Oasis Petroleum Inc.
Form 10-Q
August 06, 2014
Table of Contents

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

FORM 10-Q

ý QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the quarterly period ended June 30, 2014
or
¨ TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the transition period from to
Commission file number: 1-34776

Oasis Petroleum Inc.
(Exact name of registrant as specified in its charter)

Delaware (State or other jurisdiction of incorporation or organization)	80-0554627 (I.R.S. Employer Identification No.)
1001 Fannin Street, Suite 1500 Houston, Texas (Address of principal executive offices)	77002 (Zip Code)

(281) 404-9500
(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 ý 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 ý 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 ý	Accelerated filer ¨
Non-accelerated filer o (Do not check if a smaller reporting company)	Smaller reporting company ¨

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

Number of shares of the registrant’s common stock outstanding at August 1, 2014: 101,153,956 shares.

Table of Contents

OASIS PETROLEUM INC.
FORM 10-Q
FOR THE QUARTER ENDED JUNE 30, 2014
TABLE OF CONTENTS

Table of Contents

PART I — FINANCIAL INFORMATION
Item 1. — Financial Statements (Unaudited)
Oasis Petroleum Inc.
Condensed Consolidated Balance Sheet
(Unaudited)

	June 30, 2014	December 31, 2013
	(In thousands, except share data)	
ASSETS		
Current assets		
Cash and cash equivalents	$26,957	$91,901
Accounts receivable — oil and gas revenues	216,764	175,653
Accounts receivable — joint interest partners	147,056	139,459
Inventory	17,636	20,652
Prepaid expenses	8,907	10,191
Deferred income taxes	25,390	6,335
Derivative instruments	—	2,264
Advances to joint interest partners	97	760
Other current assets	421	391
Total current assets	443,228	447,606
Property, plant and equipment		
Oil and gas properties (successful efforts method)	5,141,582	4,528,958
Other property and equipment	231,129	188,468
Less: accumulated depreciation, depletion, amortization and impairment	(823,500)	(637,676)
Total property, plant and equipment, net	4,549,211	4,079,750
Assets held for sale	—	137,066
Derivative instruments	—	1,333
Deferred costs and other assets	44,540	46,169
Total assets	$5,036,979	$4,711,924
LIABILITIES AND STOCKHOLDERS' EQUITY		
Current liabilities		
Accounts payable	$32,402	$8,920
Revenues and production taxes payable	217,414	146,741
Accrued liabilities	288,813	241,830
Accrued interest payable	49,444	47,910
Derivative instruments	62,415	8,188
Advances from joint interest partners	6,910	12,829
Other current liabilities	3,311	—
Total current liabilities	660,709	466,418
Long-term debt	2,300,000	2,535,570
Deferred income taxes	460,897	323,147
Asset retirement obligations	37,542	35,918
Derivative instruments	11,844	139
Other liabilities	1,963	2,183
Total liabilities	3,472,955	3,363,375
Commitments and contingencies (Note 14)		
Stockholders' equity		
Common stock, $0.01 par value: 300,000,000 shares authorized; 101,396,597 and 100,866,589 shares issued at June 30, 2014 and December 31, 2013, respectively	999	996

Treasury stock, at cost: 244,729 and 167,155 shares at June 30, 2014 and December 31, 2013, respectively	(8,677)	(5,362)
Additional paid-in capital	995,024	985,023
Retained earnings	576,678	367,892
Total stockholders’ equity	1,564,024	1,348,549
Total liabilities and stockholders’ equity	$5,036,979	$4,711,924

The accompanying notes are an integral part of these condensed consolidated financial statements.

Table of Contents

Oasis Petroleum Inc.
Condensed Consolidated Statement of Operations
(Unaudited)

	Three Months Ended June 30,		Six Months Ended June 30,	
	2014	2013	2014	2013
	(In thousands, except per share data)			
Revenues				
Oil and gas revenues	$354,182	$241,842	$686,029	$483,493
Well services and midstream revenues	18,196	12,740	35,868	19,393
Total revenues	372,378	254,582	721,897	502,886
Expenses				
Lease operating expenses	40,553	18,266	80,542	37,755
Well services and midstream operating expenses	8,769	6,644	19,689	9,558
Marketing, transportation and gathering expenses	7,114	10,779	12,300	14,168
Production taxes	34,493	21,397	66,296	43,486
Depreciation, depletion and amortization	97,276	66,790	188,548	133,051
Exploration expenses	475	392	855	2,249
Impairment of oil and gas properties	42	208	804	706
General and administrative expenses	20,751	16,656	44,271	30,510
Total expenses	209,473	141,132	413,305	271,483
Gain on sale of properties	3,640	—	187,033	—
Operating income	166,545	113,450	495,625	231,403
Other income (expense)				
Net gain (loss) on derivative instruments	(65,570)	12,591	(83,173)	(2,021)
Interest expense, net of capitalized interest	(38,990)	(21,392)	(79,148)	(42,575)
Other income (expense)	135	294	288	1,074
Total other income (expense)	(104,425)	(8,507)	(162,033)	(43,522)
Income before income taxes	62,120	104,943	333,592	187,881
Income tax expense	23,287	37,824	124,806	68,911
Net income	$38,833	$67,119	$208,786	$118,970
Earnings per share:				
Basic (Note 12)	$0.39	$0.73	$2.10	$1.29
Diluted (Note 12)	0.39	0.72	2.08	1.28
Weighted average shares outstanding:				
Basic (Note 12)	99,663	92,399	99,612	92,387
Diluted (Note 12)	100,260	92,702	100,328	92,812

The accompanying notes are an integral part of these condensed consolidated financial statements.

Table of Contents

Oasis Petroleum Inc.
Condensed Consolidated Statement of Changes in Stockholders' Equity
(Unaudited)
(In thousands)

	Common Stock		Treasury Stock		Additional Paid-in Capital	Retained Earnings	Total Stockholders' Equity
	Shares	Amount	Shares	Amount			
Balance as of December 31, 2013	100,699	$996	167	$(5,362)	$985,023	$367,892	$1,348,549
Fees (2013 issuance of common stock)	—	—	—	—	(176)	—	(176)
Stock-based compensation	531	—	—	—	10,180	—	10,180
Vesting of restricted shares	—	3	—	—	(3)	—	—
Treasury stock – tax withholdings	(78)	—	78	(3,315)	—	—	(3,315)
Net income	—	—	—	—	—	208,786	208,786
Balance as of June 30, 2014	101,152	$999	245	$(8,677)	$995,024	$576,678	$1,564,024

The accompanying notes are an integral part of these condensed consolidated financial statements.

Table of Contents

Oasis Petroleum Inc.
Condensed Consolidated Statement of Cash Flows
(Unaudited)

	Six Months Ended June 30, 2014	2013
	(In thousands)	
Cash flows from operating activities:		
Net income	$208,786	$118,970
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation, depletion and amortization	188,548	133,051
Gain on sale of properties	(187,033)	—
Impairment of oil and gas properties	804	706
Deferred income taxes	118,695	67,974
Derivative instruments	83,173	2,021
Stock-based compensation expenses	9,678	5,371
Debt discount amortization and other	3,220	1,753
Working capital and other changes:		
Change in accounts receivable	(37,132)	(13,768)
Change in inventory	3,016	(4,200)
Change in prepaid expenses	1,284	(4,402)
Change in other current assets	(30)	330
Change in other assets	(1,477)	—
Change in accounts payable and accrued liabilities	91,543	48,701
Change in other current liabilities	3,311	688
Change in other liabilities	(132)	612
Net cash provided by operating activities	486,254	357,807
Cash flows from investing activities:		
Capital expenditures	(606,924)	(428,630)
Acquisition of oil and gas properties	(8,116)	—
Proceeds from sale of properties	324,888	—
Costs related to sale of properties	(2,337)	—
Redemptions of short-term investments	—	25,000
Derivative settlements	(13,644)	2,932
Advances from joint interest partners	(5,919)	(5,593)
Net cash used in investing activities	(312,052)	(406,291)
Cash flows from financing activities:		
Proceeds from revolving credit facility	100,000	—
Principal payments on revolving credit facility	(335,570)	—
Purchases of treasury stock	(3,315)	(364)
Debt issuance costs	(85)	(2,998)
Other	(176)	—
Net cash used in financing activities	(239,146)	(3,362)
Decrease in cash and cash equivalents	(64,944)	(51,846)
Cash and cash equivalents:		
Beginning of period	91,901	213,447
End of period	$26,957	$161,601
Supplemental non-cash transactions:		
Change in accrued capital expenditures	$51,129	$(6,085)

Change in asset retirement obligations	1,624	3,441

The accompanying notes are an integral part of these condensed consolidated financial statements.

4

Table of Contents

OASIS PETROLEUM INC.

Notes to Condensed Consolidated Financial Statements (Unaudited)

1. Organization and Operations of the Company

Organization

Oasis Petroleum Inc. (together with its subsidiaries, "Oasis" or the "Company") was formed on February 25, 2010, pursuant to the laws of the State of Delaware, to become a holding company for Oasis Petroleum LLC ("OP LLC"), the Company's predecessor, which was formed as a Delaware limited liability company on February 26, 2007. In connection with its initial public offering in June 2010 and related corporate reorganization, the Company acquired all of the outstanding membership interests in OP LLC in exchange for shares of the Company's common stock. In 2007, Oasis Petroleum North America LLC ("OPNA"), a Delaware limited liability company, was formed to conduct domestic oil and natural gas exploration and production activities. In 2011, the Company formed Oasis Well Services LLC ("OWS"), a Delaware limited liability company, to provide well services to OPNA, and Oasis Petroleum Marketing LLC ("OPM"), a Delaware limited liability company, to provide marketing services to OPNA. In 2013, the Company formed Oasis Midstream Services LLC ("OMS"), a Delaware limited liability company, to provide midstream services to OPNA. As part of the formation of OMS, the Company transferred substantially all of its salt water disposal and other midstream assets from OPNA to OMS.

Nature of Business

The Company is an independent exploration and production company focused on the acquisition and development of unconventional oil and natural gas resources in the Williston Basin. The Company's proved and unproved oil and natural gas properties are located in the North Dakota and Montana areas of the Williston Basin and are owned by OPNA. The Company also operates a marketing business (OPM), a well services business (OWS) and a midstream services business (OMS), all of which are complementary to its primary development and production activities. Both OWS and OMS are separate reportable business segments.

2. Summary of Significant Accounting Policies

Basis of Presentation

The accompanying condensed consolidated financial statements of the Company include the accounts of Oasis and its wholly-owned subsidiaries. All significant intercompany transactions have been eliminated in consolidation. The accompanying condensed consolidated financial statements of the Company have not been audited by the Company's independent registered public accounting firm, except that the Condensed Consolidated Balance Sheet at December 31, 2013 is derived from audited financial statements. Certain reclassifications of prior year balances have been made to conform such amounts to current year classifications. These reclassifications have no impact on net income. In the opinion of management, all adjustments, consisting of normal recurring adjustments necessary for the fair presentation, have been included. Management has made certain estimates and assumptions that affect reported amounts in the condensed consolidated financial statements and disclosures of contingencies. Actual results may differ from those estimates. The results for interim periods are not necessarily indicative of annual results.

These interim financial statements have been prepared pursuant to the rules and regulations of the Securities and Exchange Commission ("SEC") regarding interim financial reporting. Certain disclosures have been condensed or omitted from these financial statements. Accordingly, they do not include all of the information and notes required by accounting principles generally accepted in the United States of America ("GAAP") for complete consolidated financial statements and should be read in conjunction with the Company's audited consolidated financial statements and notes thereto included in the Company's Annual Report on Form 10-K for the year ended December 31, 2013 ("2013 Annual Report").

Significant Accounting Policies

There have been no material changes to the Company's critical accounting policies and estimates from those disclosed in the 2013 Annual Report other than those noted below.

Recent Accounting Pronouncements

Revenue recognition. In May 2014, the Financial Accounting Standards Board ("FASB") issued Accounting Standards Update No. 2014-09, Revenue from Contracts with Customers ("ASU 2014-09"). The objective of ASU 2014-09 is greater consistency and comparability across industries by using a five-step model to recognize revenue from customer contracts. ASU 2014-09 also contains some new disclosure requirements under GAAP and is effective for interim and annual reporting periods beginning after December 15, 2016. The Company is currently evaluating the effect that adopting this new guidance will have on its financial position, cash flows and results of operations.

Table of Contents

3. Inventory

Equipment and materials consist primarily of tubular goods, well equipment to be used in future drilling or repair operations, well fracturing equipment, chemicals and proppant, all of which are stated at the lower of cost or market value with cost determined on an average cost method. Crude oil inventory includes oil in tank and linefill and is stated at the lower of average cost or market value. Inventory consists of the following:

	June 30, 2014	December 31, 2013
	(In thousands)	
Equipment and materials	$7,222	$11,669
Crude oil inventory	10,414	8,983
Total inventory	$17,636	$20,652

4. Property, Plant and Equipment

The following table sets forth the Company's property, plant and equipment:

	June 30, 2014	December 31, 2013
	(In thousands)	
Proved oil and gas properties[1]	$4,305,827	$3,713,525
Less: Accumulated depreciation, depletion, amortization and impairment	(787,418)	(612,380)
Proved oil and gas properties, net	3,518,409	3,101,145
Unproved oil and gas properties	835,755	815,433
Total oil and gas properties, net	4,354,164	3,916,578
Other property and equipment	231,129	188,468
Less: Accumulated depreciation	(36,082)	(25,296)
Other property and equipment, net	195,047	163,172
Total property, plant and equipment, net	$4,549,211	$4,079,750

(1) Included in the Company's proved oil and gas properties are estimates of future asset retirement costs of $33.4 million and $32.6 million at June 30, 2014 and December 31, 2013, respectively.

As a result of expiring leases and periodic assessments of unproved properties, the Company recorded non-cash impairment charges on its unproved oil and natural gas properties of $42,000 and $0.8 million for the three and six months ended June 30, 2014, respectively, and $0.2 million and $0.7 million for the three and six months ended June 30, 2013, respectively. No impairment charges on proved oil and natural gas properties were recorded for the three and six months ended June 30, 2014 or 2013.

5. Divestiture

On March 5, 2014, the Company completed the sale of certain non-operated properties in its Sanish project area and other non-operated leases adjacent to its Sanish position (the "Sanish Divestiture") for cash proceeds of approximately $324.9 million, which includes, and is subject to further, customary post close adjustments. The Company recognized a $187.0 million gain on sale of properties in its Condensed Consolidated Statement of Operations for the six months ended June 30, 2014. The transaction was structured as an Internal Revenue Code Section 1031 like-kind exchange for tax purposes and as such did not give rise to any currently taxable gain.

6. Fair Value Measurements

In accordance with the FASB's authoritative guidance on fair value measurements, the Company's financial assets and liabilities are measured at fair value on a recurring basis. The Company recognizes its non-financial assets and liabilities, such as asset retirement obligations ("ARO") and proved oil and natural gas properties upon impairment, at fair value on a non-recurring basis.

As defined in the authoritative guidance, fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date (exit price). To estimate fair value, the Company utilizes market data or assumptions that market participants would use in pricing the asset or liability, including assumptions about risk and the risks inherent in the inputs to the valuation technique. These inputs can be readily observable, market corroborated or generally unobservable.

6

Table of Contents

The authoritative guidance establishes a fair value hierarchy that prioritizes the inputs used to measure fair value. The hierarchy gives the highest priority to unadjusted quoted prices in active markets for identical assets or liabilities ("Level 1" measurements) and the lowest priority to unobservable inputs ("Level 3" measurements). The three levels of the fair value hierarchy are as follows:

Level 1 — Unadjusted quoted prices are available in active markets for identical assets or liabilities as of the reporting date. Active markets are those in which transactions for the asset or liability occur in sufficient frequency and volume to provide pricing information on an ongoing basis.

Level 2 — Pricing inputs, other than unadjusted quoted prices in active markets included in Level 1, are either directly or indirectly observable as of the reporting date. Level 2 includes those financial instruments that are valued using models or other valuation methodologies. These models are primarily industry-standard models that consider various assumptions, including quoted forward prices for commodities, time value, volatility factors and current market and contractual prices for the underlying instruments, as well as other relevant economic measures. Substantially all of these assumptions are observable in the marketplace throughout the full term of the instrument and can be derived from observable data or are supported by observable levels at which transactions are executed in the marketplace.

Level 3 — Pricing inputs are generally less observable from objective sources, requiring internally developed valuation methodologies that result in management's best estimate of fair value.

Financial Assets and Liabilities

As required, financial assets and liabilities are classified in their entirety based on the lowest level of input that is significant to the fair value measurement. The Company's assessment of the significance of a particular input requires judgment and may affect the valuation of fair value assets and liabilities and their placement within the fair value hierarchy levels. The following tables set forth by level within the fair value hierarchy the Company's financial assets and liabilities that were accounted for at fair value on a recurring basis:

	At fair value as of June 30, 2014			
	Level 1	Level 2	Level 3	Total
	(In thousands)			
Assets:				
Money market funds	$742	$—	$—	$742
Total assets	$742	$—	$—	$742
Liabilities:				
Commodity derivative instruments (see Note 7)	$—	$74,259	$—	$74,259
Total liabilities	$—	$74,259	$—	$74,259

	At fair value as of December 31, 2013			
	Level 1	Level 2	Level 3	Total
	(In thousands)			
Assets:				
Money market funds	$742	$—	$—	$742
Commodity derivative instruments (see Note 7)	—	3,597	—	3,597
Total assets	$742	$3,597	$—	$4,339
Liabilities:				
Commodity derivative instruments (see Note 7)	$—	$8,327	$—	$8,327
Total liabilities	$—	$8,327	$—	$8,327

The Level 1 instruments presented in the tables above consist of money market funds included in cash and cash equivalents on the Company's Condensed Consolidated Balance Sheet at June 30, 2014 and December 31, 2013. The Company's money market funds represent cash equivalents backed by the assets of high-quality major banks and financial institutions. The Company identified the money market funds as Level 1 instruments because the money market funds have daily liquidity, quoted prices for the underlying investments can be obtained and there are active markets for the underlying investments.

The Level 2 instruments presented in the tables above consist of commodity derivative instruments, which include oil collars, swaps and deferred premium puts. The fair values of the Company’s commodity derivative instruments are based upon a third-party preparer's calculation using mark-to-market valuation reports provided by the Company's counterparties for monthly settlement purposes to determine the valuation of its derivative instruments. The Company has the third-party preparer evaluate other readily available market prices for its derivative contracts as there is an active market for these contracts. The third-party preparer performs its independent valuation using a moment matching method similar to Turnbull-Wakeman for Asian options. The significant inputs used are crude oil prices, volatility, skew, discount rate and the contract terms of the derivative instruments. However, the Company does not have access to the specific proprietary valuation models or inputs used by its counterparties or third-party preparer. The Company compares the third-party preparer's valuation to counterparty valuation statements, investigating any significant differences, and analyzes monthly valuation changes in relation to movements in crude oil forward price curves. The determination of the fair value for derivative instruments also incorporates a credit adjustment for non-performance risk, as required by GAAP. The Company calculates the credit adjustment for derivatives in a net asset position using current credit default swap values for each counterparty. The credit adjustment for derivatives in a net liability position is based on the Company's market credit spread. Based on these calculations, the Company recorded an adjustment to reduce the fair value of its net derivative liability by $2.5 million and $0.2 million at June 30, 2014 and December 31, 2013, respectively.

Fair Value of Other Financial Instruments

The Company's financial instruments, including certain cash and cash equivalents, accounts receivable and accounts payable, are carried at cost, which approximates fair value due to the short-term maturity of these instruments. At June 30, 2014, the Company's cash equivalents were all Level 1 assets. The carrying amount of the Company's long-term debt reported in the Condensed Consolidated Balance Sheet at June 30, 2014 is $2,300.0 million, which includes $2,200.0 million of senior unsecured notes and $100.0 million of borrowings under the revolving credit facility (see Note 8 – Long-Term Debt). The fair value of the Company's senior unsecured notes, which are Level 1 liabilities, is $2,380.0 million at June 30, 2014.

Nonfinancial Assets and Liabilities

Asset retirement obligations. The carrying amount of the Company's ARO in the Condensed Consolidated Balance Sheet at June 30, 2014 is $38.1 million (see Note 9 – Asset Retirement Obligations). The Company determines the ARO by calculating the present value of estimated cash flows related to the liability. Estimating the future ARO requires management to make estimates and judgments regarding timing and existence of a liability, as well as what constitutes adequate restoration. Inherent in the fair value calculation are numerous assumptions and judgments, including the ultimate costs, inflation factors, credit adjusted discount rates, timing of settlement and changes in the legal, regulatory, environmental and political environments. These assumptions represent Level 3 inputs. To the extent future revisions to these assumptions impact the fair value of the existing ARO liability, a corresponding adjustment is made to the related asset.

Impairment. The Company reviews its proved oil and natural gas properties for impairment whenever events and circumstances indicate that a decline in the recoverability of their carrying value may have occurred. The Company estimates the expected undiscounted future cash flows of its oil and natural gas properties and compares such undiscounted future cash flows to the carrying amount of the oil and natural gas properties to determine if the carrying amount is recoverable. If the carrying amount exceeds the estimated undiscounted future cash flows, the Company will adjust the carrying amount of the oil and natural gas properties to fair value. The factors used to determine fair value are subject to management's judgment and expertise and include, but are not limited to, recent sales prices of comparable properties, the present value of future cash flows, net of estimated operating and development costs using estimates of proved reserves, future commodity pricing, future production estimates, anticipated capital expenditures and various discount rates commensurate with the risk and current market conditions associated with realizing the expected cash flows