

PANHANDLE OIL & GAS INC
Form 10-Q
August 07, 2015

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

FORM 10-Q

Quarterly Report Pursuant to Section 13
or 15(d) of the Securities Exchange Act
of 1934

For ~~the~~ 30,
~~2015~~
period
ended

Transition Report Pursuant to Section 13
or 15(d) of the Securities Exchange Act
of 1934

For _____ to _____
the
transition
period
from

~~00133759~~
Company
File
Number

PANHANDLE OIL AND GAS INC.
(Exact name of registrant as specified in its
charter)

OKLAHOMA 3-1055775
(I.R.S. Employer)

(State
or
other
jurisdiction
of
incorporation/Identification No.)
or
organization)

Grand Centre Suite 300, 5400 N Grand
Blvd., Oklahoma City, Oklahoma 73112
(Address of principal executive offices)

Registrant's
telephone
number
including
area
code

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days.

YesNo

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files).

YesNo

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See definition of "large accelerated filer",

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“accelerated filer” and “smaller reporting company” in Rule 12b-2 of the Exchange Act. (Check one):

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

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).

YesNo

Outstanding 16,546,376
shares of Class
A Common
stock (voting) at
August 6, 2015:

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The following defined terms are used in this report:

“Bbl” barrel.

“Board” board of directors.

“BTU” British Thermal Units.

“Company” Panhandle Oil and Gas Inc.

“completion” the process of treating a drilled well followed by the installation of permanent equipment for the production of crude oil and/or natural gas.

“DD&A” depreciation, depletion and amortization.

“dry hole” exploratory or development well that does not produce crude oil and/or natural gas in economically producible quantities.

“ESOP” the Panhandle Oil and Gas Inc. Employee Stock Ownership and 401(k) Plan, a tax qualified, defined contribution plan.

“exploratory well” a well drilled to find a new field or to find a new reservoir in a field previously found to be productive of crude oil or natural gas in another reservoir.

“FASB” the Financial Accounting Standards Board.

“field” an area consisting of a single reservoir or multiple reservoirs all grouped on, or related to, the same individual geological structural feature or stratigraphic condition. The field name refers to the surface area, although it may refer to both the surface and the underground productive formations.

“G&A” general and administrative costs.

“gross acres” the total acres in which a working interest is owned.

“held by production” or “HBP” an oil and gas lease continued into effect into its secondary term for so long as a producing oil and/or gas well is located on any portion of the leased premises or lands pooled therewith.

“horizontal drilling” a drilling technique used in certain formations where a well is drilled vertically to a certain depth and then drilled horizontally within a specified interval.

“IDC” intangible drilling costs.

“Independent Consulting Petroleum Engineer(s)” or “Independent Consulting Petroleum Engineering Firm” DeGolyer and MacNaughton of Dallas, Texas.

“LOE” lease operating expense.

“Mcf” thousand cubic feet.

“Mcf” natural gas stated on an Mcf basis and crude oil and natural gas liquids converted to a thousand cubic feet of natural gas equivalent by using the ratio of one Bbl of crude oil or natural gas liquids to six Mcf of natural gas.

“Mmbtu” million BTU.

“minerals”, “mineral acres” or “mineral interests” fee mineral acreage owned in perpetuity by the Company.

“net acres” the sum of the fractional working interests owned in gross acres.

“NGL” natural gas liquids.

“NYMEX” New York Mercantile Exchange.

“Panhandle” Panhandle Oil and Gas Inc.

“play” term applied to identified areas with potential oil and/or natural gas reserves.

“proved reserves” the quantities of crude oil and natural gas, which, by analysis of geoscience and engineering data, can be estimated with reasonable certainty to be economically producible from a given date forward, from known reservoirs and under existing economic conditions, operating methods, and government regulations prior to the time at which contracts providing the right to operate expire, unless evidence indicates renewal is reasonably certain.

“royalty interest” well interests in which the Company does not pay a share of the costs to drill, complete and operate a well, but receives a much smaller proportionate share (as compared to a working interest) of production.

“SEC” the United States Securities and Exchange Commission.

“undeveloped acreage” lease acreage on which wells have not been drilled or completed to a point that would permit the production of commercial quantities of crude oil and/or natural gas.

“working interest” well interests in which the Company pays a share of the costs to drill, complete and operate a well and receives a proportionate share of production.

“WTI” West Texas Intermediate.

Fiscal year references

All references to years in this report, unless otherwise noted, refer to the Company’s fiscal year end of September 30. For example, references to 2015 mean the fiscal year ended September 30, 2015.

References to oil and natural gas properties

References to oil and natural gas properties inherently include natural gas liquids associated with such properties.

PART 1 FINANCIAL INFORMATION

PANHANDLE OIL AND GAS INC.

CONDENSED BALANCE SHEETS

	June 30, 2015 (unaudited)	September 30, 2014
Assets		
Current assets:		
Cash and cash equivalents	\$ 925,219	\$ 509,755
Oil, NGL and natural gas sales receivables	9,455,779	16,227,469
Refundable production taxes	585,961	625,996
Derivative contracts, net	5,402,106	1,650,563
Other	196,397	354,828
Total current assets	16,565,462	19,368,611
Properties and equipment at cost, based on successful efforts accounting:		
Producing oil and natural gas properties	438,750,515	418,237,512
Non-producing oil and natural gas properties	8,703,427	10,260,717
Other	1,390,339	1,317,725
	448,844,281	429,815,954
Less accumulated depreciation, depletion and amortization	(222,231,830)	(204,731,661)
Net properties and equipment	226,612,451	225,084,293
Investments	2,087,629	1,936,421
Derivative contracts, net	-	251,279
Total assets	\$ 245,265,542	\$ 246,640,604
Liabilities and Stockholders' Equity		
Current liabilities:		
Accounts payable	\$ 5,948,158	\$ 7,034,773
Deferred income taxes	745,100	600,100
Income taxes payable	1,041,846	523,843
Accrued liabilities and other	1,017,544	1,290,858
Total current liabilities	8,752,648	9,449,574
Long-term debt	65,500,000	78,000,000
Deferred income taxes	40,072,907	37,363,907
Asset retirement obligations	2,786,229	2,638,470
Stockholders' equity:		
Class A voting common stock, \$.0166 par value; 24,000,000 shares authorized, 16,863,004 issued at June 30, 2015, and September 30, 2014	280,938	280,938

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Capital in excess of par value	2,879,000	2,861,343
Deferred directors' compensation	3,014,024	3,110,351
Retained earnings	127,002,060	118,794,188
	133,176,022	125,046,820
Less treasury stock, at cost; 316,628 shares at June 30, 2015, and 372,364 shares at September 30, 2014	(5,022,264)	(5,858,167)
Total stockholders' equity	128,153,758	119,188,653
Total liabilities and stockholders' equity	\$ 245,265,542	\$ 246,640,604

All share and per share amounts were adjusted for the 2-for-1 stock split, effective on October 8, 2014.

(See accompanying notes)

(1)

PANHANDLE OIL AND GAS INC.

CONDENSED STATEMENTS OF OPERATIONS

	Three Months Ended June 30,		Nine Months Ended June 30,	
	2015	2014	2015	2014
	(unaudited)		(unaudited)	
Revenues:				
Oil, NGL and natural gas sales	\$ 11,443,590	\$ 19,534,545	\$ 43,400,839	\$ 59,115,928
Lease bonuses and rentals	1,663,402	137,476	1,945,743	353,422
Gains (losses) on derivative contracts	(1,443,472)	(1,427,165)	11,706,955	(3,511,095)
Income from partnerships	85,368	130,121	373,555	565,523
	11,748,888	18,374,977	57,427,092	56,523,778
Costs and expenses:				
Lease operating expenses	4,071,634	2,961,750	13,233,980	9,930,147
Production taxes	362,548	593,941	1,384,217	1,871,538
Exploration costs	19,911	6,956	48,368	70,140
Depreciation, depletion and amortization	5,729,460	5,314,777	17,680,069	15,562,630
Provision for impairment	132,118	-	3,532,760	430,143
Loss (gain) on asset sales and other	(18,459)	3,897	(27,586)	31,086
Interest expense	383,047	40,697	1,195,056	40,697
General and administrative	1,565,575	1,825,374	5,374,206	5,349,921
	12,245,834	10,747,392	42,421,070	33,286,302
Income (loss) before provision (benefit) for income taxes	(496,946)	7,627,585	15,006,022	23,237,476
Provision (benefit) for income taxes	232,000	2,505,000	4,797,000	7,534,000
Net income (loss)	\$ (728,946)	\$ 5,122,585	\$ 10,209,022	\$ 15,703,476
Basic and diluted earnings (loss) per common share (Note 3)	\$ (0.04)	\$ 0.31	\$ 0.61	\$ 0.94
Basic and diluted weighted average shares outstanding:				
Common shares	16,514,435	16,474,040	16,504,512	16,470,372
Unissued, directors' deferred compensation shares	246,893	255,670	256,084	252,102
	16,761,328	16,729,710	16,760,596	16,722,474
Dividends declared per share of common stock and paid in period	\$ 0.04	\$ 0.04	\$ 0.12	\$ 0.12

All share and per share amounts were adjusted for the 2-for-1 stock split, effective on October 8, 2014.

(See accompanying notes)

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PANHANDLE OIL AND GAS INC.

STATEMENTS OF STOCKHOLDERS' EQUITY

Nine Months Ended June 30, 2015

	Class A voting Common Stock Shares	Amount	Capital in Excess of Par Value	Deferred Directors' Compensation	Retained Earnings	Treasury Shares	Treasury Stock	Total
Balances at September 30, 2014	16,863,004	\$ 280,938	\$ 2,861,343	\$ 3,110,351	\$ 118,794,188	(372,364)	\$ (5,858,167)	\$ 119,188
Purchase of treasury stock	-	-	-	-	-	(12,719)	(242,313)	(242,313)
Restricted stock awards	-	-	740,043	-	-	-	-	740,043
Net income	-	-	-	-	10,209,022	-	-	10,209,022
Dividends (\$.12 per share)	-	-	-	-	(2,001,150)	-	-	(2,001,150)
Distribution of restricted stock to officers and directors	-	-	(738,432)	-	-	46,083	725,858	(12,574)
Distribution of deferred directors' compensation	-	-	16,046	(328,415)	-	22,372	352,358	39,989
Increase in deferred directors' compensation charged to expense	-	-	-	232,088	-	-	-	232,088
Balances at June 30, 2015 (unaudited)	16,863,004	\$ 280,938	\$ 2,879,000	\$ 3,014,024	\$ 127,002,060	(316,628)	\$ (5,022,264)	\$ 128,153

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Nine Months Ended June 30, 2014

	Class A voting Common Stock Shares	Amount	Capital in Excess of Par Value	Deferred Directors' Compensation	Retained Earnings	Treasury Shares	Treasury Stock	Total
Balances at September 30, 2013	16,863,004	\$ 280,938	\$ 2,447,424	\$ 2,756,526	\$ 96,454,449	(400,496)	\$ (6,283,851)	\$ 95,655,449
Purchase of treasury stock	-	-	-	-	-	(7,444)	(122,044)	(122,044)
Restricted stock awards	-	-	499,791	-	-	-	-	499,791
Net income	-	-	-	-	15,703,476	-	-	15,703,476
Dividends (\$.12 per share)	-	-	-	-	(1,995,812)	-	-	(1,995,812)
Distribution of restricted stock to officers and directors	-	-	(320,014)	-	-	22,192	337,198	17,184
Increase in deferred directors' compensation charged to expense	-	-	-	269,608	-	-	-	269,608
Balances at June 30, 2014 (unaudited)	16,863,004	\$ 280,938	\$ 2,627,201	\$ 3,026,134	\$ 110,162,113	(385,748)	\$ (6,068,697)	\$ 110,027,003

All share and per share amounts were adjusted for the 2-for-1 stock split, effective on October 8, 2014.

(See accompanying notes)

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PANHANDLE OIL AND GAS INC.

CONDENSED STATEMENTS OF CASH FLOWS

	Nine months ended June 30,	
	2015	2014
	(unaudited)	
Operating Activities		
Net income (loss)	\$ 10,209,022	\$ 15,703,476
Adjustments to reconcile net income (loss) to net cash provided by operating activities:		
Depreciation, depletion and amortization	17,680,069	15,562,630
Impairment	3,532,760	430,143
Provision for deferred income taxes	2,854,000	5,964,000
Exploration costs	48,368	70,140
Gain from leasing fee mineral acreage	(1,973,773)	(352,930)
Net (gain) loss on sales of assets	-	152,766
Income from partnerships	(373,555)	(565,523)
Distributions received from partnerships	535,400	734,825
Directors' deferred compensation expense	232,088	269,608
Restricted stock awards	740,043	499,791
Cash provided (used) by changes in assets and liabilities:		
Oil, NGL and natural gas sales receivables	6,771,690	(1,349,892)
Fair value of derivative contracts	(3,500,264)	2,431,427
Refundable production taxes	40,035	281,741
Other current assets	158,431	(25,098)
Accounts payable	148,384	443,438
Income taxes receivable	-	(3,160,243)
Income taxes payable	518,003	(751,992)
Accrued liabilities	(272,899)	100,229
Total adjustments	27,138,780	20,735,060
Net cash provided by operating activities	37,347,802	36,438,536
Investing Activities		
Capital expenditures, including dry hole costs	(23,613,349)	(26,693,851)
Acquisition of working interest properties	(308,180)	(86,759,445)
Acquisition of minerals and overrides	-	(56,250)
Proceeds from leasing fee mineral acreage	2,018,707	381,280
Investments in partnerships	(313,053)	(248,066)
Proceeds from sales of assets	-	92,000
Net cash used in investing activities	(22,215,875)	(113,284,332)
Financing Activities		
Borrowings under debt agreement	23,013,234	95,112,044

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Payments of loan principal	(35,513,234)	(17,521,506)
Purchases of treasury stock	(242,313)	(122,044)
Payments of dividends	(2,001,150)	(1,995,812)
Excess tax benefit on stock-based compensation	27,000	17,000
Net cash provided by (used in) financing activities	(14,716,463)	75,489,682
Increase (decrease) in cash and cash equivalents	415,464	(1,356,114)
Cash and cash equivalents at beginning of period	509,755	2,867,171
Cash and cash equivalents at end of period	\$ 925,219	\$ 1,511,057
Supplemental Schedule of Noncash Investing and Financing Activities:		
Additions to asset retirement obligations	\$ 52,017	\$ 370,536
Gross additions to properties and equipment	\$ 22,686,530	\$ 109,182,119
Net (increase) decrease in accounts payable for properties and equipment additions	1,234,999	4,327,427
Capital expenditures and acquisitions, including dry hole costs	\$ 23,921,529	\$ 113,509,546

(See accompanying notes)

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PANHANDLE OIL AND GAS INC.

NOTES TO CONDENSED FINANCIAL STATEMENTS

(Unaudited)

NOTE 1: Accounting Principles and Basis of Presentation

The accompanying unaudited condensed financial statements of Panhandle Oil and Gas Inc. have been prepared in accordance with the instructions to Form 10-Q as prescribed by the SEC. Management of the Company believes that all adjustments necessary for a fair presentation of the financial position and results of operations and cash flows for the periods have been included. All such adjustments are of a normal recurring nature. The results are not necessarily indicative of those to be expected for the full year. The Company's fiscal year runs from October 1 through September 30.

Certain amounts and disclosures have been condensed or omitted from these financial statements pursuant to the rules and regulations of the SEC. Therefore, these condensed financial statements should be read in conjunction with the financial statements and related notes thereto included in the Company's 2014 Annual Report on Form 10-K.

On September 11, 2014, the Company's Board of Directors declared a 2-for-1 stock split of the outstanding Class A Common Stock. The Class A Common Stock split was effected in the form of a stock dividend and was distributed on October 8, 2014, to stockholders of record on September 24, 2014. All references to number of shares and per share information in the accompanying financial statements have been adjusted to reflect this stock split.

NOTE 2: Income Taxes

The Company's provision for income taxes differs from the statutory rate primarily due to estimated federal and state benefits generated from estimated excess federal and Oklahoma percentage depletion, which are permanent tax benefits.

Both excess federal percentage depletion, which is limited to certain production volumes and by certain income levels, and excess Oklahoma percentage depletion, which has no limitation on production volume, reduce estimated taxable income or add to estimated taxable loss projected for any year. The federal and Oklahoma excess percentage depletion estimates will be updated throughout the year until finalized with detailed well-by-well calculations at fiscal year-end. Federal and Oklahoma excess percentage depletion, when a provision for income taxes is recorded,

decreases the effective tax rate, while the effect is to increase the effective tax rate when a benefit for income taxes is recorded. The benefits of federal and Oklahoma excess percentage depletion are not directly related to the amount of pre-tax income recorded in a period. Accordingly, in periods where a recorded pre-tax income or loss is relatively small, the proportional effect of these items on the effective tax rate may be significant. The effective tax rate for the nine months ended June 30, 2015, was 32% as compared to 32% for the nine months ended June 30, 2014. The effective tax rate for the quarter ended June 30, 2015, was -47% as compared to 33% for the quarter ended June 30, 2014. The higher estimated effective tax rate as of the end of the 2015 third quarter of 32%, as compared to 29% estimated at the end of the 2015 second quarter, resulted in a tax provision recorded during the 2015 third quarter. When a tax provision is recorded in a quarter with net loss (as opposed to a net income) before provision for income taxes, the result is a negative effective tax rate for the quarter, as was the case for the 2015 third quarter.

NOTE 3: Basic and Diluted Earnings (Loss) per Share

Basic and diluted earnings (loss) per share is calculated using net income (loss) divided by the weighted average number of voting common shares outstanding, including unissued, vested directors' deferred compensation shares during the period.

NOTE 4: Long-term Debt

The Company has a \$200,000,000 credit facility with a group of banks headed by Bank of Oklahoma (BOK) with a borrowing base of \$120,000,000 and a maturity date of November 30, 2018. The credit facility is subject to a semi-annual borrowing base determination, wherein BOK applies their own current pricing forecast and an 8% discount rate to the Company's proved reserves as calculated by the Company's Independent Consulting Petroleum Engineering Firm. The facility is secured by certain of the Company's properties with a carrying value of \$169,668,808 at June 30, 2015. The interest rate is based on BOK prime plus from 0.375% to 1.125%, or 30 day LIBOR plus from 1.875% to 2.625%. The election of BOK prime or LIBOR is at the Company's discretion. The interest rate spread from BOK prime or LIBOR will be charged based on the ratio of the loan balance to the borrowing base. The interest rate spread from LIBOR or the prime rate increases as a larger percent of the borrowing base is advanced. At June 30, 2015, the effective interest rate was 2.31%.

The Company's debt is recorded at the carrying amount on its balance sheet. The carrying amount of the Company's revolving credit facility approximates fair value because the interest rates are reflective of market rates.

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On June 19, 2015, the borrowing base was adjusted by the banks from \$130,000,000 to \$120,000,000. Determinations of the borrowing base are made semi-annually or whenever the banks, in their discretion, believe that there has been a material change in the value of the oil and natural gas properties. The loan agreement contains customary covenants which, among other things, require periodic financial and reserve reporting and limit the Company's incurrence of indebtedness, liens, dividends and acquisitions of treasury stock, and require the Company to maintain certain financial ratios. At June 30, 2015, the Company was in compliance with the covenants of the loan agreement.

NOTE 5: Deferred Compensation Plan for Non-Employee Directors

Annually, non-employee directors may elect to be included in the Deferred Compensation Plan for Non-Employee Directors. The Deferred Compensation Plan for Non-Employee Directors provides that each outside director may individually elect to be credited with future unissued shares of Company common stock rather than cash for all or a portion of the annual retainers, Board meeting fees and committee meeting fees, and may elect to receive shares, when issued, over annual time periods up to ten years. These unissued shares are recorded to each director's deferred compensation account at the closing market price of the shares (i) on the dates of the Board and committee meetings, and (ii) on the payment dates of the annual retainers. Only upon a director's retirement, termination, death, or a change-in-control of the Company will the shares recorded for such director under the Deferred Compensation Plan for Non-Employee Directors be issued to the director. The promise to issue such shares in the future is an unsecured obligation of the Company.

NOTE 6: Restricted Stock Plan

In March 2010, shareholders approved the Panhandle Oil and Gas Inc. 2010 Restricted Stock Plan (2010 Stock Plan), which made available 200,000 shares of common stock to provide a long-term component to the Company's total compensation package for its officers and to further align the interest of its officers with those of its shareholders. In March 2014, shareholders approved an amendment to increase the number of shares of common stock reserved for issuance under the 2010 Stock Plan from 200,000 shares to 500,000 shares and to allow the grant of shares of restricted stock to our directors. The 2010 Stock Plan, as amended, is designed to provide as much flexibility as possible for future grants of restricted stock so that the Company can respond as necessary to provide competitive compensation in order to retain, attract and motivate directors and officers of the Company and to align their interests with those of the Company's shareholders.

Effective in May 2014, the board of directors adopted resolutions to allow management, at their discretion, to purchase the Company's common stock, from time to time, up to an amount equal to the aggregate number of shares of common stock awarded pursuant to the Company's Amended 2010 Restricted Stock Plan, contributed by the Company to its ESOP and credited to the accounts of directors pursuant to the Deferred Compensation Plan for Non-Employee Directors.

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On March 4, 2015, the Company awarded 11,828 non-performance based shares and 35,485 performance based shares of the Company's common stock as restricted stock to certain officers. The restricted stock vests at the end of a three year period and contains nonforfeitable rights to receive dividends and voting rights during the vesting period. The non-performance and performance based shares had a fair value on their award date of \$213,969 and \$432,207, respectively. The Company recognized \$243,441 of compensation expense on the award date for performance based shares for officers that were eligible for retirement. The remaining fair value for the performance based awards as well as the entire fair value of the non-performance based awards will be recognized as compensation expense ratably over the vesting period. The fair value of the performance based shares on their award date is calculated by simulating the Company's stock prices as compared to the Dow Jones Select Oil Exploration and Production Index (DJSOEP) prices utilizing a Monte Carlo model covering the performance period (December 10, 2014, through December 10, 2017).

On March 4, 2015, the Company awarded 10,200 non-performance based shares of the Company's common stock as restricted stock to its non-employee directors. The restricted stock vests quarterly over one year starting on March 31, 2015. The restricted stock contains nonforfeitable rights to receive dividends and voting rights during the vesting period. These non-performance based shares had a fair value on their award date of \$210,018.

The following table summarizes the Company's pre-tax compensation expense for the three and nine months ended June 30, 2015 and 2014, related to the Company's performance based and non-performance based restricted stock.

	Three Months Ended		Nine Months Ended	
	June 30, 2015	2014	June 30, 2015	2014
Performance based, restricted stock	\$ 103,747	\$ 76,520	\$ 423,053	\$ 226,800
Non-performance based, restricted stock	105,053	161,097	316,990	272,991
Total compensation expense	\$ 208,800	\$ 237,617	\$ 740,043	\$ 499,791

A summary of the Company's unrecognized compensation cost for its unvested performance based and non-

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performance based restricted stock and the weighted-average periods over which the compensation cost is expected to be recognized are shown in the following table.

	As of June 30, 2015	
	Unrecognized Compensation	
	Cost	Weighted Average Period (in years)
Performance based, restricted stock	\$ 278,702	1.80
Non-performance based, restricted stock	359,796	1.54
Total	\$ 638,498	

Upon vesting, shares are expected to be issued out of shares held in treasury.

NOTE 7: Oil, NGL and Natural Gas Reserves

Management considers the estimation of the Company's crude oil, NGL and natural gas reserves to be the most significant of its judgments and estimates. Changes in crude oil, NGL and natural gas reserve estimates affect the Company's calculation of DD&A, provision for retirement of assets and assessment of the need for asset impairments. On an annual basis, with a semi-annual update, the Company's Independent Consulting Petroleum Engineer, with assistance from Company staff, prepares estimates of crude oil, NGL and natural gas reserves based on available geological and seismic data, reservoir pressure data, core analysis reports, well logs, analogous reservoir performance history, production data and other available sources of engineering, geological and geophysical information. Between periods in which reserves would normally be calculated, the Company updates the reserve calculations utilizing appropriate prices for the current period. The estimated oil, NGL and natural gas reserves were computed using the 12-month average price calculated as the unweighted arithmetic average of the first-day-of-the-month oil, NGL and natural gas price for each month within the 12-month period prior to the balance sheet date, held flat over the life of the properties. However, projected future crude oil, NGL and natural gas pricing assumptions are used by management to prepare estimates of crude oil, NGL and natural gas reserves and future net cash flows used in asset impairment assessments and in formulating management's overall operating decisions. Crude oil, NGL and natural gas prices are volatile and affected by worldwide production and consumption and are outside the control of management.

NOTE 8: Impairment

All long-lived assets, principally oil and natural gas properties, are monitored for potential impairment when circumstances indicate that the carrying value of the asset may be greater than its estimated future net cash flows. The evaluations involve significant judgment since the results are based on estimated future events, such as inflation rates,

future sales prices for oil, NGL and natural gas, future production costs, estimates of future oil, NGL and natural gas reserves to be recovered and the timing thereof, the economic and regulatory climates and other factors. The need to test a property for impairment may result from significant declines in sales prices or unfavorable adjustments to oil, NGL and natural gas reserves. Between periods in which reserves would normally be calculated, the Company updates the reserve calculations utilizing updated projected future price decks current with the period. For the three months ended June 30, 2015 and 2014, the assessment resulted in impairment provisions of \$132,118 and \$0, respectively. For the nine months ended June 30, 2015 and 2014, the assessment resulted in impairment provisions of \$3,532,760 and \$430,143, respectively. The impairment provisions for the three and nine months ended June 30, 2015, are principally the result of lower projected future prices for oil, NGL and natural gas. A reduction in oil, NGL or natural gas prices, or a decline in reserve volumes, could lead to additional impairment that may be material to the Company.

NOTE 9: Capitalized Costs

As of June 30, 2015 and 2014, non-producing oil and natural gas properties include costs of \$355,567 and \$888,505, respectively, on exploratory wells which were drilling and/or testing.

NOTE 10: Derivatives

The Company has entered into fixed swap contracts and costless collar contracts. These instruments are intended to reduce the Company's exposure to short-term fluctuations in the price of oil and natural gas. Fixed swap contracts set a fixed price and provide payments to the Company if the index price is below the fixed price, or require payments by the Company if the index price is above the fixed price. Collar contracts set a fixed floor price and a fixed ceiling price and provide payments to the Company if the index price falls below the floor or require payments by the Company if the index price rises above the ceiling. These contracts cover only a portion of the Company's natural gas and oil production and provide only partial price protection against declines in natural gas and oil prices. These derivative instruments may expose the Company to risk of financial loss and limit the benefit of future increases in prices. All of the Company's derivative contracts are with Bank of Oklahoma and are secured under its credit facility with Bank of Oklahoma. The derivative instruments have settled or will

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settle based on the prices below.

Derivative contracts in place as of June 30, 2015

Contract period	Production volume covered per month	Index	Contract price
Natural gas costless collars			
January - December 2015	100,000 Mmbtu	NYMEX Henry Hub	\$3.50 floor / \$4.10 ceiling
January - December 2015	70,000 Mmbtu	NYMEX Henry Hub	\$3.25 floor / \$4.00 ceiling
April - September 2015	70,000 Mmbtu	NYMEX Henry Hub	\$3.50 floor / \$4.05 ceiling
April - October 2015	50,000 Mmbtu	NYMEX Henry Hub	\$3.50 floor / \$4.00 ceiling
May - October 2015	70,000 Mmbtu	NYMEX Henry Hub	\$3.50 floor / \$3.95 ceiling
Oil costless collars			
July - December 2015	10,000 Bbls	NYMEX WTI	\$80.00 floor / \$86.50 ceiling
Oil fixed price swaps			
April - December 2015	5,000 Bbls	NYMEX WTI	\$94.56
July - December 2015	7,000 Bbls	NYMEX WTI	\$93.91

Derivative contracts in place as of September 30, 2014

Contract period	Production volume covered per month	Index	Contract price
Natural gas costless collars			
July - December 2014	140,000 Mmbtu	NYMEX Henry Hub	\$3.75 floor / \$4.50 ceiling
Natural gas fixed price swaps			
July - December 2014	140,000 Mmbtu	NYMEX Henry Hub	\$4.11
May - October 2014	30,000 Mmbtu	NYMEX Henry Hub	\$4.30
October - December 2014	40,000 Mmbtu	NYMEX Henry Hub	\$4.61
Oil costless collars			
January - December 2014	4,000 Bbls	NYMEX WTI	\$85.00 floor / \$100.00 ceiling

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July - December 2014	5,000 Bbls	NYMEX WTI	\$90.00 floor / \$97.00 ceiling
Oil fixed price swaps			
January - December 2014	3,000 Bbls	NYMEX WTI	\$94.50
June - December 2014	4,000 Bbls	NYMEX WTI	\$99.40
July - December 2014	4,000 Bbls	NYMEX WTI	\$95.25
July - December 2014	5,000 Bbls	NYMEX WTI	\$94.20
January - March 2015	6,000 Bbls	NYMEX WTI	\$92.85
January - June 2015	7,000 Bbls	NYMEX WTI	\$96.80
January - June 2015	5,000 Bbls	NYMEX WTI	\$97.40
January - June 2015	4,000 Bbls	NYMEX WTI	\$97.25
April - December 2015	5,000 Bbls	NYMEX WTI	\$94.56
July - December 2015	7,000 Bbls	NYMEX WTI	\$93.91

The Company has elected not to complete all of the documentation requirements necessary to permit these derivative contracts to be accounted for as cash flow hedges. The Company's fair value of derivative contracts was a net asset of \$5,402,106 as of June 30, 2015, and a net asset of \$1,901,842 as of September 30, 2014.

The fair value amounts recognized for the Company's derivative contracts executed with the same counterparty under a master netting arrangement may be offset. The Company has the choice to offset or not, but that choice must be applied consistently. A master netting arrangement exists if the reporting entity has multiple contracts with a single counterparty that are subject to a contractual agreement that provides for the net settlement of all contracts through a single payment in a single currency in the event of default on or termination of any one contract. Offsetting the fair values recognized for the derivative contracts outstanding with a single counterparty results in the net fair value of the transactions being reported as an asset or a

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liability in the Condensed Balance Sheets.

The following table summarizes and reconciles the Company's derivative contracts' fair values at a gross level back to net fair value presentation on the Company's Condensed Balance Sheets at June 30, 2015, and September 30, 2014.

The Company has offset all amounts subject to master netting agreements in the Company's Condensed Balance Sheets at June 30, 2015, and September 30, 2014.

	June 30, 2015 Fair Value (a) Commodity Contracts Current Assets	September 30, 2014 Fair Value (a) Commodity Contracts Current Assets		Non-Current Assets
			Current Liabilities	
Gross amounts recognized	\$ 5,402,106	\$ 1,658,785	\$ 8,222	\$ 251,279
Offsetting adjustments	-	(8,222)	(8,222)	-
Net presentation on Condensed Balance Sheets	\$ 5,402,106	\$ 1,650,563	\$ -	\$ 251,279

(a) See Fair Value Measurements section for further disclosures regarding fair value of financial instruments.

The fair value of derivative assets and derivative liabilities is adjusted for credit risk. The impact of credit risk was immaterial for all periods presented.

NOTE 11: Fair Value Measurements

Fair value is defined as the amount that would be received from the sale of an asset or paid for the transfer of a liability in an orderly transaction between market participants, i.e., an exit price. To estimate an exit price, a three-level hierarchy is used. The fair value hierarchy prioritizes the inputs, which refer broadly to assumptions market participants would use in pricing an asset or a liability, into three levels. Level 1 inputs are unadjusted quoted prices in active markets for identical assets and liabilities. Level 2 inputs are inputs other than quoted prices included within Level 1 that are observable for the asset or liability, either directly or indirectly. If the asset or liability has a specified (contractual) term, a Level 2 input must be observable for substantially the full term of the asset or liability. Level 2 inputs include the following: (i) quoted prices for similar assets or liabilities in active markets; (ii) quoted prices for identical or similar assets or liabilities in markets that are not active; (iii) inputs other than quoted prices that are observable for the asset or liability; or (iv) inputs that are derived principally from or corroborated by observable

market data by correlation or other means. Level 3 inputs are unobservable inputs for the financial asset or liability.

The following table provides fair value measurement information for financial assets and liabilities measured at fair value on a recurring basis as of June 30, 2015.

	Fair Value Measurement at June 30, 2015			
	Quoted Prices in Active Markets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Total Fair Value
Financial Assets (Liabilities):				
Derivative Contracts - Swaps	\$ -	\$ 3,184,829	\$ -	\$ 3,184,829
Derivative Contracts - Collars	\$ -	\$ -	\$ 2,217,277	\$ 2,217,277

Level 2 – Market Approach - The fair values of the Company’s swaps are based on a third-party pricing model which utilizes inputs that are either readily available in the public market, such as natural gas curves, or can be corroborated from active markets. These values are based upon future prices, time to maturity and other factors. These values are then compared to the values given by our counterparties for reasonableness.

Level 3 – The fair values of the Company’s costless collar contracts are based on a pricing model which utilizes inputs that are unobservable or not readily available in the public market. These values are based upon future prices, volatility, time to maturity and other factors. These values are then compared to the values given by our counterparties for reasonableness.

The significant unobservable inputs for Level 3 derivative contracts include market volatility and credit risk of counterparties. Changes in these inputs will impact the fair value measurement of our derivative contracts. An increase

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(decrease) in the volatility of oil and natural gas prices will decrease (increase) the fair value of oil and natural gas derivatives and adverse changes to our counterparties' creditworthiness will decrease the fair value of our derivatives.

The following table represents quantitative disclosures about unobservable inputs for Level 3 Fair Value Measurements.

Instrument Type	Unobservable Input	Range	Weighted Average	Fair Value June 30, 2015
Oil Collars	Oil price volatility curve	12.02% - 23.46%	17.09%	\$ 1,180,187
Natural Gas Collars	Natural gas price volatility curve	0% - 24.18%	14.42%	\$ 1,037,090

A reconciliation of the Company's derivative contracts classified as Level 3 measurements is presented below. All gains and losses are presented on the Gains (losses) on derivative contracts line item on our Statement of Operations.

	Derivatives
Balance of Level 3 as of October 1, 2014	\$ 30,044
Total gains or (losses)	
Included in earnings	24,324
Included in other comprehensive income (loss)	-
Purchases, issuances and settlements	2,162,909
Transfers in and out of Level 3	-
Balance of Level 3 as of June 30, 2015	\$ 2,217,277

The following table presents impairments associated with certain assets that have been measured at fair value on a nonrecurring basis within Level 3 of the fair value hierarchy.

Quarter Ended June 30,

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	2015		2014	
	Fair Value	Impairment	Fair Value	Impairment
Producing Properties (a)	\$ 203,216	\$ 132,118	\$ -	\$ -
	Nine Months Ended June 30,			
	2015		2014	
	Fair Value	Impairment	Fair Value	Impairment
Producing Properties (a)	\$ 4,036,434	\$ 3,532,760	\$ 628,097	\$ 430,143

(a) At the end of each quarter, the Company assesses the carrying value of its producing properties for impairment. This assessment utilizes estimates of future cash flows. Significant judgments and assumptions in these assessments include estimates of future oil and natural gas prices using a forward NYMEX curve adjusted for locational basis differentials, drilling plans, expected capital costs and an applicable discount rate commensurate with risk of the underlying cash flow estimates. These assessments identified certain properties with carrying value in excess of their calculated fair values.

At June 30, 2015, and September 30, 2014, the fair value of financial instruments approximated their carrying amounts. Financial instruments include long-term debt, which the valuation is classified as Level 3 and is based on a valuation technique that requires inputs that are both unobservable and significant to the overall fair value measurement. The fair value measurement of our long-term debt is valued using a discounted cash flow model that calculates the present value of future cash flows pursuant to the terms of the debt agreements and applies estimated current market interest rates. The estimated current market interest rates are based primarily on interest rates currently being offered on borrowings of similar amounts and terms. In addition, no valuation input adjustments were considered necessary relating to nonperformance risk for the debt agreements.

NOTE 12: Acquisitions

On June 17, 2014, the Company closed an acquisition of certain Eagle Ford Shale assets located in LaSalle and Frio Counties, Texas, in the core of the Eagle Ford Shale. The assets were purchased from private sellers and included a 16% non-

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operated working interest in 11,100 gross (1,775 net) acres. The acreage is largely contiguous, entirely held by production and, at the time of closing, contained 63 producing wells (57 Eagle Ford, 5 Pearsall and 1 Buda) and 109 undeveloped Eagle Ford locations. The adjusted purchase price at closing was \$81.5 million and was funded by utilizing the Company's bank credit facility. The purchase price was allocated to the producing wells and undeveloped locations based on fair value determined by estimated reserves and adjusted for working capital.

Actual and Pro Forma Impact of Acquisitions (Unaudited)

Revenues attributable to this acquisition included in the Company's statement of operations for the quarter and nine months ended June 30, 2015, were \$2,403,864 and \$9,154,207, respectively. Net income (loss) attributable to the acquisition included in the statement of operations for the quarter and nine months ended June 30, 2015, was (\$283,146) and \$375,601, respectively. These amounts do not include gains on derivative contracts as noted on the Statement of Operations.

The following table presents the unaudited pro forma financial information assuming the Company had acquired this business on October 1, 2013:

	For the Nine Months Ended June 30,	
	2015	2014
Revenue:		
As reported	\$ 57,427,092	\$ 56,523,778
Pro forma revenue	-	16,811,606
Pro forma	\$ 57,427,092	\$ 73,335,384
Net Income:		
As reported	\$ 10,209,022	\$ 15,703,476
Pro forma income	-	6,485,185
Pro forma	\$ 10,209,022	\$ 22,188,661

The unaudited pro forma financial information is for informational purposes only and does not purport to present what our results would actually have been had this transaction actually occurred on the date presented or to project our results of operations or financial position for any future period.

NOTE 13: Recently Adopted Accounting Pronouncements

In May 2014, the Financial Accounting Standards Board (“FASB”) issued Accounting Standard Update (“ASU”) 2014-09-Revenue from Contracts with Customers, which will supersede nearly all existing revenue recognition guidance under GAAP. The standard’s core principle is that a company will recognize revenue when it transfers promised goods or services to customers in an amount that reflects the consideration to which the company expects to be entitled in exchange for those goods or services. We are evaluating our existing revenue recognition policies to determine whether any contracts in the scope of the guidance will be affected by the new requirements. The standard is effective for us on October 1, 2018. Early adoption is not permitted. The standard allows for either “full retrospective” adoption, meaning the standard is applied to all of the periods presented, or “modified retrospective” adoption, meaning the standard is applied only to the most current period presented in the financial statements. We are currently evaluating the transition method that will be elected.

Other accounting standards that have been issued or proposed by the FASB, or other standards-setting bodies, that do not require adoption until a future date are not expected to have a material impact on the financial statements upon adoption.

ITEM 2 MANAGEMENT’S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

FORWARD-LOOKING STATEMENTS AND RISK FACTORS

Forward-Looking Statements for fiscal 2015 and later periods are made in this document. Such statements represent estimates by management based on the Company’s historical operating trends, its proved oil, NGL and natural gas reserves and other information currently available to management. The Company cautions that the Forward-Looking Statements provided herein are subject to all the risks and uncertainties incident to the acquisition, development and marketing of, and exploration for oil, NGL and natural gas reserves. Investors should also read the other information in this Form 10-Q and the Company’s 2014 Annual Report on Form 10-K where risk factors are presented and further discussed. For all the above reasons, actual results may vary materially from the Forward-Looking Statements and there is no assurance that the assumptions used are necessarily the most likely to occur.

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LIQUIDITY AND CAPITAL RESOURCES

The Company had positive working capital of \$7,812,814 at June 30, 2015, compared to \$9,919,037 at September 30, 2014.

Liquidity:

Cash and cash equivalents were \$925,219 as of June 30, 2015, compared to \$509,755 at September 30, 2014, an increase of \$415,464. Cash flows for the nine months ended June 30 are summarized as follows:

Net cash provided (used) by:

	2015	2014	Change
Operating activities	\$ 37,347,802	\$ 36,438,536	\$ 909,266
Investing activities	(22,215,875)	(113,284,332)	91,068,457
Financing activities	(14,716,463)	75,489,682	(90,206,145)
Increase (decrease) in cash and cash equivalents	\$ 415,464	\$ (1,356,114)	\$ 1,771,578

Operating activities:

Net cash provided by operating activities increased \$909,266 during the 2015 period, as compared to the 2014 period, the result of the following:

- Receipts of oil, NGL and natural gas sales (net of production taxes and gathering, transportation and marketing costs) and other decreased \$6,899,911.
- Decreased income tax payments of \$4,094,893.
- Increased net receipts on derivative contracts of \$9,063,995.

- Increased interest payments of \$1,130,985.
- Increased payments for G&A and other expenses of \$314,102.
- Increased payments for field operating expenses of \$3,904,624.

Investing activities:

Net cash used in investing activities decreased \$91,068,457 during the 2015 period, as compared to the 2014 period, due to:

- A decrease in cash used to acquire properties of \$86,507,515.
- Lower payments for drilling and completion activity during 2015 decreased capital expenditures by \$3,080,502.
- Increased receipts from leasing of fee mineral acreage of \$1,637,427.

Financing activities:

Net cash used in financing activities increased \$90,206,145 during the 2015 period, as compared to the 2014 period, the result of the following:

- During the period ended June 30, 2015, net borrowings decreased \$12,500,000; during the period ended June 30, 2014, net borrowings increased \$77,590,538 to fund the Eagle Ford Shale acquisition.

Capital Resources:

Capital expenditures to drill and complete wells decreased \$3,080,502 (12%) from the 2014 to the 2015 period. The decrease resulted primarily from the suspension of drilling activity in the Texas Eagle Ford Shale oil play late in the 2015 first

quarter, combined with a significant decrease in well proposals to the Company in all of its other plays. Also, many of the well proposals we did receive did not meet our participation criteria. However, expenditures were made during the 2015 third quarter to complete five North Dakota Bakken Shale wells whose completion had previously been suspended awaiting higher oil prices and/or cost reductions. These wells began producing in late May. Other notable drilling and completion expenditures made during the 2015 third quarter related to activity on the Company's mineral acreage in the SCOOP Woodford Shale and Springer plays in south central Oklahoma and the Arkansas Fayetteville Shale play.

Oil, NGL and natural gas production volumes increased 2% on an Mcfe basis during the 2015 period, as compared to the 2014 period. Oil production increased 55% principally due to production from the Eagle Ford Shale properties acquired in June 2014 and from drilling in the North Dakota Bakken Shale. These increases were partially offset by declining production from Texas Panhandle and western Oklahoma horizontal Cleveland, Marmaton and Granite Wash oil plays. During the second and third quarters of 2015, Eagle Ford Shale production was impacted by the delay of completion of six wells that were drilled in the first quarter of 2015. Five of the six wells are now scheduled to be completed beginning in August 2015 and production is expected to begin around October 1, 2015. Natural gas production decreased 7% as a result of declining production from the Arkansas Fayetteville Shale, declining associated natural gas production from western Oklahoma and Texas Panhandle horizontal Marmaton, Cleveland and Granite Wash oil plays and declines in the Northern Oklahoma Mississippian and Southeastern Oklahoma Woodford Shale. These decreases were partially offset by a production increase in the Anadarko Basin Woodford Shale in Oklahoma and the Eagle Ford Shale. NGL production increased 7% due to production from the Eagle Ford Shale and increased production from the Anadarko Basin Woodford Shale, partially offset by declining production from Texas Panhandle and western Oklahoma horizontal Cleveland, Marmaton and Granite Wash oil plays and in the Northern Oklahoma Mississippian and Southeastern Oklahoma Woodford Shale plays. Due to the Company receiving oil production from the Eagle Ford properties for all of 2015 (as compared to three and one-half months of fiscal 2014), combined with production from the five newly completed Bakken Shale wells, we expect 2015 oil production to increase over that of 2014. Natural gas and NGL production volumes are expected to be lower in 2015, as compared to 2014, as a result of anticipated lower 2015 capital expenditures discussed below. On an Mcfe basis, 2015 production volumes are expected to be slightly lower than that of 2014.

The Company expects the current reduced level of capital expenditures to continue during the 2015 fourth quarter as long as oil, NGL and natural gas prices remain at or near their current depressed levels. New oil production from the five newly completed Bakken Shale wells is expected to exceed the natural decline of existing wells, resulting in 2015 fourth quarter oil production exceeding that of the 2015 third quarter. Reduced capital expenditures are anticipated to result in marginally lower natural gas and NGL production volumes in the 2015 fourth quarter compared to the 2015 third quarter. Combined, lower product prices and production volumes, partially offset by realized gains on derivative contracts, are expected to result in cash provided by operating activities sufficient to fund capital expenditures, dividend payments and treasury stock purchases. Any excess cash is intended to be used to reduce bank debt.

Since the Company is not the operator of any of its oil and natural gas properties, it is extremely difficult for us to predict levels of future participation in the drilling and completion of new wells and their associated capital expenditures. This makes 2015 capital expenditures for drilling and completion projects difficult to forecast.

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With continued oil and natural gas price volatility, management continues to evaluate opportunities for product price protection through additional hedging of the Company's future oil and natural gas production. See NOTE 10 – "Derivatives" for a complete list of the Company's outstanding derivative contracts.

The use of the Company's cash provided by operating activities and resultant change to cash is summarized in the table below:

	Nine months ended June 30, 2015
Cash provided by operating activities	\$ 37,347,802
Cash provided (used) by:	
Capital expenditures - acquisitions	(308,180)
Capital expenditures - drilling and completion of wells	(23,613,349)
Quarterly dividends of \$.12 per share	(2,001,150)
Treasury stock purchases	(242,313)
Net borrowings on credit facility	(12,500,000)
Other investing and financing activities	1,732,654
Net cash used	(36,932,338)
Net increase (decrease) in cash	\$ 415,464

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Outstanding borrowings on the credit facility at June 30, 2015, were \$65,500,000.

Looking forward, the Company expects to fund overhead costs, capital additions related to the drilling and completion of wells, treasury stock purchases, if any, and dividend payments primarily from cash provided by operating activities and cash on hand. As management evaluates opportunities to acquire additional assets, additional borrowings utilizing our bank credit facility could be necessary. Also, during times of oil, NGL and natural gas price decreases, or increased capital expenditures, it may be necessary to utilize the credit facility further in order to fund these expenditures. The Company has availability (\$54,500,000 at June 30, 2015) under its revolving credit facility and is in compliance with its debt covenants (current ratio, debt to EBITDA and dividends as a percent of operating cash flow).

Based on expected capital expenditure levels and anticipated cash provided by operating activities for 2015, the Company has sufficient liquidity to fund its ongoing operations and, combined with availability under its credit facility, to fund acquisitions.

RESULTS OF OPERATIONS

THREE MONTHS ENDED JUNE 30, 2015 – COMPARED TO THREE MONTHS ENDED JUNE 30, 2014

Overview:

The Company recorded third quarter 2015 net loss of \$728,946, or \$0.04 per share, as compared to net income of \$5,122,585, or \$0.31 per share, in the 2014 quarter. The decrease in net income was principally the result of decreased oil, NGL and natural gas sales, increases in LOE, DD&A and interest expense; offset by increases in lease bonuses and rentals, decreased G&A, and decreased production and income taxes. These items are further discussed below.

Oil, NGL and Natural Gas Sales:

Oil, NGL and natural gas sales decreased \$8,090,955 or 41% for the 2015 quarter. Oil, NGL and natural gas sales were down due to decreases in NGL and natural gas sales volumes of 34% and 4%, respectively, and decreases in oil, NGL and natural gas prices of 48%, 57% and 48%, respectively. These decreases were partially offset by an increase in oil sales volumes of 56%. The following table outlines the Company's production and average sales prices for oil, NGL and natural gas for the three month periods of fiscal 2015 and 2014:

Oil Bbls Sold	Average	Mcf	Average	NGL Bbls	Average	Mcf	Average
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