments with the

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Sanchez Energy Corporation

Notes to the Condensed Consolidated Financial Statements (Continued)

(Unaudited)

Note 3. Acquisitions (Continued)

seller. The total purchase price was allocated to the assets purchased and liabilities assumed based upon their fair values on the date of acquisition as follows (in thousands):

Proved oil and natural gas properties	$	443,349
Unproved properties		127,945
Other assets acquired		2,682
Fair value of assets acquired		573,976
Asset retirement obligations		(14,723)
Fair value of net assets acquired	$	559,253

Wycross Acquisition

On October 4, 2013, we completed our acquisition of the Wycross properties (the "Wycross acquisition") for an aggregate adjusted purchase price of $229.6 million. The effective date of the transaction was July 1, 2013. The purchase price was funded with proceeds from the issuance of the Additional 7.75% Notes (defined in Note 6 "Long-Term Debt"), the issuance of 11,040,000 shares of common stock, and cash on hand. The total purchase price was allocated to the assets purchased and liabilities assumed based upon their fair values on the date of acquisition as follows (in thousands):

Proved oil and natural gas properties	$	215,265
Unproved properties		13,095
Other assets acquired		1,523
Fair value of assets acquired		229,883
Asset retirement obligations		(158)
Other liabilities assumed		(113)
Fair value of net assets acquired	$	229,612

Cotulla Acquisition

On May 31, 2013, we completed our acquisition of the Cotulla properties (the "Cotulla acquisition") for an aggregate adjusted purchase price of $280.9 million. The effective date of the transaction was March 1, 2013.

The purchase price was funded with borrowings under the Company's Amended and Restated Credit Agreement (defined in Note 6 "Long-Term Debt"), cash on hand, and proceeds from the Company's private placement of the Series B Convertible Perpetual Preferred Stock. The total purchase

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Sanchez Energy Corporation

Notes to the Condensed Consolidated Financial Statements (Continued)

(Unaudited)

Note 3. Acquisitions (Continued)

price was allocated to the assets purchased and liabilities assumed based upon their fair values on the date of acquisition as follows (in thousands):

Proved oil and natural gas properties	$	265,466
Unproved properties		16,745
Fair value of assets acquired		282,211
Asset retirement obligations		(1,138)
Other liabilities assumed		(190)
Fair value of net assets acquired	$	280,883

Pro Forma Operating Results

The following pro forma combined results for the three and nine months ended September 30, 2014 and 2013 reflect the consolidated results of operations of the Company as if the Catarina acquisition and related financing had occurred on January 1, 2013 and the Wycross and Cotulla acquisitions and related financings had occurred on January 1, 2012. The pro forma information includes adjustments primarily for revenues and expenses from the acquired properties, depreciation, depletion, amortization and accretion, interest expense and debt issuance cost amortization for acquisition debt, and stock dividends for the issuance of preferred stock.

The unaudited pro forma combined financial statements give effect to the events set forth below:

The Catarina acquisition completed on June 30, 2014.

Issuance of the Original 6.125% Notes to finance a portion of the Catarina acquisition, and the related adjustments to interest expense.

The Cotulla acquisition completed on May 31, 2013.

The increase in borrowings under the Amended and Restated Credit Agreement to finance a portion of the Cotulla acquisition, and the related adjustments to interest expense.

Issuance of Series B Convertible Perpetual Preferred Stock and related adjustments to preferred dividends.

The Wycross acquisition completed on October 4, 2013.

Issuance of the 7.75% Notes (defined in Note 6 "Long-Term Debt") to finance a portion of the Wycross acquisition, and the related adjustments to interest expense.

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Sanchez Energy Corporation

Notes to the Condensed Consolidated Financial Statements (Continued)

(Unaudited)

Note 3. Acquisitions (Continued)

Issuance of common stock to finance a portion of the Wycross acquisition and the related effect on net income (loss) per common share (in thousands, except per share amounts).

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2014	2013	2014	2013
Revenues	$ 207,350	$ 229,517	$ 652,913	$ 577,380
Net income attributable to common stockholders	$ 47,829	$ 13,295	$ 39,523	$ 23,496
Net income per common share, basic	$ 0.86	$ 0.37	$ 0.77	$ 0.66
Net income per common share, diluted	$ 0.76	$ 0.35	$ 0.77	$ 0.66

The pro forma combined financial information is for informational purposes only and is not intended to represent or to be indicative of the combined results of operations that the Company would have reported had the Catarina, Wycross and Cotulla acquisitions and related financings been completed as of the date set forth in this pro forma combined financial information and should not be taken as indicative of the Company's future combined results of operations. The actual results may differ significantly from that reflected in the pro forma combined financial information for a number of reasons, including, but not limited to, differences in assumptions used to prepare the pro forma combined financial information and actual results.

Post-Acquisition Operating Results

The amounts of revenue and excess of revenues over direct operating expenses included in the Company's condensed consolidated statements of operations for the three and nine months ended September 30, 2014 and 2013, for the Catarina, Wycross and Cotulla acquisitions are shown in the table that follows. Direct operating expenses include lease operating expenses and production and ad valorem taxes (in thousands):

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2014	2013	2014	2013
Revenues	$ 116,279	$ 40,267	$ 225,687	$ 48,741

Excess of revenues over direct operating expenses	$	83,841	$	29,890	$	170,346	$	34,819

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Sanchez Energy Corporation

Notes to the Condensed Consolidated Financial Statements (Continued)

(Unaudited)

Note 4. Cash and Cash Equivalents

As of September 30, 2014 and December 31, 2013, cash and cash equivalents consisted of the following (in thousands):

	September 30, 2014	December 31, 2013
Cash at banks	$ 96,228	$ 48,326
Money market funds	500,044	105,205
Total cash and cash equivalents	$ 596,272	$ 153,531

Note 5. Oil and Natural Gas Properties

The Company's oil and natural gas properties are accounted for using the full cost method of accounting. All direct costs and certain indirect costs associated with the acquisition, exploration and development of oil and natural gas properties are capitalized. Once evaluated, these costs, as well as the estimated costs to retire the assets, are included in the amortization base and amortized to depletion expense using the units-of-production method. Depletion is calculated based on estimated proved oil and natural gas reserves. Proceeds from the sale or disposition of oil and natural gas properties are applied to reduce net capitalized costs unless the sale or disposition causes a significant change in the relationship between costs and the estimated quantity of proved reserves.

Full Cost Ceiling Test Capitalized costs (net of accumulated depreciation, depletion and amortization and deferred income taxes) of proved oil and natural gas properties are subject to a full cost ceiling limitation. The ceiling limits these costs to an amount equal to the present value, discounted at 10%, of estimated future net cash flows from estimated proved reserves less estimated future operating and development costs, abandonment costs (net of salvage value) and estimated related future income taxes. In accordance with SEC rules, the oil and natural gas prices used to calculate the full cost ceiling are the 12-month average prices, calculated as the unweighted arithmetic average of the first-day-of-the-month price for each month within the 12-month period prior to the end of the reporting period, unless prices are defined by contractual arrangements. Prices are adjusted for "basis" or location differentials. Prices are held constant over the life of the reserves. If unamortized costs capitalized within the cost pool exceed the ceiling, the excess is charged to expense and separately disclosed during the period in which the excess occurs. Amounts thus required to be written off are not reinstated for any subsequent increase in the cost center ceiling. No impairment expense was recorded for the three and nine month periods ended September 30, 2014 or 2013.

Investments in unproved properties and major development projects are capitalized and excluded from the amortization base until proved reserves associated with the projects can be determined or until impairment occurs. Once the assessment of unproved properties is complete and when major development projects are evaluated, the costs previously excluded from amortization are transferred to the full cost pool subject to periodic amortization. The Company assesses the carrying value of its unproved properties that are not subject to amortization for impairment periodically. If the results of an assessment indicate that the properties are impaired, the amount of the asset impaired is added to the full cost pool subject to both periodic amortization and the ceiling test.

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Notes to the Condensed Consolidated Financial Statements (Continued)

(Unaudited)

Note 6. Long-Term Debt

Long-term debt as of September 30, 2014 consisted of $1.15 billion face value of 6.125% senior notes (the "6.125% Notes," consisting of $850 million in Original 6.125% Notes and $300 million in Additional 6.125% Notes (defined below), which were issued at a premium to face value of $2.3 million) maturing on January 15, 2023, and $600 million principal amount of 7.75% senior notes (the "7.75% Notes," consisting of $400 million in Original 7.75% Notes (defined below) and $200 million in Additional 7.75% Notes, which were issued at a discount to face value of $7.0 million) maturing on June 15, 2021. As of September 30, 2014, the Company's long-term debt consisted of the following:

	Interest Rate	Maturity date	Amount Outstanding (in thousands)
Second Amended and Restated Credit Agreement	Variable	June 30, 2019	$
7.75% Notes	7.75%	June 15, 2021	600,000
6.125% Notes	6.125%	January 15, 2023	1,150,000
			1,750,000
Unamortized discount on Additional 7.75% Notes			(6,063)
Unamortized premium on Additional 6.125% Notes			2,225
Total long-term debt			$ 1,746,162

Interest expense in the Company's condensed consolidated income statement includes (if applicable for a given period): (i) interest on our 7.75% Notes, (ii) interest on our 6.125% Notes, (iii) interest expense and commitment fees on our Amended and Restated Credit Agreement, (iv) interest expense and commitment fees on our Second Amended and Restated Credit Agreement (defined below), (v) amortization of debt issuance costs, (vi) amortization of the discount to face value on the Additional 7.75% Notes and (vii) amortization of the premium to face value on the Additional 6.125% Notes. For the three and nine months ended September 30, 2014 and 2013, the Company's interest expense consisted of the following:

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2014	2013	2014	2013
Interest on senior notes	$ (25,316)	$ (8,198)	$ (48,999)	$ (9,731)
Interest expense and commitment fees on credit agreements	(384)		(1,277)	(2,020)
Amortization of debt issuance costs	(1,710)	(1,230)	(7,215)	(5,830)
Amortization of discount on Additional 7.75% Notes	(227)	(32)	(679)	(32)
Amortization of premium on Additional 6.125% Notes	25		25	
Total interest expense	$ (27,612)	$ (9,460)	$ (58,145)	$ (17,613)

Credit Facility

Previous Credit Agreement: On May 31, 2013, we and our subsidiaries, SEP Holdings III, LLC ("SEP III"), SN Marquis LLC ("SN Marquis") and SN Cotulla Assets, LLC ("SN Cotulla"), collectively, as the borrowers, entered into a revolving credit facility represented by a $500 million

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Sanchez Energy Corporation

Notes to the Condensed Consolidated Financial Statements (Continued)

(Unaudited)

Note 6. Long-Term Debt (Continued)

Amended and Restated Credit Agreement with Royal Bank of Canada as the administrative agent, Capital One, National Association as the syndication agent and RBC Capital Markets as sole lead arranger and sole book runner and each of the other lenders party thereto (the "Amended and Restated Credit Agreement"). The Amended and Restated Credit Agreement was to mature on May 31, 2018.

On May 12, 2014, the Company borrowed $100 million under the Amended and Restated Credit Agreement. The Company used proceeds from the issuance of the Original 6.125% Notes to repay the $100 million outstanding.

Second Amended and Restated Credit Agreement: On June 30, 2014, the Company, as borrower, and SEP III, SN Marquis, SN Cotulla, SN Operating, LLC, SN TMS, LLC and SN Catarina, LLC as loan parties, entered into a revolving credit facility represented by a $1.5 billion Second Amended and Restated Credit Agreement with Royal Bank of Canada as the administrative agent, Capital One, National Association as the syndication agent, Compass Bank and SunTrust Bank as co-documentation agents, RBC Capital Markets as sole lead arranger and sole book runner and the lenders party thereto (the "Second Amended and Restated Credit Agreement"). The Company has elected an available commitment amount under the Second Amended and Restated Credit Agreement of $300 million. Additionally, the Second Amended and Restated Credit Agreement provides for the issuance of letters of credit, limited in the aggregate to the lesser of $50 million and the total availability thereunder. As of September 30, 2014, there were no borrowings and no letters of credit outstanding under the Second Amended and Restated Credit Agreement. Availability under the Second Amended and Restated Credit Agreement is at all times subject to customary conditions and the then applicable borrowing base and elected commitment. The borrowing base under the Second Amended and Restated Credit Agreement was set at $362.5 million upon issuance of the Additional 6.125% Notes. However, the Company elected a commitment amount of $300 million, with the ability to increase the available commitment up to the $362.5 million approved borrowing base upon written notice from the Company and compliance with certain conditions, including the consent of any lenders whose commitment is increased. All of the elected commitment was available for future revolver borrowings as of September 30, 2014.

The Second Amended and Restated Credit Agreement matures on June 30, 2019. The borrowing base under the Second Amended and Restated Credit Agreement can be subsequently redetermined up or down by the lenders based on, among other things, their evaluation of the Company's and its restricted subsidiaries' oil and natural gas reserves. Redeterminations of the borrowing base are scheduled to occur semi-annually on or before April 1 and October 1 of each year, beginning on October 1, 2014. The borrowing base is also subject to (i) automatic reduction by 25% of the amount of any increase in the Company's high yield debt, (ii) interim redetermination at the request of the Company once between each scheduled redetermination and (iii) if the required lenders so direct in connection with asset sales and swap terminations involving more than 10% of the value in the most recent reserve report. The current redetermination of the Company's borrowing base is in process, and we expect the redetermination to be completed in November 2014.

The Company's obligations under the Second Amended and Restated Credit Agreement are secured by a first priority lien on substantially all of the Company's assets and the assets of its existing and future subsidiaries not designated as "unrestricted subsidiaries," including a first priority lien on all

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Sanchez Energy Corporation

Notes to the Condensed Consolidated Financial Statements (Continued)

(Unaudited)

Note 6. Long-Term Debt (Continued)

ownership interests in existing and future subsidiaries not designated as "unrestricted subsidiaries." The obligations under the Second Amended and Restated Credit Agreement are guaranteed by all of the Company's existing and future subsidiaries not designated as "unrestricted subsidiaries."

At the Company's election, borrowings under the Second Amended and Restated Credit Agreement may be made on an alternate base rate or an adjusted eurodollar rate basis, plus an applicable margin. The applicable margin varies from 0.50% to 1.50% for alternate base rate borrowings and from 1.50% to 2.50% for eurodollar borrowings, depending on the utilization of the borrowing base. Furthermore, the Company is also required to pay a commitment fee on the unused committed amount at a rate varying from 0.375% to 0.50% per annum, depending on the utilization of the elected commitment.

The Second Amended and Restated Credit Agreement contains various affirmative and negative covenants and events of default that limit the Company's ability to, among other things, incur indebtedness, make restricted payments, grant liens, consolidate or merge, dispose of certain assets, make certain investments, engage in transactions with affiliates, hedge transactions and make certain acquisitions. The Second Amended and Restated Credit Agreement also provides for cross default between the Second Amended and Restated Credit Agreement and the other debt (including debt under the 6.125% Notes and the 7.75% Notes) and obligations in respect of hedging agreements (on a mark to market basis), of the Company and its restricted subsidiaries, in an aggregate principal amount in excess of $10 million. Furthermore, the Second Amended and Restated Credit Agreement contains financial covenants that require the Company to satisfy certain specified financial ratios, including (i) current assets to current liabilities of at least 1.0 to 1.0 at all times, commencing with the fiscal quarter ending September 30, 2014 and (ii) net debt to consolidated EBITDA of not greater than 4.0 to 1.0 as of the last day of any fiscal quarter, commencing with the fiscal quarter ending September 30, 2014.

From time to time, the agents, arrangers, book runners and lenders under the Second Amended and Restated Credit Agreement and their affiliates have provided, and may provide in the future, investment banking, commercial lending, hedging and financial advisory services to the Company and its affiliates in the ordinary course of business, for which they have received, or may in the future receive, customary fees and commissions for these transactions. As of September 30, 2014, the Company was in compliance with the covenants of the Second Amended and Restated Credit Agreement.

Bridge Commitment: In connection with the Catarina acquisition we obtained a commitment (the "Bridge Commitment") from Royal Bank of Canada, RBC Capital Markets, Credit Suisse AG, Credit Suisse Securities (USA) LLC, Capital One, National Association and SunTrust Bank to provide, arrange, bookrun and agent, as applicable, a senior unsecured bridge facility (the "Bridge Facility"), in an aggregate amount up to $300 million (reduced by the aggregate principal amount of the Additional 6.125% Notes). The Bridge Commitment was set to expire upon the earliest to occur of (a) August 19, 2014, (b) the date of execution and delivery of definitive bridge documentation by us and the lenders under the Bridge Facility or (c) the termination of the commitments by us. The Company terminated the Bridge Commitment upon the execution of the Second Amended and Restated Credit Agreement on June 30, 2014 and wrote off $3.9 million in costs associated with obtaining the Bridge Commitment to interest expense at that time.

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Notes to the Condensed Consolidated Financial Statements (Continued)

(Unaudited)

Note 6. Long-Term Debt (Continued)

7.75% Senior Notes Due 2021

On June 13, 2013, we completed a private offering of $400 million in aggregate principal amount of our 7.75% senior notes that will mature on June 15, 2021 (the "Original 7.75% Notes"). Interest is payable on each June 15 and December 15. We received net proceeds from this offering of approximately $388 million, after deducting initial purchasers' discounts and offering expenses, which we used to repay outstanding indebtedness under our credit facilities. The Original 7.75% Notes are senior unsecured obligations and are guaranteed on a joint and several senior unsecured basis by, with certain exceptions, substantially all of our existing and future subsidiaries.

On September 18, 2013, we issued an additional $200 million in aggregate principal amount of our 7.75% senior notes due 2021 (the "Additional 7.75% Notes" and, together with the Original 7.75% Notes, the 7.75% Notes) in a private offering at an issue price of 96.5% of the Additional 7.75% Notes. We received net proceeds of $188.8 million (after deducting the initial purchasers' discounts and offering expenses of $4.2 million) from the sale of the Additional 7.75% Notes. The Company also received cash for accrued interest from June 13, 2013 through the date of issuance of $4.1 million. The Additional 7.75% Notes were issued under the same indenture as the Original 7.75% Notes, and are therefore treated as a single class of securities under the indenture. We used the net proceeds from the offering to partially fund the Wycross acquisition completed in October 2013, a portion of the 2013 and 2014 capital budgets, and for general corporate purposes.

The 7.75% Notes are senior unsecured obligations and rank equally in right of payment with all of our existing and future senior unsecured indebtedness. The 7.75% Notes rank senior in right of payment to our future subordinated indebtedness. The 7.75% Notes are effectively junior in right of payment to all of our existing and future secured debt (including under our Second Amended and Restated Credit Agreement) to the extent of the value of the assets securing such debt. The 7.75% Notes are fully and unconditionally guaranteed on a joint and several senior unsecured basis by the subsidiary guarantors party to the indenture governing the 7.75% Notes. To the extent set forth in the indenture governing the 7.75% Notes, certain of our subsidiaries will be required to fully and unconditionally guarantee the 7.75% Notes on a joint and several senior unsecured basis in the future.

The indenture governing the 7.75% Notes, among other things, restricts our ability and our restricted subsidiaries' ability to: (i) incur, assume or guarantee additional indebtedness or issue certain types of equity securities; (ii) pay distributions on, purchase or redeem shares or purchase or redeem subordinated debt; (iii) make certain investments; (iv) enter into certain transactions with affiliates; (v) create or incur liens on their assets; (vi) sell assets; (vii) consolidate, merge or transfer all or substantially all of their assets; (viii) restrict distributions or other payments from the Company's restricted subsidiaries; and (ix) designate subsidiaries as unrestricted subsidiaries.

We have the option to redeem all or a portion of the 7.75% Notes, at any time on or after June 15, 2017 at the applicable redemption prices specified in the indenture plus accrued and unpaid interest. We may also redeem the 7.75% Notes, in whole or in part, at a redemption price equal to 100% of their principal amount plus a make whole premium, together with accrued and unpaid interest and additional interest, if any, to the redemption date, at any time prior to June 15, 2017. In addition, we may redeem up to 35% of the 7.75% Notes prior to June 15, 2016 under certain circumstances with an amount not greater than the net cash proceeds of one or more equity offerings at the redemption

Sanchez Energy Corporation

Notes to the Condensed Consolidated Financial Statements (Continued)

(Unaudited)

Note 6. Long-Term Debt (Continued)

price specified in the indenture. We may also be required to repurchase the 7.75% Notes upon a change of control or if we sell certain of our assets.

On July 18, 2014, we completed an exchange offer of $600 million aggregate principal amount of the 7.75% Notes that had been registered under the Securities Act of 1933, as amended (the "Securities Act"), for an equal amount of the 7.75% Notes that had not been registered under the Securities Act.

6.125% Senior Notes Due 2023

On June 27, 2014, the Company completed a private offering of the Original 6.125% Notes. Interest is payable on each July 15 and January 15. The Company received net proceeds from this offering of approximately $829 million, after deducting initial purchasers' discounts and estimated offering expenses, which the Company used to repay all of the $100 million in borrowings outstanding under its Amended and Restated Credit Agreement and to finance a portion of the purchase price of the Catarina acquisition. We intend to use the remaining proceeds from the offering to fund a portion of the remaining 2014 capital budget and for general corporate purposes. The Original 6.125% Notes are the senior unsecured obligations of the Company and are guaranteed on a joint and several senior unsecured basis by, with certain exceptions, substantially all of the Company's existing and future subsidiaries.

On September 12, 2014, we issued an additional $300 million in aggregate principal amount of our 6.125% senior notes due 2023 (the "Additional 6.125% Notes" and, together with the Original 6.125% Notes, the 6.125% Notes and, together with the 7.75% Notes, the "Senior Notes") in a private offering at an issue price of 100.75% of the Additional 6.125% Notes. We received net proceeds of $295.9 million, after deducting the initial purchasers' discounts, adding premiums to face value of $2.3 million and deducting estimated offering expenses of $6.4 million. The Company also received cash for accrued interest from June 27, 2014 through the date of the issuance of $3.8 million, for total net proceeds of $299.7 million from the sale of the Additional 6.125% Notes. The Additional 6.125% Notes were issued under the same indenture as the Original 6.125% Notes, and are therefore treated as a single class of securities under the indenture. We intend to use the net proceeds from the offering to fund a portion of the 2014 and 2015 capital budgets, and for general corporate purposes.

The 6.125% Notes are senior unsecured obligations and rank equally in right of payment with all of our existing and future senior unsecured indebtedness. The 6.125% Notes rank senior in right of payment to the Company's future subordinated indebtedness. The 6.125% Notes are effectively junior in right of payment to all of the Company's existing and future secured debt (including under the Second Amended and Restated Credit Agreement) to the extent of the value of the assets securing such debt. The 6.125% Notes are fully and unconditionally guaranteed on a joint and several senior unsecured basis by the subsidiary guarantors party to the indenture governing the 6.125% Notes. To the extent set forth in the indenture governing the 6.125% Notes, certain of our subsidiaries will be required to fully and unconditionally guarantee the 6.125% Notes on a joint and several senior unsecured basis in the future.

The indenture governing the 6.125% Notes, among other things, restricts our ability and our restricted subsidiaries' ability to: (i) incur, assume or guarantee additional indebtedness or issue certain

Sanchez Energy Corporation

Notes to the Condensed Consolidated Financial Statements (Continued)

(Unaudited)

Note 6. Long-Term Debt (Continued)

types of equity securities; (ii) pay distributions on, purchase or redeem shares or purchase or redeem subordinated debt; (iii) make certain investments; (iv) enter into certain transactions with affiliates; (v) create or incur liens on their assets; (vi) sell assets; (vii) consolidate, merge or transfer all or substantially all of their assets; (viii) restrict distributions or other payments from the Company's restricted subsidiaries; and (ix) designate subsidiaries as unrestricted subsidiaries.

The Company has the option to redeem all or a portion of the 6.125% Notes, at any time on or after July 15, 2018 at the applicable redemption prices specified in the indenture plus accrued and unpaid interest. The Company may also redeem the 6.125% Notes, in whole or in part, at a redemption price equal to 100% of their principal amount plus a make whole premium, together with accrued and unpaid interest and additional interest, if any, to the redemption date, at any time prior to July 15, 2018. In addition, the Company may redeem up to 35% of the 6.125% Notes prior to July 15, 2017 under certain circumstances with an amount not greater than the net cash proceeds of one or more equity offerings at the redemption price specified in the indenture. The Company may also be required to repurchase the 6.125% Notes upon a change of control or if we sell certain Company assets.

Note 7. Derivative Instruments

To reduce the impact of fluctuations in oil and natural gas prices on the Company's revenues, or to protect the economics of property acquisitions, the Company periodically enters into derivative contracts with respect to a portion of its projected oil and natural gas production through various transactions that fix or, through options, modify the future prices to be realized. These transactions may include price swaps whereby the Company will receive a fixed price for its production and pay a variable market price to the contract counterparty. Additionally, the Company may enter into collars, whereby it receives the excess, if any, of the fixed floor over the floating rate or pays the excess, if any, of the floating rate over the fixed ceiling price. In addition, the Company enters into option transactions, such as puts or put spreads, as a way to manage its exposure to fluctuating prices. The Company further uses enhanced swaps for a portion of its commodity price hedging activities. An enhanced swap is a product created by simultaneously selling an out of the money put and using the premium value from the sale to modify or "enhance" the value of a swap executed at the same time. The transaction provides an absolute minimum price at the enhanced swap strike price until the put strike price level is reached at which point the Company receives the market price plus the difference between the enhanced swap price and the put strike price. These hedging activities are intended to support oil and natural gas prices at targeted levels and to manage exposure to oil and natural gas price fluctuations. It is never the Company's intention to enter into derivative contracts for speculative trading purposes.

Under ASC Topic 815, "Derivatives and Hedging," all derivative instruments are recorded on the condensed consolidated balance sheets at fair value as either short-term or long-term assets or liabilities based on their anticipated settlement date. The Company will net derivative assets and liabilities for counterparties where it has a legal right of offset. Changes in the derivatives' fair values are recognized currently in earnings since the Company has elected not to designate its current derivative contracts as hedges.

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Notes to the Condensed Consolidated Financial Statements (Continued)

(Unaudited)

Note 7. Derivative Instruments (Continued)

As of September 30, 2014, the Company had the following crude oil swaps, collars, and put spreads covering anticipated future production:

Contract Period	Derivative Instrument	Barrels	Purchased	Sold	Pricing Index
October 1, 2014 - December 31, 2014	Swap	69,000	$ 92.00	n/a	NYMEX WTI
October 1, 2014 - December 31, 2014	Swap	69,000	$ 91.35	n/a	NYMEX WTI
October 1, 2014 - December 31, 2014	Swap	69,000	$ 92.45	n/a	NYMEX WTI
October 1, 2014 - December 31, 2014	Swap	92,000	$ 95.45	n/a	NYMEX WTI
October 1, 2014 - December 31, 2014	Swap	92,000	$ 93.25	n/a	NYMEX WTI
January 1, 2015 - December 31, 2015(1)	Swap	365,000	$ 89.65	n/a	NYMEX WTI
January 1, 2015 - December 31, 2015(1)	Swap	365,000	$ 90.05	n/a	NYMEX WTI
January 1, 2015 - December 31, 2015(1)	Swap	365,000	$ 88.48	n/a	NYMEX WTI
January 1, 2015 - December 31, 2015	Swap	365,000	$ 88.35	n/a	NYMEX WTI
October 1, 2014 - December 31, 2014	Collar	92,000	$ 90.00	$ 99.10	NYMEX WTI
October 1, 2014 - December 31, 2014	Put Spread	92,000	$ 90.00	$ 75.00	NYMEX WTI

(1) In October 2014, the Company modified these crude oil swaps to create crude oil enhanced swaps. See Note 17 "Subsequent Events" for a description of the modified transactions covering anticipated future production.

As of September 30, 2014, the Company had the following crude oil enhanced swaps covering anticipated future production:

Contract Period	Barrels	Purchased	Put	Pricing Index
January 1, 2015 - December 31, 2015	365,000	$ 91.46	$ 75.00	NYMEX WTI
January 1, 2015 - December 31, 2015	365,000	$ 93.13	$ 75.00	NYMEX WTI
January 1, 2015 - December 31, 2015	365,000	$ 92.20	$ 75.00	NYMEX WTI
January 1, 2015 - December 31, 2015	365,000	$ 91.46	$ 75.00	NYMEX WTI
January 1, 2015 - December 31, 2015	182,500	$ 92.00	$ 75.00	NYMEX WTI

As of September 30, 2014, the Company had the following natural gas swaps and collars covering anticipated future production:

Contract Period	Derivative Instrument	Mmbtu	Purchased	Sold	Pricing Index
October 1, 2014 - December 31, 2014	Swap	184,000	$ 4.23	n/a	NYMEX NG
October 1, 2014 - December 31, 2014	Swap	184,000	$ 4.23	n/a	NYMEX NG
October 1, 2014 - December 31, 2014	Swap	184,000	$ 4.24	n/a	NYMEX NG
October 1, 2014 - December 31, 2014	Swap	184,000	$ 4.61	n/a	NYMEX NG
January 1, 2015 - December 31, 2015	Swap	3,650,000	$ 4.01	n/a	NYMEX NG
October 1, 2014 - December 31, 2014	Collar	184,000	$ 4.00	$ 4.50	NYMEX NG

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Sanchez Energy Corporation

Notes to the Condensed Consolidated Financial Statements (Continued)

(Unaudited)

Note 7. Derivative Instruments (Continued)

As of September 30, 2014, the Company had the following natural gas enhanced swaps covering anticipated future production:

Contract Period	Mmbtu	Purchased	Put	Pricing Index
January 1, 2015 - December 31, 2015	2,190,000	$ 4.44	$ 3.75	NYMEX NG
January 1, 2015 - December 31, 2015	1,095,000	$ 4.40	$ 3.75	NYMEX NG
January 1, 2015 - December 31, 2015	730,000	$ 4.50	$ 3.75	NYMEX NG
January 1, 2015 - December 31, 2015	3,650,000	$ 4.21	$ 3.75	NYMEX NG

As of September 30, 2014, the Company had the following three-way crude oil collar contracts that combine a long and short put with a short call:

Contract Period	Barrels	Short Put	Long Put	Short Call	Pricing Index
October 1, 2014 - December 31, 2014	138,000	$ 65.00	$ 85.00	$ 102.25	NYMEX WTI
October 1, 2014 - December 31, 2014	92,000	$ 75.00	$ 95.00	$ 107.50	LLS
October 1, 2014 - December 31, 2014	92,000	$ 75.00	$ 90.00	$ 96.22	NYMEX WTI
January 1, 2015 - December 31, 2015	365,000	$ 70.00	$ 85.00	$ 95.00	NYMEX WTI
January 1, 2015 - December 31, 2015	365,000	$ 70.00	$ 85.00	$ 95.00	NYMEX WTI
January 1, 2015 - December 31, 2015	365,000	$ 70.00	$ 85.00	$ 94.75	NYMEX WTI
January 1, 2015 - December 31, 2015	365,000	$ 75.00	$ 90.00	$ 97.00	NYMEX WTI
January 1, 2015 - December 31, 2015	365,000	$ 75.00	$ 90.00	$ 97.25	NYMEX WTI

As of September 30, 2014, the Company had the following three-way natural gas contracts that combine a long and short put with a short call:

Contract Period	Mmbtu	Short Put	Long Put	Short Call	Pricing Index
October 1, 2014 - December 31, 2015	2,285,000	$ 3.50	$ 4.00	$ 4.90	NYMEX NG
October 1, 2014 - December 31, 2015	2,285,000	$ 3.50	$ 4.00	$ 4.90	NYMEX NG

The Company deferred the payment of premiums associated with certain of its oil derivative instruments. On September 30, 2014 and December 31, 2013, the balances of deferred payments totaled $5.2 million and $5.6 million, respectively. The monthly premiums are being paid to the counterparty with each monthly settlement until maturity in January 2015 and 2016, respectively.

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Sanchez Energy Corporation

Notes to the Condensed Consolidated Financial Statements (Continued)

(Unaudited)

Note 7. Derivative Instruments (Continued)

The following table sets forth a reconciliation of the changes in fair value of the Company's commodity derivatives for the nine months ended September 30, 2014 and the year ended December 31, 2013 (in thousands):

	September 30, 2014	December 31, 2013
Beginning fair value of commodity derviatives	$ (3,397)	$ 2,145
Net gains (losses) on crude oil derivatives	5,614	(16,891)
Net gains (losses) on natural gas derivatives	785	(47)
Net settlements on derivative contracts:		
Crude oil	9,382	5,755
Natural gas	270	32
Net premiums incurred on derivative contracts:		
Crude oil		5,609
Ending fair value of commodity derivatives	$ 12,654	$ (3,397)

Balance Sheet Presentation

The Company's derivatives are presented on a net basis as "Fair value of derivative instruments" on the condensed consolidated balance sheets. The following information summarizes the gross fair values of derivative instruments, presenting the impact of offsetting the derivative assets and liabilities on the Company's condensed consolidated balance sheets (in thousands):

	September 30, 2014		
	Gross Amount of Recognized Assets	Gross Amounts Offset in the Condensed Consolidated Balance Sheets	Net Amounts Presented in the Condensed Consolidated Balance Sheets
Offsetting Derivative Assets:			
Current asset	$ 17,212	$ (7,464)	$ 9,748
Long-term asset	6,684	(3,609)	3,075
Total asset	$ 23,896	$ (11,073)	$ 12,823
Offsetting Derivative Liabilities:			
Current liability	$ (7,502)	$ 7,464	$ (38)
Long-term liability	(3,740)	3,609	(131)

Total liability	$	(11,242)	$	11,073	$	(169)

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Sanchez Energy Corporation

Notes to the Condensed Consolidated Financial Statements (Continued)

(Unaudited)

Note 7. Derivative Instruments (Continued)

	December 31, 2013		
	Gross Amount of Recognized Assets	Gross Amounts Offset in the Condensed Consolidated Balance Sheets	Net Amounts Presented in the Condensed Consolidated Balance Sheets
Offsetting Derivative Assets:			
Current asset	$ 4,049	$ (4,049)	$
Long-term asset	3,310	(2,006)	1,304
Total asset	$ 7,359	$ (6,055)	$ 1,304
Offsetting Derivative Liabilities:			
Current liability	$ (8,672)	$ 4,049	$ (4,623)
Long-term liability	(2,084)	2,006	(78)
Total liability	$ (10,756)	$ 6,055	$ (4,701)

Note 8. Fair Value of Financial Instruments

Measurements of fair value of derivative instruments are classified according to the fair value hierarchy, which prioritizes the inputs to the valuation techniques used to measure fair value. Fair value is the price that would be received upon the sale of an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. Fair value measurements are classified and disclosed in one of the following categories:

Level 1: Measured based on unadjusted quoted prices in active markets that are accessible at the measurement date for identical, unrestricted assets or liabilities. Active markets are considered those in which transactions for the assets or liabilities occur in sufficient frequency and volume to provide pricing information on an ongoing basis.

Level 2: Measured based on quoted prices in markets that are not active, or inputs which are observable, either directly or indirectly, for substantially the full term of the asset or liability. This category includes those derivative instruments that can be valued using observable market data. Substantially all of these inputs are observable in the marketplace throughout the term of the derivative instrument, can be derived from observable data, or supported by observable levels at which transactions are executed in the marketplace.

Level 3: Measured based on prices or valuation models that require inputs that are both significant to the fair value measurement and less observable from objective sources (i.e. supported by little or no market activity). The valuation models used to value derivatives associated with the Company's oil and natural gas production are primarily industry standard models that consider various inputs including: (a) quoted forward prices for commodities, (b) time value and (c) current market and contractual prices for the underlying instruments, as well as other relevant economic measures. Although third party quotes are utilized to assess the reasonableness of the prices and valuation techniques, there is not sufficient corroborating evidence to support classifying these assets and liabilities as Level 2.

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Sanchez Energy Corporation

Notes to the Condensed Consolidated Financial Statements (Continued)

(Unaudited)

Note 8. Fair Value of Financial Instruments (Continued)

Financial assets and liabilities are classified based on the lowest level of input that is significant to the fair value measurement. Management's assessment of the significance of a particular input to the fair value measurement requires judgment, and may affect the valuation of the fair value of assets and liabilities and their placement within the fair value hierarchy levels.

Fair Value on a Recurring Basis

The following tables set forth, by level within the fair value hierarchy, the Company's financial assets and liabilities that were accounted for at fair value on a recurring basis as of September 30, 2014 and December 31, 2013 (in thousands):

	As of September 30, 2014			
	Active Market for Identical Assets (Level 1)	Observable Inputs (Level 2)	Unobservable Inputs (Level 3)	Total Carrying Value
Cash and cash equivalents:				
Money market funds	$ 500,044	$	$	$ 500,044
Oil derivative instruments:				
Swaps		2,833		2,833
Enhanced Swaps			4,746	4,746
Three-way collars			3,827	3,827
Collars			179	179
Puts			28	28
Gas derivative instruments:				
Swaps		206		206
Enhanced Swaps			486	486
Three-way collars			342	342
Collars			7	7
Total	$ 500,044	$ 3,039	$ 9,615	$ 512,698

	As of December 31, 2013			
	Active Market for Identical Assets (Level 1)	Observable Inputs (Level 2)	Unobservable Inputs (Level 3)	Total Carrying Value
Cash and cash equivalents:				
Money market funds	$ 105,205	$	$	$ 105,205
Oil derivative instruments:				
Swaps		(2,841)		(2,841)
Three-way collars			(398)	(398)
Collars			3	3
Puts			(146)	(146)

Gas derivative instruments:								
Swaps				(37)				(37)
Collars						22		22
Total	$	105,205	$	(2,878)	$	(519)	$	101,808

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Sanchez Energy Corporation

Notes to the Condensed Consolidated Financial Statements (Continued)

(Unaudited)

Note 8. Fair Value of Financial Instruments (Continued)

Financing arrangements: The Company filed a registration statement for its 7.75% Notes in an exchange offer filed with the SEC, which became effective on June 20, 2014, creating an active market for the 7.75% Notes, and as such, results in a Level 1 fair value measurement. The estimated fair value of the 7.75% Notes was $645 million as of September 30, 2014, and was calculated using quoted market prices based on trades of such debt as of that date. The Company uses a market approach to determine fair value of its unregistered 6.125% Notes using observable market data, which results in a Level 2 fair value measurement. The estimated fair value of the 6.125% Notes was $1,138.5 million as of September 30, 2014, and was calculated using quoted market prices based on trades of such debt as of that date.

Financial Instruments: The Level 1 instruments presented in the table above consist of money market funds included in cash and cash equivalents on the Company's condensed consolidated balance sheet as of September 30, 2014 and December 31, 2013. The Company's money market funds represent cash equivalents backed by the assets of high-quality banks and financial institutions. The Company identified the money market funds as Level 1 instruments due to the fact that the money market funds have daily liquidity, quoted prices for the underlying investments can be obtained and there are active markets for the underlying investments.

The Level 2 instruments presented in the table above consist of commodity derivatives. These asset values can be closely approximated using simple models and extrapolation methods using known, observable prices as parameters.

The Company's derivative instruments, which consist of swaps, enhanced swaps, collars and puts, are classified as either Level 2 or Level 3 in the table above. The fair values of the Company's derivatives are based on third party pricing models which utilize inputs that are either readily available in the public market, such as forward curves, or can be corroborated from active markets of broker quotes. These values are then compared to the values given by the Company's counterparties for reasonableness. Since swaps do not include optionality and therefore generally have no unobservable inputs, they are classified as Level 2. The Company's enhanced swaps, puts, collars and three-way collars include some level of unobservable input, such as volatility curves, and are therefore classified as Level 3. Derivative instruments are also subject to the risk that counterparties will be unable to meet their obligations. Such non-performance risk is considered in the valuation of the Company's derivative instruments, but to date has not had a material impact on estimates of fair values. Significant changes in the quoted forward prices for commodities and changes in market volatility generally lead to corresponding changes in the fair value measurement of the Company's derivative instruments.

The fair values of the Company's derivative instruments classified as Level 3 as of September 30, 2014 and December 31, 2013 were $9.6 million and ($0.5) million, respectively. The significant unobservable inputs for Level 3 contracts include unpublished forward prices of commodities, market volatility and credit risk of counterparties. Changes in these inputs will impact the fair value measurement of the Company's derivative contracts.

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Sanchez Energy Corporation

Notes to the Condensed Consolidated Financial Statements (Continued)

(Unaudited)

Note 8. Fair Value of Financial Instruments (Continued)

The following table sets forth a reconciliation of changes in the fair value of the Company's derivative instruments classified as Level 3 in the fair value hierarchy (in thousands):

	Significant Unobservable Inputs (Level 3)			
	Three Months Ended September 30,		Nine Months Ended September 30,	
	2014	2013	2014	2013
Beginning balance	$ (16,774)	$ 3,003	$ (519)	$ 3,015
Total gains (losses) included in earnings	26,189	(4,305)	8,389	(4,154)
Net settlements on derivative contracts	200	718	1,745	555
Ending balance	$ 9,615	$ (584)	$ 9,615	$ (584)
Gains (losses) included in earnings related to derivatives still held as of September 30, 2014 and 2013	$ 26,747	$ (3,338)	$ 10,492	$ (2,445)

Fair Value on a Non-Recurring Basis

The Company follows the provisions of ASC 820-10 for nonfinancial assets and liabilities measured at fair value on a non-recurring basis. Fair value measurements of assets acquired and liabilities assumed in business combinations are based on inputs that are not observable in the market and thus represent Level 3 inputs. The fair value of acquired properties is based on market and cost approaches. Our purchase price allocations for the Catarina, Cotulla and Wycross acquisitions are presented in Note 3 "Acquisitions." Liabilities assumed include asset retirement obligations existing at the date of acquisition. The asset retirement obligation estimates are derived from historical costs as well as management's expectation of future cost environments. As there is no corroborating market activity to support the assumptions, the Company has designated these liabilities as Level 3. A reconciliation of the beginning and ending balances of the Company's asset retirement obligations is presented in Note 9 "Asset Retirement Obligations."

In connection with the exchange agreements entered into in February, May and August 2014 by the Company with certain holders of the Company's Series A Preferred Stock and Series B Preferred Stock, the Company issued common stock according to the conversion rate pursuant to each agreement and additional shares to induce the holders of the preferred stock to convert prior to the date the Company could mandate conversion. The fair value of the common stock issued is based on the price of the Company's common stock on the date of issuance. As there is an active market for the Company's common stock, the Company has designated this fair value measurement as Level 1. A detailed description of the Company's common stock and preferred stock issuances and redemptions is presented in Note 12 "Stockholders' Equity."

Note 9. Asset Retirement Obligations

Asset retirement obligations represent the present value of the estimated cash flows expected to be incurred to plug, abandon and remediate producing properties, excluding salvage values, at the end of their productive lives in accordance with applicable laws. The significant unobservable inputs to this fair value measurement include estimates of plugging, abandonment and remediation costs, well life, 27

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Sanchez Energy Corporation

Notes to the Condensed Consolidated Financial Statements (Continued)

(Unaudited)

Note 9. Asset Retirement Obligations (Continued)

inflation and credit-adjusted risk-free rate. The inputs are calculated based on historical data as well as current estimates. When the liability is initially recorded, the carrying amount of the related long-lived asset is increased. Over time, accretion of the liability is recognized each period, and the capitalized cost is amortized over the useful life of the related asset. Upon settlement of the liability, any gain or loss is treated as an adjustment to the full cost pool.

The changes in the asset retirement obligation for the nine months ended September 30, 2014 and the year ended December 31, 2013 were as follows (in thousands):

	Nine Months Ended September 30, 2014	Year Ended December 31, 2013
Abandonment liability, beginning of period	$ 4,130	$ 546
Liabilities incurred during period	2,475	1,122
Acquisitions	14,723	1,296
Revisions	2,038	968
Accretion expense	682	198
Abandonment liability, end of period	$ 24,048	$ 4,130

During the first quarter of 2014, the Company reviewed its asset retirement obligation estimates. A quote was obtained from a third party that indicated anticipated costs for future abandonment had increased from previous estimates. As a result, the Company increased its estimates of future asset retirement obligations by $2.0 million to reflect anticipated increased costs for plugging and abandonment. During the first quarter of 2013, the Company performed a similar exercise to update its asset retirement obligation estimates. As a result, the Company increased its estimates of future asset retirement obligations by $1.0 million to reflect anticipated increased costs for plugging and abandonment.

Note 10. Related Party Transactions

Sanchez Oil & Gas Corporation ("SOG"), headquartered in Houston, Texas, is a private full service oil and natural gas company engaged in the exploration and development of oil and natural gas primarily in the South Texas and onshore Gulf Coast areas on behalf of its affiliates. The Company refers to SOG, Sanchez Energy Partners I, LP, and their affiliates (but excluding the Company), collectively, as the "Sanchez Group."

The Company does not have any employees. On December 19, 2011, it entered into a services agreement with SOG pursuant to which specified employees of SOG provide certain services with respect to the Company's business under the direction, supervision and control of SOG. Pursuant to this arrangement, SOG performs centralized corporate functions for the Company, such as general and administrative services, geological, geophysical and reserve engineering, lease and land administration, marketing, accounting, operational services, information technology services, compliance, insurance maintenance and management of outside professionals. The Company compensates SOG for the services at a price equal to SOG's cost of providing such services, including all direct costs and indirect administrative and overhead costs (including the allocable portion of salary, bonus, incentive compensation and other amounts paid to persons that provide the services on SOG's behalf) allocated

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Sanchez Energy Corporation

Notes to the Condensed Consolidated Financial Statements (Continued)

(Unaudited)

Note 10. Related Party Transactions (Continued)

in accordance with SOG's regular and consistent accounting practices, including for any such costs arising from amounts paid directly by other members of the Sanchez Group on SOG's behalf or borrowed by SOG from other members of the Sanchez Group, in each case, in connection with the performance by SOG of services on the Company's behalf. The Company also reimburses SOG for sales, use or other taxes, or other fees or assessments imposed by law in connection with the provision of services to the Company (other than income, franchise or margin taxes measured by SOG's net income or margin and other than any gross receipts or other privilege taxes imposed on SOG) and for any costs and expenses arising from or related to the engagement or retention of third party service providers.

Salaries and associated benefit costs of SOG employees are allocated to the Company based on the actual time spent by the professional staff on the properties and business activities of the Company. General and administrative costs, such as office rent, utilities, supplies, and other overhead costs, are allocated to the Company based on a fixed percentage that is reviewed quarterly and adjusted, if needed, based on the activity levels of services provided to the Company. General and administrative costs that are specifically incurred by or for the specific benefit of the Company are charged directly to the Company. Expenses allocated to the Company for general and administrative expenses for the three and nine months ended September 30, 2014 and 2013 are as follows (in thousands):

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2014	2013	2014	2013
Administrative fees	$ 5,982	$ 4,638	$ 18,444	$ 10,540
Third party expenses	2,452	2,287	5,135	4,571
Total included in general and administrative expenses	$ 8,434	$ 6,925	$ 23,579	$ 15,111

As of September 30, 2014 and December 31, 2013, the Company had a net payable to SOG and other members of the Sanchez Group of $1.2 million and $1.0 million, respectively, which are reflected as "Accounts payable related entities" in the condensed consolidated balance sheets. The net payables consist primarily of obligations for general and administrative costs due to SOG and revenue payable to affiliated entities.

TMS Asset Purchase

In August 2013, we acquired approximately 40,000 net undeveloped acres in what we believe to be the core of the TMS for cash and shares of our common stock plus an initial 3 gross (1.5 net) well drilling carry. In connection with the TMS transactions, we established an Area of Mutual Interest ("AMI") in the TMS with SR Acquisition I, LLC ("SR"), a subsidiary of our affiliate Sanchez Resources, LLC ("Sanchez Resources"). Sanchez Resources is indirectly owned, in part, by our President and Chief Executive Officer and the Executive Chairman of the Company's Board of Directors (the "Board"), who each also serve on our Board. Additionally, Eduardo Sanchez, Patricio Sanchez and Ana Lee Sanchez Jacobs, each an immediate family member of our President and Chief Executive Officer and the Executive Chairman of our Board, collectively, either directly or indirectly,

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Sanchez Energy Corporation

Notes to the Condensed Consolidated Financial Statements (Continued)

(Unaudited)

Note 10. Related Party Transactions (Continued)

own a majority of the equity interests of Sanchez Resources. Sanchez Resources is managed by Eduardo Sanchez, who is the brother of our President and Chief Executive Officer and the son of our Executive Chairman of the Board.

As part of the transaction, we acquired all of the working interests in the AMI owned at closing from three sellers (two third parties and one related party of the Company, SR) resulting in our owning an undivided 50% working interest across the AMI through the TMS. The AMI holds rights to approximately 115,000 gross acres and 80,000 net acres.

Total consideration for the TMS transactions consisted of approximately $70 million in cash and the issuance of 342,760 common shares of the Company, valued at $7.5 million. The cash consideration provided to SR was $14.4 million. The acquisitions were accounted for as the purchase of assets at cost on the acquisition date.

We have also committed, as a part of the total consideration, to carry SR for its 50% working interest in an initial 3 gross (1.5 net) TMS wells to be drilled within the AMI. In the event that we do not fulfill our obligations in a timely manner with regard to the initial TMS well commitment, we must re-assign the working interests acquired from SR. At the point that the minimum commitment is met, we will have fully paid for and earned all of our rights to the TMS acreage. We also have the right to continue drilling within the AMI after fulfilling the minimum well commitment by carrying SR for an additional 3 gross (1.5 net) TMS wells. We intend to carry SR in the additional 3 gross (1.5 net) TMS wells. We expect to meet our well carry commitments for the full 6 gross (3 net) TMS wells in early 2015.

Note 11. Accrued Liabilities

The following information summarizes accrued liabilities as of September 30, 2014 and December 31, 2013 (in thousands):

	September 30, 2014	December 31, 2013
Capital expenditures	$ 121,671	$ 86,883
General and administrative costs	6,590	550
Production taxes	5,126	2,903
Ad valorem taxes	5,859	981
Lease operating expenses	25,347	8,977
Interest payable	31,515	2,161
Total accrued liabilities	$ 196,108	$ 102,455

Note 12. Stockholders' Equity

Common Stock Offerings On September 18, 2013, the Company completed a public offering of 11,040,000 shares of common stock (including 1,440,000 shares purchased pursuant to the full exercise of the underwriters' overallotment option), at an issue price of $23.00 per share. The Company received net proceeds from this offering of $241.4 million, after deducting underwriters' fees and offering expenses of $12.5 million. The Company used the net proceeds from the offering to partially

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Sanchez Energy Corporation

Notes to the Condensed Consolidated Financial Statements (Continued)

(Unaudited)

Note 12. Stockholders' Equity (Continued)

fund the Wycross acquisition completed in October 2013 and a portion of the 2013 and 2014 capital budgets, and for general corporate purposes.

On June 12, 2014, the Company completed a public offering of 5,000,000 shares of common stock, at an issue price of $35.25 per share. The Company received net proceeds from this offering of $167.6 million, after deducting underwriters' fees and offering expenses of $8.7 million. The Company intends to use the net proceeds from the offering to partially fund the 2014 capital budget and for general corporate purposes.

Series A Convertible Perpetual Preferred Stock Offering On September 17, 2012, the Company completed a private placement of 3,000,000 shares of Series A Convertible Perpetual Preferred Stock, which were sold to a group of qualified institutional buyers pursuant to the Rule 144A exemption from registration under the Securities Act. The issue price of each share of the Series A Convertible Perpetual Preferred Stock was $50.00. The Company received net proceeds from the private placement of $144.5 million, after deducting initial purchasers' discounts and commissions and offering costs payable by the Company of $5.5 million. Pursuant to the Certificate of Designations for the Series A Convertible Perpetual Preferred Stock, each share of Series A Convertible Perpetual Preferred Stock is convertible at any time at the option of the holder thereof at an initial conversion rate of 2.325 shares of common stock per share of Series A Convertible Perpetual Preferred Stock (which is equal to an initial conversion price of $21.51 per share of common stock) and is subject to specified adjustments. Based on the initial conversion price, 4,275,640 shares of common stock would be issuable upon conversion of all of the outstanding shares of the Series A Convertible Perpetual Preferred Stock.

The annual dividend on each share of Series A Convertible Perpetual Preferred Stock is 4.875% on the liquidation preference of $50.00 per share and is payable quarterly, in arrears, on each January 1, April 1, July 1 and October 1, when, as and if declared by the Board. No dividends were accrued or accumulated prior to September 17, 2012. The Company may, at its option, pay dividends in cash and, subject to certain conditions, common stock or any combination thereof. As of September 30, 2014, all dividends accumulated through that date had been paid.

Except as required by law or the Company's Amended and Restated Certificate of Incorporation, holders of the Series A Convertible Perpetual Preferred Stock will have no voting rights unless dividends fall into arrears for six or more quarterly periods (whether or not consecutive). In that event and until such arrearage is paid in full, the holders of the Series A Convertible Perpetual Preferred Stock and the holders of the Series B Convertible Perpetual Preferred Stock, voting as a single class, will be entitled to elect two directors and the number of directors on the Board will increase by that same number.

At any time on or after October 5, 2017, the Company may at its option cause all outstanding shares of the Series A Convertible Perpetual Preferred Stock to be automatically converted into common stock at the conversion price, if, among other conditions, the closing sale price (as defined) of the Company's common stock equals or exceeds 130% of the conversion price for a specified period prior to the conversion.

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Sanchez Energy Corporation

Notes to the Condensed Consolidated Financial Statements (Continued)

(Unaudited)

Note 12. Stockholders' Equity (Continued)

If a holder elects to convert shares of Series A Convertible Perpetual Preferred Stock upon the occurrence of certain specified fundamental changes, the Company will be obligated to deliver an additional number of shares above the applicable conversion rate to compensate the holder for lost option time value of the shares of Series A Convertible Perpetual Preferred Stock as a result of the fundamental change.

Series B Convertible Perpetual Preferred Stock Offering On March 26, 2013, the Company completed a private placement of 4,500,000 shares of Series B Convertible Perpetual Preferred Stock. The issue price of each share of the Series B Convertible Perpetual Preferred Stock was $50.00. The Company received net proceeds from the private placement of $216.6 million, after deducting placement agent's fees and offering costs of $8.4 million.

Each share of Series B Convertible Perpetual Preferred Stock is convertible at any time at the option of the holder thereof at an initial conversion rate of 2.337 shares of common stock per share of Series B Convertible Perpetual Preferred Stock (which is equal to an initial conversion price of $21.40 per share of common stock) and is subject to specified adjustments. Based on the initial conversion price, 8,255,055 shares of common stock would be issuable upon conversion of all of the outstanding shares of the Series B Convertible Perpetual Preferred Stock.

The annual dividend on each share of Series B Convertible Perpetual Preferred Stock is 6.500% on the liquidation preference of $50.00 per share and is payable quarterly, in arrears, on each January 1, April 1, July 1 and October 1, when, as and if declared by the Board. The Company may, at its option, pay dividends in cash and, subject to certain conditions, common stock or any combination thereof. As of September 30, 2014, all dividends accumulated through that date had been paid.

Except as required by law or the Company's Amended and Restated Certificate of Incorporation, holders of the Series B Convertible Perpetual Preferred Stock will have no voting rights unless dividends fall into arrears for six or more quarterly periods (whether or not consecutive). In that event and until such arrearage is paid in full, the holders of the Series B Convertible Perpetual Preferred Stock and the holders of the Series A Convertible Perpetual Preferred Stock, voting as a single class, will be entitled to elect two directors and the number of directors on the Board will increase by that same number.

At any time on or after April 6, 2018, the Company may at its option cause all outstanding shares of the Series B Convertible Preferred Stock to be automatically converted into common stock at the conversion price, if, among other conditions, the closing sale price (as defined) of the Company's common stock equals or exceeds 130% of the conversion price for a specified period prior to the conversion.

If a holder elects to convert shares of Series B Convertible Perpetual Preferred Stock upon the occurrence of certain specified fundamental changes, the Company will be obligated to deliver an additional number of shares above the applicable conversion rate to compensate the holder for lost option time value of the shares of Series B Convertible Perpetual Preferred Stock as a result of the fundamental change.

Preferred Stock Exchanges On February 12, 2014 and February 13, 2014, the Company entered into exchange agreements with certain holders (the "February 2014 Holders") of the Company's

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Sanchez Energy Corporation

Notes to the Condensed Consolidated Financial Statements (Continued)

(Unaudited)

Note 12. Stockholders' Equity (Continued)

Series A Convertible Perpetual Preferred Stock, and of Series B Convertible Perpetual Preferred Stock, pursuant to which such holders agreed to exchange an aggregate of (i) 947,490 shares of Series A Convertible Perpetual Preferred Stock (and waive their rights to any accrued and unpaid dividends thereon) for 2,425,574 shares of the Company's common stock, and (ii) 756,850 shares of the Series B Convertible Perpetual Preferred Stock (and waive their rights to any accrued and unpaid dividends thereon) for 2,021,066 shares of common stock.

Additionally, on May 29, 2014, the Company entered into exchange agreements with certain holders (the "May 2014 Holders") of the Company's Series A Convertible Perpetual Preferred Stock, and of Series B Convertible Perpetual Preferred Stock, pursuant to which such holders agreed to exchange an aggregate of (i) 166,025 shares of Series A Convertible Perpetual Preferred Stock (and waive their rights to any accrued and unpaid dividends thereon) for 418,715 shares of the Company's common stock, and (ii) 210,820 shares of the Series B Convertible Perpetual Preferred Stock (and waive their rights to any accrued and unpaid dividends thereon) for 553,980 shares of common stock.

Further, on August 28, 2014, the Company entered into exchange agreements with certain holders (the "August 2014 Holders," and together with the May 2014 Holders and the February 2014 Holders, the "Holders") of the Company's Series A Convertible Perpetual Preferred Stock, pursuant to which such holders agreed to exchange an aggregate of 47,500 shares of Series A Convertible Perpetual Preferred Stock (and waive their rights to any accrued and unpaid dividends thereon) for 119,320 shares of the Company's common stock.

Since the Holders were not entitled to any consideration over and above the initial conversion rates of 2.325 and 2.337 common shares for each preferred share exchanged for Series A Convertible Perpetual Preferred Stock and Series B Convertible Perpetual Preferred Stock, respectively, any consideration is considered an inducement for the Holders to convert earlier than the Company could have forced conversion.

The Company has determined the fair value of consideration transferred to the Holders and the fair value of consideration transferrable pursuant to the original conversion terms. The $13.9 million, $3.1 million and $0.3 million excess of the fair value of the shares of common stock issued over the carrying value of the Series A Preferred Stock and Series B Preferred Stock redeemed in connection with the exchange agreements entered into in February, May and August, respectively, has been reflected as an additional preferred stock dividend, that is, as a reduction of retained earnings to arrive at net income attributable to common shareholders in our condensed consolidated financial statements.

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Sanchez Energy Corporation

Notes to the Condensed Consolidated Financial Statements (Continued)

(Unaudited)

Note 12. Stockholders' Equity (Continued)

Earnings (Loss) Per Share The following table shows the computation of basic and diluted net income (loss) per share for the three and nine months ended September 30, 2014 and 2013 (in thousands, except per share amounts):

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2014	**2013**	**2014**	**2013**
Net income	$ 49,031	$ 3,880	$ 40,318	$ 12,696
Less:				
Preferred stock dividends	(4,274)	(5,485)	(29,599)	(13,041)
Net income allocable to participating securities[(1)(2)]	(2,068)		(495)	
Net income (loss) attributable to common stockholders	$ 42,689	$ (1,605)	$ 10,224	$ (345)
Weighted average number of unrestricted outstanding common shares used to calculate basic net income (loss) per share	55,732	34,737	51,153	33,651
Dilutive shares[(3)(4)(5)(6)]	12,608			
Denominator for diluted net income (loss) per common share	68,340	34,737	51,153	33,651
Net income (loss) per common share basic	$ 0.77	$ (0.05)	$ 0.20	$ (0.01)
Net income (loss) per common share diluted	$ 0.69	$ (0.05)	$ 0.20	$ (0.01)

(1) The Company's restricted shares of common stock are participating securities.

(2) For the three and nine months ended September 30, 2013, no losses were allocated to participating restricted stock because such securities do not have a contractual obligation to share in the Company's losses.

(3)
The nine months ended September 30, 2014 excludes 1,290,637 shares of weighted average restricted stock and 13,863,738 shares of common stock resulting from an assumed conversion of the Company's Series A Convertible Perpetual Preferred Stock and Series B Convertible Perpetual Preferred Stock from the calculation of the denominator for diluted earnings per common share as these shares were anti-dilutive.

(4)
The three months ended September 30, 2014 includes 12,607,521 shares of common stock resulting from an assumed conversion of the Company's Series A Convertible Perpetual Preferred Stock and Series B Convertible Perpetual Preferred Stock in the calculation of the denominator for diluted earnings per common share as these shares were dilutive. In addition, the related preferred stock dividends of $4,274,445 were not deducted from net income in computing the numerator used in the calculation of diluted earnings per common share.

(5)
The three months ended September 30, 2014 excludes 863,412 shares of weighted average restricted stock in the calculation of the denominator for diluted net income per common share as these shares were anti-dilutive.

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Sanchez Energy Corporation

Notes to the Condensed Consolidated Financial Statements (Continued)

(Unaudited)

Note 12. Stockholders' Equity (Continued)

(6) The three and nine months ended September 30, 2013 excludes 410,779 and 625,920 shares of weighted average restricted stock and 17,491,500 and 14,141,800 shares of common stock resulting from an assumed conversion of the Company's Series A Convertible Perpetual Preferred Stock and Series B Convertible Perpetual Preferred Stock from the calculation of the denominator for diluted earnings per common share as these shares were anti-dilutive.

Note 13. Stock-Based Compensation

At the Annual Meeting of Stockholders of the Company held on May 23, 2012, the Company's stockholders approved the Sanchez Energy Corporation Amended and Restated 2011 Long Term Incentive Plan (the "LTIP"). The Board had previously approved the amendment of the LTIP on April 16, 2012, subject to stockholder approval.

The Company's directors and consultants as well as employees of the Sanchez Group who provide services to the Company are eligible to participate in the LTIP. Awards to participants may be made in the form of restricted shares, phantom shares, share options, share appreciation rights and other share-based awards. The maximum number of shares that may be delivered pursuant to the LTIP is limited to 15% of the Company's issued and outstanding shares of common stock. This maximum amount automatically increases to 15% of the issued and outstanding shares of common stock immediately after each issuance by the Company of its common stock, unless the Board determines to increase the maximum number of shares of common stock by a lesser amount. Shares withheld to satisfy tax withholding obligations are not considered to be delivered under the LTIP. In addition, if an award is forfeited, canceled, exercised, paid or otherwise terminates or expires without the delivery of shares, the shares subject to such award are then available for new awards under the LTIP. Shares delivered pursuant to awards under the LTIP may be newly issued shares, shares acquired by the Company in the open market, shares acquired by the Company from any other person, or any combination of the foregoing.

The LTIP is administered by the Board. The Board may terminate or amend the LTIP at any time with respect to any shares for which a grant has not yet been made. The Board has the right to alter or amend the LTIP or any part of the LTIP from time to time, including increasing the number of shares that may be granted, subject to shareholder approval as may be required by the exchange upon which the common shares are listed at that time, if any. No change may be made in any outstanding grant that would materially reduce the benefits of the participant without the consent of the participant. The LTIP will expire upon its termination by the Board or, if earlier, when no shares remain available under the LTIP for awards. Upon termination of the LTIP, awards then outstanding will continue pursuant to the terms of their grants.

The Company records stock-based compensation expense for awards granted to its directors (for their services as directors) in accordance with the provisions of ASC 718, "Compensation Stock Compensation." Stock-based compensation expense for these awards is based on the grant-date fair value and recognized over the vesting period using the straight-line method.

Awards granted to employees of the Sanchez Group (including those employees of the Sanchez Group who also serve as the Company's officers) and consultants in exchange for services are considered awards to non-employees and the Company records stock-based compensation expense for

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Sanchez Energy Corporation

Notes to the Condensed Consolidated Financial Statements (Continued)

(Unaudited)

Note 13. Stock-Based Compensation (Continued)

these awards at fair value in accordance with the provisions of ASC 505-50, "Equity-Based Payments to Non-Employees." For awards granted to non-employees, the Company records compensation expenses equal to the fair value of the stock-based award at the measurement date, which is determined to be the earlier of the performance commitment date or the service completion date. Compensation expense for unvested awards to non-employees is revalued at each period end and is amortized over the vesting period of the stock-based award. Stock-based payments are measured based on the fair value of the equity instruments granted, as it is more determinable than the value of the services rendered.

For the restricted stock awards granted to non-employees, stock-based compensation expense is based on fair value remeasured at each reporting period and recognized over the vesting period using the straight-line method. Compensation expense for these awards will be revalued at each period end until vested.

The Company recognized the following stock-based compensation expense for the periods indicated which is reflected as general and administrative expense in the condensed consolidated statements of operations (in thousands):

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2014	2013	2014	2013
Restricted stock awards, directors	$ 171	$ 242	$ 731	$ 473
Restricted stock awards, non-employees	(161)	6,415	25,157	13,896
Total stock-based compensation expense	$ 10	$ 6,657	$ 25,888	$ 14,369

Based on the $26.26 per share closing price of the Company's common stock on September 30, 2014, there was $48.7 million of unrecognized compensation cost related to these non-vested restricted shares outstanding. The cost is expected to be recognized over an average period of approximately 1.8 years.

A summary of the status of the non-vested shares as of September 30, 2014 is presented below (in thousands):

	Number of Non-Vested Shares
Non-vested common stock as of December 31, 2013	1,758
Granted	1,966
Vested	(692)
Forfeited	(313)
Non-vested common stock as of September 30, 2014	2,719

As of September 30, 2014, approximately 4.6 million shares remain available for future issuance to participants.

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Sanchez Energy Corporation

Notes to the Condensed Consolidated Financial Statements (Continued)

(Unaudited)

Note 14. Income Taxes

The Company's estimated annual effective income tax rates are used to allocate expected annual income tax expense to interim periods. The rates are determined based on the ratio of estimated annual income tax expense to estimated annual income before income taxes by taxing jurisdiction, except for discrete items, which are significant, unusual or infrequent items for which income taxes are computed and recorded in the interim period in which the specific transaction occurs. The estimated annual effective income tax rates are applied to the year-to-date income before income taxes by taxing jurisdiction to determine the income tax expense allocated to the interim period. The Company updates its estimated annual effective income tax rate at the end of each quarterly period considering the geographic mix of income based on the tax jurisdictions in which the Company operates. Actual results that are different from the assumptions used in estimating the annual effective income tax rate will impact future income tax expense. The difference between the statutory federal income taxes calculated using a U.S. Federal statutory corporate income tax rate of 35% and the Company's effective tax rate of 35.2% for the three and nine months ended September 30, 2014 is related to non-deductible general and administrative expenses recorded during the period.

As of September 30, 2014, the Company had estimated net operating loss carryforwards of $707.4 million, which will begin to expire in 2031.

In recording deferred income tax assets, the Company considers whether it is more likely than not that some portion or all of the deferred income tax assets will be realized. The ultimate realization of deferred income tax assets is dependent upon the generation of future taxable income during the periods in which those deferred income tax assets would be deductible. The Company believes that after considering all the available objective evidence, both positive and negative, historical and prospective, with greater weight given to historical evidence, it is more likely than not that the deferred tax assets will be realized and therefore reversed the valuation allowance against its net deferred tax asset in the third quarter of 2013. There was no change in the valuation allowance during the three and nine months ended September 30, 2014. The Company will continue to assess the valuation allowance against deferred tax assets considering all available information obtained in future reporting periods.

As of September 30, 2014, the Company had no material uncertain tax positions.

Note 15. Commitments and Contingencies

From time to time, the Company may be involved in lawsuits that arise in the normal course of its business. On December 4, 13 and 16, 2013, three derivative actions were filed in the Court of Chancery of the State of Delaware against the Company, certain of its officers and directors, Sanchez Resources, Altpoint Capital Partners LLC and Altpoint Sanchez Holdings, LLC (the "Consolidated Derivative Actions," Friedman v. A.R. Sanchez, Jr. et al., No. 9158; City of Roseville Employees' Retirement System v. A.R. Sanchez, Jr. et al., No. 9132; and Delaware County Employees Retirement Fund v. A.R. Sanchez, Jr. et al., No. 9165).

On December 20, 2013, the Consolidated Derivative Actions were consolidated, co-lead counsel for the plaintiffs was appointed and the plaintiffs were ordered to file an amended consolidated complaint (In re Sanchez Energy Derivative Litigation, Consolidated C.A. No. 9132-VCG, hereinafter, the "Delaware Derivative Action"). On January 28, 2014, a verified consolidated stockholder derivative complaint was filed. The Consolidated Derivative Actions concern the Company's purchase of working

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Sanchez Energy Corporation

Notes to the Condensed Consolidated Financial Statements (Continued)

(Unaudited)

Note 15. Commitments and Contingencies (Continued)

interests in the TMS from Sanchez Resources. Plaintiffs alleged breaches of fiduciary duty against the individual defendants as directors of the Company; breaches of fiduciary duty against Antonio R. Sanchez, III as an executive director of the Company; aiding and abetting breaches of fiduciary duty against Sanchez Resources, Eduardo Sanchez, Altpoint Capital Partners LLC and Altpoint Sanchez Holdings, LLC; and unjust enrichment against A.R. Sanchez, Jr. and Antonio R. Sanchez, III. All of the defendants filed a motion to dismiss on April 1, 2014. Briefing concerning the motions to dismiss concluded on June 27, 2014. A hearing was held on August 11, 2014, on the motions to dismiss, but the court has not ruled at this time. The Consolidated Derivative Actions are in their preliminary stages, and the Company is unable to reasonably predict an outcome or to reasonably estimate a range of possible loss.

On January 9, 2014, a derivative action was filed in 333rd district court in Harris County, Texas against the Company and certain of its officers and directors, styled Martin v. Sanchez, No. 2014-01028 (333rd Dist. Harris County, Texas) (the "Texas State Derivative Action"). The complaint alleged a breach of fiduciary duty, corporate waste and unjust enrichment against various officers and directors. No action has been taken to date and damages are unspecified. On March 14, 2014, this action was stayed following a ruling on the motion to dismiss in the Delaware Derivative Action. This action is in its preliminary stages and currently subject to the stay, and the Company is unable to reasonably predict an outcome or to estimate a range of reasonably possible loss.

On February 12, 2014, a derivative action was filed in the United States District Court for the Southern District of Texas, Houston Division, against the Company and certain of its officers and directors, styled Bartlinski v. Sanchez, No. 4:14-cv-00341 (S.D. Tex.) (the "Texas Federal Derivative Action"). The complaint alleged a violation of Section 14(a) of the Exchange Act and SEC Rule 14a-9. Defendants filed a motion to dismiss on April 10, 2014, and the motion was granted on August 8, 2014. After the court granted the motion to dismiss, the plaintiff filed a motion asking for permission to file an amended complaint. Defendants oppose this motion, and it is still pending.

Defendants believe that the allegations contained in the matters described above are without merit and intend to vigorously defend themselves against the claims raised.

In addition, in connection with the TMS transactions, the Company has committed to carry SR for its 50% working interest in an initial 3 gross (1.5 net) TMS wells to be drilled within the AMI. In the event that we do not fulfill in a timely manner our obligations with regard to the initial TMS well commitment we must re-assign the working interests acquired from SR. At the point that the minimum commitment is met, we will have fully paid for and earned all rights to the TMS acreage. We also have the right to continue drilling within the AMI after fulfilling the minimum well commitment by carrying SR for an additional 3 gross (1.5 net) TMS wells. We intend to carry SR in the additional 3 gross (1.5 net) TMS wells. We expect to meet our well carry commitments for the full 6 gross (3 net) TMS wells in early 2015.

In connection with the Catarina acquisition, the 77,000 acres of undeveloped acreage that were included in the acquisition are subject to a continuous drilling obligation. Initially, such drilling obligation requires us to drill, but not complete, (i) 50 wells in each annual period commencing on July 1, 2014 and (ii) at least one well in any consecutive 120-day period in order to maintain rights to any future undeveloped acreage. Initially, up to 30 wells drilled in excess of the minimum 50 wells in a

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Sanchez Energy Corporation

Notes to the Condensed Consolidated Financial Statements (Continued)

(Unaudited)

Note 15. Commitments and Contingencies (Continued)

given annual period can be carried over to satisfy part of the 50 well requirement in the subsequent annual period on a well for well basis. The lease also created a customary security interest in the production therefrom in order to secure royalty payments to the lessor and other lease obligations. Our current capital budget and plans include the drilling of at least the minimum number of wells required to maintain access to such undeveloped acreage.

As of September 30, 2014, the Company had $51.8 million in lease payment obligations that satisfy operating lease criteria. These obligations include: (i) $36.1 million for a new corporate office lease that commences in the fourth quarter of 2014 and has an expiration date in March 2025, (ii) $8.0 million for a ground lease agreement for land owned by the Calhoun Port Authority that commenced during the third quarter of 2014 and has an expiration date in August 2024 and (iii) $7.7 million for an acreage lease agreement for a promotional ranch managed by the Company in Kenedy County, Texas. This acreage lease agreement includes a contractual requirement for the Company to spend a minimum of $4 million to make permanent improvements over the ten year life of the lease. The lease agreement does not specify the timing for such improvements to be made within the lease term.

The Company's ground lease with the Calhoun Port Authority is terminable upon 180 days written notice by the Company to the lessor in addition to a $1 million termination payment. The Company has the right to terminate its lease obligation for its acreage in Kenedy County, Texas at any time without penalty with six months advanced written notice and payment of any accrued leasehold expenses.

Note 16. Subsidiary Guarantors

The Company filed a registration statement on Form S-3 with the SEC, which became effective on January 14, 2013 and registered, among other securities, debt securities. The subsidiaries of the Company named therein are co-registrants with the Company, and the registration statement registered guarantees of debt securities by such subsidiaries. As of September 30, 2014, such subsidiaries are 100 percent owned by the Company and any guarantees by these subsidiaries will be full and unconditional (except for customary release provisions). In the event that more than one of these subsidiaries provide guarantees of any debt securities issued by the Company, such guarantees will constitute joint and several obligations.

The Company also filed a registration statement on Form S-4 with the SEC, which became effective on June 20, 2014, pursuant to which the Company completed an offering of debt securities which are guaranteed by its subsidiaries named therein. As of September 30, 2014, such guarantor subsidiaries are 100 percent owned by the Company and the guarantees by these subsidiaries are full and unconditional (except for customary release provisions) and are joint and several.

The Company has no assets or operations independent of its subsidiaries and there are no significant restrictions upon the ability of its subsidiaries to distribute funds to the Company.

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Sanchez Energy Corporation

Notes to the Condensed Consolidated Financial Statements (Continued)

(Unaudited)

Note 17. Subsequent Events

In October 2014, the Company entered into the following crude oil swaps:

Contract Period	Derivative Instrument	Barrels	Purchased	Sold	Pricing Index
January 1, 2015 - December 31, 2015	Swap	182,500	$ 85.50	n/a	NYMEX WTI
January 1, 2016 - December 31, 2016	Swap	366,000	$ 80.00	n/a	NYMEX WTI
January 1, 2016 - December 31, 2016	Swap	183,000	$ 80.15	n/a	NYMEX WTI
January 1, 2016 - December 31, 2016	Swap	366,000	$ 80.15	n/a	NYMEX WTI
January 1, 2016 - December 31, 2016	Swap	183,000	$ 80.15	n/a	NYMEX WTI

In October 2014, the Company entered into the following natural gas swaps:

Contract Period	Derivative Instrument	Mmbtu	Purchased	Sold	Pricing Index
January 1, 2015 - December 31, 2015	Swap	3,650,000	$ 3.91	n/a	NYMEX NG
January 1, 2016 - December 31, 2016	Swap	3,660,000	$ 3.92	n/a	NYMEX NG

In October 2014, the Company modified certain crude oil swaps to create the following crude oil enhanced swaps:

Contract Period	Derivative Instrument	Barrels	Purchased	Put	Pricing Index
January 1, 2015 - December 31, 2015	Enhanced Swap	365,000	$ 92.15	$ 72.50	NYMEX WTI
January 1, 2015 - December 31, 2015	Enhanced Swap	365,000	$ 92.60	$ 72.50	NYMEX WTI
January 1, 2015 - December 31, 2015	Enhanced Swap	365,000	$ 90.93	$ 72.50	NYMEX WTI

The modifications to these derivative transactions did not change the contract periods, volumes or counterparties. Further, there were no changes to the respective fair values of each crude oil swap on the condensed consolidated balance sheet as of September 30, 2014.

In November 2014, the Company entered into the following natural gas enhanced swap:

Contract Period	Derivative Instrument	Mmbtu	Purchased	Sold	Pricing Index
January 1, 2015 - December 31, 2015	Enhanced Swap	3,650,000	$ 4.27	$ 3.75	NYMEX NG

Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations

The following discussion and analysis of our financial condition and results of operations should be read in conjunction with our condensed consolidated financial statements and related notes appearing in Part I, Item 1 of this Quarterly Report on Form 10-Q and information contained in our 2013 Annual Report. The following discussion contains "forward-looking statements" that reflect our future plans, estimates, beliefs and expected performance. Please see "Cautionary Note Regarding Forward-Looking Statements."

Business Overview

Sanchez Energy Corporation, a Delaware corporation formed in August 2011, is an independent exploration and production company focused on the exploration, acquisition and development of unconventional oil and natural gas resources in the onshore U.S. Gulf Coast, with a current focus on the Eagle Ford Shale in South Texas and, to a lesser extent, the TMS in Mississippi and Louisiana. We have accumulated approximately 226,000 net leasehold acres in the oil and condensate, or black oil and volatile oil, windows of the Eagle Ford Shale and approximately 61,000 net leasehold acres in what we believe to be the core of the TMS. We are currently focused on the horizontal development of significant resource potential from the Eagle Ford Shale, with plans to invest approximately 92% of our 2014 drilling and completion capital budget in this area. We are continuously evaluating opportunities to grow both our acreage and our producing assets through acquisitions. Our successful acquisition of such assets will depend on both the opportunities and the financing alternatives available to us at the time we consider such opportunities. During 2013, we significantly expanded our proved reserves, production and undeveloped acreage through a series of acquisitions beginning with the Cotulla acquisition in the Eagle Ford Shale in South Texas, which we closed on May 31, 2013. We acquired 44,461 net acres in Dimmit, Frio, LaSalle and Zavala Counties of South Texas with 53 gross wells producing an estimated average of approximately 4,950 boe/d for the month of May 2013. The acquisition included estimated proved reserves as of March 31, 2013 of 14.2 mboe, 66% oil, 13% NGLs and 21% natural gas, with proved developed reserves estimated to account for approximately 48% of total proved reserves. We combined our new Cotulla assets with our previous Maverick area to form one operating area now known as our Cotulla area.

In July 2013, we acquired approximately 10,300 net acres and approximately 250 boe/d of estimated production in Fayette, Gonzales and Lavaca Counties, Texas for approximately $29 million. This acquisition, now known as our Five Mile Creek development within our Marquis Area, is directly to the northwest of our Prost development project.

On August 16, 2013, we completed an asset acquisition of approximately 40,000 net undeveloped acres in the TMS in Southwest Mississippi and Southeast Louisiana and the formation of an area of mutual interest and a 50/50 joint venture with our affiliate, SR. The joint venture currently controls approximately 138,000 gross and 100,000 net acres in what we believe to be the core of the TMS.

On October 4, 2013, we closed our Wycross acquisition in the Eagle Ford Shale. At the effective date of July 1, 2013, this acquisition added approximately 11 mboe of net proved reserves, 2,000 boe/d of production and 3,600 net contiguous acres of leasehold in McMullen County, Texas.

On June 30, 2014, we closed our Catarina acquisition in the Eagle Ford Shale with an effective date of January 1, 2014. Including the approximate $51 million deposit paid prior to closing, total consideration for the acquisition was approximately $559 million, comprised of the $639 million purchase price less approximately $80 million in normal and customary closing adjustments. The purchase price is subject to customary post-closing adjustments. Proved reserves as of the effective date were estimated to be approximately 60 mboe and were 57 mboe as of June 30, 2014 as a result of normal declines. The reserves that were produced were not replaced from the effective time to the

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closing date due to the substantial decrease in drilling and completion activity by the seller. Production during the time period from effective date to closing averaged approximately 22,200 boe/d.

All proved reserves are covered under lease acreage that is held by production, which acreage amounted to approximately 29,000 acres. Under the lease we have a 100% working interest and 75% net revenue interest in the lease acreage over the Eagle Ford Shale formation from the top of the Austin Chalk formation to the base of the Buda Lime formation. Each producing horizontal well that is not in an existing unit already held by production holds 320 acres by its production. The 77,000 acres of undeveloped acreage that were included in the acquisition are subject to a continuous drilling obligation. Initially, such drilling obligation requires us to drill, but not complete, (i) 50 wells in each annual period commencing on July 1, 2014 and (ii) at least one well in any consecutive 120-day period in order to maintain rights to any future undeveloped acreage. Initially, up to 30 wells drilled in excess of the minimum 50 wells in a given annual period can be carried over to satisfy part of the 50 well requirement in the subsequent annual period on a well for well basis. The lease also created a customary security interest in the production therefrom in order to secure royalty payments to the lessor and other lease obligations. Our current capital budget and plans include the drilling of at least the minimum number of wells required to maintain access to such undeveloped acreage.

Basis of Presentation

The condensed consolidated financial statements have been prepared in accordance with U.S. GAAP.

Our Properties

Eagle Ford Shale

We and our predecessor entities have a long history in the Eagle Ford Shale, where we have assembled approximately 226,000 net leasehold acres with an average working interest of approximately 93%. Using approximately 40 acre well-spacing for our Cotulla and Palmetto areas, approximately 60 acre well-spacing for our Marquis area, and approximately 75 acre well-spacing for our Catarina area plus up to 650 additional upper Eagle Ford Catarina locations, and assuming 80% of the acreage is drillable for Cotulla, Marquis and Catarina, and 90% of the acreage is drillable for Palmetto, we believe that there could be up to 3,600 gross (3,400 net) locations for potential future drilling. Consistent with other operators in this area, we perform multi-stage hydraulic fracturing up to 30 stages on each well depending upon the length of the lateral section. For the year 2014, we plan to invest substantially all of our capital budget in the Eagle Ford Shale.

In our Marquis area, we have approximately 71,000 net operated acres, the majority of which are in southwest Fayette and northeast Lavaca Counties, Texas with a 100% working interest. We believe that our Marquis acreage lies in the volatile oil window, where we anticipate drilling, completion and facilities costs on our acreage to be between $7 million and $11 million per well based on our historical well costs. We have drilled 40 horizontal wells in our Prost area of Marquis that had average 30 day production rates of approximately 700 boe/d. We have drilled 6 horizontal wells in our Five Mile Creek area of Marquis that had average 30 day production rates of approximately 500 boe/d. We have identified up to 900 gross and net locations based on 60 acre well-spacing for potential future drilling on our Marquis acreage. For the year 2014, we plan to spend $270 - $285 million to spud 35 net wells and complete 32 net wells in our Marquis area.

In our Cotulla area, we have approximately 40,000 net acres in Dimmit, Frio, LaSalle, Zavala and McMullen Counties, Texas with an average working interest of approximately 85%. We believe that our Cotulla acreage lies in the black oil window, where we anticipate drilling, completion and facilities costs on our acreage to be between $5.5 million and $9.0 million per well based on our historical well costs. Our primary focus areas in our Cotulla area are our Alexander Ranch and Wycross development projects. In our Alexander Ranch development project, 42 wells have been brought online with average 30 day production rates of approximately 500 boe/d. In our Wycross development project, 27 wells have been brought online with average 30 day production rates of approximately 600 boe/d. We have identified up to 740 gross (700 net) locations based on 40 acre well-spacing for potential future drilling on our Cotulla area. For the year 2014, we plan to spend $190 - $210 million to spud and complete 28 net wells in our Cotulla area.

In our Palmetto area, we have approximately 9,000 net acres in Gonzales County, Texas with an average working interest of approximately 48%. We believe that our Palmetto acreage lies in the volatile oil window, where we anticipate drilling, completion and facilities costs on our acreage to be between $7 million and $11 million per well based on our historical well costs. We have participated in the drilling of 59 gross wells on our acreage that had an average 30 day production rates of approximately 900 boe/d. We have identified up to 365 gross (175 net) locations based on 40 acre well-spacing for potential future drilling in our Palmetto area. For the year 2014, we plan to spend $45 - $55 million to spud 5 and complete 8 net wells in our Palmetto area.

In our Catarina area, we have approximately 106,000 net acres in Dimmit, LaSalle and Webb Counties, Texas with a 100% working interest. We recently brought online 9 upper Eagle Ford wells that were drilled by the previous operator with initial average 24 hour production rates of approximately 1,400 boe/d. For the year 2014, we plan to spend $205 - $215 million to spud 25 and complete 37 net wells in our Catarina area.

Tuscaloosa Marine Shale

In August 2013, we acquired approximately 40,000 net undeveloped acres in what we believe to be the core of the TMS for cash and shares of our common stock plus an initial 3 gross (1.5 net) well drilling carry. In connection with the TMS transactions, we established an AMI in the TMS with SR. As part of the transaction, we acquired all of the working interests in the AMI owned at closing from three sellers (two third parties and one related party of the Company, SR), resulting in our owning an undivided 50% working interest across the AMI through the TMS formation. The AMI currently holds rights to approximately 138,000 gross acres and 100,000 net acres.

Total consideration for the transactions consisted of approximately $70 million in cash and the issuance of 342,760 common shares of the Company, valued at $7.5 million. The total cash consideration provided to SR, an affiliate of the Company, was $14.4 million. The acquisitions were accounted for as the purchase of assets at cost at the acquisition date.

We have also committed, as a part of the total consideration, to carry SR for its 50% working interest in an initial 3 gross (1.5 net) TMS wells to be drilled within the AMI. In the event that we do not fulfill in a timely manner our obligations with regard to the initial TMS well commitment we must re-assign the working interests acquired from SR. At the point that the minimum commitment is met, we will have fully paid for and earned all rights to the TMS acreage. We also have the right to continue drilling within the AMI after fulfilling the minimum well commitment by carrying SR for an additional 3 gross (1.5 net) TMS wells. We intend to carry SR in the additional 3 gross (1.5 net) TMS wells. We expect to meet our well carry commitments for the full 6 gross (3 net) TMS wells in early 2015.

Recent well results by other operators in the area are encouraging with respect to both strong well performance and decreasing drilling and completion costs. We plan to allocate approximately 7%, or $60 - $65 million of our total 2014 capital budgets to this area. The average remaining lease term on the acreage is over 3 years, giving us ample time to allow other industry participants to further de-risk the play.

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Outlook

As an oil and natural gas company, we face the challenge of natural production declines. As initial reservoir pressures are depleted, oil and natural gas production from a given well or formation decreases. Our future growth will depend on our ability to continue to add new reserves in excess of our production. Accordingly, we plan to maintain our focus on adding reserves through development projects associated with our current property base, improving the economics of producing oil and natural gas from our properties and selected step-out and exploratory drilling activities. In addition, we regularly review acquisition opportunities from third parties or other members of the Sanchez Group. Our ability to add estimated reserves through acquisitions and development projects is dependent on many factors, including our ability to raise capital, obtain regulatory approvals and procure contract drilling rigs and personnel. Volatility in commodity prices and sustained periods of low prices for oil or natural gas could materially and adversely affect our financial position, our results of operations, the quantities of oil and natural gas reserves that we can economically produce, the price of our common stock, and our access to capital.

The average oil price, WTI Cushing, used in the SEC pricing methodology for calculating the PV-10 and Standardized Measures and for performing impairment tests under the full cost method, calculated as the unweighted arithmetic average of the first-day-of-the-month price for each month within the 12-month period ended September 30, 2014 was $99.08 per barrel and the average natural gas price, at Henry Hub, and calculated in the same manner, was $4.24 per Mmbtu. The first-day-of-the-month oil prices for October and November 2014 were $90.73 and $80.54 per barrel, respectively, resulting in an average oil price for the 12-month period ended November 30, 2014 of $96.96 per barrel, a decrease of approximately 2% as compared to the 12-month period ended September 30, 2014 average price. The first-day-of-the-month natural gas prices for October and November 2014 were $4.14 and $3.80, respectively, resulting in an average natural gas price for the 12-month period ended November 30, 2014 of $4.31 per Mmbtu, an increase of approximately 2%. If the current downward trend in oil prices continues, there is a reasonable likelihood that the Company could incur an impairment to our full cost pool in 2015.

The Company manages its exposure to volatile commodity prices in several ways. First, the Company actively manages a commodity price hedging program. Currently, approximately 41% of the mid-point of our estimated 2015 oil and natural gas production is hedged with an average floor or swap price of approximately $90 per barrel of oil and approximately $4.15 per Mmbtu of natural gas. Second, the Company believes that cautious use of leverage and the maintenance of substantial liquidity is an important tool in managing exposure to fluctuating commodity prices and with respect to overall financial management. For the twelve month period ended September 30, 2014, the Company had a total debt to pro forma Adjusted EBITDA ratio of 2.7x and net debt to pro forma Adjusted EBITDA ratio of 1.8x. The Company has reconciled reported net income (loss) to pro forma Adjusted EBITDA for the twelve month period ended September 30, 2014 in "Non-GAAP Financial Measures" below. Available liquidity (cash and cash equivalents along with the elected commitment amount under our unused borrowing base) was approximately $896 million. Third, even after consideration of the drilling requirements resulting from our Catarina acquisition, referenced in Note 15 "Commitments and Contingencies," the Company has considerable flexibility with respect to its capital spending plans as its acreage position is largely either held by production and/or has acceptable lease renewal terms and as a matter of policy the Company has not made material long term commitments for critical service sector needs such as drilling rigs. As such, the Company has the ability to manage its capital spending in response to a changing commodity price environment.

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Results of Operations

Three Months Ended September 30, 2014 Compared to Three Months Ended September 30, 2013

Revenue and Production

The following table summarizes production, average sales prices and operating revenue for our oil, NGLs and natural gas operations for the periods indicated (in thousands, except average sales price and percentages):

	Three Months Ended September 30,		Increase (Decrease) 2014 vs 2013	
	2014	**2013**	**$**	**%**
Net Production:				
Oil (mbo)	1,682	826	856	104%
Natural gas liquids (mbbl)	964	106	858	*
Natural gas (mmcf)	5,440	906	4,534	*
Total oil equivalent (mboe)	3,552	1,083	2,469	228%
Average Sales Price[(1)]:				
Oil ($ per bo)	$ 93.87	$ 105.86	$ (11.99)	(11)%
Natural gas liquids ($ per bbl)	$ 28.34	$ 30.03	$ (1.69)	(6)%
Natural gas ($ per mcf)	$ 4.07	$ 3.94	$ 0.13	3%
Oil equivalent ($ per boe)	$ 58.37	$ 86.96	$ (28.59)	(33)%
REVENUES[(1)]:				
Oil sales	$ 157,907	$ 87,436	$ 70,471	81%
Natural gas liquids sales	27,309	3,190	24,119	*
Natural gas sales	22,134	3,574	18,560	*
Total revenues	$ 207,350	$ 94,200	$ 113,150	120%