TRANS ENERGY INC
Form 10-Q
November 19, 2014
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UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

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

For the quarterly period ended September 30, 2014

OR

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

For the transition period from __________ to __________

Commission File Number 0-23530

TRANS ENERGY, INC.

(Exact name of registrant as specified in its charter)

Nevada	**93-0997412**
(State or other jurisdiction of	**(I.R.S. Employer**
incorporation or organization)	**Identification No.)**

210 Second Street, P.O. Box 393, St. Marys, West Virginia 26170

(Address of principal executive offices)

Registrant s telephone number, including area code: (304) 684-7053

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 past 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes x No ¨

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 x No ¨

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See the definitions of large accelerated filer, accelerated filer and smaller reporting company in Rule 12b-2 of the Exchange Act.

Large accelerated filer ¨	Accelerated filer ¨
Non-accelerated filer ¨ (Do not check if smaller reporting company)	Smaller reporting company x

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

Indicate the number of shares outstanding of each of the issuer s classes of common stock, as of the latest practicable date.

Class	Outstanding as of November 19, 2014
Common Stock, $0.001 par value	**14,404,260**

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PART I FINANCIAL INFORMATION

Item 1. Financial Statements

TRANS ENERGY, INC. AND SUBSIDIARIES

Condensed Consolidated Balance Sheets

Unaudited

	September 30, 2014 Unaudited	December 31, 2013 Audited
ASSETS		
CURRENT ASSETS		
Cash	$ 1,316,254	$ 2,727,832
Accounts receivable, trade	6,883,543	4,460,535
Accounts receivable from drilling operator	562,000	
Accounts receivable, related parties	18,500	18,500
Derivative assets	780,148	
Advance royalties		16,937
Prepaid expenses	1,090,689	1,065,061
Deferred financing costs, net of amortization of $337,054 and $1,308,817, respectively	1,028,142	817,938
Total current assets	11,679,276	9,106,803
OIL AND GAS PROPERTIES, USING SUCCESSFUL EFFORTS ACCOUNTING		
Proved properties	99,952,561	77,961,183
Unproved properties	7,536,331	15,092,783
Pipelines	1,259,052	1,397,440
Accumulated depreciation, depletion and amortization	(21,036,700)	(14,473,069)
Oil and gas properties, net	87,711,244	79,978,337
PROPERTY AND EQUIPMENT, net of accumulated depreciation of $344,518 and $317,704, respectively	524,718	587,218
OTHER ASSETS		
Deferred financing costs	3,341,461	139,076
Other assets	355,381	303,887
Total other assets	3,696,842	442,963
TOTAL ASSETS	$ 103,612,080	$ 90,115,321

See notes to unaudited condensed consolidated financial statements.

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TRANS ENERGY, INC. AND SUBSIDIARIES

Condensed Consolidated Balance Sheets (continued)

Unaudited

	September 30, 2014 Unaudited	December 31, 2013 Audited
LIABILITIES AND STOCKHOLDERS EQUITY		
CURRENT LIABILITIES		
Accounts payable, trade	$ 359,836	$ 632,795
Accounts payable due to drilling operator	6,382,401	2,698,302
Accounts payable, related party	1,500	1,500
Accrued expenses	4,418,063	5,302,816
Deferred gain on sale of assets	6,959,817	
Environmental settlement and related costs	3,600,000	
Revenue payable	45,284	127,106
Commodity derivative liability	217,451	58,176
Notes payable current	104,325,704	14,897
Notes payable, related party		205,314
Total current liabilities	126,310,056	9,040,906
LONG-TERM LIABILITIES		
Notes payable, net	0	89,204,102
Environmental settlement and related costs	3,000,000	
Asset retirement obligations	78,556	41,440
Commodity derivative liability	831,106	67,597
Total long-term liabilities	108,227,177	89,313,139
Total liabilities	3,909,662	98,354,045
COMMITMENTS AND CONTINGENCIES		
STOCKHOLDERS EQUITY		
Preferred stock; 10,000,000 shares authorized at $0.001 par value; -0- shares issued and outstanding		
Common stock; 500,000,000 shares authorized at $0.001 par value; 14,406,260 and 13,457,978 shares issued, respectively, and 14,404,260 and 13,455,978 shares outstanding, respectively	14,406	13,458
Additional paid-in capital	43,970,530	42,556,292
Treasury stock, at cost, 2,000 shares	(1,950)	(1,950)
Accumulated deficit	(70,590,624)	(50,806,524)
Total stockholders equity (deficit)	(26,607,638)	(8,238,724)
TOTAL LIABILITIES AND STOCKHOLDERS EQUITY	$ 103,612,080	$ 90,115,321

See notes to unaudited condensed consolidated financial statements.

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TRANS ENERGY, INC. AND SUBSIDIARIES

Condensed Consolidated Statements of Operations (Unaudited)

	For the Three Months Ended September 30, 2014	For the Three Months Ended September 30, 2013	For the Nine Months Ended September 30, 2014	For the Nine Months Ended September 30, 2013
OPERATING REVENUES				
Oil and gas sales	$ 6,667,618	$ 4,343,739	$ 24,816,633	$ 12,559,344
Gas transportation, gathering, and processing	44,256	35,203	121,875	97,093
Other income	63,407	25,801	69,840	28,790
Total operating revenues	6,775,281	4,404,743	25,008,348	12,685,227
OPERATING COSTS AND EXPENSES				
Production costs	3,258,132	2,795,073	10,003,364	7,363,564
Depreciation, depletion, amortization and accretion	3,088,104	986,670	7,448,799	2,365,280
Environmental settlement and related costs	6,600,000		6,600,000	
Selling, general and administrative	1,176,853	1,633,112	4,159,149	4,733,539
Total operating costs and expenses	14,123,089	5,414,855	28,211,312	14,462,383
(Loss) Gain on sale of assets	(18,480)	6,887	188,616	(1,900)
LOSS FROM OPERATIONS	(7,366,288)	(1,003,225)	(3,014,348)	(1,779,056)
OTHER INCOME (EXPENSES)				
Interest income	550	3,463	2,045	18,142
Interest expense	(2,903,312)	(5,200,628)	(16,709,264)	(11,002,002)
Gain on warrant derivatives		3,806		595,245
Gain (loss) on derivative assets	2,963,096	100,796	(62,533)	760,152
Total other income (expenses)	60,334	(5,092,563)	(16,769,752)	(9,628,463)
NET LOSS BEFORE INCOME TAXES	(7,305,954)	(6,095,788)	(19,784,100)	(11,407,519)
INCOME TAX				
NET LOSS	$ (7,305,954)	$ (6,095,788)	$ (19,784,100)	$ (11,407,519)
NET LOSS PER SHARE BASIC AND DILUTED	$ (.52)	$ (.46)	$ (1.44)	$ (.86)
WEIGHTED AVERAGE SHARES BASIC AND DILUTED	14,026,790	13,317,978	13,742,149	13,264,077

See notes to unaudited condensed consolidated financial statements.

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TRANS ENERGY, INC. AND SUBSIDIARIES

Condensed Consolidated Statements of Cash Flows

(Unaudited)

	For the Nine Months Ended September 30, 2014	2013
CASH FLOWS FROM OPERATING ACTIVITIES:		
Net loss	$ (19,784,100)	$ (11,407,519)
Adjustments to reconcile net loss to net cash provided (used) by operating activities:		
Depreciation, depletion, amortization and accretion	7,448,799	2,365,280
Amortization of financing costs and debt discount	8,426,119	3,484,843
Share-based compensation	698,122	919,755
(Gain) loss on sale of assets	(188,616)	1,900
Interest and legal expense added to principal	1,818,240	3,329,349
Unrealized gain on warrant derivative		(595,245)
Unrealized loss (gain) on commodity derivative assets	142,636	(522,733)
Realized gain on commodity derivative assets	(80,103)	
Changes in operating assets and liabilities:		
Accounts receivable, trade	(2,423,008)	(453,245)
Accounts receivable due from operator, net	(562,000)	(2,098,899)
Prepaid expenses and other current assets	(8,691)	(250,662)
Other assets	(51,494)	(1,471)
Accounts payable and accrued expenses	47,444	1,646,322
Environmental settlement and related costs	6,600,000	
Revenue payable	(81,822)	(75,659)
Net cash provided (used) by operating activities	2,001,526	(3,657,984)
CASH FLOWS FROM INVESTING ACTIVITIES:		
Proceeds from sale of assets	15,259,668	2,625,025
Expenditures for oil and gas properties	(24,064,991)	(23,829,183)
Expenditures for property and equipment	(8,470)	(9,141)
Net cash used by investing activities	(8,813,793)	(21,213,299)
CASH FLOWS FROM FINANCING ACTIVITIES:		
Financing costs paid	(4,706,656)	(122,230)
Payments on notes payable	(98,703,469)	(16,212)
Proceeds from notes payable	108,093,750	25,000,000
Stock options exercised	717,064	13,750
Net cash provided by financing activities	5,400,689	24,875,308
NET CHANGE IN CASH	(1,411,578)	4,025

CASH, BEGINNING OF PERIOD		2,727,832		1,009,084
CASH, END OF PERIOD	$	1,316,254	$	1,013,109
SUPPLEMENTAL DISCLOSURES FOR CASH FLOW INFORMATION:				
CASH PAID FOR:				
Interest	$	8,550,179	$	4,482,229
Income taxes				
Non-cash investing and financing activities:				
Accrued expenditures for oil and gas properties	$	3,684,099	$	1,112,214
Increase in asset retirement obligation	$	37,116	$	689
Accrued expenditures for debt financing	$		$	401,625

See notes to unaudited condensed consolidated financial statements.

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TRANS ENERGY, INC. AND SUBSIDIARIES

Notes to Condensed Consolidated Financial Statements (Unaudited)

NOTE 1 BASIS OF FINANCIAL STATEMENT PRESENTATION AND SIGNIFICANT ACCOUNTING POLICIES

The accompanying unaudited interim condensed consolidated financial statements have been prepared by Trans Energy, Inc., (Trans Energy, we, our, us, or the Company), in accordance with accounting principles generally accepted in the United States of America (GAAP) for interim financial information and with the instructions to Form 10-Q and Rule 8-03 of Regulation S-X. Accordingly, they do not include certain information and footnote disclosures normally included in a full set of financial statements prepared in accordance with GAAP. The information furnished in the interim condensed consolidated financial statements includes normal recurring adjustments and reflects all adjustments, which, in the opinion of management, are necessary for a fair presentation of such financial statements. Although management believes the disclosures and information presented are adequate to make the information not misleading, these interim consolidated financial statements should be read in conjunction with our most recent audited consolidated financial statements and notes thereto included in our December 31, 2013 Annual Report on Form 10-K. Operating results for the nine months ended September 30, 2014 are not necessarily indicative of the results that may be expected for the year ending December 31, 2014.

On May 21, 2014 (Funding Date), the Company s wholly-owned subsidiary, American Shale Development Inc. (American Shale), entered into a purchase and sale agreement (the Republic PSA) with its joint venture partner, Republic Energy Ventures (Republic). Under the Republic PSA, for $15 million, American Shale sold (i) an undivided interest across certain of its undeveloped leasehold amounting to approximately 2,239 net acres, (ii) an over-riding royalty interest of 1.5% in certain of its leasehold in Wetzel County, West Virginia, and (iii) an over-riding royalty interest of 1.0% in six (6) wells that are currently being drilled in Marshall County, West Virginia. The consideration was paid in the form of a credit against expenses incurred by Republic on behalf of American Shale. American Shale reserved the right to receive 25% of the net profits earned by Republic on the assets sold by American Shale under the Republic PSA. American Shale has the option to repurchase the undivided interest across all of its undeveloped leasehold, plus the over-riding royalty interest in its Wetzel County leasehold, for $15 million if (i) such payment is made within six (6) months of the Funding Date, or (ii) a purchase and sale agreement that would allow for such repayment by American Shale is signed within such period and the transaction contemplated therein is closed prior to December 31, 2014. The Company has recognized a deferred gain on sale of assets in the current liabilities section of the Condensed Consolidated Balance Sheet in the amount of $6,959,816 because the Company has the option of repurchasing the undivided interest across all of its undeveloped leasehold, plus the overriding royalty interest in its Wetzel County leasehold by December 31, 2014.

Although the deferred gain of $6,959,816 noted above represents a credit on our balance sheet that will never be repaid in cash (i.e., it will either be realized in earnings upon expiration of American Shale s repurchase option, or will be reclassified back to American Shale s property balance upon its exercise of the repurchase option), we believe that such amount results in our current ratio not exceeding 1-to-1 as of September 30, 2014, as required by the covenants of our out credit agreement (the Credit Agreement) with Morgan Stanley Capital Group Inc. (Morgan Stanley), as the administrative agent, and several lenders thereunder (collectively, the Lenders).

The Credit Agreement provides that the failure to observe any financial covenant will constitute an event of default, and Morgan Stanley, at the request of the majority Lenders, may terminate the commitments under the Credit Agreement and cause all of the Company s obligations under the Credit Agreement to immediately become due and payable, upon notice to the Company. The event of default is deemed continuing until waived in writing by the

Lenders. The Company has entered into discussions with the Lenders in hopes of obtaining a favorable resolution to the situation. No assurances can be given at this time that the matter will be resolved in a satisfactory manner.

In the event we are unable to obtain a waiver of default from the Lenders, there would be substantial doubt about our ability to continue as a going concern as all outstanding obligations under the Credit Agreement would come due. Consequently, all outstanding obligations under the Credit Agreement as of September 30, 2014 are reflected on the balance sheet as current maturities on long-term debt.

Significant Accounting Policies

The accounting policies followed by the Company are set forth in Note 1 to the Company s consolidated financial statements in the 2013 Form 10-K, and are supplemented by the notes to the unaudited condensed consolidated financial statements in this report.

Nature of Operations and Organization

We are an independent energy company engaged in the acquisition, exploration, development, exploitation and production of oil and natural gas. Our operations are presently focused in the State of West Virginia.

Principles of Consolidation

The unaudited consolidated financial statements include Trans Energy and our wholly-owned subsidiaries, Prima Oil Company, Inc. (Prima), Ritchie County Gathering Systems, Inc., Tyler Construction Company, Inc., American Shale Development, Inc. (American Shale or ASD), and Tyler Energy, Inc., and interests with joint venture partners, which are accounted for under the proportional consolidation method. All significant inter-company balances and transactions have been eliminated in consolidation.

Use of Estimates

The preparation of financial statements in conformity with GAAP 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. Actual results could differ from those estimates. Our financial statements are based on a number of significant estimates, including oil and gas reserve quantities which are the basis for the calculation of depreciation, depletion, amortization, and impairment of oil and gas properties, timing and costs associated with our asset retirement obligations, estimates of fair value of derivative instruments and estimates used in stock-based compensation calculations. Reserve estimates are by their nature inherently imprecise.

Financing Costs

In connection with obtaining the Morgan Stanley financing in May 2014 and subsequent borrowings, we incurred fees and expenses of $4,706,656. These fees and expenses were recorded as financing costs and are being amortized over the life of the loan using the straight-line method, which approximates the effective interest method.

In October 2013 we reached a settlement with Oppenheimer & Co., Inc. (Opco) which related to the amount of the fee which was earned by Opco acting as our investment banker in assisting the Company in obtaining funding (Tranche A) with Chambers Energy Capital (Chambers). We recorded $401,625 in financing fees related to the settlement. The Opco financing fees were being amortized over the same period as the Tranche A loan. In addition, when we obtained new financing in February 2013 and April 2012, we incurred $122,230 in fees d