

LEGACY RESERVES LP
Form 10-Q
May 03, 2017

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 quarterly period ended March 31, 2017

or

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

For the transition period from _____ to _____

Commission File Number 1-33249
Legacy Reserves LP
(Exact name of registrant as specified in its charter)

Delaware 16-1751069
(State or other jurisdiction of incorporation or organization) (I.R.S. Employer Identification No.)

303 W. Wall, Suite 1800 79701
Midland, Texas
(Address of principal executive offices) (Zip code)
(432) 689-5200
(Registrant's telephone number, including area code)

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

Yes No

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files).

Yes No

Edgar Filing: LEGACY RESERVES LP - Form 10-Q

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, a 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.

Large accelerated filer

Accelerated filer

Non-accelerated filer (Do not check if a smaller reporting company)

Smaller reporting company

Emerging growth company

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

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

Yes No

72,623,551 units representing limited partner interests in the registrant were outstanding as of May 1, 2017.

TABLE OF CONTENTS

Glossary of Terms	<u>Page 3</u>
Part I - Financial Information	
Item 1. Financial Statements.	
Condensed Consolidated Balance Sheets as of March 31, 2017 and December 31, 2016 (Unaudited).	<u>Page 6</u>
Condensed Consolidated Statements of Operations for the three months ended March 31, 2017 and 2016 (Unaudited).	<u>Page 8</u>
Condensed Consolidated Statements of Partners' Deficit for the three months ended March 31, 2017 (Unaudited).	<u>Page 9</u>
Condensed Consolidated Statements of Cash Flows for the three months ended March 31, 2017 and 2016 (Unaudited).	<u>Page 10</u>
Notes to Condensed Consolidated Financial Statements (Unaudited).	<u>Page 11</u>
Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations.	<u>Page 30</u>
Item 3. Quantitative and Qualitative Disclosures About Market Risk.	<u>Page 43</u>
Item 4. Controls and Procedures.	<u>Page 43</u>
Part II - Other Information	
Item 1. Legal Proceedings.	<u>Page 45</u>
Item 1A. Risk Factors.	<u>Page 45</u>
Item 2. Unregistered Sales of Equity Securities and Use of Proceeds.	<u>Page 45</u>
Item 6. Exhibits.	<u>Page 46</u>
Signatures	<u>Page 47</u>

GLOSSARY OF TERMS

Bbl. One stock tank barrel or 42 U.S. gallons liquid volume.

Bcf. Billion cubic feet.

Boe. One barrel of oil equivalent, determined using a ratio of six Mcf of natural gas to one Bbl of crude oil, condensate or natural gas liquids.

Boe/d. Barrels of oil equivalent per day.

Btu. British thermal unit, which is the heat required to raise the temperature of a one-pound mass of water from 58.5 to 59.5 degrees Fahrenheit.

Developed acreage. The number of acres that are allocated or assignable to productive wells or wells capable of production.

Development project. A drilling or other project which may target proven reserves, but which generally has a lower risk than that associated with exploration projects.

Development well. A well drilled within the proved area of an oil or natural gas reservoir to the depth of a stratigraphic horizon known to be productive.

Dry hole or well. A well found to be incapable of producing hydrocarbons in sufficient quantities such that proceeds from the sale of such production would exceed production expenses and taxes.

Field. An area consisting of a single reservoir or multiple reservoirs all grouped on or related to the same individual geological structural feature and/or stratigraphic condition.

Gross acres or gross wells. The total acres or wells, as the case may be, in which a working interest is owned.

Hydrocarbons. Oil, NGL and natural gas are all collectively considered hydrocarbons.

Liquids. Oil and NGLs.

MBbls. One thousand barrels of crude oil or other liquid hydrocarbons.

MBoe. One thousand barrels of crude oil equivalent, using a ratio of six Mcf of natural gas to one Bbl of crude oil, condensate or natural gas liquids.

Mcf. One thousand cubic feet.

MGal. One thousand gallons of natural gas liquids or other liquid hydrocarbons.

MMBbls. One million barrels of crude oil or other liquid hydrocarbons.

MMBoe. One million barrels of crude oil equivalent, using a ratio of six Mcf of natural gas to one Bbl of crude oil, condensate or natural gas liquids.

MMBtu. One million British thermal units.

MMcf. One million cubic feet.

Net acres or net wells. The sum of the fractional working interests owned in gross acres or gross wells, as the case may be.

NGL or natural gas liquids. The combination of ethane, propane, butane and natural gasolines that when removed from natural gas become liquid under various levels of higher pressure and lower temperature.

NYMEX. New York Mercantile Exchange.

Page 3

Oil. Crude oil and condensate.

Productive well. A well that is found to be capable of producing hydrocarbons in sufficient quantities such that proceeds from the sale of such production exceed production expenses and taxes.

Proved developed reserves or PDPs. Reserves that can be expected to be recovered through: (i) 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 or PDNPs. Proved oil and natural gas reserves that are developed behind pipe, shut-in 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 reserves. Proved oil and gas reserves are those quantities of oil and 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 that renewal is reasonably certain, regardless of whether deterministic or probabilistic methods are used for the estimation.

Proved undeveloped drilling location. A site on which a development well can be drilled consistent with spacing rules for purposes of recovering proved undeveloped reserves.

Proved undeveloped reserves or PUDs. Proved undeveloped oil and gas reserves 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.

(i) Proved reserves on undrilled acreage shall be limited to those directly offsetting development spacing areas that are reasonably certain of production when drilled, unless evidence using reliable technology exists that establishes reasonable certainty of economic producibility at greater distances.

(ii) Proved undrilled locations can be classified as having undeveloped reserves only if a development plan has been adopted indicating that they are scheduled to be drilled within five years, unless the specific circumstances, justify a longer time.

(iii) Under no circumstances shall estimates for proved undeveloped reserves be attributable to any acreage for which an application of fluid injection or other improved recovery technique is contemplated, unless such techniques have been proved effective by actual projects in the same reservoir or an analogous reservoir or by other evidence using reliable technology establishing reasonable certainty.

Recompletion. The completion for production of an existing wellbore in another formation from that which the well has been previously completed.

Reserve acquisition cost. The total consideration paid for an oil and natural gas property or set of properties, which includes the cash purchase price and any value ascribed to units issued to a seller adjusted for any post-closing items.

R/P ratio (reserve life). The reserves as of the end of a period divided by the production volumes for the same period.

Reserve replacement. The replacement of oil and natural gas produced with reserve additions from acquisitions, reserve additions and reserve revisions.

Reserve replacement cost. An amount per Boe equal to the sum of costs incurred relating to oil and natural gas property acquisition, exploitation, development and exploration activities (as reflected in our year-end financial statements for the relevant year) divided by the sum of all additions and revisions to estimated proved reserves, including reserve purchases. The calculation of reserve additions for each year is based upon the reserve report of our independent engineers. Management uses reserve replacement cost to compare our company to others in terms of our historical ability to increase our reserve base in an economic manner. However, past performance does not necessarily reflect future reserve replacement cost performance. For example, increases in oil and natural gas prices in recent years have increased the economic life of reserves, adding additional reserves with

no required capital expenditures. On the other hand, increases in oil and natural gas prices have increased the cost of reserve purchases and reserves added through development projects. The reserve replacement cost may not be indicative of the economic value added of the reserves due to differing lease operating expenses per barrel and differing timing of production.

Reservoir. A porous and permeable underground formation containing a natural accumulation of producible oil and/or natural gas that is confined by impermeable rock or water barriers and is individual and separate from other reserves.

Standardized measure. The present value of estimated future net revenues to be generated from the production of proved reserves, determined in accordance with assumptions required by the Financial Accounting Standards Board and the Securities and Exchange Commission (using the average annual prices based on the unweighted arithmetic average of the first-day-of-the-month price for each month) without giving effect to non-property related expenses such as general and administrative expenses, debt service and future income tax expenses or to depreciation, depletion and amortization and discounted using an annual discount rate of 10%. Because we are a limited partnership that allocates our taxable income to our unitholders, no provisions for federal or state income taxes have been provided for in the calculation of standardized measure. Standardized measure does not give effect to derivative transactions.

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 oil and natural gas regardless of whether such acreage contains proved reserves.

Working interest. The operating interest that gives the owner the right to drill, produce and conduct operating activities on the property and a share of production.

Workover. Operations on a producing well to restore or increase production.

Part I – FINANCIAL INFORMATION

Item 1. Financial Statements.

LEGACY RESERVES LP
 CONDENSED CONSOLIDATED BALANCE SHEETS
 (UNAUDITED)
 ASSETS

	March 31, 2017	December 31, 2016
	(In thousands)	
Current assets:		
Cash	\$ 1,860	\$ 2,555
Accounts receivable, net:		
Oil and natural gas	45,890	43,192
Joint interest owners	21,116	23,414
Other	2	2
Fair value of derivatives (Notes 4 and 5)	14,080	6,162
Prepaid expenses and other current assets (Note 1)	10,343	7,447
Total current assets	93,291	82,772
Oil and natural gas properties using the successful efforts method, at cost:		
Proved properties	3,328,625	3,305,856
Unproved properties	18,518	13,448
Accumulated depletion, depreciation, amortization and impairment	(2,169,324)	(2,137,395)
	1,177,819	1,181,909
Other property and equipment, net of accumulated depreciation and amortization of \$10,742 and \$10,412, respectively	3,154	3,423
Operating rights, net of amortization of \$5,468 and \$5,369, respectively	1,548	1,648
Fair value of derivatives (Notes 4 and 5)	31,631	20,553
Other assets	7,996	8,874
Investments in equity method investees	658	647
Total assets	\$ 1,316,097	\$ 1,299,826

See accompanying notes to condensed consolidated financial statements.

LEGACY RESERVES LP
 CONDENSED CONSOLIDATED BALANCE SHEETS
 (UNAUDITED)
 LIABILITIES AND PARTNERS' DEFICIT

	March 31, 2017	December 31, 2016
	(In thousands)	
Current liabilities:		
Accounts payable	\$4,193	\$ 9,092
Accrued oil and natural gas liabilities (Note 1)	72,367	53,248
Fair value of derivatives (Notes 4 and 5)	1,555	9,743
Asset retirement obligation (Note 6)	2,980	2,980
Other	20,003	11,546
Total current liabilities	101,098	86,609
Long-term debt (Note 2)	1,148,151	1,161,394
Asset retirement obligation (Note 6)	271,049	269,168
Fair value of derivatives (Notes 4 and 5)	—	4,091
Other long-term liabilities	643	643
Total liabilities	1,520,941	1,521,905
Commitments and contingencies (Note 3)		
Partners' deficit (Note 7):		
Series A Preferred equity - 2,300,000 units issued and outstanding at March 31, 2017 and December 31, 2016	55,192	55,192
Series B Preferred equity - 7,200,000 units issued and outstanding at March		