TRANS ENERGY INC
Form 10-Q
August 12, 2009
UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

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

For the quarterly period ended June 30, 2009

OR

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

For the transition period from _______ to _______

Commission File Number 0-23530

TRANS ENERGY, INC.

(Exact name of registrant as specified in its charter)

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

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

(Address of principal executive offices)

Registrant's telephone no., including area code: (304) 684-7053

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the past 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes (X) No ( )

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes ( ) No ( )

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

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

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

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

Class	Outstanding as of July 31, 2009
Common Stock, $0.001 par value	10,808,065

See notes to unaudited consolidated financial statements.

2

Table of Contents

PART I

Item 1. Financial Statements

TRANS ENERGY, INC. AND SUBSIDIARIES
Consolidated Balance Sheets

	June 30, 2009 Unaudited	December 31, 2008 Audited
ASSETS		
CURRENT ASSETS		
Cash	$ 366,020	$ 1,806,008
Accounts receivable – trade	2,226,263	769,430
Accounts receivable – related parties	33,000	1,233,536
Accounts receivable due from non-operator, net	1,060,836	1,352,681
Note receivable - current	304,560	138,545
Deferred financing costs	215,754	167,429
Derivative assets – current	542,260	513,724
Prepaid expenses	68,764	-
Total Current Assets	4,817,457	5,981,353
PROPERTY AND EQUIPMENT, net of accumulated depreciation of $382,706 and $311,769, respectively	1,155,715	1,094,970
OIL AND GAS PROPERTIES, USING SUCCESSFUL EFFORTS ACCOUNTING		
Proved properties	24,432,540	19,799,868
Unproved properties	1,148,111	627,853
Pipelines	4,759,580	4,729,274
Accumulated depreciation, depletion and amortization	(3,553,899)	(2,711,689)
Oil and gas properties, net	26,786,332	22,445,306
OTHER ASSETS		
Deferred financing costs, net of amortization of $413,560 and $304,399, respectively	-	157,386
Note receivable – non-current	211,949	163,735

Derivative assets – non-current	512,419	703,435
Advances to operator	9,000	9,000
Other assets	52,098	52,098
Total Other Assets	785,466	1,085,654
TOTAL ASSETS	$ 33,544,970	$ 30,607,283

See notes to unaudited consolidated financial statements

4

TRANS ENERGY, INC. AND SUBSIDIARIES
Consolidated Balance Sheets (continued)

	June 30, 2009 Unaudited	December 31, 2008 Audited
LIABILITIES AND STOCKHOLDERS' DEFICIT		
CURRENT LIABILITIES		
Accounts payable - trade	$ 4,053,760	$ 2,360,076
Accounts payable – related party	2,150	2,150
Accrued expenses	772,886	762,978
Notes payable – current, net of unamortized discount of $308,129 and $0, respectively	29,783,257	86,714
Total Current Liabilities	34,612,053	3,211,918
LONG-TERM LIABILITIES		
Notes payable, net of unamortized discount of $0 and $467,932, respectively	14,308	27,588,599
Asset retirement obligations	193,810	178,954
Total Long-Term Liabilities	208,118	27,767,553
Total Liabilities	34,820,171	30,979,471
COMMITMENTS AND CONTINGENCIES	-	-
STOCKHOLDERS' DEFICIT		
Preferred stock; 10,000,000 shares authorized at $0.001 par value; -0- shares issued and outstanding	-	-
Common stock; 500,000,000 shares authorized at $0.001 par value; 10,809,065 and 10,559,065 shares issued, respectively, and 10,808,065 and 10 ,525,815 shares outstanding, respectively	10,809	10,559
Additional paid-in capital	35,701,094	35,131,058
Treasury stock, at cost, 1,000 shares	(750)	(750)
Accumulated deficit	(36,986,354)	(35,513,055)
Total Stockholders' Deficit	(1,275,201)	(372,188)
TOTAL LIABILITIES AND STOCKHOLDERS' DEFICIT	$ 33,544,970	$ 30,607,283

See notes to unaudited consolidated financial statements.

TRANS ENERGY, INC. AND SUBSIDIARIES
Consolidated Statements of Operations
(Unaudited)

	For the Three Months Ended June 30, 2009	For the Three Months Ended June 30, 2008	For the Six Months Ended June 30, 2009	For the Six Months Ended June 30, 2008
REVENUES	$ 1,504,773	$ 1,229,074	$ 3,037,034	$ 1,656,720
COSTS AND EXPENSES				
Production costs	492,597	350,788	1,017,383	607,852
Dry hole costs	-	94,216	-	94,216
Depreciation, depletion, amortization and accretion	520,901	224,718	934,545	376,582
Selling, general and administrative	786,641	435,491	1,407,037	1,130,066
Loss (gain) on sale of assets	1,312	(3,152)	1,812	(1,866)
Total Costs and Expenses	1,801,451	1,102,061	3,360,777	2,206,850
(LOSS) INCOME FROM OPERATIONS	(296,678)	127,013	(323,743)	(550,130)
OTHER INCOME (EXPENSES)				
Interest income	9,786	2,651	13,960	10,042
Other income	-	92,396	-	92,396
Interest expense	(618,355)	(444,522)	(1,354,983)	(920,715)
Gain (loss) on derivative contracts	86,664	(75,624)	191,467	(143,389)
Total Other Expenses	(521,905)	(425,099)	(1,149,556)	(961,666)
NET LOSS BEFORE INCOME TAXES	(818,583)	(298,086)	(1,473,299)	(1,511,796)
INCOME TAXES	-	-	-	-
NET LOSS	$ (818,583)	$ (298,086)	$(1,473,299)	$(1,511,796)
LOSS PER SHARE – BASIC AND DILUTED	$ (0.08)	$ (0.03)	$ (0.14)	$ (0.15)
WEIGHTED AVERAGE SHARES OUTSTANDING – BASIC AND DILUTED	10,677,815	10,442,565	10,618,768	10,242,579

See notes to unaudited consolidated financial statements.

6

TRANS ENERGY, INC. AND SUBSIDIARIES
Consolidated Statement of Stockholders' Deficit
For the Six Months Ended June 30, 2009
(Unaudited)

	Common Stock		Additional Paid in	Treasury	Accumulated	
	Shares	Amount	Capital	Stock	Deficit	Total
Balance, December 31, 2008	10,559,065	$ 10,559	$ 5,131,058	$ (750)	$(35,513,055)	$ (372,188)
Shares issued for services	250,000	250	411,125	-	-	411,375
Stock Option Compensation Expense	-	-	158,911	-	-	158,911
Net loss for the six months ended June 30, 2009	-	-	-	-	(1,473,299)	(1,473,299)
Balance, June 30, 2009	10,809,065	$ 10,809	$35,701,094	$ (750)	(36,986,354)	$ (1,275,201)

See notes to unaudited consolidated financial statements.

TRANS ENERGY, INC. AND SUBSIDIARIES
Consolidated Statements of Cash Flows
(Unaudited)

	For the Six Months Ended June 30, 2009	2008
CASH FLOWS FROM OPERATING ACTIVITIES:		
Net loss	$ (1,473,299)	$ (1,511,796)
Adjustments to reconcile net loss to net cash used by operating activities:		
Depreciation, depletion, amortization and accretion	934,545	376,582
Amortization of financing cost and debt discount	268,864	244,157
Share-based compensation	570,286	330,972
Loss (gain) on sale of assets	1,812	(1,866)
(Gain) loss on derivative contract	(191,467)	143,389
Changes in operating assets and liabilities:		
Accounts receivable	(1,456,833)	(407,071)
Accounts receivable – related parties	1,200,536	(407,687)
Accounts receivable due from non-operator, net	291,845	797,711
Advances to operator, net	-	548,715
Prepaid expenses and other assets	(68,764)	7,552
Accounts payable and accrued expenses	(832,566)	50,862
Accounts payable – related party	-	(35,972)
Net cash (used) provided by operating activities	(755,041)	135,548
CASH FLOWS FROM INVESTING ACTIVITIES:		
Investment in note receivable	(311,440)	-
Proceeds from payments on note receivable	97,211	-
Proceeds from sale of assets	10,200	5,000
Expenditures for oil and gas properties	(2,644,328)	(7,479,647)
Expenditures for property and equipment	(152,986)	(234,235)
Net cash used by investing activities	(3,001,343)	(7,708,882)
CASH FLOWS FROM FINANCING ACTIVITIES:		
Proceeds from derivative contracts	353,947	-
Proceeds from notes payable	2,014,586	7,286,854
Payments on notes payable	(52,137)	(42,077)
Net cash provided by financing activities	2,316,396	7,244,777
NET CHANGE IN CASH	(1,439,988)	(328,557)
CASH, BEGINNING OF PERIOD	1,806,008	1,702,373
CASH, END OF PERIOD	$ 366,020	$ 1,373,816

SUPPLEMENTAL DISCLOSURES FOR CASH FLOW INFORMATION:		
Cash paid for interest	$ 1,037,729	$ 648,828
Cash paid for income taxes	$ -	$ -
Non-cash investing and financing activities:		
Accrued expenditures for oil and gas properties	$ 2,536,158	$ 519,789
Increase in asset retirement obligation	$ 2,749	$ 6,711
Revision of asset retirement obligation	$ -	$ 14,282
Common shares issued for stock compensation payable	$ -	$ 516,600

See notes to unaudited consolidated financial statements.

TRANS ENERGY, INC. AND SUBSIDIARIES

Notes to Consolidated Financial Statements

(Unaudited)

NOTE 1 – BASIS OF FINANCIAL STATEMENT PRESENTATION AND SIGNIFICANT ACCOUNTING POLICIES

The accompanying unaudited interim consolidated financial statements have been prepared by Trans Energy, Inc., (Trans Energy or the Company), pursuant to the rules and regulations of the Securities and Exchange Commission. Certain information and footnote disclosures normally included in financial statements prepared in accordance with accounting principles generally accepted in the United States of America have been omitted in accordance with such rules and regulations. The information furnished in the interim consolidated financial statements includes normal recurring adjustments and reflects all adjustments, which, in the opinion of management, are necessary for a fair presentation of such financial statements. Although management believes the disclosures and information presented are adequate to make the information not misleading, it is suggested that these interim consolidated financial statements be read in conjunction with Trans Energy’s most recent audited consolidated financial statements and notes thereto included in its December 31, 2008 Annual Report on Form 10-K. Operating results for the six months ended June 30, 2009 are not necessarily indicative of the results that may be expected for the year ending December 31, 2009.

Certain reclassifications have been made to amounts in prior periods to conform to the current period presentation.

Nature of Operations and Organization

Trans Energy is an independent energy company engaged in the exploration, development, exploitation and production of oil and natural gas. Its operations are presently focused in the State of West Virginia.

Principles of Consolidation

The consolidated financial statements include Trans Energy and its wholly-owned subsidiaries, Prima Oil Company, Inc., Ritchie County Gathering Systems, Inc., Tyler Construction Company, Inc, and Tyler Energy, Inc. All significant inter-company balances and transactions have been eliminated in consolidation.

Asset Retirement Obligations

The Company follows Statement of Financial Accounting Standards (“SFAS”) No. 143, “Accounting for Asset Retirement Obligations,” which requires the fair value of a liability for an asset retirement obligation to be recognized in the period in which it is incurred if a reasonable estimate of fair value can be made. For the Company, these obligations include dismantlement, plugging and abandonment of oil and gas wells and associated pipelines and equipment. The associated asset retirement costs are capitalized as part of the carrying amount of the long-lived asset. The liability is accreted to its then present value each period, and the capitalized cost is depleted over the estimated useful life of the related asset.

The following is a description of the changes to Trans Energy's asset retirement obligations for the six months ended June 30, 2009:

Asset retirement obligations at beginning of period	$ 178,954
Liabilities incurred during the period	2,749
Accretion expense	12,107
Asset retirement obligations at end of period	$ 193,810

Revenue and Cost Recognition

Trans Energy uses the sales method to account for sales of crude oil and natural gas. Under this method, revenues are recognized based on actual volumes of oil and gas sold to purchasers. The volumes sold may differ from the volumes to which Trans Energy is entitled based on our interest in the properties. These differences create imbalances which are recognized as a liability only when the imbalance exceeds the estimate of remaining reserves. Trans Energy had no imbalances as of June 30, 2009 and December 31, 2008. Costs associated with production are expensed in the period incurred. Trans Energy recognizes gas revenues upon delivery of the gas to the customers' pipeline from Trans Energy's pipelines when recorded as received by the customer's meter. Trans Energy recognizes oil revenues when pumped and measured by the customer.

Note Receivables

Note receivables are carried at the expected net realizable value. No allowance for doubtful accounts is deemed necessary based on management's continued assessment of the collectability of debtors.

Concentration of Credit Risk

Financial instruments that potentially subject the Company to a concentration of credit risk include cash. The Company did not have any cash deposits in excess of FDIC insured limits. The Company has not experienced any losses on its deposits of cash.

Use of Estimates

The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates. The Company’s financial statements are based on a number of significant estimates, including oil and gas reserve quantities which are the basis for the calculation of depreciation, depletion and impairment of oil and gas properties, and timing and costs associated with its asset retirement obligations.

Income Taxes

At June 30, 2009, the Company had net operating loss carry forwards (NOLS) for future years of approximately $36,951,914. These NOLS will expire at various dates through 2029. Utilization of the NOLs could be limited if there is a substantial change in ownership of the Company and is contingent on future earnings.

The Company has provided a valuation allowance equal to 100% of the total net deferred asset in recognition of the uncertainty regarding the ultimate amount of the net deferred tax asset that will be realized.

Commitments and Contingencies

The Company operates exclusively in the United States, entirely in West Virginia, in the business of oil and gas acquisition, exploration, development and production. The Company operates in an environment with many financial risks, including, but not limited to, the ability to acquire additional economically recoverable oil and gas reserves, the inherent risks of the search for, development of and production of oil and gas, the ability to sell oil and gas at prices which will provide attractive rates of return, the volatility and seasonality of oil and gas production and prices, and the highly competitive and, at times, seasonal nature of the industry and worldwide economic conditions. The Company’s ability to expand its reserve base and diversify its operations is also dependent upon the Company’s ability to obtain the necessary capital through operating cash flow, borrowings or equity offerings. Various federal, state and governmental agencies are considering, and some have adopted, laws and regulations regarding environmental protection which could adversely affect the proposed business activities of the Company. The Company cannot predict what effect, if any, current and future regulations may have on the operations of the Company.

The Company has natural gas delivery commitments to Dominion Field Services, Inc. Management believes the Company can meet its delivery commitments based on estimated production. If, however, the Company cannot meet its delivery commitments, it will purchase gas at market prices to meet such commitments which will result in a gain or loss for the difference between the delivery commitment price and the price the Company is able to purchase the gas for redelivery (resale) to its customers.

Fair Value of Financial Instruments

Effective January 1, 2008, Trans Energy adopted SFAS No. 157 for financial assets and liabilities. SFAS No. 157 establishes a framework for measuring fair value and expands disclosures about fair value measurements by establishing a fair value hierarchy that prioritizes the inputs and defines valuation techniques used to measure fair value. The hierarchy gives the highest priority to Level 1 inputs and lowest priority to Level 3 inputs. The three levels of the fair value hierarchy under SFAS No. 157 are described below:

Basis of Fair Value Measurement

Level 1 Observable inputs that reflect quoted prices (unadjusted) for identical assets or liabilities in active markets.

Level 2 Inputs reflect quoted prices for identical assets or liabilities in markets that are not active; quoted prices for similar assets or liabilities in active markets; inputs other than quoted prices that are observable for the asset or the liability; or inputs that are derived principally from or corroborated by observable market data by correlation or other means.

Level 3 Unobservable inputs reflecting Trans Energy's own assumptions incorporated in valuation techniques used to determine fair value. These assumptions are required to be consistent with market participant assumptions that are reasonably available.

Trans Energy believes that the fair value of its financial instruments comprising cash, certificates of deposit, accounts receivable, notes receivable, accounts payable, and notes payable approximate their carrying amounts. The interest rates payable by Trans Energy on its notes payable approximate market rates. The fair values of Trans Energy’s Level 2 financial assets consist of derivative assets, which are based on quoted commodity prices of the underlying commodity. As of June 30, 2009 and December 31, 2008, Trans Energy did not have any Level 1 or 3 financial assets or liabilities. The following tables summarize fair value measurement information for Trans Energy’s financial assets:

11

As of June 30, 2009					
			Fair Value Measurements Using:		
	Carrying Amount	Total Fair Value	Quoted Prices in Active Markets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Financial Assets:					
Derivative assets	$1,077,012	$1,077,012	$-	$1,077,012	$-

As of December 31, 2008					
			Fair Value Measurements Using:		
	Carrying Amount	Total Fair Value	Quoted Prices in Active Markets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Financial Assets:					
Derivative assets	$1,217,159	$1,217,159	$-	$1,217,159	$-

New Accounting Standards

In March 2008, the FASB issued SFAS No. 161, *Disclosures about Derivative Instruments and Hedging Activities—an amendment of FASB Statement No. 133*, or SFAS No. 161, which required enhanced disclosures about an entity's derivative and hedging activities and was intended to improve the transparency of financial reporting. SFAS No. 161 applies to all derivative instruments, including bifurcated derivative instruments and related hedging items accounted for under SFAS No. 133 and its related interpretations. SFAS No. 161 amends and expands the disclosure requirements of SFAS No. 133 with the intent to provide users of financial statements with an enhanced understanding of: (i) how and why an entity uses derivative instruments, (ii) how derivative instruments and related hedged items are accounted for under SFAS No. 133 and its related interpretations and (iii) how derivative instruments and related hedged items affect an entity's financial position, financial performance and cash flows. The provisions of this standard do not require disclosures for earlier periods presented for comparative purposes at initial adoption. SFAS No. 161 was effective for fiscal years and interim periods beginning after November 15, 2008. Trans Energy adopted SFAS No. 161 on January 1, 2009 and it has reflected the impact on its consolidated financial statements.

In May 2009, the FASB issued SFAS No. 165, *Subsequent Events* (SFAS 165). SFAS No. 165 establishes general standards of accounting for and disclosure of events that occur after the balance sheet date but before financial statements are issued. This statement is effective for interim and annual periods ending after June 15, 2009. SFAS No. 165 will be effective for the Company beginning the third quarter of fiscal 2009. Trans Energy does not expect the adoption of this standard to have a material effect on its consolidated financial statements.

In June 2009, the FASB issued Statement No. 168, *The FASB Accounting Standards Codification and the Hierarchy of Generally Accepted Accounting Principles* ("SFAS No. 168"). SFAS No. 168 will become the single source of authoritative nongovernmental U.S. generally accepted accounting principles ("GAAP"), superseding existing FASB, American Institute of Certified Public Accountants ("AICPA"), Emerging Issues Task Force ("EITF"), and related accounting literature. SFAS No. 168 reorganizes the thousands of GAAP pronouncements into roughly 90 accounting topics and displays them using a consistent structure. Also included is relevant Securities and Exchange Commission guidance organized using the same topical structure in separate sections. SFAS No. 168 will be effective for financial statements issued for reporting periods that end after September 15, 2009. This will have an impact on the Company's financial statements since all future references to authoritative accounting literature will be references in accordance with SFAS No. 168.

Trans Energy does not expect the adoption of any other recently issued accounting pronouncements to have a significant effect on its financial statements.

NOTE 2 – GOING CONCERN

Trans Energy's unaudited interim consolidated financial statements are prepared using accounting principles generally accepted in the United States of America applicable to a going concern, which contemplates the realization of assets and liquidation of liabilities in the normal course of business. Trans Energy has incurred cumulative operating losses through June 30, 2009 of $36,951,914 and had a stockholders' deficit of $1,240,761 at June 30, 2009. Revenues during the six months ended June 30, 2009 were not sufficient to cover its operating costs. We expect positive operating cash flow from existing wells and new drilling which will allow us to continue as a going concern. There can be no assurance that Trans Energy can or will be able to complete any debt or equity financing that might be needed to fund operations in the future. Trans Energy's unaudited interim consolidated financial statements do not include any adjustments that might result from the outcome of this uncertainty.

NOTE 3 – NOTE RECEIVABLE

Trans Energy holds a promissory note agreement with Warren Drilling Co., Inc., an Ohio Corporation. The purpose of the promissory note was to fund certain drilling equipment necessary to equip the rig for horizontal drilling. An initial advance in the amount of $302,280 was made on December 22, 2008, with a second advance in the amount of $311,440 made on February 4, 2009. The note bears interest in the amount of 6.5% per annum, payable in monthly installments of $27,443 for 24 months. As of June 30, 2009, the outstanding balance was $516,509, of which $304,560 was classified as current. The note is secured by equipment of Warren Drilling, Co., for which an executed security agreement was filed with the promissory note. Trans Energy has evaluated their relationship with Warren Drilling, pursuant to FIN 46(R) *Consolidation of Variable Interest Entities*, and has determined that Trans Energy does not have a controlling financial interest in Warren Drilling which would require consolidation.

NOTE 4 – OIL AND GAS PROPERTIES

Total additions for oil and gas properties during the six months ended June 30, 2009 and June 30, 2008 were $5,180,487 and $7,999,436, respectively. Trans Energy also incurred $152,986 and $234,235, respectively, for additional property, plant and equipment.

Depreciation, depletion, and amortization expenses on oil and gas properties were $842,210 and $289,905 for the six months ended June 30, 2009 and 2008, respectively. Depreciation, depletion and amortization expenses for non oil and gas properties were $80,228 and $86,677 for the six months ended June 30, 2009 and 2008, respectively.

NOTE 5 – DERIVATIVE AND OTHER HEDGING INSTRUMENTS

Trans Energy entered into derivative commodity price contracts to provide a measure of stability in the cash flows associated with Trans Energy's oil and gas production and to manage exposure to commodity price fluctuations. Trans Energy does not designate its derivative financial instruments as hedging instruments for financial accounting purposes, and as a result, recognizes the change in the respective instruments' fair value in earnings.

On July 13, 2007, as required by the CIT Creditor Agreement, Trans Energy purchased a commodity put option on natural gas. In addition, on May 22, 2008, Trans Energy entered into a participating commodity put and call option on oil as a costless collar.

Natural Gas Derivatives

Trans Energy entered into participating commodity put options on natural gas whereby Trans Energy receives a floor price. The natural gas commodity put options are indexed to NYMEX Henry Hub prices. The following table shows the monthly volumes and the floor price.