

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

FORM 10-Q

(Mark One)

- QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934 FOR THE QUARTERLY PERIOD ENDED September 30, 2020**
- TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934 FOR THE TRANSITION PERIOD FROM _____ TO _____**

COMMISSION FILE NUMBER: 001-16071

ABRAXAS PETROLEUM CORPORATION

(Exact name of registrant as specified in its charter)

Nevada
(State of Incorporation)

74-2584033
(I.R.S. Employer Identification No.)

18803 Meisner Drive, San Antonio, TX 78258
(Address of principal executive offices) (Zip Code)

210-490-4788
(Registrant's telephone number, including area code)

Not Applicable

(Former name, former address and former fiscal year, if changed since last report)

Securities registered pursuant to Section 12(b) of the Act:

Title of each class	Trading Symbol	Name of each exchange on which registered:
Common Stock, par value \$.01 per share	AXAS	The NASDAQ Stock Market, LLC

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 the filing requirements for the past 90 days. Yes No

Indicate by check mark whether the registrant has submitted electronically every Interactive Data File required to be submitted 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 such files). Yes No

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

- Large accelerated filer Accelerated filer
Non-accelerated filer Smaller reporting company
Emerging growth company

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

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

The number of shares of the issuer's common stock outstanding as of November 6, 2020 was 8,403,465.

The terms “Abraxas,” “Abraxas Petroleum,” “we,” “us,” “our” or the “Company” refer to Abraxas Petroleum Corporation and all of its subsidiaries, including Raven Drilling, LLC.

All share and per share data has been retroactively adjusted to reflect the 1-for-20 reverse stock split effective October 19, 2020, as described in Note 2 to our consolidated financial statements.

Forward-Looking Information

We make forward-looking statements throughout this report. Whenever you read a statement that is not simply a statement of historical fact (such as statements including words like “believe,” “expect,” “anticipate,” “intend,” “will,” “plan,” “seek,” “may,” “estimate,” “could,” “potentially” or similar expressions), you must remember that these are forward-looking statements, and that our expectations may not be correct, even though we believe they are reasonable. The forward-looking information contained in this report is generally located in the material set forth under the headings “Management’s Discussion and Analysis of Financial Condition and Results of Operations” but may be found in other locations as well. These forward-looking statements generally relate to our plans and objectives for future operations and are based upon our management’s reasonable estimates of future results or trends. The factors that may affect our expectations regarding our operations include, among others, the following:

- the prices we receive for our production and the effectiveness of our hedging activities;
- the availability of capital including under our credit facility;
- our success in development, exploitation and exploration activities;
- declines in our production of oil and gas;
- our indebtedness and the significant amount of cash required to service our indebtedness;
- the proximity, capacity, cost and availability of pipelines and other transportation facilities;
- limits on our growth and our ability to finance our operations, fund our capital needs and respond to changing conditions imposed by our bank credit facility and restrictive debt covenants;
- our ability to make planned capital expenditures;
- ceiling test write-downs resulting, and that could result in the future, from lower oil and natural gas prices;
- global or national health concerns, including the outbreak of pandemic or contagious disease, such as the coronavirus (COVID-19);
- political and economic conditions in oil producing countries, especially those in the Middle East;
- price and availability of alternative fuels;
- our ability to procure services and equipment for our drilling and completion activities;
- our acquisition and divestiture activities;
- weather conditions and events; and
- other factors discussed elsewhere in this report.

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

GLOSSARY OF TERMS

Unless otherwise indicated in this report, gas volumes are stated at the legal pressure base of the State or area in which the reserves are located at 60 degrees Fahrenheit. Oil and gas equivalents are determined using the ratio of six Mcf of gas to one barrel of oil, condensate or natural gas liquids.

The following definitions apply to the technical terms used in this report.

Terms used to describe quantities of oil and gas:

“**Bbl**” – barrel or barrels.

“**Bcf**” – billion cubic feet of gas.

“**Bcfe**” – billion cubic feet of gas equivalent.

“**Boe**” – barrels of oil equivalent.

“**Boed or Boepd**” – barrels of oil equivalent per day.

“**MBbl**” – thousand barrels.

“**MBoe**” – thousand barrels of oil equivalent.

“**Mcf**” – thousand cubic feet of gas.

“**Mcfe**” – thousand cubic feet of gas equivalent.

“**MMBbl**” – million barrels.

“**MBoe**” – million barrels of oil equivalent.

“**MMBtu**” – million British Thermal Units of gas.

“**MMcf**” – million cubic feet of gas.

“**MMcfe**” – million cubic feet of gas equivalent.

“**NGL**” – natural gas liquids measured in barrels.

Terms used to describe our interests in wells and acreage:

“**Developed acreage**” means acreage which consists of leased acres spaced or assignable to productive wells.

“**Development well**” is a well drilled within the proved area of an oil or gas reservoir to the depth or stratigraphic horizon (rock layer or formation) noted to be productive for the purpose of extracting reserves.

“**Dry hole**” is an exploratory or development well found to be incapable of producing either oil or gas in sufficient quantities to justify completion.

“**Exploratory well**” is a well drilled to find and produce oil and or gas in an unproved area, to find a new reservoir in a field previously found to be producing in another reservoir, or to extend a known reservoir.

“**Gross acres**” are the number of acres in which we own a working interest.

“**Gross well**” is a well in which we own a working interest.

“**Net acres**” are the sum of fractional ownership working interests in gross acres (e.g., a 50% working interest in a lease covering 320 gross acres is equivalent to 160 net acres).

“**Net well**” is the sum of fractional ownership working interests in gross wells.

“**Productive well**” is an exploratory or a development well that is not a dry hole.

“**Undeveloped acreage**” means those leased acres on which wells have not been drilled or completed to a point that would permit the production of economic quantities of oil and gas, regardless of whether such acreage contains proved reserves.

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Terms used to assign a present value to or to classify our reserves:

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

- (i) Through existing wells with existing equipment and operating methods or in which the cost of the required equipment is relatively minor compared to the cost of a new well; and
- (ii) Through installed extraction equipment and infrastructure operational at the time of the reserves estimate if the extraction is by means not involving a well.

“**Proved developed non-producing reserves***” are those quantities of oil and gas reserves that are developed behind pipe in an existing well bore, from a shut-in well bore or that can be recovered through improved recovery only after the necessary equipment has been installed, or when the costs to do so are relatively minor. Shut-in reserves are expected to be recovered from (1) completion intervals which are open at the time of the estimate but which have not started producing, (2) wells that were shut-in for market conditions or pipeline connections, or

(3) wells not capable of production for mechanical reasons. Behind-pipe reserves are expected to be recovered from zones in existing wells that will require additional completion work or future recompletion prior to the start of production.

“Proved developed reserves” Reserves that can be expected to be recovered through existing wells with existing equipment and operating methods.

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

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

“PV-10” means estimated future net revenue, discounted at a rate of 10% per annum, before income taxes and with no price or cost escalation or de-escalation, calculated in accordance with guidelines promulgated by the Securities and Exchange Commission (“SEC”). PV-10 is considered a non-GAAP financial measure under SEC regulations because it does not include the effects of future income taxes, as is required in computing the standardized measure of discounted future net cash flows. We believe that PV-10 is an important measure that can be used to evaluate the relative significance of our oil and gas properties and that PV-10 is widely used by securities analysts and investors when evaluating oil and gas companies. Because many factors that are unique to each individual company impact the amount of future income taxes to be paid, the use of a pre-tax measure provides greater comparability of assets when evaluating companies. We believe that most other companies in the oil and gas industry calculate PV-10 on the same basis. PV-10 is computed on the same basis as the standardized measure of discounted future net cash flows but without deducting income taxes.

“Standardized Measure” means estimated future net revenue, discounted at a rate of 10% per annum, after income taxes and with no price or cost escalation or de-escalation, calculated in accordance with Accounting Standards Codification (“ASC”) 932, “Disclosures About Oil and Gas Producing Activities.”

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

* This definition is an abbreviated version of the complete definition set forth in Rule 4-10(a) of Regulation S-X. For the complete definition, see: http://www.ecfr.gov/cgi-bin/retrieveECFR?gp=1&SID=aa25d3cede06103c0ecec861362497d&ty=HTML&h=L&n=pt17.3.210&r=PART#se17.3.210_14_610

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ABRAXAS PETROLEUM CORPORATION
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Part I
FINANCIAL STATEMENTS

Item 1. Financial Statements

ABRAXAS PETROLEUM CORPORATION
CONDENSED CONSOLIDATED BALANCE SHEETS
(in thousands)

	September 30, 2020 (Unaudited)	December 31, 2019
Assets		
Current assets:		
Cash and cash equivalents	\$ 583	\$ -
Accounts receivable:		
Joint owners, net	1,368	2,397
Oil and gas production sales	6,067	16,985
Other	52	263
Total accounts receivable	7,487	19,645
Derivative asset - short-term	17,353	83
Other current assets	1,129	1,193
Total current assets	26,552	20,921
Property and equipment:		
Proved oil and gas properties, full cost method	1,168,504	1,162,094
Other property and equipment	39,453	39,295
Total	1,207,957	1,201,389
Less accumulated depreciation, depletion, amortization and impairment	(1,027,283)	(872,431)
Total property and equipment, net	180,674	328,958
Operating lease right-of-use assets	250	327
Derivative asset - long-term	17,505	4,170
Other assets	255	255
Total assets	\$ 225,236	\$ 354,631

All share and per share data has been retroactively adjusted to reflect the 1-for-20 reverse stock split effective October 19, 2020, as described in Note 2 to our condensed consolidated financial statements.

See accompanying notes to condensed consolidated financial statements (unaudited).

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ABRAXAS PETROLEUM CORPORATION
CONDENSED CONSOLIDATED BALANCE SHEETS (CONTINUED)
(in thousands, except share and per share data)

	September 30, 2020 (Unaudited)	December 31, 2019
Liabilities and Stockholders' Equity		
Current liabilities:		
Accounts payable	\$ 6,482	\$ 19,280
Joint interest oil and gas production payable	6,390	18,050
Accrued interest	103	133
Accrued expenses	1,183	361
Operating lease liabilities - current	76	98
Derivative liabilities - short-term	1,483	10,688
Current maturities of long-term debt	291	280
Other current liabilities	332	582
Total current liabilities	16,340	49,472
Long-term debt – less current maturities	203,931	192,718
Operating lease liabilities	147	203
Other long-term liabilities	1,375	—
Derivative liabilities - long-term	—	999
Future site restoration	7,681	7,420
Total liabilities	229,474	250,812

Stockholders' Equity:

Preferred stock, par value \$0.01 per share – authorized 1,000,000 shares; -0- shares issued and outstanding	—	—
Common stock, par value \$0.01 per share, authorized 20,000,000 shares; 8,403,465 and 8,418,053 issued and outstanding at September 30, 2020 and December 31, 2019, respectively	84	84
Additional paid-in capital	429,111	421,740
Accumulated deficit	(433,433)	(318,005)
Total stockholders' equity (deficit)	<u>(4,238)</u>	<u>103,819</u>
Total liabilities and stockholders' equity	<u>\$ 225,236</u>	<u>\$ 354,631</u>

See accompanying notes to condensed consolidated financial statements (unaudited).

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ABRAXAS PETROLEUM CORPORATION
CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS
(Unaudited)
(in thousands except per share data)

	Three Months Ended September		Nine Months Ended September	
	30,		30,	
	2020	2019	2020	2019
Revenues:				
Oil and gas production revenues				
Oil	\$ 12,466	\$ 31,228	\$ 29,971	\$ 97,355
Gas	75	226	183	2,107
Natural gas liquids	52	61	152	1,382
Other	2	21	8	26
Total revenue	<u>12,595</u>	<u>31,536</u>	<u>30,314</u>	<u>100,870</u>
Operating costs and expenses:				
Lease operating	3,935	5,647	12,280	21,447
Production and ad valorem taxes	1,520	2,495	3,613	8,519
Rig expense	130	—	669	672
Depreciation, depletion, amortization and accretion	7,019	12,605	19,053	38,367
Proved property impairment	54,552	—	136,109	—
General and administrative (including stock-based compensation of \$348, \$504, \$947 and \$1,398 respectively)	2,100	2,736	6,506	8,169
Total operating cost and expenses	<u>69,256</u>	<u>23,483</u>	<u>178,230</u>	<u>77,174</u>
Operating (loss) income	<u>(56,661)</u>	<u>8,053</u>	<u>(147,916)</u>	<u>23,696</u>
Other (income) expense:				
Interest income	(6)	(27)	(24)	(50)
Interest expense	5,676	2,951	15,569	8,706
Amortization of deferred financing fees	546	169	1,067	418
Loss on debt extinguishment	4,108	—	4,108	—
Loss (gain) on derivative contracts	6,630	(12,081)	(53,208)	11,358
Total other expense (income)	<u>16,954</u>	<u>(8,988)</u>	<u>(32,488)</u>	<u>20,432</u>
(Loss) income before income tax	<u>(73,615)</u>	<u>17,041</u>	<u>(115,428)</u>	<u>3,264</u>
Income tax (expense) benefit	—	—	—	—
Net (loss) income	<u>\$ (73,615)</u>	<u>\$ 17,041</u>	<u>\$ (115,428)</u>	<u>\$ 3,264</u>
Net (loss) income per common share - basic	<u>\$ (8.80)</u>	<u>\$ 2.05</u>	<u>\$ (13.80)</u>	<u>\$ 0.39</u>
Net (loss) income per common share - diluted	<u>\$ (8.80)</u>	<u>\$ 2.01</u>	<u>\$ (13.80)</u>	<u>\$ 0.39</u>
Weighted average shares outstanding:				
Basic	8,362	8,329	8,366	8,302
Diluted	8,362	8,480	8,366	8,324

See accompanying notes to condensed consolidated financial statements (unaudited).

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ABRAXAS PETROLEUM CORPORATION
CONDENSED CONSOLIDATED STATEMENTS OF STOCKHOLDERS' EQUITY
(Unaudited)
(in thousands, except share data)

	Common Stock		Additional Paid in Capital	Accumulated Deficit	Total
	Shares	Amount			
Balance at December 31, 2019	8,418,053	\$ 84	\$ 421,740	\$ (318,005)	\$ 103,819
Net loss	-	-	-	(115,428)	(115,428)
Stock-based compensation	-	-	947	-	947
Issuance of warrant	-	-	6,424	-	6,424
Stock options exercised	-	-	-	-	-
Restricted stock issued, net of forfeitures	(14,588)	-	-	-	-
Balance at September 30, 2020	<u>8,403,465</u>	<u>\$ 84</u>	<u>\$ 429,111</u>	<u>\$ (433,433)</u>	<u>\$ (4,238)</u>

	Common Stock		Additional Paid in Capital	Accumulated Deficit	Total
	Shares	Amount			
Balance at December 31, 2018	8,335,689	\$ 83	\$ 419,428	\$ (253,001)	\$ 166,510
Net income	-	-	-	3,264	3,264
Stock-based compensation	-	-	1,398	-	1,398
Stock options exercised	21,168	1	400	-	401
Restricted stock issued, net of forfeitures	63,125	-	-	-	-
Balance at September 30, 2019	<u>8,419,982</u>	<u>\$ 84</u>	<u>\$ 421,226</u>	<u>\$ (249,737)</u>	<u>\$ 171,573</u>

	Common Stock		Additional Paid in Capital	Accumulated Deficit	Total
	Shares	Amount			
Balance at June 30, 2020	8,403,465	\$ 84	\$ 422,339	\$ (359,818)	\$ 62,605
Net loss	-	-	-	(73,615)	(73,615)
Stock-based compensation	-	-	348	-	348
Issuance of warrant	-	-	6,424	-	6,424
Restricted stock issued, net of forfeitures	-	-	-	-	-
Balance at September 30, 2020	<u>8,403,465</u>	<u>\$ 84</u>	<u>\$ 429,111</u>	<u>\$ (433,433)</u>	<u>\$ (4,238)</u>

	Common Stock		Additional Paid in Capital	Accumulated Deficit	Total
	Shares	Amount			
Balance at June 30, 2019	8,422,603	\$ 84	\$ 420,722	\$ (266,778)	\$ 154,028
Net income	-	-	-	17,041	17,041
Stock-based compensation	-	-	504	-	504
Stock options exercised	-	-	-	-	-
Restricted stock issued, net of forfeitures	(2,621)	-	-	-	-
Balance at September 30, 2019	<u>8,419,982</u>	<u>\$ 84</u>	<u>\$ 421,226</u>	<u>\$ (249,737)</u>	<u>\$ 171,573</u>

See accompanying notes to condensed consolidated financial statements (unaudited).

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ABRAXAS PETROLEUM CORPORATION
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
(Unaudited)
(in thousands)

	Nine Months Ended September 30,	
	2020	2019
Operating Activities		
Net income (loss)	\$ (115,428)	\$ 3,264
Adjustments to reconcile net income (loss) to net cash provided by operating activities:		
Net (gain) loss on derivative contracts	(53,208)	11,358
Net cash settlements paid on derivative contracts	12,400	(2,930)
Depreciation, depletion and amortization	19,053	38,367
Proved property impairment	136,109	-
Amortization of deferred financing fees and issuance discount	2,226	418
Loss on debt extinguishment	4,108	-
Stock-based compensation	947	1,398
Settlement of asset retirement obligation	310	(474)
Non-cash interest expense	8,323	-
Changes in operating assets and liabilities:		
Accounts receivable	12,158	16,367
Other assets	1,459	(502)
Accounts payable and accrued expenses	(17,723)	(6,249)
Net cash provided by operating activities	<u>10,734</u>	<u>61,017</u>

Investing Activities

Capital expenditures, including purchases and development of properties	(13,187)	(89,621)
Proceeds from the sale of oil and gas properties	-	16,765
Net cash used in investing activities	(13,187)	(72,856)
Financing Activities		
Proceeds from long-term borrowings	8,000	38,000
Payments on long-term borrowings	(3,987)	(20,199)
Deferred financing fees	(977)	(91)
Exercise of stock options	-	401
Net cash provided by financing activities	3,036	18,111
Increase (decrease) in cash and cash equivalents	583	6,272
Cash and cash equivalents at beginning of period	-	867
Cash and cash equivalents at end of period	<u>\$ 583</u>	<u>\$ 7,139</u>
Supplemental disclosures of cash flow information:		
Interest paid	<u>\$ 6,085</u>	<u>\$ 8,706</u>
Non-cash investing and financing activities:		
Non-cash interest paid in kind	\$ 8,323	\$ -
Properties classified as held for sale	\$ -	\$ 7,876
Change in capital expenditures included in accounts payable	\$ (6,619)	\$ (3,445)
Change in asset retirement obligations	\$ -	\$ (379)

See accompanying notes to condensed consolidated financial statements (unaudited).

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ABRAXAS PETROLEUM CORPORATION
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(Unaudited)
(tabular amounts in thousands, except per share data)

1. Basis of Presentation

The accounting policies we follow as of January 1, 2020 are set forth in the notes to our audited consolidated financial statements in the Annual Report on Form 10-K for the year ended December 31, 2019 filed with the SEC on June 26, 2020. The accompanying interim condensed consolidated financial statements have not been audited by our independent registered public accountants. In the opinion of management, these statements reflect all adjustments necessary for a fair presentation of the financial position and results of operations. Any and all adjustments are of a normal and recurring nature. Although management believes the unaudited interim related disclosures in these condensed consolidated financial statements are adequate to make the information presented not misleading, certain information and footnote disclosures normally included in annual audited consolidated financial statements prepared in accordance with accounting principles generally accepted in the United States of America ("GAAP") have been condensed or omitted pursuant to the rules and regulations of the SEC. The results of operations for the three and nine month periods ended September 30, 2020 and the statement of cash flows for the nine months ended September 30, 2020, are not necessarily indicative of the results to be expected for the full year. The condensed consolidated financial statements included herein should be read in conjunction with the consolidated audited financial statements and the notes thereto included in our Annual Report on Form 10-K for the year ended December 31, 2019.

COVID-19

On January 30, 2020, the World Health Organization ("WHO") announced a global health emergency because of a new strain of coronavirus ("COVID-19") and the risks to the international community as the virus spreads globally beyond its point of origin. In March 2020, the WHO classified the COVID-19 as a pandemic, based on the rapid increase in exposure globally. In addition, in March 2020, members of OPEC failed to agree on production levels which is expected to cause an increased supply and has led to a substantial decrease in oil prices and an increasingly volatile market.

The price of both oil and gas has decreased primarily as a result of oil demand concerns due to the economic impacts of the COVID-19 virus and anticipated increases in supply from Russia and OPEC, particularly Saudi Arabia. Declines in oil and natural gas prices affect the Company's liquidity, however the Company's commodity hedges partially protect its cash flows from such price declines. Additionally, if oil or natural gas prices remain depressed or continue to decline the Company will be required to record additional impairments to its oil and gas properties.

Consumer demand has decreased due to the spread of the COVID-19 outbreak and travel restrictions placed by governments in an effort to curtail the spread of the coronavirus. The full impact of the coronavirus and the decrease in oil prices continue to evolve as of the date of this report. As such, it is uncertain as to the full magnitude that they will have on the Company's financial condition, liquidity and future results of operations. Management is actively monitoring the global situation and the impact or adverse effect on the Company's results of future operations, financial position and liquidity in fiscal year 2020. Due to the recent oil price volatility, the Company has curtailed its 2020 capital spending program. The Company has also laid off selected employees, reduced officer salaries from 20% - 40% and reduced all other salaries from 5% - 20%. The Company has also eliminated substantially all overtime for field employees. The Company began shutting in production in mid- March 2020 and began bringing wells back on production in mid- June 2020 as prices began to recover. As of September 30, 2020, a majority of such wells have been brought back on production.

In early March 2020, global oil and natural gas prices declined sharply, have since been volatile, and may decline again. The Company expects ongoing oil price volatility over the short term. Continued depressed oil prices have had and will continue to have a material adverse impact on the Company's oil revenue, which is mitigated somewhat by the Company's hedge contracts.

Reclassifications

Certain reclassifications have been made to the prior year financial statements to conform to the current period presentation. These reclassifications were to share and per share data related to the 1 for 20 reverse stock split effective October 19, 2020, and had no effect on our previously reported results of operations.

Consolidation Principles

The terms “Abraxas,” “Abraxas Petroleum,” “we,” “us,” “our” or the “Company” refer to Abraxas Petroleum Corporation and all of its subsidiaries, including Raven Drilling, LLC (“Raven Drilling”).

Rig Accounting

In accordance with SEC Regulation S-X, no income is recognized in connection with contractual drilling services performed in connection with properties in which we or our affiliates hold an ownership, or other economic interest. Any income not recognized as a result of this limitation is credited to the full cost pool and recognized through lower amortization as reserves are produced.

Use of Estimates

The preparation of financial statements in conformity with US GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities as of the date of the financial statements and reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

Stock-Based Compensation, Option Plans and Warrants**Stock Options**

We currently utilize a standard option-pricing model (i.e., Black-Scholes) to measure the fair value of stock options granted to employees and directors.

The following table summarizes our stock-based compensation expense related to stock options for the periods presented:

Three Months Ended September 30,		Nine Months Ended September 30,	
2020	2019	2020	2019
\$ 11	\$ 76	\$ 73	\$ 301

The following table summarizes our stock option activity for the nine months ended September 30, 2020, (in thousands):

	Number of Shares	Weighted Average Option Exercise Price Per Share	Weighted Average Grant Date Fair Value Per Share
Outstanding, December 31, 2019	296	\$ 49.41	\$ 34.98
Cancelled/Forfeited	-	\$ 78.20	\$ 56.32
Expired	(98)	\$ 49.54	\$ 35.36
Balance, September 30, 2020	198	\$ 49.34	\$ 34.78

As of September 30, 2020, there was approximately \$0.07 million of unamortized compensation expense related to outstanding stock options that will be recognized from 2020 through 2022.

Restricted Stock Awards

Restricted stock awards are awards of common stock that are subject to restrictions on transfer and to a risk of forfeiture if the recipient of the award terminates employment with us prior to the lapse of the restrictions. The fair value of such stock was determined using the closing price on the grant date and compensation expense is recorded over the applicable vesting periods.

The following table summarizes our restricted stock activity for the nine months ended September 30, 2020:

	Number of Shares (thousands)	Weighted Average Grant Date Fair Value Per Share
Unvested, December 31, 2019	89	\$ 31.67
Vested/Released	(33)	\$ 32.11
Cancelled/Forfeited	(15)	\$ 31.53
Unvested, September 30, 2020	41	\$ 31.37

The following table summarizes our stock-based compensation expense related to restricted stock for the periods presented:

Three Months Ended September 30,				Nine Months Ended September 30,			
2020		2019		2020		2019	
\$	203	\$	273	\$	675	\$	694

As of September 30, 2020, there was approximately \$0.8 million of unamortized compensation expense relating to outstanding restricted shares that will be recognized from 2020 through 2022.

Performance Based Restricted Stock

We issue performance-based shares of restricted stock to certain officers and employees under the Abraxas Petroleum Corporation Amended and Restated 2005 Employee Long-Term Equity Incentive Plan. The shares will vest in three years from the grant date upon the achievement of performance goals based on our Total Shareholder Return (“TSR”) as compared to a peer group of companies. The number of shares which would vest depends upon the rank of our TSR as compared to the peer group at the end of the three-year vesting period and can range from zero percent of the initial grant up to 200% of the initial grant.

The table below provides a summary of Performance Based Restricted Stock as of the date indicated:

	Number of Shares (thousands)	Weighted Average Grant Date Fair Value Per Share
Unvested, December 31, 2019	58	\$ 34.34
Cancelled/Forfeited	(13)	\$ 34.29
Unvested, September 30, 2020	45	\$ 33.73

Compensation expense associated with the performance based restricted stock is based on the grant date fair value of a single share as determined using a Monte Carlo Simulation model which utilizes a stochastic process to create a range of potential future outcomes given a variety of inputs. As the Compensation Committee intends to settle the performance based restricted stock awards with shares of our common stock, the awards are accounted for as equity awards and the expense is calculated on the grant date assuming a 100% target payout and amortized over the life of the awards.

The following table summarizes our stock-based compensation expense related to performance based restricted stock for the periods presented:

Three Months Ended September 30,				Nine Months Ended September 30,			
2020		2019		2020		2019	
\$	134	\$	155	\$	200	\$	403

As of September 30, 2020, there was approximately \$0.5 million of unamortized compensation expense relating to outstanding performance based restricted shares that will be recognized from 2020 through 2022.

Warrants for Common Stock

As of September 30, 2020, outstanding warrants to purchase shares of common stock were as follows:

<u>Issuance Date</u>	<u>Exercisable for</u>	<u>Expiration Date</u>	<u>Exercise Price</u>	<u>Number of Shares</u>
August 11, 2020	Common Stock	August 11, 2025	\$ 0.20	1,672,290

In connection with the amended Second Lien Credit Agreement, on August 11, 2020, the Company issued a warrant to the lender to purchase a total of 33,445,792 shares of common stock at an exercise price of \$0.01 per share. As described in Note 2, on October 19, 2020 the Company effected a reverse stock split of the Company's authorized, issued and outstanding shares of common stock at a ratio of 1-for-20, thus the warrant was adjusted to provide that the lender may purchase a total of 1,672,290 shares of common stock at an exercise price of \$0.20 per share the warrant is exercisable immediately, in whole or in part, on or before five years from the issuance date. The fair value of the warrant was recorded as debt issuance costs, presented in the consolidated balance sheets as a deduction from the carrying amount of the note payable, and is being amortized over the loan term.

Oil and Gas Properties

We follow the full cost method of accounting for oil and gas properties. Under this method, all direct costs and certain indirect costs associated with the acquisition of properties and successful and unsuccessful exploration and development activities are capitalized. Depreciation, depletion, and amortization of capitalized oil and gas properties and estimated future development costs, excluding unproved properties, are based on the unit-of-production method based on proved reserves. Net capitalized costs of oil and gas properties, less related deferred taxes, are limited by country, to the lower of unamortized cost or the cost ceiling, defined as the sum of the present value of estimated future net revenues from proved reserves based on unescalated prices discounted at 10%, plus the cost of properties not being amortized, if any, plus the lower of cost or estimated fair value of unproved properties included in the costs being amortized, if any, less related income taxes. Costs in excess of the present value of estimated net revenue from proved reserves discounted at 10% are charged to proved property impairment expense. No gain or loss is recognized upon sale or disposition of oil and gas properties for full cost accounting companies with proceeds accounted for as an adjustment of capitalized cost. An exception to this rule occurs when the adjustment to the full cost pool results in a significant alteration of the relationship between capitalized cost and proved reserves. We apply the full cost ceiling test on a quarterly basis on the date of the latest balance sheet presented. At September 30, 2020 our net capitalized costs of oil and gas properties exceeded the cost ceiling of our estimated proved reserves resulting in an impairment of \$54.6 million and \$136.1 million, for the three and nine months ended September 30, 2020. At September 30, 2019, our net capitalized costs of oil and gas properties did not exceed the cost ceiling of our estimated proved reserves. We expect that we will have future impairments.

Restoration, Removal and Environmental Liabilities

We are subject to extensive federal, state and local environmental laws and regulations. These laws regulate the discharge of materials into the environment and may require us to remove or mitigate the environmental effects of the disposal or release of petroleum substances at various sites. Environmental expenditures are expensed or capitalized depending on their future economic benefit. Expenditures that relate to an existing condition caused by past operations and that have no future economic benefit are expensed.

Liabilities for expenditures of a non-capital nature are recorded when environmental assessments and/or remediation is probable, and the costs can be reasonably estimated. Such liabilities are generally undiscounted unless the timing of cash payments for the liability or component is fixed or reliably determinable.

We account for future site restoration obligations based on the guidance of ASC 410 which addresses accounting and reporting for obligations associated with the retirement of tangible long-lived assets and the associated asset retirement costs. ASC 410 requires that the fair value of a liability for an asset's retirement obligation be recorded in the period in which it is incurred and the corresponding cost capitalized by increasing the carrying amount of the related long-lived asset. The liability is accreted to its then present value each period, and the capitalized cost is depreciated over the estimated useful life of the related asset. For all periods presented, we have included estimated future costs of abandonment and dismantlement in our full cost amortization base and amortize these costs as a component of our depletion expense in the accompanying condensed consolidated financial statements.

The following table summarizes our future site restoration obligation transactions for the nine months ended September 30, 2020 and the year ended December 31, 2019:

	<u>September 30, 2020</u>	<u>December 31, 2019</u>
Beginning future site restoration obligation	\$ 7,420	\$ 7,492
New wells placed on production and other	42	80
Deletions related to property disposals	(19)	(473)
Deletions related to plugging costs	(120)	(890)
Accretion expense	310	436
Revisions and other	48	775
Ending future site restoration obligation	<u>\$ 7,681</u>	<u>\$ 7,420</u>

Recently Adopted Accounting Standards

Effective January 1, 2020, the Company adopted Accounting Standards Update ("ASU") 2016-13 and its related amendments. This ASU primarily applies to the Company's accounts receivable, of which the majority are due within 30 days. The Company monitors the credit quality of its counterparties through review of collections, credit ratings, and other analysis. The Company develops its estimated allowance for credit losses primarily using an aging method and analysis of historical loss rates as well as consideration of current and future conditions that could impact its counterparties' credit quality and liquidity. The adoption and implementation of this ASU did not have a material impact on the Company's financial statements.

Recently Issued Accounting Standards

In November 2019, the FASB issued ASU 2019-12 – Income Taxes ("Topic 740"): Simplifying the Accounting for Income Taxes. The amendments in ASU 2019-12 are part of an initiative to reduce complexity in accounting standards and simplify the accounting for income taxes by removing certain exceptions from Topic 740 and making minor improvements to the codification. ASU 2019-12 and its related amendments will be effective for public entities for fiscal years, and interim periods within those fiscal years, beginning after December 15, 2020. The provisions of this update are not expected to have a material impact on the Company's financial position or results of operations.

In March 2020, the FASB issued ASU No. 2020-04, "Reference Rate Reform (Topic 840): Facilitation of the Effects of Reference Rate Reform on Financial Reporting" ("ASU 2020-04"), which provides companies with optional guidance to ease the potential accounting burden associated with transitioning away from reference rates (e.g., London Interbank Offered Rate ("LIBOR")) that are expected to be discontinued. ASU 2020-04 allows, among other things, certain contract modifications, such as those within the scope of Topic 470 on debt, to be accounted as a continuation of the existing contract. This ASU was effective upon the issuance and its optional relief can be applied through December 31, 2022. The Company will consider this optional guidance prospectively, if applicable.

In May 2020, the SEC adopted final rules that amend the financial statement requirements for significant business acquisitions and dispositions. Among other changes, the final rules modify the significance tests and improve the disclosure requirements for acquired or to be acquired businesses and related pro forma financial information, the periods those financial statements must cover, and the form and content of the pro forma financial information. The final rules do not modify requirements for the acquisition and disposition of significant amounts of assets that do not constitute a business. The final rules are effective January 1, 2021, but earlier compliance is permitted. The Company will consider these final rules and update its disclosures, as applicable.

2. Reverse Stock Split

On October 19, 2020, the Company effected a 1-for-20 reverse stock split of its issued and outstanding shares of common stock, \$0.01 par value. The Company effected the reverse stock split pursuant to the Company's filing of a Certificate of Change with the Secretary of State of the State of Nevada on September 29, 2020. Under Nevada law, no amendment to the Company's Articles of Incorporation was required in connection with the reverse stock split. The Company was authorized to issue 400,000,000 shares of common stock. As a result of the reverse stock split, the Company is authorized to issue 20,000,000 shares of common stock. As a result of the reverse split, 168,069,305 outstanding shares of the Company's common stock were exchanged for approximately 8,403,465 shares of the Company's common stock (subject to adjustment due to the effect of rounding fractional shares into whole shares). The reverse stock split will not have any effect on the stated par value of the common stock. All per share amounts and number of shares in the condensed consolidated financial statements and related notes have been retroactively restated to reflect the reverse stock split, resulting in the transfer of \$1.6 million from common stock to additional paid in capital at September 30, 2020 and December 31, 2019.

Additionally on October 19, 2020, all options, warrants and other convertible securities of the Company outstanding immediately prior to the reverse stock split will be adjusted by dividing the number of shares of common stock into which the options, warrants and other convertible securities are exercisable or convertible by 20, and multiplying the exercise or conversion price thereof by 20, all in accordance with the terms of the plans, agreements or arrangements governing such options, warrants and other convertible securities and subject to rounding to the nearest whole share.

The common stock began trading on a split-adjusted basis on the NASDAQ at the market open on October 19, 2020. The trading symbol for the common stock remains "AXAS".

The reverse stock split was intended to bring the Company into compliance with the Nasdaq Stock Market Listing Rule 5550(a)(2) and the \$1.00 per share minimum bid price requirement for continued listing on the NASDAQ. On November 2, 2020, the Company received written notice from the NASDAQ that the Company has regained compliance with the Listing Rule 5550(a)(2) and the \$1.00 per share minimum bid price requirement.

3. Revenue from Contracts with Customers

Revenue Recognition

Sales of oil, gas and natural gas liquids ("NGL") are recognized at the point in time when control of the product is transferred to the customer and collectability is reasonably assured. Our contracts' pricing provisions are tied to a market index, with certain adjustments based on, among other factors, physical location, quality of the oil or gas, and prevailing supply and demand conditions. As a result, the price of the oil, gas and NGL fluctuates to remain competitive with other available oil, gas and NGL supplies in the market. We believe that the pricing provisions of our oil, gas and NGL contracts are customary in the industry.

Oil sales

Our oil sales contracts are generally structured such that we sell our oil production to a purchaser at a contractually specified delivery point at or near the wellhead. The crude oil production is priced on the delivery date based upon prevailing index prices less certain deductions related to oil quality,

physical location and transportation costs incurred by the purchaser subsequent to delivery. We recognize revenue when control transfers to the purchaser upon delivery at or near the wellhead at the net price received from the purchaser.

Gas and NGL Sales

Under our gas processing contracts, we deliver wet gas to a midstream processing entity at the wellhead or the inlet of the midstream processing entity's system. The midstream processing entity processes the natural gas and remits proceeds to us based upon either (i) the resulting sales price of NGL and residue gas received by the midstream processing entity from third party customers, or (ii) the prevailing index prices for NGL and residue gas in the month of delivery to the midstream processing entity. Gathering, processing, transportation and other expenses incurred by the midstream processing entity are typically deducted from the proceeds that we receive.

In these scenarios, we evaluate whether the midstream processing entity is the principal or the agent in the transaction. In our gas purchase contracts, we have concluded that the midstream processing entity is the agent, and thus, the midstream processing entity is our customer. Accordingly, we recognize revenue upon delivery to the midstream processing entity based on the net amount of the proceeds received from the midstream processing entity.

Disaggregation of Revenue

We are focused on the development of oil and natural gas properties primarily located in the following two operating regions in the United States: (i) the Permian/Delaware Basin and (ii) Rocky Mountain. We sold our remaining South Texas assets, which closed on November 1, 2019. Revenue attributable to each of those regions is disaggregated in the tables below.

	Three Months Ended September 30,					
	2020			2019		
	Oil	Gas	NGL	Oil	Gas	NGL
Operating Regions:						
Permian/Delaware Basin	\$ 7,676	\$ 77	\$ 52	\$ 14,315	\$ 66	\$ 80
Rocky Mountain	\$ 4,790	\$ (2)	\$ -	\$ 16,157	\$ 14	\$ (19)
South Texas	\$ -	\$ -	\$ -	\$ 756	\$ 146	\$ -

	Nine Months Ended September 30,					
	2020			2019		
	Oil	Gas	NGL	Oil	Gas	NGL
Operating Regions:						
Permian/Delaware Basin	\$ 16,748	\$ 111	\$ 62	\$ 38,940	\$ 377	\$ 421
Rocky Mountain	\$ 13,223	\$ 72	\$ 90	\$ 55,524	\$ 1,176	\$ 958
South Texas	\$ -	\$ -	\$ -	\$ 2,891	\$ 554	\$ 3

Significant JudgmentsPrincipal versus agent

We engage in various types of transactions in which midstream entities process our gas and subsequently market resulting NGL and residue gas to third-party customers on our behalf, such as our percentage-of-proceeds and gas purchase contracts. These types of transactions require judgment to determine whether we are the principal or the agent in the contract and, as a result, whether revenues are recorded gross or net.

Transaction price allocated to remaining performance obligations

A significant number of our product sales are short-term in nature with a contract term of one year or less. For those contracts, we have utilized the practical expedient in ASC Topic 606-10-50-14 exempting us from disclosure of the transaction price allocated to remaining performance obligations if the performance obligation is part of a contract that has an original expected duration of one year or less.

For product sales that have a contract term greater than one year, we have utilized the practical expedient in ASC Topic 606-10-50-14(a) which states we are not required to disclose the transaction price allocated to remaining performance obligations if the variable consideration is allocated entirely to a wholly unsatisfied performance obligation. Under these sales contracts, each unit of product generally represents a separate performance obligation; therefore, future volumes are wholly unsatisfied, and disclosure of the transaction price allocated to remaining performance obligations is not required.

Contract balances

Under our product sales contracts, we are entitled to payment from purchasers once our performance obligations have been satisfied upon delivery of the product, at which point payment is unconditional. We record invoiced amounts as “Accounts receivable - Oil and gas production sales” in the accompanying condensed consolidated balance sheet.

To the extent actual volumes and prices of oil and natural gas are unavailable for a given reporting period because of timing or information not received from third parties, the expected sales volumes and prices for those properties are estimated and also recorded as “Accounts receivable - Oil and gas production sales” in the accompanying condensed consolidated balance sheets. In this scenario, payment is also unconditional, as we have satisfied our performance obligations through delivery of the relevant product. As a result, we have concluded that our product sales do not give rise to contract assets or liabilities under ASU 2014-09. At September 30, 2020 and December 31, 2019, our receivables from contracts with customers were \$6.1 million and \$17.0 million, respectively.

Prior-period performance obligations

We record revenue in the month production is delivered to the purchaser. However, settlement statements for certain gas and NGL sales may not be received for 30 to 60 days after the date production is delivered, and as a result, we are required to estimate the amount of production that was delivered to the midstream purchaser and the price that will be received for the sale of the product. Additionally, to the extent actual volumes and prices of oil are unavailable for a given reporting period because of timing or information not received from third party purchasers, the expected sales volumes and prices for those barrels of oil are also estimated.

We record the differences between our estimates and the actual amounts received for product sales in the month that payment is received from the purchaser. Any identified differences between our revenue estimates and actual revenue received historically have not been significant. For the three and nine months ended September 30, 2020, and 2019 revenue recognized in the reporting period related to performance obligations satisfied in prior reporting periods was not material.

4. Income Taxes

Deferred tax assets and liabilities are determined based on differences between financial reporting and tax basis of assets and liabilities and are measured using the tax rates and laws expected to be in effect when the differences are expected to reverse.

For the three and nine months ended September 30, 2020, and 2019, there was no income tax benefit due to net operating loss carryforwards (“NOLs”) and we recorded a full valuation allowance against our net deferred tax asset.

At December 31, 2019, we had, subject to the limitation discussed below, \$245.2 million of pre-2018 NOLs and \$64.7 million of post 2018 NOL carryforwards for U.S. tax purposes. Our pre-2018 NOLs will expire in varying amounts from 2022 through 2037, if not utilized. Any NOLs arising in 2018, 2019, and 2020 can generally be carried back five years, carried forward indefinitely and can offset 100% of taxable income for tax years for 2020 and up to 80% of future taxable income for tax years after December 31, 2020. Any NOLs arising on or after January 1, 2021 can generally be carried forward indefinitely and can offset up to 80% of future taxable income. The use of our NOLs will be limited if there is an “ownership change” in our common stock, generally a cumulative ownership change exceeding 50% during a three year period, as determined under Section 382 of the Internal Revenue Code. As of September 30, 2020, we have not had an ownership change as defined by Section 382.

Given historical losses, uncertainties exist as to the future utilization of the NOL carryforwards. Therefore, we established a valuation allowance of \$76.2 million for deferred tax assets at December 31, 2019 and of \$67.4 million at September 30, 2020.

As of September 30, 2020, we did not have any accrued interest or penalties related to uncertain tax positions. The tax years 2014 through 2019 remain open to examination by the tax jurisdictions to which we are subject.

The Coronavirus Aid, Relief, and Economic Security Act that was enacted March 27, 2020 includes income tax provisions that allow NOLs to be carried back, allows interest expense to be deducted up to a higher percentage of adjusted taxable income, and modifies tax depreciation of qualified improvement property, among other provisions. These provisions have no material impact on the Company.

5. Long-Term Debt

The following is a description of our debt as of September 30, 2020 and December 31, 2019 (in thousands):

	September 30, 2020	December 31, 2019
First Lien Credit Facility	\$ 100,000	\$ 95,778
Second Lien Credit Facility	108,278	100,000
Exit fee - Second Lien Credit Facility	10,000	-
Real estate lien note	2,882	3,091
	221,160	198,869
Less current maturities	(291)	(280)
	220,869	198,589
Deferred financing fees and debt issuance cost, net	(16,938)	(5,871)
Total long-term debt, net of deferred financing fees and debt issuance costs	\$ 203,931	\$ 192,718

First Lien Credit Facility

The Company has a senior secured First Lien Credit Facility with Société Générale, as administrative agent and issuing lender, and certain other lenders. As of September 30, 2020, \$100.0 million was outstanding under the First Lien Credit Facility.

Outstanding amounts under the First Lien Credit Facility accrues interest at a rate per annum equal to (a)(i) for borrowings that we elect to accrue interest at the reference rate at the greater of (x) the reference rate announced from time to time by Société Générale, (y) the federal funds rate plus 0.5%, and (z) daily one-month LIBOR plus, in each case, 1.5%-2.5%, depending on the utilization of the borrowing base, and (ii) for borrowings that we elect to accrue interest at the Eurodollar rate, LIBOR plus 2.5%-3.5% depending on the utilization of the borrowing base and (b) at any time an event of default exists, 3.0% plus the amounts set forth above. At September 30, 2020, the interest rate on the First Lien Credit Facility was approximately 3.6%.

Subject to earlier termination rights and events of default, the stated maturity date of the First Lien Credit Facility is May 16, 2022. Interest is payable quarterly on reference rate advances and not less than quarterly on LIBOR advances. The Company is permitted to terminate the First Lien Credit Facility and is able, from time to time, to permanently reduce the lenders' aggregate commitment under the First Lien Credit Facility in compliance with certain notice and dollar increment requirements.

Each of the Company's subsidiaries has guaranteed our obligations under the First Lien Credit Facility on a senior secured basis. Obligations under the First Lien Credit Facility are secured by a first priority perfected security interest, subject to certain permitted encumbrances, in all of the Company and its subsidiary guarantors' material property and assets. As of September 30, 2020, the collateral is required to include properties comprising at least 90% of the PV-9 of the Company's proven reserves and 95% of the PV-9 of the Company's PDP reserves.

Under the amended First Lien Credit Facility, the Company is subject to customary covenants, including financial covenants and reporting covenants. The amendment to the First Lien Credit Facility dated June 25, 2020 (the "1L Amendment") modified certain provisions of the First Lien Credit Facility, including (i) the addition of monthly mandatory prepayments from excess cash (defined as available cash minus certain cash set-asides and a \$3.0 million working capital reserve) with corresponding reductions to the borrowing base; (ii) the elimination of scheduled redeterminations (which were previously made every six months) and interim redeterminations (which were previously made at the request of the lenders no more than once in the six month period between scheduled redeterminations) of the borrowing base; (iii) the replacement of total debt leverage ratio and minimum asset ratio covenants with a first lien debt leverage ratio covenant (comparing the outstanding debt of the First Lien Credit Facility to the consolidated EBITDAX of the Company and requiring that the ratio not exceed 2.75 to 1.00 as of the last day of each fiscal quarter) and a minimum first lien asset coverage ratio covenant (comparing the sum of, without duplication, (A) the PV-15 of producing and developed proven reserves of the Company, (B) the PV-9 of the Company's hydrocarbon hedge agreements and (C) the PV-15 of proved reserves of the Company classified as "drilled uncompleted" (up to 20% of the sum of (A), (B) and (C)) to the outstanding debt of the First Lien Credit Facility and requiring that the ratio exceed 1.15 to 1.00 as of the last day of each fiscal quarter ending on or before December 31, 2020, and 1.25 to 1.00 for fiscal quarters ending thereafter); (iv) the elimination of current ratio and interest coverage ratio covenants; (v) additional restrictions on (A) capital expenditures (limiting capital expenditures to \$3.0 million in any four fiscal quarter period (commencing with the four fiscal quarter period ended June 30, 2020 and calculated on an annualized basis for the 1, 2 and 3 quarter periods ending on June 30, 2020, September 30, 2020 and December 31, 2020, respectively, subject to certain exceptions, including capital expenditures financed with the proceeds of newly permitted, structurally subordinated debt and capital expenditures made when (1) the first lien asset coverage ratio is at least 1.60 to 1.00, (2) the Company is in compliance with the first lien leverage ratio, (3) the amounts outstanding under the First Lien Credit Facility are less \$50.0 million, (4) no default exists under the First Lien Credit Facility and (5) all representations and warranties in the First Lien Credit Facility and the related credit documents are true and correct in all material respects), (B) outstanding accounts payable (limiting all outstanding and undisputed accounts payable to \$7.5 million, undisputed accounts payable outstanding for more than 60 days to \$2.0 million and undisputed accounts payable outstanding for more than 90 days to \$1.0 million and (C) general and administrative expenses (limiting cash general and administrative expenses the Company may make or become legally obligated to make in any four fiscal quarter period to \$9.0 million for the four fiscal quarter period ended June 30, 2020, \$8.25 million for the four fiscal quarter period ended September 30, 2020, \$6.9 million for the four fiscal quarter period ending December 31, 2020, and \$6.5 million for the fiscal quarter from March 31, 2021 through December 31, 2021 and \$5.0 million thereafter; in all cases, general and administrative expense excludes up to \$1.0 million in certain legal and professional fees; and (vi) permission for up to an additional \$25.0 million in structurally subordinated debt to finance capital expenditures. Under the 1L Amendment, the borrowing base was adjusted to \$102.0 million. The borrowing base will be reduced by any mandatory prepayments from excess cash flow (in an amount equal to such prepayment) and upon the disposition of the Company's oil and gas properties.

As of September 30, 2020 we were in compliance with the financial covenants under the First Lien Credit Facility, as amended.

The First Lien Credit Facility contains a number of covenants that, among other things, restrict our ability to:

- incur or guarantee additional indebtedness;
- transfer or sell assets;
- create liens on assets;
- pay dividends or make other distributions on capital stock or make other restricted payments;
- engage in transactions with affiliates other than on an “arm’s length” basis;
- make any change in the principal nature of our business; and
- permit a change of control.

The First Lien Credit Facility also contains customary events of default, including nonpayment of principal or interest, violations of covenants, cross default and cross acceleration to certain other indebtedness, bankruptcy and material judgments and liabilities.

Second Lien Credit Facility

On November 13, 2019, we entered into the Term Loan Credit Agreement, with Angelo Gordon Energy Servicer, LLC, as administrative agent, and certain other lenders party thereto, which we refer to as the Second Lien Credit Facility. The Second Lien Credit facility was amended on June 25, 2020. The Second Lien Credit Facility has a maximum commitment of \$100.0 million. On November 13, 2019, \$95.0 million of the net proceeds obtained from the Second Lien Credit Facility were used to permanently reduce the borrowings outstanding on the First Lien Credit Facility. As of September 30, 2020, the outstanding balance on the Second Lien Credit Facility was \$118.3 million, which includes a \$10.0 million exit fee.

The stated maturity date of the Second Lien Credit Facility is November 13, 2022. Prior to the latest amendments of the Second Lien Credit Facility, accrued interest was payable quarterly on reference rate loans and at the end of each three-month interest period on Eurodollar loans. We are permitted to prepay the loans in whole or in part, in compliance with certain notice and dollar increment requirements, and, if such prepayment is made prior to November 13, 2020, subject to payment of a Make Whole Amount, where applicable. “Make Whole Amount” is defined as, the sum of the interest payments (calculated on the basis of the interest rate as of the date of the relevant prepayment without discount) that would have accrued and been paid from the date of prepayment to November 13, 2020 on the principal amount of such prepaid loans, whether such prepayments are optional, mandatory or as a result of acceleration.

Each of our subsidiaries has guaranteed our obligations under the Second Lien Credit Facility. Obligations under the Second Lien Credit Facility are secured by a first priority perfected security interest, subject to certain permitted liens, including those securing the indebtedness under the First Lien Credit Facility to the extent permitted by the Intercreditor Agreement, of even date with the Second Lien Credit Facility, among us, our subsidiaries, Angelo Gordon Energy Servicer, LLC and Société Générale, in all of our subsidiary guarantors’ material property and assets. As of September 30, 2020, the collateral is required to include properties comprising at least 90% of the PV-9 of the Company’s proven reserves and 95% of the PV-9 of the Company’s PDP reserves.

Under the amended Second Lien Credit Facility, the Company is subject to customary covenants, including financial covenants and reporting covenants. The amendment to the Second Lien Credit Facility dated June 25, 2020 (the "2L Amendment") modified certain provisions of the Second Lien Credit Facility, including (i) a requirement that, while the obligations under the First Lien Credit Facility are outstanding, scheduled payments of accrued interest under the Second Lien Credit Facility will be paid in the form of capitalized interest; (ii) an increase in the interest rate by 200bps for interest payable in cash and 500bps for interest payable in kind; (iii) modification of the minimum asset ratio covenant to be the sum of, without duplication, (A) the PV-15 of producing and developed proven reserves of the Company, (B) the PV-9 of the Company's hydrocarbon hedge agreements and (C) the PV-15 of proved reserves of the Company classified as "drilled uncompleted" (up to 20% of the sum of (A), (B) and (C)) to the total outstanding debt of the Company and requiring that the ratio not exceed 1.45 to 1.00 as of the last day of each fiscal quarter ending between September 30, 2021 to December 31, 2021, and 1.55 to 1.00 for fiscal quarters ending thereafter); (iv) modification of the total leverage ratio covenant to set the first test date to occur on September 30, 2021; (v) modification of the current ratio to eliminate the exclusion of certain valuation accounts associated with hedge contracts from current assets and from current liabilities, (vi) additional restrictions on (A) capital expenditures (limiting capital expenditures to those expenditures set forth in a plan of development approved by Angelo Gordon Energy Servicer, LLC, subject to certain exceptions, including capital expenditures financed with the proceeds of newly permitted, structurally subordinated debt), (B) outstanding accounts payable (limiting all outstanding and undisputed accounts payable to \$7.5 million, undisputed accounts payable outstanding for more than 60 days to \$2.0 million and undisputed accounts payable outstanding for more than 90 days to \$1.0 million and (C) general and administrative expenses (limiting cash general and administrative expenses the Company may make or become legally obligated to make in any four fiscal quarter period to \$9.0 million for the four fiscal quarter period ended June 30, 2020, \$8.25 million for the four fiscal quarter period ended September 30, 2020, \$6.5 million for fiscal quarter period from March 31, 2021 through December 31, 2021 and \$5.0 million thereafter.

As of September 30, 2020 we were in compliance with the financial covenants under the Second Lien Credit Facility, as amended.

The Second Lien Credit Facility contains a number of covenants that, among other things, restrict our ability to:

- incur or guarantee additional indebtedness;
- transfer or sell assets;
- create liens on assets;
- pay dividends or make other distributions on capital stock or make other restricted payments;
- engage in transactions with affiliates other than on an "arm's length" basis;
- make any change in the principal nature of our business; and
- permit a change of control

The Second Lien Credit Facility also contains customary events of default, including nonpayment of principal or interest, violation of covenants, cross default and cross acceleration to certain other indebtedness, bankruptcy and material judgments and liabilities.

In connection with the amendment to the Second Lien Credit Facility on June 25, 2020, the Company entered into an Exit Fee and Warrant Agreement subject to NASDAQ approval for the issuance of the issuance of certain warrants. This agreement was finalized on August 11, 2020 at which time the Company issued a warrant to the lender to purchase a total of 33,445,792 shares of common stock at an exercise price of \$0.01 per share. On October 19, 2020, the Company effected a reverse stock split of the Company's authorized, issued and outstanding shares of common stock at a ratio of 1-for-20, thus the warrant was adjusted to provide that the lender may purchase a total of 1,672,290 shares of common stock at an exercise price of \$0.20 per share. The warrant is exercisable immediately in whole or in part, on or before five years from the issuance date. The fair value of the warrant and exit fee were recorded as debt issuance costs, presented in the consolidated balance sheets as a deduction from the carrying amount of the note payable, and are being amortized over the loan term. The Exit Fee shall be due and payable in cash on the earliest to occur of maturity of the obligation under the Second Lien Credit Agreement or the earlier acceleration or payment in full of the same. The 2L Amendment, including the impact of the Exit Fee and Warrant Agreement finalized on August 11, 2020, resulted in the 2L Amendment meeting the criteria of debt extinguishment under the guidance of ASC 470: *Debt*. Accordingly, all debt issuance cost, including the original discount, of the original Second Lien Credit Facility, were charged to debt extinguishment loss in the accompanying Condensed Consolidated Statement of Operation in the amount of \$4.1 million.

Real Estate Lien Note

We have a real estate lien note secured by a first lien deed of trust on the property and improvements which serves as our corporate headquarters. The outstanding principal accrues interest at a fixed rate of 4.9%. The note is payable in monthly installments of principal and accrues interest in the amount of \$35,672. The maturity date of the note is July 20, 2023. As of September 30, 2020 and December 31, 2019, \$2.9 million and \$3.1 million, respectively, were outstanding on the note.

6. Earnings per Share

The following table sets forth the computation of basic and diluted earnings per share:

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2020	2019	2020	2019
Numerator:				
Net (loss) income	\$ (73,615)	\$ 17,041	\$ (115,428)	\$ 3,264
Denominator:				
Denominator for basic earnings per share – weighted-average common shares outstanding	8,362	8,329	8,366	8,302
Effect of dilutive securities:				
Stock options, restricted shares and warrants	-	151	-	22
Denominator for diluted earnings per share – adjusted weighted-average shares and assumed exercise of options and restricted shares	<u>8,362</u>	<u>8,480</u>	<u>8,366</u>	<u>8,324</u>
Net (loss) income per common share - basic	<u>\$ (8.80)</u>	<u>\$ 2.05</u>	<u>\$ (13.80)</u>	<u>\$ 0.39</u>
Net (loss) income per common share - diluted	<u>\$ (8.80)</u>	<u>\$ 2.01</u>	<u>\$ (13.80)</u>	<u>\$ 0.39</u>

Basic earnings per share, excluding any dilutive effects of stock options and unvested restricted stock, is computed by dividing net income available to common stockholders by the weighted average number of common shares outstanding for the period. Diluted net income per share is computed similar to basic; however diluted income per share reflects the assumed conversion of all potentially dilutive securities. For the three and nine month periods ended September 30, 2020 there was no dilutive potential shares relating to stock options and restricted stock due to our depressed stock price and losses in the periods.

7. Hedging Program and Derivatives

The derivative contracts we utilize are based on index prices that may and often differ from the actual oil and gas prices realized in our operations. Our derivative contracts do not qualify for hedge accounting; therefore, fluctuations in the market value of the derivative contracts are recognized in earnings during the current period. There are no netting agreements relating to these derivative contracts and there is no policy to offset.

The following table sets forth the summary position of our derivative contracts as of September 30, 2020:

Contract Periods	Oil - WTI	
	Daily Volume (Bbl)	Swap Price (per Bbl)
Fixed Swaps		
2020 October - December	3,436	\$ 54.99
2021 January - December	2,889	\$ 57.62
2022 January - December	2,412	\$ 50.60
2023 January - December	1,498	\$ 50.60
2024 January - December	1,589	\$ 50.60
Basis Swaps		
2020 October - December	4,000	\$ 2.98

The following table illustrates the impact of derivative contracts on our balance sheet:

Fair Value of Derivative Contracts as of September 30, 2020

Derivatives not designated as hedging instruments	Asset Derivatives		Liability Derivatives	
	Balance Sheet Location	Fair Value	Balance Sheet Location	Fair Value
Commodity price derivatives	Derivatives – current	\$ 17,353	Derivatives – current	\$ 1,483
Commodity price derivatives	Derivatives – long-term	17,505	Derivatives – long-term	-
		<u>\$ 34,858</u>		<u>\$ 1,483</u>

Fair Value of Derivative Contracts as December 31, 2019

Derivatives not designated as hedging instruments	Asset Derivatives		Liability Derivatives	
	Balance Sheet Location	Fair Value	Balance Sheet Location	Fair Value
Commodity price derivatives	Derivatives – current	\$ 83	Derivatives – current	\$ 10,688
Commodity price derivatives	Derivatives – long-term	4,170	Derivatives – long-term	999
		<u>\$ 4,253</u>		<u>\$ 11,687</u>

8. Financial Instruments

Assets and liabilities measured at fair value are categorized into one of three different levels depending on the observability of the inputs employed in the measurement. The three levels are defined as follows:

- Level 1 – inputs to the valuation methodology are quoted prices (unadjusted) for identical assets or liabilities in active markets.
- Level 2 - inputs to the valuation methodology include quoted prices for similar assets and liabilities in active markets, and inputs that are observable for the asset or liability, either directly or indirectly, for substantially the full term of the financial instrument.
- Level 3 - inputs to the valuation methodology are unobservable and significant to the fair value measurement.

A financial instrument's categorization within the valuation hierarchy is based upon the lowest level of input that is significant to the fair value measurement. Our assessment of the significance of a particular input to the fair value measurement in its entirety requires judgment and considers factors specific to the asset or liability. We are further required to assess the creditworthiness of the counter-party to the derivative contract. The results of the assessment of non-performance risk, based on the counter-party's credit risk, could result in an adjustment of the carrying value of the derivative instrument. The following tables sets forth information about our assets and liabilities measured at fair value on a recurring basis as of September 30, 2020 and December 31, 2019, and indicate the fair value hierarchy of the valuation techniques utilized by us to determine such fair value:

	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Balance as of September 30, 2020
Assets:				
NYMEX fixed price derivative contracts	\$ —	\$ 34,858	\$ —	\$ 34,858
NYMEX basis differential swap contracts	—	—	—	—
Total Assets	\$ —	\$ 34,858	\$ —	\$ 34,858
Liabilities:				
NYMEX fixed price derivative contracts	\$ —	\$ —	\$ —	\$ —
NYMEX basis differential swaps	—	—	1,483	1,483
Total Liabilities	\$ —	\$ —	\$ 1,483	\$ 1,483
	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Balance as of December 31, 2019
Assets:				
NYMEX fixed price derivative contracts	\$ —	\$ 4,253	\$ —	\$ 4,253
Total Assets	\$ —	\$ 4,253	\$ —	\$ 4,253
Liabilities:				
NYMEX fixed price derivative contracts	\$ —	\$ 5,583	\$ —	\$ 5,583
NYMEX basis differential swaps	—	—	6,104	6,104
Total Liabilities	\$ —	\$ 5,583	\$ 6,104	\$ 11,687

As of September 30, 2020 and December 31, 2019 our derivative contracts consisted of NYMEX-based fixed price swaps and basis differential swaps. Under fixed price swaps, we receive a fixed price for our production and pay a variable market price to the contract counter-party. Under basis swaps, if the market price is above the fixed price, we pay the counter-party, if the market price is below the fixed price, the counter-party pays us. The NYMEX-based fixed price derivative swaps and basis differential swap contracts are indexed to NYMEX futures contracts, which are actively traded, for the underlying commodity and are commonly used in the energy industry. A number of financial institutions and large energy companies act as counter-parties to these types of derivative contracts. As the fair value of NYMEX-based fixed price swaps are based on a number of inputs, including contractual volumes and prices stated in each derivative contract, current and future NYMEX commodity prices, and quantitative models that are based upon readily observable market parameters that are actively quoted and can be validated through external sources, we have characterized these derivative contracts as Level 2. In order to verify the third party valuation, we enter the various inputs into a model and compare our results to the third party for reasonableness. The fair value of the basis differential swap instruments are based on inputs that are not as observable as the fixed price swaps. In addition to the actively quoted market price, variables such as time value, volatility and other unobservable inputs are used. Accordingly, these instruments have been classified as Level 3.

The following is additional information for our recurring fair value measurements using significant unobservable inputs (Level 3 inputs) for the nine months ended September 30, 2020.

Unobservable inputs at January 1, 2020	\$ (6,104)
Changes in market value	1,182
Settlements during the period	3,439
Unobservable inputs at September 30, 2020	<u>\$ (1,483)</u>

Nonrecurring Fair Value Measurements

Non-financial assets and liabilities measured at fair value on a nonrecurring basis included certain non-financial assets and liabilities as may be acquired in a business combination and thereby measured at fair value and the initial recognition of asset retirement obligations for which fair value is used. Unproved oil and gas properties are assessed periodically, at least annually, to determine whether impairment has occurred. The assessment considers the following factors, among others: intent to drill, remaining lease term, geological and geophysical evaluations, drilling results and activity, the assignment of proved reserves, the economic viability of development if proved reserves were assigned and other current market conditions. During any period in which these factors indicate an impairment, the cumulative drilling costs incurred to date for such property and all or a portion of the associated leasehold costs are transferred to the full cost pool and are then subject to amortization.

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 used, the Company has designated these liabilities as Level 3. A reconciliation of the beginning and ending balances of the Company's asset retirement obligation is presented in Note 1.

Other Financial Instruments

The carrying amounts of our cash, cash equivalents, restricted cash, accounts receivable and accounts payable approximate fair value because of the short-term maturities and/or liquid nature of these assets and liabilities. The carrying value of our debt approximates fair value as the interest rates are market rates and this debt is considered Level 2.

9. Leases

Nature of Leases

We lease certain real estate, field equipment and other equipment under cancelable and non-cancelable leases to support our operations. A more detailed description of our significant lease types is included below.

Real Estate Leases

We rent a residence in North Dakota from a third party for living accommodations for certain field employees. Our real estate lease is non-cancelable with a term of five years, expiring August 31, 2024. We have concluded our real estate agreements represent operating leases with a lease term that equals the primary non-cancelable contract term. Upon completion of the primary term, both parties have substantive rights to terminate the lease. As a result, enforceable rights and obligations do not exist under the rental agreements subsequent to the primary term.

Field Equipment

We rent various field equipment from third parties in order to facilitate the downstream movement of our production from our drilling operations to market. Our compressor and cooler arrangements are typically structured with a non-cancelable primary term of one year and continue thereafter on a month-to-month basis subject to termination by either party with thirty days' notice. These leases are considered short term and are not capitalized. We have a small number of compressor leases that are longer than twelve months. We have concluded that our equipment rental agreements represent operating leases with a lease term that equals the primary non-cancelable contract term. Upon completion of the primary term, both parties have substantive rights to terminate the lease. As a result, enforceable rights and obligations do not exist under the rental agreement subsequent to the primary term. We enter into daywork contracts for drilling rigs with third parties to support our drilling activities. Our drilling rig arrangements are typically structured with a term that is in effect until drilling operations are completed on a contractually specified well or well pad. Upon mutual agreement with the contractor, we typically have the option to extend the contract term for additional wells or well pads by providing thirty days' notice prior to the end of the original contract term. We have concluded that our drilling rig arrangements represent short-term operating leases. The accounting guidance requires us to make an assessment at contract commencement if we are reasonably certain that we will exercise the option to extend the term. Due to the continuously evolving nature of our drilling schedules and the potential volatility in commodity prices in an annual period, our strategy to enter into shorter term drilling rig arrangements allows us the flexibility to respond to changes in our operating and economic environment. We exercise our discretion in choosing to extend or not extend contracts on a rig by rig basis depending on the conditions present at the time the contract expires. At the time of contract commencement, we have determined we cannot conclude with reasonable certainty if we will choose to extend the contract beyond its original term. Pursuant to the full cost method, these costs are capitalized as part of natural gas and oil properties on our balance sheet when paid.

Discount Rate

Our leases typically do not provide an implicit rate. Accordingly, we are required to use our incremental borrowing rate in determining the present value of lease payments based on the information available at commencement date. Our incremental borrowing rate reflects the estimated rate of interest that we would pay to borrow on a collateralized basis over a similar term an amount equal to the lease payments in a similar economic environment. We use the implicit rate in the limited circumstances in which that rate is readily determinable.

Practical Expedients and Accounting Policy Elections

Certain of our lease agreements include lease and non-lease components. For all existing asset classes with multiple component types, we have utilized the practical expedient that exempts us from separating lease components from non-lease components. Accordingly, we account for the lease and non-lease components in an arrangement as a single lease component. In addition, for all of our existing asset classes, we have made an accounting policy election not to apply the lease recognition requirements to our short-term leases (that is, a lease that, at commencement, has a lease term of 12 months or less and does not include an option to purchase the underlying asset that we are reasonably certain to exercise). Accordingly, we recognize lease payments related to our short-term leases in our statement of operations on a straight-line basis over the lease term which has not changed from our prior recognition. To the extent that there are variable lease payments, we recognize those payments in our statement of operations in the period in which the obligation for those payments is incurred. None of our current leases contain variable payments. Refer to “Nature of Leases” above for further information regarding those asset classes that include material short-term leases.

The components of our total lease expense for the three and nine months ended September 30, 2020, the majority of which is included in lease operating expense, are as follows:

	Three Months Ended September 30, 2020	Nine Months Ended September 30, 2020
Operating lease cost	\$ 26	\$ 89
Short-term lease expense (1)	\$ 574	\$ 1,676
Total lease expense	<u>\$ 600</u>	<u>\$ 1,765</u>
Short-term lease costs (2)	\$ -	\$ 973

- (1) Short-term lease expense represents expense related to leases with a contract term of 12 months or less.
(2) These short-term lease costs are related to leases with a contract term of 12 months or less which are related to drilling rigs and are capitalized as part of natural gas and oil properties on our balance sheet.

Supplemental balance sheet information related to our operating leases is included in the table below:

	September 30, 2020
Operating lease ROU assets	\$ 250
Operating lease liability - current	\$ 76
Operating lease liabilities - long-term	\$ 147

Our weighted average remaining lease term and weighted average discount rate for our operating leases are as follows:

	September 30, 2020
Weighted Average Remaining Lease Term (in years)	9.95
Weighted Average Discount Rate	6%

Our lease liabilities with enforceable contract terms that are greater than one year mature as follows:

	Operating Leases
Remainder of 2020	\$ 76
2021	49
2022	42
2023	37
2024	4
Thereafter	98
Total lease payments	<u>306</u>
Less imputed interest	(83)
Total lease liability	<u>\$ 223</u>

At September 30, 2020 we had only a lease on a residence and compressor equipment, with minimum lease payments with commitments that had initial or remaining lease terms in excess of one year.

Supplemental cash flow information related to our operating leases is included in the table below:

	Three Months Ended September 30, 2020	Nine Months Ended September 30, 2020
Cash paid for amounts included in the measurement of lease liabilities	\$ -	\$ -
ROU assets added in exchange for lease obligations (since adoption)	\$ -	\$ -

10. Commitments and Contingencies

From time to time, we are involved in litigation relating to claims arising out of our operations in the normal course of business. At September 30, 2020, we were not involved in any legal proceedings that are expected, individually or in the aggregate, to have a material adverse effect on our financial position or results of operations.

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

The following is a discussion and analysis of our financial condition, results of operations, liquidity and capital resources and should be read in conjunction with our consolidated financial statements and the notes thereto, included in this Quarterly Report on Form 10-Q and the consolidated financial statements and notes thereto as of and for the year ended December 31, 2019 and the related Management's Discussion and Analysis of Financial Condition and Results of Operations, both of which are contained in our Annual Report on Form 10-K for the year ended December 31, 2019 filed with the SEC on June 26, 2020. Please see "Forward Looking Information" above.

Except as otherwise noted, all tabular amounts are in thousands, except per unit values.

Critical Accounting Policies

There have been no changes from the Critical Accounting Policies described in our Annual Report on Form 10-K for the year ended December 31, 2019, except for the adoption of Accounting Standards Update 2016-13, Financial Instruments - Credit Losses which was effective January 1, 2020. See "Recently Issued Accounting Standards" for more information.

General

We are an independent energy company primarily engaged in the acquisition, development and production of oil and gas in the United States. Historically, we have grown through the acquisition and subsequent development of producing properties, principally through the development of shale or tight oil reservoirs in areas known to be productive of oil and gas utilizing new technologies such as modern log analysis and reservoir modeling techniques as well as 3-D seismic surveys and horizontal drilling and stage fracturing. As a result of these activities, we believe that we have a number of development opportunities on our properties.

COVID-19 Overview

In the first quarter of 2020, a new strain of coronavirus ("COVID-19") emerged, creating a global health emergency that has been classified by the World Health Organization as a pandemic. As a result of the COVID-19 pandemic, consumer demand for both oil and gas has decreased as a direct result of travel restrictions placed by governments in an effort to curtail the spread of COVID-19. In addition, in March 2020, members of OPEC failed to agree on production levels, which has caused an increased supply and has led to a substantial decrease in oil prices and an increasingly volatile market. OPEC agreed to cut global petroleum output but did not go far enough to offset the impact of COVID-19 on demand. As a result of this decrease in demand and increase in supply, the price of oil and gas has decreased, which has affected our liquidity. On one hand, the Company's commodity hedges protect its cash flows from such price decline but, on the other hand, if oil or natural gas prices remain depressed or continue to decline the Company will be required to record oil and gas property write-downs.

In early March 2020, global oil and natural gas prices declined sharply, have since been volatile, and may decline again. The Company expects ongoing oil and gas price volatility over the short term. The full impact of the coronavirus and the decrease in oil prices continues to evolve as of the date of this report. As such, it is uncertain as to the full magnitude that will have on the Company. Management is actively monitoring the global situation and the impact on the Company's future operations, financial position and liquidity in fiscal year 2020. In response to the price volatility, the Company has taken action to reduce general and administrative costs, including shutting in production in mid-March 2020, but subsequently started restoring production in mid-June, we have also suspended our capital expenditures indefinitely. As of September 30, 2020, a majority of such wells have been brought back on production.

Factors Affecting Our Financial Results

Our financial results depend upon many factors which significantly affect our results of operations including the following:

- commodity prices and the effectiveness of our hedging arrangements;
- the level of total sales volumes of oil and gas;
- the availability of and our ability to raise additional capital resources and provide liquidity to meet cash flow needs;
- the level of and interest rates on borrowings; and
- the level and success of exploration and development activity.

Commodity Prices and Hedging Arrangements.

The results of our operations are highly dependent upon the prices received for our oil and gas production. The prices we receive for our production are dependent upon spot market prices, differentials and the effectiveness of our derivative contracts, which we sometimes refer to as hedging arrangements. Substantially all of our sales of oil and gas are made in the spot market, or pursuant to contracts based on spot market prices, and not pursuant to long-term, fixed-price contracts. Accordingly, the prices received for our oil and gas production are dependent upon numerous factors beyond our control. Significant declines in prices for oil and gas could have a material adverse effect on our financial condition, results of operations, cash flows and quantities of reserves recoverable on an economic basis.

Oil and gas prices have been volatile and are expected to continue to be volatile. As a result of the many uncertainties associated with the world political environment, worldwide supplies of oil, NGL and gas, the availability of other worldwide energy supplies and the relative competitive relationships of the various energy sources in the view of consumers, we are unable to predict what changes may occur in oil, NGL and gas prices in the future. The market price of oil and condensate, NGL and gas in 2020 will impact the amount of cash generated from operating activities, which will in turn impact our financial position.

During the nine months ended September 30, 2020, the NYMEX future price for oil averaged \$38.51 per Bbl as compared to \$56.92 per Bbl in the same period of 2019. During the nine months ended September 30, 2020, the NYMEX future spot price for gas averaged \$1.92 per MMBtu compared to \$2.56 per MMBtu in the same period of 2019. Prices closed on nine months ended September 30, 2020 at \$40.22 per Bbl of oil and \$2.53 per MMBtu of gas, compared to closing on September 30, 2019 at \$58.47 per Bbl of oil and \$2.31 per MMBtu of gas. On November 4, 2020 prices closed at \$39.15 per Bbl of oil and \$3.05 per MMBtu of gas. If commodity prices decline, our revenue and cash flow from operations will also likely decline. In addition, lower commodity prices could also reduce the amount of oil and gas that we can produce economically. If oil and gas prices decline, our revenues, profitability and cash flow from operations will also likely decrease which could cause us to alter our business plans, including reducing our drilling activities. Such declines have required, and in future periods could also require us to write down the carrying value of our oil and gas assets which would also cause a reduction in net income. The prices that we receive are also impacted by basis differentials, which can be significant, and are dependent on actual delivery points. Finally, low commodity prices will likely cause a reduction of our proved reserves.

The realized prices that we receive for our production differ from NYMEX futures and spot market prices, principally due to:

- basis differentials which are dependent on actual delivery location;
- adjustments for BTU content;
- quality of the hydrocarbons; and
- gathering, processing and transportation costs.

The following table sets forth our average differentials for the nine month periods ended September 30, 2020 and 2019:

	Oil - NYMEX		Gas - NYMEX	
	2020	2019	2020	2019
Average realized price (1)	\$ 36.88	\$ 52.05	\$ 0.13	\$ 0.69
Average NYMEX price	38.51	56.92	1.92	2.56
Differential	\$ (1.63)	\$ (4.87)	\$ (1.79)	\$ (1.87)

(1) Excludes the impact of derivative activities.

At September 30, 2020, our derivative contracts consisted of NYMEX-based fixed price swaps and NYMEX basis differential swaps. Under fixed price swaps, we receive a fixed price for our production and pay a variable market price to the contract counter-party. Under basis differential swaps, we receive payment if the basis differential is greater than our swap price and pay when the differential is less than our swap price.

Our derivative contracts equate to approximately 101% of the estimated oil production from our net proved developed producing reserves (based on reserve estimates at September 30, 2020) from October 1 through December 31, 2020, 107% in 2021, 114% in 2022, 85% in 2023 and 104% in 2024 removing a portion of price volatility on our future oil and gas production, we believe we will mitigate, but not eliminate, the potential effects of changing commodity prices on our cash flow from operations for those periods. However, when prevailing market prices are higher than our contract prices, we will not realize increased cash flow. We have in the past and will in the future sustain losses on our derivative contracts if market prices are higher than our contract prices. Conversely, when prevailing market prices are lower than our contract prices, we will sustain gains on our commodity derivative contracts. For the nine months ended September 30, 2020, we realized a gain of \$53.2 million, consisting of a gain of \$14.8 million on closed contracts and a gain of \$38.4 million related to open contracts. For the nine months ended September 30, 2019, we realized a loss of \$11.4 million consisting of a loss of \$4.0 million on closed contracts and a loss of \$7.4 million related to open contracts. We have not designated any of these derivative contracts as hedges as prescribed by applicable accounting rules.

The following table sets forth our derivative contracts at September 30, 2020:

Contract Periods	Oil - WTI	
	Daily Volume (Bbl)	Swap Price (per Bbl)
Fixed Swaps		
2020 October - December	3,436	\$ 54.99
2021 January - December	2,889	\$ 57.62
2022 January - December	2,412	\$ 50.60
2023 January - December	1,498	\$ 50.60
2024 January - December	1,589	\$ 50.60
Basis Swaps		
2020 October - December	4,000	\$ 2.98

At September 30, 2020, the aggregate fair market value of our commodity derivative contracts was a net asset of approximately \$33.4 million.

Production Volumes. Our proved reserves will decline as oil and gas is produced, unless we find, acquire or develop additional properties containing proved reserves or conduct successful exploration and development activities. Based on the reserve information set forth in our reserve report as of December 31, 2019, our average annual estimated decline rate for our net proved developed producing reserves is 41%; 19%; 15%; 12% and 11% in 2020, 2021, 2022, 2023 and 2024, respectively, 8% in the following five years, and approximately 8% thereafter. These rates of decline are estimates and actual production declines could be materially different. While we have had some success in finding, acquiring and developing additional reserves, we have not always been able to fully replace the production volumes lost from natural field declines and property sales. Our ability to acquire or find additional reserves in the future will be dependent, in part, upon the amount of available funds for acquisition, exploration and development projects. In addition, the 1L Amendment limits capex to \$3.0 million over any four consecutive quarters beginning with the quarter ended June 30, 2020. This limit is effective until the First Lien Credit Facility is paid down to \$50.0 million, which will further limit our ability to replace production volumes. The decline in oil prices that occurred in March 2020, due to COVID-19, has resulted in the suspension of our 2020 drilling program as well as shutting in production for some period of time. Both of these measures will impact our production volumes going forward.

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We had capital expenditures during the nine months ended September 30, 2020 of \$6.1 million related to our exploration and development activities, net of changes in capital expenditures in accounts payable and changes in the asset retirement obligation balance. Our capital expenditure budget for 2020 has been suspended indefinitely. Management and the board of directors are also considering additional operating and overhead cost efficiencies that could be realized in connection with the 2020 budget. The amendments to our credit facilities, described in the "Liquidity and Capital Resources" section below, limit our capital expenditures to \$3.0 million in any four consecutive quarters, beginning with the quarter ended June 30, 2020. Our capital expenditures will not be able to offset oil and gas production decreases caused by natural field declines.

The following table presents historical net production volumes for the three and nine months ended September 30, 2020, and 2019:

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2020	2019	2020	2019
Total production (MBoe)	492	911	1,265	2,760
Average daily production (Boepd)	5,346	9,899	4,616	10,112
% Oil	71%	66%	64%	68%

The following table presents our net oil, gas and NGL production, the average sales price per Bbl of oil and NGL and per Mcf of gas produced and the average cost of production per Boe of production sold, for the three and nine months ended September 30, 2020, and 2019, by our major operating regions:

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2020	2019	2020	2019
Oil production (MBbls)				
Rocky Mountain	138	319	376	1,085
Permian/Delaware Basin	209	268	437	736
South Texas	-	13	-	49
Total	347	600	813	1,870
Gas production (MMcf)				
Rocky Mountain	331	605	966	1,706
Permian/Delaware Basin	123	311	438	1,079
South Texas	-	86	-	267
Total	454	1,002	1,404	3,052
NGL production (MBbls)				
Rocky Mountain	55	103	168	272
Permian/Delaware Basin	14	41	50	109
South Texas	-	-	-	-
Total	69	144	218	381
Total production (MBoe) (1)				
	492	911	1,265	2,760
Average sales price per Bbl of oil (2)				
Rocky Mountain	\$ 34.76	\$ 50.60	\$ 35.13	\$ 51.17
Permian/Delaware Basin	36.68	53.55	38.38	52.87
South Texas	-	57.40	-	59.11
Composite	35.92	52.07	36.88	52.05
Average sales price per Mcf of gas (2)				
Rocky Mountain	\$ (0.01)	\$ 0.02	\$ 0.07	\$ 0.69
Permian/Delaware Basin	0.63	0.21	0.25	0.35
South Texas	-	1.71	-	2.07
Composite	0.17	0.23	0.13	0.69
Average sales price per Bbl of NGL				
Rocky Mountain	\$ -	\$ (0.19)	\$ 0.54	\$ 3.52
Permian/Delaware Basin	3.74	1.96	1.23	3.86
South Texas	-	-	-	-
Composite	0.76	0.42	0.70	3.63
Average sales price per Boe (2)				
	\$ 25.60	\$ 34.60	\$ 23.96	\$ 36.53
Average cost of production per Boe produced (3)				
Rocky Mountain	\$ 8.36	\$ 5.02	\$ 7.52	\$ 5.02
Permian/Delaware Basin	7.63	7.28	12.60	11.56
South Texas	-	17.33	-	16.60
Composite	7.99	6.29	9.78	7.84

(1) Oil and gas were combined by converting gas to Boe on the basis of 6 Mcf of gas to 1 Bbl of oil.

(2) Before the impact of hedging activities.

(3) Production costs include direct lease operating costs but exclude ad valorem taxes and production taxes.

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Availability of Capital. As described more fully under "Liquidity and Capital Resources" below, our sources of capital are cash flow from operating activities, proceeds from the sale of properties, monetizing of derivative instruments, and if an appropriate opportunity presents itself, the sale of debt or equity securities, although we may not be able to complete any asset sales or financing on terms acceptable to us, if at all. Our credit facilities were amended in June 2020. The borrowing base under our First Lien Credit Facility was reduced to the then outstanding balance of \$102.0 million, resulting in no additional availability. Additionally, any excess cash, as defined in the First Lien Credit Facility, will be applied to the outstanding balance on a monthly

basis, and the borrowing base will be reduced to the new outstanding balance. As a result, with the exception of \$3.0 million of funds available for working capital purposes, we expect to have limited available capital.

Borrowings and Interest. At September 30, 2020, we had a total of \$100.0 million outstanding under our First Lien Credit Facility, \$118.3 million under our Second Lien Credit facility, including a \$10.0 million exit fee, and total indebtedness of \$221.2 million (including the current portion). If interest expense increases as a result of higher interest rates or increased borrowings, more cash flow from operations would be used to meet debt service requirements. Although as noted above, under the terms of the amended Second Lien Credit Facility, interest under the 2nd Lien Notes is now paid-in-kind.

Exploration and Development Activity. We believe that our high quality asset base, high degree of operational control and inventory of drilling projects position us for future growth should oil and gas prices rebound in the future. At December 31, 2019, we operated properties accounting for virtually all of our PV-10, giving us substantial control over the timing and incurrence of operating and capital expenditures. We have identified numerous additional drilling locations on our existing leaseholds, the successful development of which we believe could significantly increase our production and proved reserves. However, the amendments to our First Lien Credit Facility and Second Lien Credit facility place severe restrictions on our future capital expenditures and we have suspended any planned drilling activity for 2020 indefinitely.

Our future oil and gas production, and therefore our success, is highly dependent upon our ability to find, acquire and develop additional reserves that are profitable to produce. The rate of production from our oil and gas properties and our proved reserves will decline as our reserves are produced unless we acquire additional properties containing proved reserves, conduct successful development and exploration activities or, through engineering studies, identify additional behind-pipe zones or secondary recovery reserves. We cannot assure you that we will have any significant exploration and development activities in the near term or that they will result in increases in our proved reserves. If our proved reserves decline in the future, our production may also decline and, consequently, our cash flow from operations will decline. Approximately 28% of our estimated proved reserves on a Boe basis at September 30, 2020 were undeveloped. By their nature, estimates of undeveloped reserves are less certain. Recovery of such reserves will require significant capital expenditures and successful drilling operations. We will be unable to acquire or develop additional reserves or develop our existing undeveloped reserves, in which case our results of operations and financial condition are expected to be adversely affected.

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Results of Operations

Selected Operating Data. The following table sets forth operating data from continuing operations for the periods presented.

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2020	2019	2020	2019
Operating revenue (1):				
Oil sales	\$ 12,466	\$ 31,228	\$ 29,971	\$ 97,355
Gas sales	75	226	183	2,107
NGL sales	52	61	152	1,382
Other	2	21	8	26
Total operating revenues	\$ 12,595	\$ 31,536	\$ 30,314	\$ 100,870
Operating (loss) income	\$ (56,661)	\$ 8,053	\$ (147,916)	\$ 23,696
Oil sales (MBbls)	347	600	813	1,870
Gas sales (MMcf)	454	1,002	1,404	3,052
NGL sales (MBbls)	69	144	218	381
Oil equivalents (MBoe)	492	911	1,265	2,760
Average oil sales price (per Bbl)(1)	\$ 35.92	\$ 52.07	\$ 36.88	\$ 52.05
Average gas sales price (per Mcf)(1)	\$ 0.17	\$ 0.23	\$ 0.13	\$ 0.69
Average NGL sales price (per Bbl)	\$ 0.76	\$ 0.42	\$ 0.70	\$ 3.63
Average oil equivalent sales price (Boe) (1)	\$ 25.60	\$ 34.60	\$ 23.96	\$ 36.53

(1) Revenue and average sales prices are before the impact of hedging activities.

Comparison of Three Months Ended September 30, 2020 to Three Months Ended September 30, 2019

Operating Revenue. During the three months ended September 30, 2020, operating revenue decreased to \$12.6 million from \$31.5 million for the same period of 2019. The decrease in revenue was primarily due to lower sales volumes as well as lower commodity prices during the three months ended September 30, 2020 as compared to the same period of 2019. Lower sales volumes were the result of our decision to shut-in a significant amount of our production in mid-March as a result of the drastic price drop in early March due predominantly to the COVID 19 pandemic as well as geopolitical issues impacting supply and demand. We started bringing the shut in wells back on production in June 2020, and as of September 3, 2020, a majority of such wells have been brought back on production. Lower sales volumes for all products had a negative impact of \$13.3 million and lower realized commodity prices for all products had a negative impact of \$5.6 million on operating revenue for the three months ended September 30, 2020.

Oil sales volumes decreased to 347 MBbl during the three months ended September 30, 2020 from 600 MBbl for the same period of 2019. The decrease in oil sales volume was primarily due to wells being shut in for most of the second quarter due to severely depressed prices. We started bringing the shut in wells back on production in June, and as of September 30, 2020, a majority of such wells have been brought back on production. Gas sales volumes decreased to 454 MMcf for the three months ended September 30, 2020 from 1,002 MMcf for the same period of 2019. Overall production of oil and gas was down, primarily as a result of the COVID-19 virus and other geopolitical issues affecting the supply and demand for oil and natural gas, and accordingly, so were the prices we received. We made the decision to begin shutting in wells in mid-March. The majority of our oil production was shut in from mid-March through mid-June, when prices had partially recovered. We began bringing wells back on production in mid-June, and had a significant amount of our oil production back on line in July. As of September 30, 2020, a majority of such wells have been brought back on production. The decrease in gas production was primarily due to shut in wells as discussed above.

Lease Operating Expenses (“LOE”). LOE for the three months ended September 30, 2020 decreased to \$3.9 million from \$5.6 million for the same period of 2019. The decrease in LOE was primarily due to the disposition of our south Texas properties during the fourth quarter of 2019 and lower non-

recurring LOE in 2020 as compared to 2019. Additionally, during the first nine months of 2020, we purchased certain production equipment that we had previously been renting and brought electrical power into most of our West Texas locations eliminating the need for generator rentals. We also reduced our work force in North Dakota in May 2020 and eliminated substantially all field overtime. LOE per Boe for the three months ended September 30, 2020 was \$8.00 compared to \$6.20 for the same period of 2019. The increase per Boe was due primarily to our intentional reduction in sales volumes, offset by lower total costs for the three months ended September 30, 2020 as compared to the same period of 2019. Due to management's decision to shut in substantially all production for most of the second quarter, management believes the absolute decrease in cost is more relevant than the cost per BOE.

Production and Ad Valorem Taxes. Production and ad valorem taxes for the three months ended September 30, 2020 decreased to \$1.5 million from \$2.5 million for the same period of 2019. Production and ad valorem taxes for the three months ended September 30, 2020 were 12% of total oil, gas and NGL sales as compared to 8% for the same period of 2019. The increase in the percentage of revenue is primarily due to ad valorem taxes that are not impacted by production tax rates.

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General and Administrative (“G&A”) Expense. G&A expenses, excluding stock-based compensation, was decreased to \$1.8 million for the three months ended September 30, 2020 as compared to \$2.2 million in the same period of 2019. The reduction in total G&A expense was primarily due to a reduction in personnel in the corporate office, as well as reductions in salaries. Officer salaries were reduced by 20% effective March 1, 2020, and our CEO took an additional 20% reduction in salary effective April 1, 2020. G&A per Boe, excluding stock-based compensation, was \$3.56 for the quarter ended September 30, 2020 compared to \$2.45 for the same period of 2019. The increase per Boe was primarily due to lower sales volumes. Due to management's decision to shut in substantially all production for most of the second quarter and a portion of the third quarter, management believes the absolute decrease in cost is more relevant than the cost per BOE.

Stock-Based Compensation. Options granted to employees and directors are valued at the date of grant and expense is recognized over the options' vesting period. In addition to options, restricted shares of our common stock have been granted and are valued at the date of grant and expense is recognized over their vesting period. For the three months ended September 30, 2020, stock-based compensation expense was \$0.3 million compared to \$0.5 million for the same period of 2019. The decrease was primarily due to the cancellation, forfeiture of restricted stock and performance based restricted stock.

Depreciation, Depletion and Amortization (“DD&A”) Expense. DD&A expense, excluding accretion of future site development, for the three months ended September 30, 2020 decreased to \$6.9 million from \$12.6 million for the same period of 2019. The decrease was primarily due to lower future development cost included in the September 30, 2020 internal reserve report, as well as lower production volumes during the three months ended September 30, 2020 as compared to the same period of 2019. DD&A expense per Boe for the three months ended September 30, 2020 was \$14.06 compared to \$13.84 in the same period of 2019. The increase in DD&A expense per Boe was primarily due to a lower full cost pool as the result of the impairment incurred as of December 31, 2019 and September 30, 2020.

Ceiling Limitation Write-Down. We record the carrying value of our oil and gas properties using the full cost method of accounting for oil and gas properties. Under this method, we capitalize the cost to acquire, explore for and develop oil and gas properties. Under the full cost accounting rules, the net capitalized cost of oil and gas properties less related deferred taxes, are limited by country, to the lower of the unamortized cost or the cost ceiling, defined as the sum of the present value of estimated unescalated future revenues from proved reserves, discounted at 10%, plus the cost of properties not being amortized, if any, plus the lower of cost or estimated fair value of unproved properties included in the costs being amortized, if any, less related income taxes. If the net capitalized cost of oil and gas properties exceeds the ceiling limit, we are subject to a ceiling limitation write-down to the extent of such excess. A ceiling limitation write-down is a charge to earnings which does not impact cash flow from operating activities. However, such write-downs do impact the amount of our stockholders' equity and reported earnings. As of September 30, 2020, our net capitalized costs of oil and gas properties exceeded the cost ceiling of our estimated proved reserves, resulting in the recognition of an impairment of \$54.6 million for the three months ended September 30, 2020. As of September 30, 2019, our net capitalized costs of oil and gas properties did not exceed the cost ceiling of our estimated proved reserves.

The risk that we will be required to write-down the carrying value of our oil and gas assets increases when oil and gas prices are depressed or volatile. In addition, write-downs may occur if we have substantial downward revisions in our estimated proved reserves. We cannot assure you that we will not experience additional write-downs in the future. The decline in commodity prices, due to COVID-19, may result in our proved reserves being revised downward, requiring further write-down of the carrying value of our oil and gas properties during the remainder of 2020.

Interest Expense. Interest expense for the three months ended September 30, 2020 increased to \$5.7 million compared to \$3.0 million for the same period of 2019. The increase in interest expense in 2020 was due to higher levels of debt during the three months ended September 30, 2020 as compared to the same period of 2019, as well as higher overall interest rates in 2020 as compared to 2019. For the three months ended September 30, 2020 the interest rate on our first lien credit facility averaged 3.7% as compared to 5.8% for the same period of 2019. For the three months ended September 30, 2020 the interest rate on our second lien credit facility averaged 15.8%. We anticipate higher interest rates and increased interest expense in the future as a result of the amendments to our credit facilities. For the three months ended September 30, 2020, approximately \$4.2 million in interest expense on our Second Lien Credit Facility was paid in kind.

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Loss (Gain) on Derivative Contracts. Derivative gains or losses are determined by actual derivative settlements during the period and on the periodic mark to market valuation of derivative contracts in place at period end. We have elected not to apply hedge accounting to our derivative contracts; therefore, fluctuations in the market value of the derivative contracts are recognized in earnings during the current period. Our derivative contracts consisted of NYMEX-based fixed price swaps and basis differential swaps as of September 30, 2020, and September 30, 2019. The net estimated value of our commodity derivative contracts was a net asset of approximately \$33.4 million as of September 30, 2020. When our derivative contract prices are higher than prevailing market prices, we incur gains and, conversely, when our derivative contract prices are lower than prevailing market prices, we incur losses. For the three months ended September 30, 2020, we recognized a loss on our commodity derivative contracts of \$6.6 million, consisting of a gain on closed contracts of \$3.6 million and a loss of \$10.2 million related to open contracts. For the three months ended September 30, 2019, we recognized a gain on our commodity derivative contracts of \$12.1 million, consisting of a loss of \$1.2 million on closed contracts and a gain of \$13.3 million related to open contracts.

Income Tax Expense. For the three months ended September 30, 2020 and September 30, 2019 there was no income tax expense recognized due to our NOL carryforwards. The Coronavirus Aid, Relief, and Economic Security Act (the "CARES Act"), that was enacted March 27, 2020, includes income tax provisions that allow net operating losses ("NOLs") to be carried back, allows interest expense to be deducted up to a higher percentage of adjusted taxable income, and modifies tax depreciation of qualified improvement property, among other provisions. These provisions did not have a material impact on the Company.

Comparison of Nine Months Ended September 30, 2020 to Nine Months Ended September 30, 2019

Operating Revenue. During the nine months ended September 30, 2020, operating revenue decreased to \$30.3 million from \$100.9 million for the same period of 2019. The decrease in revenue was primarily due to lower commodity prices as well as lower sales volumes during the nine months ended September 30, 2020 as compared to the same period of 2019. Lower realized commodity prices for all products had a negative impact of \$15.2 million on operating revenue, lower sales volumes for all products negatively impacted revenue by \$55.4 million for the nine months ended September 30, 2020.

Oil sales volumes decreased to 813 MBbl during the nine months ended September 30, 2020 from 1,870 MBbl for the same period of 2019. Overall production of oil and gas was down, primarily as a result of the COVID-19 virus and other geopolitical issues affecting the supply and demand for oil and natural gas, and accordingly the prices we received. We made the decision to begin shutting in wells in mid-March. The majority of our oil production was shut in from mid-March through mid-June, when prices had recovered somewhat. We began bringing wells back on production in mid-June and had a significant amount of our oil production back on line in July. As of September 30, 2020, a majority of such wells have been brought back on production. The decrease in gas production was primarily due to shut in wells as discussed above. Additionally, we have had a number of dry gas wells in west Texas shut in since approximately April 2019 due to negative gas prices.

Lease Operating Expenses ("LOE"). LOE for the nine months ended September 30, 2020 decreased to \$12.3 million from \$21.4 million for the same period of 2019. The decrease in LOE was primarily due to the disposition of our south Texas properties during the fourth quarter of 2019, and lower non-recurring LOE in 2020 as compared to the same period of 2019. LOE per Boe for the nine months ended September 30, 2020 was \$9.71 compared to \$7.77 for the same period of 2019. The increase per Boe was due to primarily to lower sales volumes, offset by lower total costs for the nine months ended September 30, 2020 as compared to the same period of 2019. Due to management's decision to shut in substantially all production for most of the second quarter, management believes the absolute decrease in cost is more relevant than the cost per BOE.

Production and Ad Valorem Taxes. Production and ad valorem taxes for the nine months ended September 30, 2020 decreased to \$3.6 million from \$8.5 million for the same period of 2019. Production and ad valorem taxes for the nine months ended September 30, 2020 were 12% of total oil, gas and NGL sales as compared to 8% for the same period of 2019. The increase in the percentage of revenue is due to more revenue coming from North Dakota which has a higher tax rate.

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General and Administrative ("G&A") Expense. G&A expenses, excluding stock-based compensation, was decreased to \$5.6 million for the nine months ended September 30, 2020 as compared to \$6.8 million during the same period of 2019. The reduction in total G&A expense was primarily due to a reduction in personnel in the corporate office, as well as reductions in salaries. Officers salaries were reduced by 20% effective March 1, 2020, and our CEO took an additional 20% reduction in salary effective April 1, 2020. G&A expense per Boe, excluding stock-based compensation, was \$4.39 for the quarter ended September 30, 2020 compared to \$2.45 for the same period of 2019. The increase per Boe was primarily due to lower sales volumes. Due to management's decision to shut in substantially all production for most of the second quarter, management believes the absolute decrease in cost is more relevant than the cost per BOE.

Stock-Based Compensation. Options granted to employees and directors are valued at the date of grant and expense is recognized over the options' vesting period. In addition to options, restricted shares of our common stock have been granted and are valued at the date of grant and expense is recognized over their vesting period. For the nine months ended September 30, 2020, stock-based compensation expense was \$0.9 million compared to \$1.4 million for the same period of 2019. The decrease was primarily due to the cancellation, forfeiture of restricted stock and performance based restricted stock.

Depreciation, Depletion and Amortization ("DD&A") Expense. DD&A expense, excluding accretion of future site development, for the nine months ended September 30, 2020 decreased to \$18.7 million from \$38.4 million for the same period of 2019. The decrease was primarily due to lower future development cost included in the September 30, 2020 internal reserve report, as well as lower production volumes during the nine months ended September 30, 2020 as compared to the same period of 2019. DD&A expense per Boe for the nine months ended September 30, 2020 was \$14.82 compared to \$13.90 in the same period of 2019. The increase in DD&A expense per Boe was primarily due to a lower full cost pool as the result of the impairment incurred as of December 31, 2019 and June 30, 2020.

Ceiling Limitation Write-Down. We record the carrying value of our oil and gas properties using the full cost method of accounting for oil and gas properties. Under this method, we capitalize the cost to acquire, explore for and develop oil and gas properties. Under the full cost accounting rules, the net capitalized cost of oil and gas properties less related deferred taxes, are limited by country, to the lower of the unamortized cost or the cost ceiling, defined as the sum of the present value of estimated unescalated future revenues from proved reserves, discounted at 10%, plus the cost of properties not being amortized, if any, plus the lower of cost or estimated fair value of unproved properties included in the costs being amortized, if any, less related income taxes. If the net capitalized cost of oil and gas properties exceeds the ceiling limit, we are subject to a ceiling limitation write-down to the extent of such excess. A ceiling limitation write-down is a charge to earnings which does not impact cash flow from operating activities. However, such write-downs do impact the amount of our stockholders' equity and reported earnings. As of September 30, 2020 our net capitalized costs of oil and gas properties exceeded the cost ceiling of our estimated proved reserves, resulting in the recognition of an impairment of \$136.1 million. As of September 30, 2019, our net capitalized costs of oil and gas properties did not exceed the cost ceiling of our estimated proved reserves.

The risk that we will be required to write-down the carrying value of our oil and gas assets increases when oil and gas prices are depressed or volatile. In addition, write-downs may occur if we have substantial downward revisions in our estimated proved reserves. We cannot assure you that we will not experience additional write-downs in the future. The decline in commodity prices due to COVID-19 and geopolitical issues affecting supply and demand, may result in our proved reserves being revised downward, requiring further write-down of the carrying value of our oil and gas properties during the remainder of 2020.

Interest Expense. Interest expense for the nine months ended September 30, 2020 increased to \$15.6 million compared to \$8.7 million for the same period of 2019. The increase in interest expense in 2020 was due to higher levels of debt during the nine months ended September 30, 2020, as compared to the same period in 2019, as well as higher overall interest rates in 2020 as compared to 2019. For the nine months ended September 30, 2020 the interest rate on our First Lien Credit Facility averaged 4.2% as compared to 5.9% for the same period of 2019. For the nine months ended September 30, 2020 the interest rate on our Second Lien Credit Facility averaged 15.8%. We anticipate higher interest rates and increased interest expense in the future as a result of the amendments to our credit facilities. For the nine months ended September 30, 2020, approximately \$8.3 million of the interest paid on the Second Lien Credit Facility was paid in kind.

Loss (Gain) on Derivative Contracts. Derivative gains or losses are determined by actual derivative settlements during the period and on the periodic mark to market valuation of derivative contracts in place at period end. We have elected not to apply hedge accounting to our derivative contracts; therefore, fluctuations in the market value of the derivative contracts are recognized in earnings during the current period. Our derivative contracts consisted of NYMEX-based fixed price swaps and basis differential swaps as of September 30, 2020, and September 30, 2019. The net estimated value of our commodity derivative contracts was a net asset of approximately \$33.4 million as of September 30, 2020. When our derivative contract prices are higher than prevailing market prices, we incur gains and, conversely, when our derivative contract prices are lower than prevailing market prices, we incur losses. For the nine months ended September 30, 2020, we recognized a gain on our commodity derivative contracts of \$53.2 million, consisting of a gain on closed contracts of \$14.8 million and a gain of \$38.4 million related to open contracts. For the nine months ended September 30, 2019, we recognized a loss on our commodity derivative contracts of \$11.4 million, consisting of a loss of \$4.0 million on closed contracts and a loss of \$7.4 million related to open contracts.

Income Tax Expense. For the nine months ended September 30, 2020 and September 30, 2019 there was no income tax expense recognized due to our NOL carryforwards. The CARES Act, that was enacted March 27, 2020 includes income tax provisions that allow net operating losses (NOL's) to be carried back, allows interest expense to be deducted up to a higher percentage of adjusted taxable income, and modifies tax depreciation of qualified improvement property, among other provisions. These provisions did not have a material impact on the Company.

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Liquidity and Capital Resources

General. The oil and gas industry is a highly capital intensive and cyclical business. Our capital requirements are driven principally by our obligations to service debt and to fund the following:

- the development and exploration of existing properties, including drilling and completion costs of wells;
- acquisition of interests in additional oil and gas properties; and
- production and transportation facilities.

The amount of capital expenditures we are able to make has a direct impact on our ability to increase cash flow from operations and, thereby, will directly affect our ability to service our debt obligations and to grow the business through the development of existing properties and the acquisition of new properties. In January 2019, we announced that we had engaged Petrie Partners to assist us in identifying and assessing our options for our Bakken properties. In October 2019 we announced that we had broadened the engagement of Petrie Partners to include a more thorough review of our business and strategic plans, competitive positioning and potential alternative transactions that might further enhance shareholder value. Petrie's expanded mandate to assess options for Abraxas is a broad one, which might include sales of assets, merger or acquisition transactions, additional financing alternatives or other strategic transactions. Due to the drastic decrease in oil prices that began in early March 2020 as a result of the OPEC price war and the COVID-19 pandemic, we have suspended capital expenditures for 2020. Subsequently, further negotiations in April 2020 between members of OPEC and Russia led to an agreement to reduce production volumes in an effort to stabilize global oil prices. While prices have recovered from the lows in March 2020, they remain at depressed levels. If oil prices remain at depressed levels, we may incur additional impairments in 2020, which could include impairment of our proved undeveloped reserves.

Our principal sources of capital are cash flows from operations, proceeds from the sale of properties, and if an opportunity presents itself, the sale of debt or equity securities, although we may not be able to sell properties or complete any financings on terms acceptable to us, if at all. We believe that our cash flow from these sources going forward, will be adequate to fund our operations. In June 2020, the borrowing base on our First Lien Credit Facility was reduced to the then outstanding balance of \$102.0 million, with no further availability. Additionally, any excess cash, as defined in the First Lien Credit Facility, will be applied to the outstanding balance on a monthly basis, and the borrowing base will be reduced to the new outstanding balance. We shut in production in mid-March resulting in future cash flows being driven by hedge settlements, and our ability to successfully implement cost reductions and restart production. We started bringing the shut-in wells back on production in June 2020, and as of September 30, 2020, the majority of such wells have been brought back on production.

Working Capital (Deficit). At September 30, 2020, our current assets \$26.6 million exceeded our current liabilities of \$16.3 million resulting in a working capital surplus of \$10.3 million. This compares to a working capital deficit of \$28.6 million at December 31, 2019. Current assets as of September 30, 2020 primarily consisted of accounts receivable of \$7.5 million, current portion of our derivative asset of \$17.4 million and other current assets of \$1.1 million. Current liabilities at September 30, 2020 primarily consisted of trade payables of \$6.5 million, revenues due third parties of \$6.4 million, current maturities of long-term debt of \$0.3 million, the current portion of our derivative liability of \$1.5 million accrued interest of \$0.1 million and other accrued expenses and other of \$1.2 million.

Capital Expenditures. Capital expenditures for the nine months ended September 30, 2020, and 2019 were \$6.6 million and \$89.6 million, respectively.

The table below sets forth the components of these capital expenditures:

	Nine Months Ended September 30,	
	2020	2019
	(In thousands)	
Expenditure category:		
Exploration/Development	\$ 6,410	\$ 89,493
Acquisitions	-	-

During the nine months ended September 30, 2020 and 2019 our capital expenditures were primarily for development of our existing properties. Cash basis capital expenditures for the nine months ended September 30, 2020 of \$13.2 million includes \$6.6 million for a decrease in capital expenditures in accounts payable, resulting in net accrual basis capital expenditures of \$6.6 million. As previously described our amended credit facilities limit capital expenditures to \$3.0 million for any four consecutive quarters beginning with the quarter ended June 30, 2020. Based on our capital expenditure limits, the Company will not be able to offset oil and gas production decreases caused by natural field declines.

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Sources of Capital. The net funds provided by and/or used in each of the operating, investing and financing activities are summarized in the following table and discussed in further detail below:

	Nine Months Ended September 30,	
	2020	2019
	(In thousands)	
Net cash provided by operating activities	\$ 10,734	\$ 61,017
Net cash used in investing activities	(13,187)	(72,856)
Net cash provided by financing activities	3,036	18,111
Total	<u>\$ 583</u>	<u>\$ 6,272</u>

Operating activities for the nine months ended September 30, 2020 provided \$10.7 million in cash compared to providing \$61.0 million in the same period of 2019. Lower net income offset by higher unrealized gains on derivatives and changes in operating assets and liabilities accounted for most of these funds. Investing activities used \$13.2 million during the nine months ended September 30, 2020 primarily for the development of our existing properties, investing activities also included a reduction in accounts payable related to capital expenditures of \$6.6 million. Investing activities used \$72.9 million during the nine months ended September 30, 2019 primarily for the development of our existing properties. Financing activities provided \$3.0 million for the nine months ended September 30, 2020 compared to providing \$18.1 million for the same period of 2019. Funds provided during the nine months ended September 30, 2020 and 2019, were primarily net proceeds from borrowings under our credit facility.

Future Capital Resources.

Our principal sources of capital going forward, for 2020 and beyond, are cash flows from operations, proceeds from the sale of properties, monetizing of derivative instruments and if an opportunity presents itself, the sale of debt or equity securities, although we may not be able to complete the sale of properties or financing on terms acceptable to us, if at all.

Cash from operating activities is dependent upon commodity prices and production volumes. A decrease in commodity prices from current levels would likely reduce our cash flows from operations. Unless we otherwise expand and develop reserves, our production volumes will decline as reserves are produced. In the future we may continue to sell producing properties, which could further reduce our production volumes. To offset the loss in production volumes resulting from natural field declines and sales of producing properties, we must conduct successful exploration and development activities, acquire additional producing properties or identify and develop additional behind-pipe zones or secondary recovery reserves. We believe our numerous drilling opportunities will allow us to increase our production volumes; however, our drilling activities are subject to numerous risks, including the risk that no commercially productive oil and gas reservoirs will be found. If our proved reserves decline in the future, our production will also decline and, consequently, our cash flows from operations will decline. The risk of not finding commercially productive reservoirs will be compounded by the fact that 28% of our total estimated proved reserves on a Boe basis at September 30, 2020 were classified as undeveloped, in addition, under the amendments to our credit facilities, we have limited capital available to develop these reserves. We believe that given our limited capital expenditure for the remainder of 2020, and our hedge gains that will mitigate the decline in commodity pricing, we have adequate liquidity for the short term. However, should commodity prices remain at the current depressed levels or further decline, it is uncertain that we will have the resources to develop our undeveloped reserves, which will lead to material impairments in 2020 and going forward.

Contractual Obligations. We are committed to making cash payments in the future on the following types of agreements:

- Long-term debt, and
- Operating leases.

Below is a schedule of the future payments that we are obligated to make based on agreements in place as of September 30, 2020:

Contractual Obligations	Payments due in twelve month periods ending:				
	Total	September 30, 2021	September 30, 2022- 2023	September 30, 2024- 2025	Thereafter
Long-term debt (1)	\$ 221,160	\$ 291	\$ 220,869	\$ -	\$ -
Interest on long-term debt (2)	6,356	3,836	2,520	-	-
Paid in kind interest on long-term debt (3)	39,650	17,054	22,596	-	-
Lease obligations	306	76	91	41	98
Total	<u>\$ 267,472</u>	<u>\$ 21,257</u>	<u>\$ 246,076</u>	<u>\$ 41</u>	<u>\$ 98</u>

- (1) These amounts represent the balances outstanding under our credit facilities and the real estate lien note. These payments assume that we will not borrow additional funds.
- (2) Interest expense assumes the balances of our First Lien Credit Facility and Real Estate Lien Note at the end of the period and current effective interest rates.
- (3) Represents interest expense paid in kind on our Second Lien Credit Facility, accrued interest is added to the outstanding balance and is payable at maturity.

We maintain a reserve for costs associated with future site restoration related to the retirement of tangible long-lived assets. At September 30, 2020, our reserve for these obligations totaled \$7.7 million for which no contractual commitments exist. For additional information relating to this obligation, see Note 1 of the Notes to Condensed Consolidated Financial Statements.

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Off-Balance Sheet Arrangements. At September 30, 2020, we had no existing off-balance sheet arrangements, as defined under SEC regulations, that have, or are reasonably likely to have a current or future material effect on our financial condition, revenues or expenses, results of operations, liquidity, capital expenditures or capital resources that are material to investors.

Contingencies. From time to time, we are involved in litigation relating to claims arising out of our operations in the normal course of business. At September 30, 2020, we were not engaged in any legal proceedings that are expected, individually or in the aggregate, to have a material adverse effect on us.

Paycheck Protection Program Loan

On May 4, 2020, the Company entered into an unsecured loan with the U.S. Small Business Administration (the "SBA") in the amount of \$1.4 million under the Paycheck Protection Program (the "PPP Loan") with an interest rate of 1.0% and maturity date two years from the effective date of the PPP Loan. The Paycheck Protection Program was established under the CARES Act and is administered by the SBA. Payments are required to be made in seventeen monthly installments of principal and interest, with the first payment being due on the date that is seven months after the date of the PPP Loan. Under the CARES Act, as amended by the Paycheck Protection Program Flexibility Act of 2020, the PPP Loan is eligible for forgiveness for the portion of the PPP Loan proceeds used for payroll costs and other designated operating expenses, provided at least 60% of the PPP Loan's proceeds are used for payroll costs and the Company meets all necessary criteria for forgiveness. Receipt of these funds requires the Company to, in good faith, certify that the PPP Loan was necessary to support ongoing operations of the Company during the economic uncertainty created by the COVID-19 pandemic. This certification further requires the Company to take into account current business activity and the ability to access other sources of liquidity sufficient to support ongoing operations in a manner that is not significantly detrimental to the business. Additionally, the SBA provides no assurance that the Company will obtain forgiveness of the PPP Loan in whole or in part.

Long-Term Indebtedness.

Long-term debt consisted of the following (in thousands):

	<u>September 30, 2020</u>	<u>December 31, 2019</u>
First Lien Credit Facility	\$ 100,000	\$ 95,778
Second Lien Credit Facility	108,278	100,000
Exit fee - Second Lien Credit Facility	10,000	-
Real estate lien note	<u>2,882</u>	<u>3,091</u>
	221,160	198,869
Less current maturities	<u>(291)</u>	<u>(280)</u>
	220,869	198,589
Deferred financing fees and debt issuance cost, net	<u>(16,938)</u>	<u>(5,871)</u>
Total long-term debt, net of deferred financing fees and debt issuance costs	<u>\$ 203,931</u>	<u>\$ 192,718</u>

First Lien Credit Facility

The Company has a senior secured First Lien Credit Facility with Société Générale, as administrative agent and issuing lender, and certain other lenders. As of September 30, 2020, \$100.0 million was outstanding under the First Lien Credit Facility.

Outstanding amounts under the First Lien Credit Facility accrues interest at a rate per annum equal to (a)(i) for borrowings that we elect to accrue interest at the reference rate at the greater of (x) the reference rate announced from time to time by Société Générale, (y) the federal funds rate plus 0.5%, and (z) daily one-month LIBOR plus, in each case, 1.5%-2.5%, depending on the utilization of the borrowing base, and (ii) for borrowings that we elect to accrue interest at the Eurodollar rate, LIBOR plus 2.5%-3.5% depending on the utilization of the borrowing base and (b) at any time an event of default exists, 3.0% plus the amounts set forth above. At September 30, 2020, the interest rate on the First Lien Credit Facility was approximately 3.7%.

Subject to earlier termination rights and events of default, the stated maturity date of the First Lien Credit Facility is May 16, 2022. Interest is payable quarterly on reference rate advances and not less than quarterly on LIBOR advances. The Company is permitted to terminate the First Lien Credit Facility and is able, from time to time, to permanently reduce the lenders' aggregate commitment under the First Lien Credit Facility in compliance with certain notice and dollar increment requirements.

Each of the Company's subsidiaries has guaranteed our obligations under the First Lien Credit Facility on a senior secured basis. Obligations under the First Lien Credit Facility are secured by a first priority perfected security interest, subject to certain permitted encumbrances, in all of the Company and its subsidiary guarantors' material property and assets. As of March 31, 2020, the collateral is required to include properties comprising at least 90% of the PV-9 of the Company's proven reserves and 95% of the PV-9 of the Company's PDP reserves.

Under the First Lien Credit Facility, the Company is subject to customary covenants, including financial covenants and reporting covenants. The amendment to the First Lien Credit Facility (the "1L Amendment") modified certain provisions of the First Lien Credit Facility, including (i) the addition of monthly mandatory prepayments from excess cash (defined as available cash minus certain cash set-asides and a \$3.0 million working capital reserve) with corresponding reductions to the borrowing base; (ii) the elimination of scheduled redeterminations (which were previously made every six months) and interim redeterminations (which were previously made at the request of the lenders no more than once in the six month period between scheduled redeterminations) of the borrowing base; (iii) the replacement of total debt leverage ratio and minimum asset ratio covenants with a first lien debt leverage ratio covenant (comparing the outstanding debt of the First Lien Credit Facility to the consolidated EBITDAX of the Company and requiring that the ratio not exceed 2.75 to 1.00 as of the last day of each fiscal quarter) and a minimum first lien asset coverage ratio covenant (comparing the sum of, without

duplication, (A) the PV-15 of producing and developed proven reserves of the Company, (B) the PV-9 of the Company's hydrocarbon hedge agreements and (C) the PV-15 of proved reserves of the Company classified as "drilled uncompleted" (up to 20% of the sum of (A), (B) and (C)) to the outstanding debt of the First Lien Credit Facility and requiring that the ratio exceed 1.15 to 1.00 as of the last day of each fiscal quarter ending on or before December 31, 2020, and 1.25 to 1.00 for fiscal quarters ending thereafter); (iv) the elimination of current ratio and interest coverage ratio covenants; (v) additional restrictions on (A) capital expenditures (limiting capital expenditures to \$3.0 million in any four fiscal quarter period (commencing with the four fiscal quarter period ended June 30, 2020 and calculated on an annualized basis for the 1, 2 and 3 quarter periods ending on June 30, 2020, September 30, 2020 and December 31, 2020, respectively, subject to certain exceptions, including capital expenditures financed with the proceeds of newly permitted, structurally subordinated debt and capital expenditures made when (1) the first lien asset coverage ratio is at least 1.60 to 1.00, (2) the Company is in compliance with the first lien leverage ratio, (3) the amounts outstanding under the First Lien Credit Facility are less than \$50.0 million, (4) no default exists under the First Lien Credit Facility and (5) and all representations and warranties in the First Lien Credit Facility and the related credit documents are true and correct in all material respects), (B) outstanding accounts payable (limiting all outstanding and undisputed accounts payable to \$7.5 million, undisputed accounts payable outstanding for more than 60 days to \$2.0 million and undisputed accounts payable outstanding for more than 90 days to \$1.0 million and (C) general and administrative expenses (limiting cash general and administrative expenses the Company may make or become legally obligated to make in any four fiscal quarter period to \$9.0 million for the four fiscal quarter period ended June 30, 2020, \$8.25 million for the four fiscal quarter period ended September 30, 2020, \$6.9 million for the four fiscal quarter period ending December 31, 2020, and \$6.5 million for the fiscal quarter from March 31, 2021 through December 31, 2021 and \$5.0 million thereafter; in all cases, general and administrative expense excludes up to \$1.0 million in certain legal and professional fees; and (vi) permission for up to an additional \$25.0 million in structurally subordinated debt to finance capital expenditures. Under the 1L Amendment, the borrowing base was adjusted from \$135.0 million to \$102.0 million. The borrowing base will be reduced by any mandatory prepayments from excess cash flow (in an amount equal to such prepayment) and upon the disposition of the Company's oil and gas properties.

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As of September 30, 2020 we were in compliance with the financial covenants under the First Lien Credit Facility.

The First Lien Credit Facility contains a number of covenants that, among other things, restrict our ability to:

- incur or guarantee additional indebtedness;
- transfer or sell assets;
- create liens on assets;
- pay dividends or make other distributions on capital stock or make other restricted payments;
- engage in transactions with affiliates other than on an "arm's length" basis;
- make any change in the principal nature of our business; and
- permit a change of control.

The First Lien Credit Facility also contains customary events of default, including nonpayment of principal or interest, violations of covenants, cross default and cross acceleration to certain other indebtedness, bankruptcy and material judgments and liabilities.

Second Lien Credit Facility

On November 13, 2019, we entered into the Term Loan Credit Agreement, with Angelo Gordon Energy Servicer, LLC, as administrative agent, and certain other lenders party thereto, which we refer to as the Second Lien Credit Facility. The Second Lien Credit facility was amended on June 25, 2020. The Second Lien Credit Facility has a maximum commitment of \$100.0 million. On November 13, 2019, \$95.0 million of the net proceeds obtained from the Second Lien Credit Facility were used to permanently reduce the borrowings outstanding on the Second Lien Credit Facility. As of September 30, 2020, the outstanding balance on the Second Lien Credit Facility was \$118.3 million, including an exit fee of \$10.0 million.

The stated maturity date of the Second Lien Credit Facility is November 13, 2022. Prior to the latest amendments to the Second Lien Credit Facility, accrued interest was payable quarterly on reference rate loans and at the end of each three-month interest period on Eurodollar loans. We are permitted to prepay the loans in whole or in part, in compliance with certain notice and dollar increment requirements, and, if such prepayment is made prior to November 13, 2020, subject to payment of a Make Whole Amount, where applicable. "Make Whole Amount" is defined as, the sum of the interest payments (calculated on the basis of the interest rate as of the date of the relevant prepayment without discount) that would have accrued and been paid from the date of prepayment to November 13, 2020 on the principal amount of such prepaid loans, whether such prepayments are optional, mandatory or as a result of acceleration.

Each of our subsidiaries has guaranteed our obligations under the Second Lien Credit Facility. Obligations under the Second Lien Credit Facility are secured by a first priority perfected security interest, subject to certain permitted liens, including those securing the indebtedness under the First Lien Credit Facility to the extent permitted by the Intercreditor Agreement, of even date with the Second Lien Credit Facility, among us, our subsidiaries, Angelo Gordon Energy Servicer, LLC and Société Générale, in all of our subsidiary guarantors' material property and assets. As of September 30, 2020, the collateral is required to include properties comprising at least 90% of the PV-9 of the Company's our proven reserves and 95% of the PV-9 of the Company's PDP reserves.

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Under the Second Lien Credit Facility, the Company is subject to customary covenants, including financial covenants and reporting covenants. The amendment to the Second Lien Credit Facility dated June 25, 2020 (the "2L Amendment") modified certain provisions of the Second Lien Credit Facility, including (i) a requirement that, while the obligations under the First Lien Credit Facility are outstanding, scheduled payments of accrued interest under the Second Lien Credit Facility will be paid in the form of capitalized interest; (ii) an increase in the interest rate by 200bps for interest payable in cash and 500bps for interest payable in kind; (iii) modification of the minimum asset ratio covenant to be the sum of, without duplication, (A) the PV-15 of producing and developed proven reserves of the Company, (B) the PV-9 of the Company's hydrocarbon hedge agreements and (C) the PV-15 of proved reserves of the Company classified as "drilled uncompleted" (up to 20% of the sum of (A), (B) and (C)) to the total outstanding debt of the Company and requiring that the ratio not exceed 1.45 to 1.00 as of the last day of each fiscal quarter ending between September 30, 2021 to December 31, 2021, and 1.55 to 1.00 for fiscal quarters ending thereafter); (iv) modification of the total leverage ratio covenant to set the first test date to occur on September 30, 2021;

(v) modification of the current ratio to eliminate the exclusion of certain valuation accounts associated with hedge contracts from current assets and from current liabilities, (vi) additional restrictions on (A) capital expenditures (limiting capital expenditures to those expenditures set forth in a plan of development approved by Angelo Gordon Energy Servicer, LLC, subject to certain exceptions, including capital expenditures financed with the proceeds of newly permitted, structurally subordinated debt), (B) outstanding accounts payable (limiting all outstanding and undisputed accounts payable to \$7.5 million, undisputed accounts payable outstanding for more than 60 days to \$2.0 million and undisputed accounts payable outstanding for more than 90 days to \$1.0 million and (C) general and administrative expenses (limiting cash general and administrative expenses the Company may make or become legally obligated to make in any four fiscal quarter period to \$9.0 million for the four fiscal quarter period ending June 30, 2020, \$8.25 million for the four fiscal quarter period ending September 30, 2020, \$6.5 million for fiscal quarter period from March 31, 2021 through December 31, 2021 and \$5.0 million thereafter.

As of September 30, 2020 we were in compliance with the financial covenants under the Second Lien Credit Facility as amended.

The Second Lien Credit Facility contains a number of covenants that, among other things, restrict our ability to:

- incur or guarantee additional indebtedness;
- transfer or sell assets;
- create liens on assets;
- pay dividends or make other distributions on capital stock or make other restricted payments;
- engage in transactions with affiliates other than on an “arm’s length” basis;
- make any change in the principal nature of our business; and
- permit a change of control.

The Second Lien Credit Facility also contains customary events of default, including nonpayment of principal or interest, violation of covenants, cross default and cross acceleration to certain other indebtedness, bankruptcy and material judgments and liabilities.

In connection with the amendment to the Second Lien Credit Facility on June 25, 2020, the Company entered into an Exit Fee and Warrant Agreement, subject to NASDAQ approval for the issuance of certain warrants. This agreement was finalized on August 11, 2020 at which time the Company issued a warrant to the lender to purchase a total of 33,445,792 shares of common stock at an exercise price of \$0.01 per share. On October 19, 2020, the Company effected a reverse stock split of the Company's authorized, issued and outstanding shares of common stock at a ratio of 1-for-20, thus the warrant was adjusted to provide that the lender may purchase a total of 1,672,290 shares of common stock at an exercise price of \$0.20 per share. The warrant is exercisable immediately in whole or in part, on or before five years from the issuance date. The fair value of the warrant and exit fee were recorded as debt issuance costs, presented in the consolidated balance sheets as a deduction from the carrying amount of the note payable, and are being amortized over the loan term. The Exit Fee shall be due and payable in cash on the earliest to occur of maturity of the obligation under the Second Lien Credit Facility or the earlier acceleration or payment in full of the same. The 2L Amendment, including the impact of the Exit Fee and Warrant Agreement finalized on August 11, 2020, resulted in the 2L Amendment meeting the criteria of debt extinguishment under the guidance of ASC 470: *Debt*. Accordingly, all debt issuance cost, including the original discount of the original Second Lien Credit Facility, were charged to debt extinguishment loss in the accompanying Condensed Consolidated Statement of Operation in the amount of \$4.1 million.

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Real Estate Lien Note

We have a real estate lien note secured by a first lien deed of trust on the property and improvements which serves as our corporate headquarters. The note was modified on June 20, 2018 to a fixed rate of 4.9% and is payable in monthly installments of \$35,672. The maturity date of the note is July 20, 2023. As of September 30, 2020 and December 31, 2019, \$2.9 million and \$3.1 million, respectively, were outstanding on the note.

Hedging Activities

Our results of operations are significantly affected by fluctuations in commodity prices and we seek to reduce our exposure to price volatility by hedging our production through swaps, options and other commodity derivative instruments. We have entered into commodity swaps on approximately 101% of our estimated oil production from our net proved developed producing reserves (based on reserve estimates at September 30, 2020) from October through December 31, 2020, 107% for 2021, 114% for 2022; 85% for 2023; and 104% for 2024.

By removing a portion of price volatility on our future oil and gas production, we believe that we will mitigate, but not eliminate, the potential effects of changing commodity prices on our cash flow from operations. However, when prevailing market prices are higher than our contract prices, we will not realize increased cash flow on the portion of the production that has been hedged. We have sustained, and in the future, will sustain, losses on our derivative contracts when market prices are higher than our contract prices. Conversely, when prevailing market prices are lower than our contract prices, we will sustain gains on our commodity derivative contracts.

If the disparity between our contract prices and market prices continues, we will sustain gains or losses on our derivative contracts. While gains and losses resulting from the periodic mark to market of our open contracts do not impact our cash flow from operations, gains and losses from settlements of our closed contracts do impact our cash flow from operations.

In addition, as our derivative contracts expire over time, we expect to enter into new derivative contracts at then-current market prices. If the prices at which we hedge future production are significantly lower than our existing derivative contracts, our future cash flow from operations would likely be materially lower.

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Item 3. Quantitative and Qualitative Disclosures about Market Risk.

Commodity Price Risk

As an independent oil and gas producer, our revenue, cash flow from operations, other income and profitability, reserve values, access to capital and future rate of growth are substantially dependent upon the prevailing prices of oil and gas. Declines in commodity prices will adversely affect our financial condition, liquidity, ability to obtain financing and operating results. Lower commodity prices may reduce the amount of oil and gas that we can produce economically. Prevailing prices for such commodities are subject to wide fluctuation in response to relatively minor changes in supply and demand and a variety of additional factors beyond our control, such as global, political and economic conditions. Historically, prices received for our oil and gas production have been volatile and unpredictable, and such volatility is expected to continue. Most of our production is sold at market prices. Generally, if the commodity indexes fall, the price that we receive for our production will also decline. Therefore, the amount of revenue that we realize is partially determined by factors beyond our control. Assuming the production levels we attained during the nine months ended September 30, 2020, a 10% decline in oil and gas prices would have reduced our operating revenue, cash flow and net income by approximately \$3.0 million. If commodity prices decline from current levels, the impact on operating revenues and cash flow, could be much more significant. However, we do have derivative contracts in place that will mitigate the impact of low commodity prices.

Derivative Instrument Sensitivity

At September 30, 2020, the aggregate fair market value of our commodity derivative contracts was a net asset of approximately \$33.4 million. The fair market value of our commodity derivative contracts is sensitive to changes in the market price for oil and gas. When our derivative contract prices are higher than prevailing market prices, we incur gains and conversely, when our derivative contract prices are lower than prevailing market prices, we incur losses.

Interest Rate Risk

We are subject to interest rate risk associated with borrowings under our credit facility and our second lien credit facility. As of September 30, 2020, we had \$100.0 million of outstanding indebtedness under our First Lien Credit Facility and \$108.3 million outstanding under our Second Lien Credit Facility, excluding an exit fee of \$10.0 million, each with a variable interest rate. At September 30, 2020, the interest rate on the credit facility was approximately 3.7% based on 1-month LIBOR borrowings and level of utilization. An increase in the interest rate of 1% would increase our interest expense by \$1.0 million on an annual basis, based on the outstanding balance at September 30, 2020. At September 30, 2020, the interest rate on the Second Lien Credit Facility was approximately 15.75% based on 3-month LIBOR borrowings. An increase of 1% would increase our interest expense by \$1.0 million on an annual basis, based on the outstanding balance at September 30, 2020.

Item 4. Controls and Procedures.

Evaluation of Disclosure Controls and Procedures

As of the end of the period covered by this report, an evaluation of the effectiveness of the design and operation of our disclosure controls and procedures (as defined in Rule 13a-15(e) under the Exchange Act) was performed under the supervision and with the participation of management, including our Chief Executive Officer and Chief Financial Officer. Based upon that evaluation, the Chief Executive Officer and the Chief Financial Officer concluded that, due to the material weakness described below, the Company's disclosure controls and procedures were not effective as of the end of the period covered by this Form 10-Q to provide reasonable assurance that information required to be disclosed by us in our reports filed or submitted under the Exchange Act is recorded, processed, summarized and reported within the time periods specified in the SEC's rules and forms and were not effective as of the end of the period covered by this Form 10-Q to provide reasonable assurance that such information is accumulated and communicated to our management, including our principal executive and financial officers, as appropriate to allow timely discussions regarding required disclosure.

Changes in Internal Control over Financial Reporting

As of the end of the period covered by this report, our Chief Executive Officer and Chief Financial Officer carried out an evaluation of the effectiveness of our "disclosure controls and procedures" (as defined in the Securities Exchange Act of 1934 Rules 13a-15(e) and 15d-15(e)) and concluded that the disclosure controls and procedures were effective and that the deficiency noted at December 31, 2019 has been remediated.

There were no changes in our internal controls over financial reporting during the three months ended September 30, 2020 covered by this report that could materially affect, or are reasonably likely to materially affect, our financial reporting.

PART II

Item 1. Legal Proceedings.

From time to time, we are involved in litigation relating to claims arising out of its operations in the normal course of business. At September 30, 2020, we were not engaged in any legal proceedings that are expected, individually or in the aggregate, to have a material adverse impact on our financial position or results of operations.

Item 1A. Risk Factors.

In addition to the other information set forth in this report, you should carefully consider the factors discussed in Part I, "Item 1A. Risk Factors" in our Annual Report on Form 10-K for the year ended December 31, 2019, which could materially affect our business, financial condition or future results. The risks described in our Annual Report on Form 10-K are not the only risks facing Abraxas. Additional risks and uncertainties not currently known to us or that we currently deem to be immaterial also may materially adversely affect our business, financial condition and/or operating results.

Item 2. Unregistered Sales of Equity Securities and Use of Proceeds.

None

Item 3. Defaults Upon Senior Securities.

None

Item 4. Mine Safety Disclosure.

Not applicable

Item 5. Other Information.

None

Item 6. Exhibits.

(a) Exhibits

Exhibit 31.1	Certification - Robert L.G. Watson, CEO
Exhibit 31.2	Certification - Steven P. Harris, CFO
Exhibit 32.1	Certification pursuant to 18 U.S.C. Section 1350 - Robert L.G. Watson, CEO
Exhibit 32.2	Certification pursuant to 18 U.S.C. Section 1350 - Steven P. Harris, CFO
101.INS	Inline XBRL Instance Document (the Instance Document does not appear in the Interactive Data File because its XBRL tags are embedded within the Inline XBRL document)
101.SCH	Inline XBRL Taxonomy Extension Schema Document
101.CAL	Inline XBRL Taxonomy Extension Calculation Linkbase Document
101.DEF	Inline XBRL Taxonomy Extension Definition Linkbase Document
101.LAB	Inline XBRL Taxonomy Extension Label Linkbase Document
101.PRE	Inline XBRL Taxonomy Extension Presentation Linkbase Document
104	Cover Page Interactive Data File (formatted as Inline XBRL and contained in Exhibit 101)

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ABRAXAS PETROLEUM CORPORATION

SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934, as amended the Registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

Date	November 9, 2020	<u>By: /s/Robert L.G. Watson</u> ROBERT L.G. WATSON, President and Principal Executive Officer
Date	November 9, 2020	<u>By: /s/Steven P. Harris</u> STEVEN P. HARRIS Vice President and Principal Financial Officer
Date	November 9, 2020	<u>By: /s/G. William Krog, Jr.</u> G. WILLIAM KROG, JR., Vice President and Principal Accounting Officer

CERTIFICATIONS

I, Robert L. G. Watson, certify that:

1. I have reviewed this quarterly report on Form 10-Q of Abraxas Petroleum Corporation.
2. Based on my knowledge, this annual report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report.
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report.
4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal controls over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:
 - (a) designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
 - (b) designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
 - (c) evaluated the effectiveness of the registrant's disclosure controls and procedures, and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
 - (d) disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's fourth fiscal quarter that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting.
5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):
 - (a) all significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
 - (b) any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: November 9, 2020

/s/ Robert L.G. Watson

Robert L.G. Watson

Chairman of the Board, President and

Principal Executive Officer

CERTIFICATIONS

I, Steven P. Harris, certify that:

1. I have reviewed this quarterly report on Form 10-Q of Abraxas Petroleum Corporation.
2. Based on my knowledge, this annual report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report.
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report.
4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal controls over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:
 - (a) designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
 - (b) designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
 - (c) evaluated the effectiveness of the registrant's disclosure controls and procedures, and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
 - (d) disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's fourth fiscal quarter that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting.
5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):
 - (a) all significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
 - (b) any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: November 9, 2020

/s/ Steven P. Harris

Steven P. Harris

Vice President and

Principal Financial Officer

**CERTIFICATION PURSUANT TO
18 U.S.C. SECTION 1350,
AS ADOPTED PURSUANT TO
SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002**

In connection with the Quarterly Report of Abraxas Petroleum Corporation (the "Company") on Form 10-Q for the quarter ended September 30, 2020 as filed with the Securities and Exchange Commission on the date hereof (the "Report"), I, Robert L.G. Watson, Chairman of the Board, President and Chief Executive Officer of the Company, certify, pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, that:

- (1) The Report fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934; and
- (2) The information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

/s/ Robert L.G. Watson

Robert L.G. Watson

Chairman of the Board, President and Chief Executive Officer

November 9, 2020

This certification accompanies the Report pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 and shall not, except to the extent required by the Sarbanes-Oxley Act of 2002, be deemed filed by the Company for purposes of §18 of the Securities Exchange Act of 1934, as amended.

A signed original of this written statement required by Section 906 has been provided to the Company and will be retained by the Company and furnished to the Securities and Exchange Commission or its staff upon request.

**CERTIFICATION PURSUANT TO
18 U.S.C. SECTION 1350,
AS ADOPTED PURSUANT TO
SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002**

In connection with the Quarterly Report of Abraxas Petroleum Corporation (the "Company") on Form 10-Q for the quarter ended September 30, 2020 as filed with the Securities and Exchange Commission on the date hereof (the "Report"), I, Steven P. Harris, Vice President and Chief Financial Officer of the Company, certify, pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, that:

- (1) The Report fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934; and
- (2) The information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

/s/Steven P. Harris
Steven P. Harris
Vice President and Chief Financial Officer
November 9, 2020

This certification accompanies the Report pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 and shall not, except to the extent required by the Sarbanes-Oxley Act of 2002, be deemed filed by the Company for purposes of §18 of the Securities Exchange Act of 1934, as amended.

A signed original of this written statement required by Section 906 has been provided to the Company and will be retained by the Company and furnished to the Securities and Exchange Commission or its staff upon request.