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PDC ENERGY, INC.

Form 10-Q

May 02, 2019

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pdce:Wells utreg:MBbls iso4217:USD xbrli:shares iso4217:USD

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**UNITED STATES  
SECURITIES AND EXCHANGE COMMISSION**

Washington, D.C. 20549

## FORM 10-Q

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

For the quarterly period ended March 31, 2019

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 001-37419

## PDC ENERGY, INC.

(Exact name of registrant as specified in its charter)

Delaware 95-2636730

(State of incorporation) (I.R.S. Employer Identification No.)

1775 Sherman Street, Suite 3000

Denver, Colorado 80203

(Address of principal executive offices) (Zip code)

**Registrant's telephone number, including area code: (303) 860-5800**

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 every Interactive Data File required to be submitted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit such files). Yes  No

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

Indicate the number of shares outstanding of each of the issuer's classes of common stock, as of the latest practicable date: 66,282,650 shares of the Company's Common Stock (\$0.01 par value) were outstanding as of April 22, 2019.

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**PDC ENERGY, INC.**

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## **SPECIAL NOTE REGARDING FORWARD-LOOKING STATEMENTS**

This Quarterly Report on Form 10-Q contains forward-looking statements within the meaning of Section 27A of the Securities Act of 1933 ("Securities Act"), Section 21E of the Securities Exchange Act of 1934 ("Exchange Act") and the United States ("U.S.") Private Securities Litigation Reform Act of 1995 regarding our business, financial condition, results of operations and prospects. All statements other than statements of historical fact included in and incorporated by reference into this report are "forward-looking statements." Words such as expect, anticipate, intend, plan, believe, seek, estimate, schedule and similar expressions or variations of such words are intended to identify forward-looking statements herein. Forward-looking statements include, among other things, statements regarding future: production, costs and cash flows; drilling locations, zones and growth opportunities; commodity prices and differentials; capital expenditures and projects, including the number of rigs employed, and that cash flows from operations will exceed expected capital investments in crude oil and natural gas properties for 2019 and 2020; anticipated stock repurchase program, which may be modified or discontinued at any time, and expected timing and amount of such program; financial ratios and compliance with covenants in our revolving credit facility and other debt instruments; impacts of certain accounting and tax changes; anticipated sale of our Delaware Basin midstream assets and the timing of those sales and whether closing will occur timely or at all; timing and adequacy of infrastructure projects of our midstream providers and the related impact on our midstream capacity and related curtailments; fractionation capacity; impacts of Colorado political matters; ability to meet our volume commitments to midstream providers; ongoing compliance with our consent decree; and reclassification of the Denver Metro/North Front Range NAA ozone classification to serious.

The above statements are not the exclusive means of identifying forward-looking statements herein. Although forward-looking statements contained in this report reflect our good faith judgment, such statements can only be based on facts and factors currently known to us. Forward-looking statements are always subject to risks and uncertainties, and become subject to greater levels of risk and uncertainty as they address matters further into the future. Throughout this report or accompanying materials, we may use the term "projection" or similar terms or expressions, or indicate that we have "modeled" certain future scenarios. We typically use these terms to indicate our current thoughts on possible outcomes relating to our business or our industry in periods beyond the current fiscal year. Because such statements relate to events or conditions further in the future, they are subject to increased levels of uncertainty.

Important factors that could cause actual results to differ materially from the forward-looking statements include, but are not limited to:

- changes in global production volumes and demand, including economic conditions that might impact demand and prices for the products we produce;
- volatility of commodity prices for crude oil, natural gas and natural gas liquids ("NGLs") and the risk of an extended period of depressed prices;
- impact to our operations, personnel retention, strategy, stock price and expenses caused by the actions of activist shareholders;
- volatility and widening of differentials;
- reductions in the borrowing base under our revolving credit facility;
- impact of governmental policies and/or regulations, including changes in environmental and other laws, the interpretation and enforcement of those laws and regulations, liabilities arising thereunder and the costs to comply with those laws and regulations;
- declines in the value of our crude oil, natural gas and NGLs properties resulting in impairments;
- changes in estimates of proved reserves;
- inaccuracy of reserve estimates and expected production rates;



- potential for production decline rates from our wells being greater than expected;
  - timing and extent of our success in discovering, acquiring, developing and producing reserves;
  - availability of sufficient pipeline, gathering and other transportation facilities and related infrastructure to process and
  - transport our production and the impact of these facilities and regional capacity on the prices we receive for our production;
  - timing and receipt of necessary regulatory permits;
  - risks incidental to the drilling and operation of crude oil and natural gas wells;
  - difficulties in integrating our operations as a result of any significant acquisitions or acreage exchanges;
  - increases or changes in costs and expenses;
  - availability of supplies, materials, contractors and services that may delay the drilling or completion of our wells;
  - potential losses of acreage due to lease expirations or otherwise;
  - increases or changes in costs and expenses;
-

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future cash flows, liquidity and financial condition;  
possibility that one or more sales of our Delaware Basin midstream assets will not close when expected or at all;  
competition within the oil and gas industry;  
availability and cost of capital;  
our success in marketing crude oil, natural gas and NGLs;  
effect of crude oil and natural gas derivative activities;  
impact of environmental events, governmental and other third-party responses to such events and our ability to insure adequately against such events;  
cost of pending or future litigation;  
effect that acquisitions we may pursue have on our capital requirements;  
our ability to retain or attract senior management and key technical employees; and  
success of strategic plans, expectations and objectives for our future operations.

Further, we urge you to carefully review and consider the cautionary statements and disclosures, specifically those under the heading "*Risk Factors*," made in this Quarterly Report on Form 10-Q, our Annual Report on Form 10-K for the year ended December 31, 2018 filed with the U.S. Securities and Exchange Commission ("SEC") on February 28, 2019 (the "2018 Form 10-K") and our other filings with the SEC for further information on risks and uncertainties that could affect our business, financial condition, results of operations and prospects, which are incorporated by this reference as though fully set forth herein. We caution you not to place undue reliance on the forward-looking statements, which speak only as of the date of this report. **We undertake no obligation to update any forward-looking statements in order to reflect any event or circumstance occurring after the date of this report or currently unknown facts or conditions or the occurrence of unanticipated events. All forward-looking statements are qualified in their entirety by this cautionary statement.**

## REFERENCES

Unless the context otherwise requires, references in this report to "PDC Energy," "PDC," "the Company," "we," "us," "our" or "ours" refer to the registrant, PDC Energy, Inc. and all subsidiaries consolidated for the purposes of its financial statements, including our proportionate share of the financial position, results of operations, cash flows and operating activities of our affiliated partnerships.

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Table of contents**PART I - FINANCIAL INFORMATION****ITEM 1. FINANCIAL STATEMENTS****PDC ENERGY, INC.****Condensed Consolidated Balance Sheets***(unaudited; in thousands, except share and per share data)*

	<b>March 31, 2019</b>	<b>December 31, 2018</b>
<b>Assets</b>		
Current assets:		
Cash and cash equivalents	\$ 1,112	\$ 1,398
Accounts receivable, net	190,844	181,434
Fair value of derivatives	13,330	84,492
Prepaid expenses and other current assets	7,870	7,136
Total current assets	213,156	274,460
Properties and equipment, net	4,121,649	4,002,862
Assets held-for-sale, net	152,847	140,705
Fair value of derivatives	24,225	93,722
Other assets	52,051	32,396
<b>Total Assets</b>	<b>\$4,563,928</b>	<b>\$ 4,544,145</b>
<b>Liabilities and Stockholders' Equity</b>		
Liabilities		
Current liabilities:		
Accounts payable	\$ 215,555	\$ 181,864
Production tax liability	55,430	60,719
Fair value of derivatives	43,899	3,364
Funds held for distribution	91,615	105,784
Accrued interest payable	15,194	14,150
Other accrued expenses	68,836	75,133
Total current liabilities	490,529	441,014
Long-term debt	1,289,046	1,194,876
Deferred income taxes	160,609	198,096
Asset retirement obligations	82,497	85,312
Liabilities held-for-sale	4,614	4,111
Fair value of derivatives	1,815	1,364
Other liabilities	125,063	92,664
Total liabilities	2,154,173	2,017,437
Commitments and contingent liabilities		
Stockholders' equity		
Common shares - par value \$0.01 per share, 150,000,000 authorized, 66,196,863 and 66,148,609 issued as of March 31, 2019 and December 31, 2018, respectively	662	661
Additional paid-in capital	2,521,558	2,519,423
Retained earnings (deficit)	(111,449 )	8,727
Treasury shares - at cost, 22,635 and 45,220 as of March 31, 2019 and December 31, 2018, respectively	(1,016 )	(2,103 )

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Total stockholders' equity	2,409,755	2,526,708
<b>Total Liabilities and Stockholders' Equity</b>	<b>\$4,563,928</b>	<b>\$ 4,544,145</b>

*See accompanying Notes to Condensed Consolidated Financial Statements*

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Table of contents**PDC ENERGY, INC.****Condensed Consolidated Statements of Operations***(unaudited; in thousands, except per share data)*

	<b>Three Months Ended March 31,</b>	
	<b>2019</b>	<b>2018</b>
<b>Revenues</b>		
Crude oil, natural gas and NGLs sales	\$321,099	\$305,225
Commodity price risk management loss, net	(190,074 )	(47,240 )
Other income	3,475	2,615
Total revenues	134,500	260,600
<b>Costs, expenses and other</b>		
Lease operating expenses	35,221	29,636
Production taxes	22,168	20,169
Transportation, gathering and processing expenses	11,424	7,313
Exploration, geologic and geophysical expense	2,643	2,646
Impairment of properties and equipment	7,875	33,188
General and administrative expense	39,598	35,696
Depreciation, depletion and amortization	151,422	126,788
Accretion of asset retirement obligations	1,584	1,288
(Gain) loss on sale of properties and equipment	(369 )	1,432
Other expenses	3,554	2,768
Total costs, expenses and other	275,120	260,924
<b>Loss from operations</b>	<b>(140,620 )</b>	<b>(324 )</b>
Interest expense	(16,978 )	(17,529 )
Interest income	10	148
<b>Loss before income taxes</b>	<b>(157,588 )</b>	<b>(17,705 )</b>
Income tax benefit	37,412	4,566
<b>Net loss</b>	<b>\$(120,176 )</b>	<b>\$(13,139 )</b>
<b>Earnings per share:</b>		
Basic	\$(1.82 )	\$(0.20 )
Diluted	\$(1.82 )	\$(0.20 )
<b>Weighted-average common shares outstanding:</b>		
Basic	66,182	65,957
Diluted	66,182	65,957

See accompanying Notes to Condensed Consolidated Financial Statements

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**PDC ENERGY, INC.**  
**Condensed Consolidated Statements of Cash Flows**  
*(unaudited; in thousands)*

	<b>Three Months Ended March 31,</b>	
	<b>2019</b>	<b>2018</b>
<b>Cash flows from operating activities:</b>		
Net loss	\$(120,176 )	\$(13,139 )
Adjustments to net loss to reconcile to net cash from operating activities:		
Net change in fair value of unsettled commodity derivatives	181,622	21,202
Depreciation, depletion and amortization	151,422	126,788
Impairment of properties and equipment	7,875	33,188
Accretion of asset retirement obligations	1,584	1,288
Non-cash stock-based compensation	4,683	5,261
(Gain) loss on sale of properties and equipment	(369 )	1,432
Amortization of debt discount and issuance costs	3,349	3,246
Deferred income taxes	(37,487 )	(4,809 )
Other	21	515
Changes in assets and liabilities	(10,671 )	30,177
Net cash from operating activities	181,853	205,149
<b>Cash flows from investing activities:</b>		
Capital expenditures for development of crude oil and natural gas properties	(266,940 )	(196,917 )
Capital expenditures for other properties and equipment	(4,826 )	(1,066 )
Acquisition of crude oil and natural gas properties	—	(180,825 )
Proceeds from sale of properties and equipment	102	20
Proceeds from divestiture	—	39,023
Restricted cash	—	1,249
Net cash from investing activities	(271,664 )	(338,516 )
<b>Cash flows from financing activities:</b>		
Proceeds from revolving credit facility	432,000	35,000
Repayment of revolving credit facility	(340,500 )	(35,000 )
Purchase of treasury stock	(1,460 )	(2,255 )
Other	(515 )	(379 )
Net cash from financing activities	89,525	(2,634 )
<b>Net change in cash, cash equivalents and restricted cash</b>	<b>(286 )</b>	<b>(136,001 )</b>
<b>Cash, cash equivalents and restricted cash, beginning of period</b>	<b>9,399</b>	<b>189,925</b>
<b>Cash, cash equivalents and restricted cash, end of period</b>	<b>\$9,113</b>	<b>\$53,924</b>

*See accompanying Notes to Condensed Consolidated Financial Statements*

Table of contents**PDC ENERGY, INC.****Condensed Consolidated Statement of Equity***(unaudited; in thousands, except share data)*

	<b>Three Months Ended March 31, 2019</b>						
	<b>Common Stock</b>			<b>Treasury Stock</b>		<b>Retained Earnings (Deficit)</b>	<b>Total Stockholders' Equity</b>
	<b>Shares</b>	<b>Amount</b>	<b>Additional Paid-in Capital</b>	<b>Shares</b>	<b>Amount</b>		
<b>Balance, December 31, 2018</b>	66,148,609	\$ 661	\$2,519,423	(45,220 )	\$(2,103 )	\$8,727	\$ 2,526,708
Net loss	—	—	—	—	—	(120,176 )	(120,176 )
Purchase of treasury shares	—	—	—	(41,787 )	(1,460 )	—	(1,460 )
Issuance of treasury shares	(64,372 )	1	(1 )	64,372	—	—	—
Non-employee directors' deferred compensation plan	—	—	—	—	—	—	—
Issuance of stock awards, net of forfeitures	112,626	—	(2,547 )	—	2,547	—	—
Stock-based compensation expense	—	—	4,683	—	—	—	4,683
Other	—	—	—	—	—	—	—
<b>Balance, March 31, 2019</b>	66,196,863	\$ 662	\$2,521,558	(22,635 )	\$(1,016 )	\$(111,449 )	\$ 2,409,755

	<b>Three Months Ended March 31, 2018</b>						
	<b>Common Stock</b>			<b>Treasury Stock</b>		<b>Retained Earnings (Deficit)</b>	<b>Total Stockholders' Equity</b>
	<b>Shares</b>	<b>Amount</b>	<b>Additional Paid-in Capital</b>	<b>Shares</b>	<b>Amount</b>		
<b>Balance, December 31, 2017</b>	65,955,080	\$ 659	\$2,503,294	(55,927 )	\$(3,008 )	\$6,704	\$ 2,507,649
Net loss	—	—	—	—	—	(13,139 )	(13,139 )
Purchase of treasury shares	—	—	—	(41,357 )	(2,255 )	—	(2,255 )
Issuance of treasury shares	—	—	(3,891 )	70,603	3,891	—	—
Non-employee directors' deferred compensation plan	—	—	—	(2,574 )	(142 )	—	(142 )
Issuance of stock awards, net of forfeitures	43,930	1	(1 )	—	—	—	—
Stock-based compensation expense	—	—	5,261	—	—	—	5,261
<b>Balance, March 31, 2018</b>	65,999,010	\$ 660	\$2,504,663	(29,255 )	\$(1,514 )	\$(6,435 )	\$ 2,497,374

See accompanying Notes to Condensed Consolidated Financial Statements

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**PDC ENERGY, INC.**

**NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**

**March 31, 2019**

*(unaudited)*

**NOTE 1 - NATURE OF OPERATIONS AND BASIS OF PRESENTATION**

PDC Energy, Inc. is a domestic independent exploration and production company that acquires, explores and develops properties for the production of crude oil, natural gas and NGLs, with operations in the Wattenberg Field in Colorado and the Delaware Basin in Texas. Our operations in the Wattenberg Field are focused in the rural areas of the horizontal Niobrara and Codell plays and our Delaware Basin operations are primarily focused in the Wolfcamp zones. We previously operated properties in the Utica Shale in Southeastern Ohio; however, we divested these properties during the first quarter of 2018. As of March 31, 2019, we owned an interest in approximately 2,800 gross productive wells. We are engaged in two operating segments: our oil and gas exploration and production segment and our gas marketing segment. Our gas marketing segment does not meet the quantitative thresholds to require disclosure as a separate reportable segment. All of our material operations are attributable to our exploration and production business; therefore, all of our operations are presented as a single segment for all periods presented.

In 2018, we began the process of actively marketing our Delaware Basin crude oil gathering, natural gas gathering and produced water gathering and disposal assets for sale. In the second quarter of 2019, we entered into definitive agreements to divest the natural gas gathering and produced water gathering and disposal assets. These transactions are expected to close in mid-2019. We are also in the final stages of negotiations regarding the sale of our crude oil gathering assets.

The accompanying unaudited condensed consolidated financial statements include the accounts of PDC, our wholly-owned subsidiaries and our proportionate share of our affiliated partnerships. Pursuant to the proportionate consolidation method, our accompanying condensed consolidated financial statements include our pro rata share of assets, liabilities, revenues and expenses of the entities which we proportionately consolidate. All material intercompany accounts and transactions have been eliminated in consolidation.

In our opinion, the accompanying condensed consolidated financial statements contain all adjustments, consisting of normal recurring adjustments, necessary for a fair statement of our financial statements for interim periods in accordance with accounting principles generally accepted in the United States of America ("U.S. GAAP") and with the instructions to Form 10-Q and Article 10 of Regulation S-X of the SEC. Accordingly, pursuant to such rules and regulations, certain notes and other financial information included in audited financial statements have been condensed or omitted. The December 31, 2018 condensed consolidated balance sheet data was derived from audited statements, but does not include all disclosures required by U.S. GAAP. The information presented in this Quarterly Report on Form 10-Q should be read in conjunction with our audited consolidated financial statements and notes thereto included in our 2018 Form 10-K. Our results of operations and cash flows for the three months ended March 31, 2019 are not necessarily indicative of the results to be expected for the full year or any other future period.

**NOTE 2 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES**

*Cash, cash equivalents and restricted cash.* The following table provides a reconciliation of cash and cash equivalents and restricted cash reported on the condensed consolidated balance sheets at March 31, 2019 and 2018 and December 31, 2018 and 2017, which sum to the total of cash, cash equivalents and restricted cash in the consolidated statements of cash flows:

<b>March 31, 2019</b>	<b>December 31, 2018</b>	<b>March 31, 2018</b>	<b>December 31, 2017</b>
<i>(in thousands)</i>			



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Cash and cash equivalents	\$1,112	\$ 1,398	\$ 45,923	\$ 180,675
Restricted cash	8,001	8,001	8,001	9,250
Cash, cash equivalents and restricted cash shown in the consolidated statements of cash flows	\$9,113	\$ 9,399	\$ 53,924	\$ 189,925

Restricted cash is included in other assets on the condensed consolidated balance sheets.

**Recently Adopted Accounting Standards**

In February 2016, the FASB issued an accounting update and subsequent amendments aimed at increasing the transparency and comparability among organizations by recognizing lease assets and liabilities on the balance sheet and

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Table of contents**PDC ENERGY, INC.****NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS****March 31, 2019***(unaudited)*

disclosing key information about related leasing arrangements (the “New Lease Standard”). For leases with terms of more than 12 months, the accounting update requires lessees to recognize a right-of-use (“ROU”) asset and lease liability for its right to use the underlying asset and the corresponding lease obligation. As provided by practical expedients, we made accounting policy elections to not recognize ROU assets and lease liabilities that arise from short-term leases and to not separate lease and non-lease components for any class of underlying asset. The FASB issued an accounting update which provides an optional transition practical expedient for the adoption of the New Lease Standard that, if elected, permits an organization to not evaluate the accounting for existing land easements that are not accounted for under the previous lease accounting standard. We elected this practical expedient, and accordingly, existing land easements at December 31, 2018 were not assessed. All new or modified land easements entered into after January 1, 2019 will be evaluated under the New Lease Standard. The New Lease Standard does not apply to leases of mineral rights to explore for or use crude oil and natural gas. Adoption of the New Lease Standard resulted in increases to other assets of \$20.1 million, other accrued expenses of \$4.6 million and other liabilities of \$15.5 million at January 1, 2019, with no adjustment to the opening balance of retained earnings.

**NOTE 3 - REVENUE RECOGNITION**

Crude oil, natural gas and NGLs revenues are recognized when we have transferred control of crude oil, natural gas or NGLs production to the purchaser. We consider the transfer of control to have occurred when the purchaser has the ability to direct the use of, and obtain substantially all of the remaining benefits from, the crude oil, natural gas or NGLs production. We record sales revenue based on an estimate of the volumes delivered at estimated prices as determined by the applicable sales agreement. We estimate our sales volumes based on company-measured volume readings. We then adjust our crude oil, natural gas and NGLs sales in subsequent periods based on the data received from our purchasers that reflects actual volumes delivered and prices received. We receive payment for sales one to two months after actual delivery has occurred. The differences in sales estimates and actual sales are recorded one to two months later. Historically, these differences have not been material.

**Disaggregated Revenue.** The following table presents crude oil, natural gas and NGLs sales disaggregated by commodity and operating region for the three months ended March 31, 2019 and 2018 (in thousands):

Revenue by Commodity and Operating Region	Three Months Ended March 31,		Percent Change	
	2019	2018		
Crude oil				
Wattenberg Field	\$ 180,426	\$ 170,306	5.9	%
Delaware Basin	50,657	53,418	(5.2)	%
Utica Shale (1)	—	2,696	(100.0)	%
Total	\$ 231,083	\$ 226,420	2.1	%
Natural gas				
Wattenberg Field	\$ 46,701	\$ 29,772	56.9	%
Delaware Basin	5,770	7,679	(24.9)	%
Utica Shale (1)	—	1,110	(100.0)	%
Total	\$ 52,471	\$ 38,561	36.1	%
NGLs				
Wattenberg Field	\$ 27,722	\$ 28,770	(3.6)	%
Delaware Basin	9,823	10,635	(7.6)	%

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Utica Shale (1)	—	839	(100.0)%
Total	\$37,545	\$40,244	(6.7 )%
Revenue by Operating Region			
Wattenberg Field	\$254,849	\$228,848	11.4 %
Delaware Basin	66,250	71,732	(7.6 )%
Utica Shale (1)	—	4,645	(100.0)%
Total	\$321,099	\$305,225	5.2 %

(1) In March 2018, we completed the disposition of our Utica Shale properties.

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**PDC ENERGY, INC.**

**NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**

**March 31, 2019**

*(unaudited)*

## **NOTE 4 - FAIR VALUE OF FINANCIAL INSTRUMENTS**

### **Determination of Fair Value**

Our fair value measurements are estimated pursuant to a fair value hierarchy that requires us to maximize the use of observable inputs and minimize the use of unobservable inputs when measuring fair value. The valuation hierarchy is based upon the transparency of inputs to the valuation of an asset or liability as of the measurement date, giving the highest priority to quoted prices in active markets (Level 1) and the lowest priority to unobservable data (Level 3). In some cases, the inputs used to measure fair value might fall in different levels of the fair value hierarchy. The lowest level input that is significant to a fair value measurement in its entirety determines the applicable level in the fair value hierarchy. Assessing the significance of a particular input to the fair value measurement in its entirety requires judgment, considering factors specific to the asset or liability and may affect the valuation of the assets and liabilities and their placement within the fair value hierarchy levels. The three levels of inputs that may be used to measure fair value are defined as:

*Level 1* – Quoted prices (unadjusted) for identical assets or liabilities in active markets.

*Level 2* – Inputs other than quoted prices included within Level 1 that are either directly or indirectly observable for the asset or liability, including quoted prices for similar assets or liabilities in active markets, quoted prices for identical or similar assets or liabilities in inactive markets, inputs other than quoted prices that are observable for the asset or liability and inputs that are derived from observable market data by correlation or other means.

*Level 3* – Unobservable inputs for the asset or liability, including situations where there is little, if any, market activity.

### **Derivative Financial Instruments**

We measure the fair value of our derivative instruments based upon a pricing model that utilizes market-based inputs, including, but not limited to, the contractual price of the underlying position, current market prices, crude oil and natural gas forward curves, discount rates such as the LIBOR curve for a similar duration of each outstanding position, volatility factors and nonperformance risk. Nonperformance risk considers the effect of our credit standing on the fair value of derivative liabilities and the effect of our counterparties' credit standings on the fair value of derivative assets. Both inputs to the model are based on published credit default swap rates and the duration of each outstanding derivative position.

We validate our fair value measurement through the review of counterparty statements and other supporting documentation, determination that the source of the inputs is valid, corroboration of the original source of inputs through access to multiple quotes, if available, or other information and monitoring changes in valuation methods and assumptions.

Our crude oil and natural gas fixed-price swaps are included in Level 2. Our collars are included in Level 3. Our basis swaps are included in Level 2 and Level 3. The following table presents, for each applicable level within the fair value hierarchy, our derivative assets and liabilities, including both current and non-current portions, measured at fair value on a recurring basis:

**March 31, 2019**

**December 31, 2018**

**Total**

**Total**

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	<b>Significant Other Observable Inputs (Level 2)</b>	<b>Significant Unobservable Inputs (Level 3)</b>		<b>Significant Other Observable Inputs (Level 2)</b>	<b>Significant Unobservable Inputs (Level 3)</b>	
	<i>(in thousands)</i>					
Total assets	\$21,177	\$ 16,378	\$37,555	\$118,521	\$ 59,693	\$178,214
Total liabilities	(42,326 )	(3,388 )	(45,714 )	(3,364 )	(1,364 )	(4,728 )
Net asset (liability)	\$(21,149 )	\$ 12,990	\$(8,159 )	\$115,157	\$ 58,329	\$173,486

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The following table presents a reconciliation of our Level 3 assets measured at fair value:

	<b>Three Months Ended March 31,</b>	
	<b>2019</b>	<b>2018</b>
	<i>(in thousands)</i>	
Fair value of Level 3 instruments, net asset (liability) beginning of period	\$58,329	\$(9,687)
Changes in fair value included in condensed consolidated statement of operations line item:		
Commodity price risk management loss, net	(43,520 )	(2,152 )
Settlements included in condensed consolidated statement of operations line items:		
Commodity price risk management loss, net	(1,819 )	3,006
Fair value of Level 3 instruments, net liability end of period	\$12,990	\$(8,833)
Net change in fair value of Level 3 unsettled derivatives included in condensed consolidated statement of operations line item:		
Commodity price risk management loss, net	\$(38,680)	\$1,205

The significant unobservable input used in the fair value measurement of our derivative contracts is the implied volatility curve, which is provided by a third-party vendor. A significant increase or decrease in the implied volatility, in isolation, would have a directionally similar effect resulting in a significantly higher or lower fair value measurement of our Level 3 derivative contracts. There has been no change in the methodology we apply to measure the fair value of our Level 3 derivative contracts during the periods covered by the financial statements.

**Non-Derivative Financial Assets and Liabilities**

The carrying value of the financial instruments included in current assets and current liabilities approximate fair value due to the short-term maturities of these instruments.

We utilize fair value on a nonrecurring basis to review our proved crude oil and natural gas properties for possible impairment when events and circumstances indicate a possible decline in the recoverability of the carrying value of such assets. The fair value of the properties is determined based upon estimated future discounted cash flow, a Level 3 input, using estimated production and prices at which we reasonably expect the crude oil and natural gas will be sold. The portion of our long-term debt related to our revolving credit facility approximates fair value due to the variable nature of related interest rates. We have not elected to account for the portion of our debt related to our senior notes under the fair value option; however, we have determined an estimate of the fair values based on measurements of trading activity and broker and/or dealer quotes, respectively, which are published market prices, and therefore are Level 2 inputs. The table below presents these estimates of the fair value of the portion of our long-term debt related to our senior notes and convertible notes as of:

As of March 31, 2019	As of December 31, 2018
Estimated Fair Value Percent of Par	Estimated Fair Value Percent of Par
<i>(in millions)</i>	

**Senior notes:**

2021 Convertible Notes	\$ 188.1	94.1 %	\$ 175.4	87.7 %
2024 Senior Notes	398.9	99.7 %	370.2	92.5 %
2026 Senior Notes	583.7	97.3 %	532.4	88.7 %

### **Concentration of Risk**

*Derivative Counterparties.* A portion of our liquidity relates to commodity derivative instruments that enable us to manage a portion of our exposure to price volatility from producing crude oil and natural gas. These arrangements expose us to credit risk of nonperformance by our counterparties. We primarily use financial institutions who are also lenders under our

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revolving credit facility as counterparties to our commodity derivative contracts. To date, we have had no derivative counterparty default losses. We have evaluated the credit risk of our derivative assets from our counterparties using relevant credit market default rates, giving consideration to amounts outstanding for each counterparty and the duration of each outstanding derivative position. Based on our evaluation, we have determined that the potential impact of nonperformance of our current counterparties on the fair value of our derivative instruments is not significant at March 31, 2019.

*Cash and Cash Equivalents.* We consider all highly liquid instruments purchased with an original maturity of three months or less to be cash equivalents. Cash and cash equivalents potentially subject us to a concentration of credit risk as substantially all of our deposits held in financial institutions were in excess of the FDIC insurance limits at March 31, 2019 and December 31, 2018. We maintain our cash and cash equivalents in the form of money market and checking accounts with financial institutions that we believe are creditworthy and are also lenders under our revolving credit facility.

**NOTE 5 - COMMODITY DERIVATIVE FINANCIAL INSTRUMENTS**

Our results of operations and operating cash flows are affected by changes in market prices for crude oil, natural gas and NGLs. To manage a portion of our exposure to price volatility from producing crude oil and natural gas we enter into commodity derivative contracts to protect against price declines in future periods. While we structure these commodity derivatives to reduce our exposure to decreases in commodity prices, they also limit the benefit we might otherwise receive from price increases.

We believe our commodity derivative instruments continue to be effective in achieving the risk management objectives for which they were intended. As of March 31, 2019, we had derivative instruments, which were comprised of collars, fixed-price swaps and basis protection swaps, in place for a portion of our anticipated 2019, 2020 and 2021 production. Our commodity derivative contracts have been entered into at no upfront cost to us as we hedge our anticipated production at the then-prevailing commodity market prices, without adjustment for premium or discount.

As of March 31, 2019, we had the following outstanding derivative contracts. When aggregating multiple contracts, the weighted average contract price is disclosed.

Commodity/ Index/ Maturity Period	Collars			Fixed-Price Swaps		Fair Value March 31, 2019 (1) (in thousands)
	Quantity (Crude oil - MBls Natura Gas - BBtu)	Weighted-Average Contract Price Floors	Ceilings	Quantity (Crude Oil - MBbls Gas and Basis- BBtu )	Weighted- Average Contract Price	
<b>Crude Oil</b>						
<b>NYMEX</b>						
2019	2,050	\$ 56.22	\$ 67.77	6,150	\$ 54.25	\$(35,191 )
2020	3,600	55.00	71.68	5,600	61.55	27,831
2021	—	—	—	600	57.23	350
<b>Total Crude Oil</b>	<b>5,650</b>			<b>12,350</b>		<b>\$(7,010 )</b>



**Natural Gas****NYMEX**

2019	—	\$ —	\$ —	22,746	\$ 2.91	\$ 2,641
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**Dominion South**

2019	—	—	—	113	2.56	6
2020	—	—	—	14	2.54	—
<b>Total Natural Gas</b>	—			22,873		\$ 2,647

**Basis Protection - Natural Gas****CIG**

2019	—	\$ —	\$ —	22,683	\$ (0.76 )	\$ (3,796 )
<b>Total Basis Protection - Natural Gas</b>	—			22,683		\$ (3,796 )

**Commodity Derivatives Fair Value**

\$(8,159 )

(1) Approximately 43.6 percent of the fair value of our commodity derivative assets and 7.4 percent of the fair value of our commodity derivative liabilities were measured using significant unobservable inputs (Level 3).

We have not elected to designate any of our derivative instruments as cash flow hedges; therefore, these instruments do not qualify for hedge accounting. Accordingly, changes in the fair value of our derivative instruments are recorded in the condensed consolidated statements of operations.

The following table presents the balance sheet location and fair value amounts of our derivative instruments on the condensed consolidated balance sheets:

Derivative Instruments:	Condensed Consolidated Balance Sheet Line Item	Fair Value	
		March 31, 2019	December 31, 2018
		<i>(in thousands)</i>	
<b>Derivative assets:</b>			
Current			
Commodity derivative contracts	Fair value of derivatives	\$ 13,330	\$ 84,492
Non-current			
Commodity derivative contracts	Fair value of derivatives	24,225	93,722
<b>Total derivative assets</b>		\$ 37,555	\$ 178,214
<b>Derivative liabilities:</b>			
Current			
Commodity derivative contracts	Fair value of derivatives	\$ 40,103	\$ 748
Basis protection derivative contracts	Fair value of derivatives	3,796	2,616
		43,899	3,364
Non-current			
Commodity derivative contracts	Fair value of derivatives	1,815	1,364
<b>Total derivative liabilities</b>		\$ 45,714	\$ 4,728

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The following table presents the impact of our derivative instruments on our condensed consolidated statements of operations:

<b>Condensed Consolidated Statement of Operations Line Item</b>	<b>Three Months Ended</b>	
	<b>2019</b>	<b>2018</b>
	<i>(in thousands)</i>	
Commodity price risk management loss, net		
Net settlements	\$ (8,452 )	\$ (26,038 )
Net change in fair value of unsettled derivatives	(181,622 )	(21,202 )
Total commodity price risk management loss, net	\$ (190,074 )	\$ (47,240 )

Our financial derivative agreements contain master netting provisions that provide for the net settlement of contracts through a single payment in the event of early termination. We have elected not to offset the fair value positions recorded on our condensed consolidated balance sheets.

The following table reflects the impact of netting agreements on gross derivative assets and liabilities:

<b>As of March 31, 2019</b>	<b>Derivative Instruments, Gross</b>	<b>Effect of Master Netting Agreements</b>	<b>Derivative Instruments, Net</b>
	<i>(in thousands)</i>		
<b>Asset derivatives:</b>			
Derivative instruments, at fair value	\$ 37,555	\$ (27,793 )	\$ 9,762
<b>Liability derivatives:</b>			
Derivative instruments, at fair value	\$ 45,714	\$ (27,793 )	\$ 17,921

<b>As of December 31, 2018</b>	<b>Derivative Instruments, Gross</b>	<b>Effect of Master Netting Agreements</b>	<b>Derivative Instruments, Net</b>
	<i>(in thousands)</i>		
<b>Asset derivatives:</b>			
Derivative instruments, at fair value	\$ 178,214	\$ (3,985 )	\$ 174,229
<b>Liability derivatives:</b>			
Derivative instruments, at fair value	\$ 4,728	\$ (3,985 )	\$ 743

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The following table presents the components of properties and equipment, net of accumulated depreciation, depletion and amortization ("DD&A"):

	<b>March 31, 2019</b>	<b>December 31, 2018</b>
	<i>(in thousands)</i>	
<b>Properties and equipment, net:</b>		
Crude oil and natural gas properties		
Proved	\$5,681,685	\$5,452,613
Unproved	485,571	492,594
Total crude oil and natural gas properties	6,167,256	5,945,207
Infrastructure and other	59,510	60,612
Land and buildings	12,497	11,243
Construction in progress	404,229	356,095
Properties and equipment, at cost	6,643,492	6,373,157
Accumulated DD&A	(2,521,843 )	(2,370,295 )
Properties and equipment, net	\$4,121,649	\$4,002,862

*Classification of Assets and Liabilities as Held-for-Sale.* During the fourth quarter of 2018, as part of our plans to divest certain of our Delaware Basin crude oil gathering, natural gas gathering and produced water gathering and disposal assets, we began actively marketing the assets for sale; therefore, these assets are classified as held-for-sale as they met the criteria for such classification at March 31, 2019 and December 31, 2018. The planned disposition of our Delaware Basin crude oil gathering, natural gas gathering and produced water gathering and disposal assets does not represent a strategic shift in our operations or have a significant impact on our operations or financial results; therefore, we will not account for the disposition as a discontinued operation. Also included in assets held-for-sale are certain non-core Delaware Basin crude oil and natural gas properties.

The following table presents balance sheet data related to assets and liabilities held-for-sale:

	<b>March 31, 2019</b>	<b>December 31, 2018</b>
	<i>(in thousands)</i>	
<b>Assets</b>		
Properties and equipment, net	\$ 150,360	\$ 137,448
Other assets	2,487	3,257
Total assets	\$ 152,847	\$ 140,705
<b>Liabilities</b>		
Asset retirement obligation	\$4,614	\$ 4,111
Total liabilities	\$4,614	\$ 4,111

The following table presents impairment charges recorded for crude oil and natural gas properties:

**Three Months  
Ended March  
31,  
2019 2018**  
*(in thousands)*

Impairment of proved and unproved properties	\$7,875	\$33,130
Amortization of individually insignificant unproved properties	—	58
Impairment of crude oil and natural gas properties	\$7,875	\$33,188

During the three months ended March 31, 2019 and 2018, we recorded impairment charges totaling \$7.9 million and \$26.9 million, respectively, related to the divestiture of leaseholds and the then-current and anticipated near-term leasehold expirations within our non-focus areas of the Delaware Basin and made the determination that we would no longer pursue plans

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to develop these properties. We determined the fair value of the properties based upon estimated future discounted cash flow, a Level 3 input, using estimated production and prices at which we reasonably expect the crude oil and natural gas will be sold.

During the three months ended March 31, 2018, we also corrected an error in our calculation of the unproved properties and goodwill impairment originally reported in the quarter ended September 30, 2017. The correction of the error resulted in an additional impairment charge of \$6.3 million, recorded in the three months ended March 31, 2018, which we have included in the impairment of properties and equipment expense line in our condensed consolidated statement of operations. We evaluated the error under the guidance of Accounting Standards Codification 250, *Accounting Changes and Error Corrections* ("ASC 250"). Based on the guidance in ASC 250, we determined that the impact of the error did not have a material impact on our previously-issued financial statements or those of the period of correction.

*Suspended Well Costs.* The following table presents the capitalized exploratory well cost pending determination of proved reserves and included in properties and equipment, net on the condensed consolidated balance sheets:

	<b>March 31, 2019</b>	<b>December 31, 2018</b>
	<i>(in thousands, except for number of wells)</i>	
Beginning balance	\$ 12,188	\$ 15,448
Additions to capitalized exploratory well costs pending the determination of proved reserves	12,853	35,127
Reclassifications to proved properties	—	(38,387 )
Ending balance	\$ 25,041	\$ 12,188
Number of wells pending determination at period end	2	2

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**Other Accrued Expenses.** The following table presents the components of other accrued expenses as of:

	<b>March 31, 2019</b>	<b>December 31, 2018</b>
	<i>(in thousands)</i>	
Employee benefits	\$ 10,188	\$ 25,811
Asset retirement obligations	28,798	25,598
Environmental expenses	3,554	3,038
Operating and finance leases	6,645	—
Other	19,651	20,686
Other accrued expenses	\$ 68,836	\$ 75,133

**Other Liabilities.** The following table presents the components of other liabilities as of:

	<b>March 31, 2019</b>	<b>December 31, 2018</b>
	<i>(in thousands)</i>	
Production taxes	\$ 78,805	\$ 61,310
Deferred oil gathering credit	22,207	22,710
Operating and finance leases	20,063	—
Other	3,988	8,644
Other liabilities	\$ 125,063	\$ 92,664

**Deferred Oil Gathering Credit.** In January 2018, we received a payment from a midstream service provider for the execution of an amendment to an existing crude oil PSA signed in December 2017. The amendment was effective contingent upon certain events which occurred in late January 2018. The amendment, among other things, dedicates crude oil from the majority of our Wattenberg Field acreage to the midstream provider's gathering lines and extends the term of the agreement through December 2029. The payment is being amortized using the straight-line method over the life of the amendment. Amortization charges totaling approximately \$0.5 million and \$0.4 million for the three months ended March 31, 2019 and 2018, respectively, related to the deferred oil gathering credit are included as a reduction to transportation, gathering and processing expenses in our condensed consolidated statements of operations.

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Long-term debt consisted of the following as of:

	<b>March 31, 2019</b>	<b>December 31, 2018</b>
	<i>(in thousands)</i>	
<b>Senior Notes:</b>		
<b>1.125% Convertible Notes due September 2021:</b>		
Principal amount	\$ 200,000	\$ 200,000
Unamortized discount	(20,807)	(22,766)
Unamortized debt issuance costs	(2,397)	(2,640)
Net of unamortized discount and debt issuance costs	176,796	174,594
<b>6.125% Senior Notes due September 2024:</b>		
Principal amount	400,000	400,000
Unamortized debt issuance costs	(5,346)	(5,590)
Net of unamortized debt issuance costs	394,654	394,410
<b>5.75% Senior Notes due May 2026:</b>		
Principal amount	600,000	600,000
Unamortized debt issuance costs	(6,404)	(6,628)
Net of unamortized debt issuance costs	593,596	593,372
Total senior notes	1,165,046	1,162,376
<b>Revolving Credit Facility:</b>		
Revolving credit facility due May 2023	124,000	32,500
Total long-term debt, net of unamortized discount and debt issuance costs	\$ 1,289,046	\$ 1,194,876

**Senior Notes**

*2021 Convertible Notes.* In September 2016, we issued \$200 million of 1.125% convertible notes due September 15, 2021 (the "2021 Convertible Notes"). Interest is payable in cash semi-annually on March 15 and September 15. The conversion price at maturity is \$85.39 per share. We allocated the gross proceeds of the 2021 Convertible Notes between the liability and equity components of the debt. The initial \$160.5 million liability component was determined based on the fair value of similar debt instruments, excluding the conversion feature, priced on the same day we issued the 2021 Convertible Notes. Approximately \$4.8 million in costs associated with the issuance of the 2021 Convertible Notes were capitalized as debt issuance costs. As of March 31, 2019, the unamortized debt discount will be amortized over the remaining contractual term to maturity of the 2021 Convertible Notes using the effective interest method.

Upon conversion, the 2021 Convertible Notes may be settled, at our sole election, in shares of our common stock, cash or a combination of cash and shares of our common stock. We have initially elected a combination settlement method to satisfy our conversion obligation, which allows us to settle the principal amount of the 2021 Convertible

Notes in cash and to settle the excess conversion value, if any, in shares of our common stock, with cash paid in lieu of fractional shares.

*2024 Senior Notes.* In September 2016, we issued \$400 million aggregate principal amount of 6.125% senior notes due September 15, 2024 (the "2024 Senior Notes"). The 2024 Senior Notes accrue interest from the date of issuance and interest is payable semi-annually on March 15 and September 15. Approximately \$7.8 million in costs associated with the issuance of the 2024 Senior Notes were capitalized as debt issuance costs and are being amortized as interest expense over the life of the notes using the effective interest method.

*2026 Senior Notes.* In November 2017, we issued \$600 million aggregate principal amount of 5.75% senior notes due May 15, 2026 (the "2026 Senior Notes"). The 2026 Senior Notes accrue interest from the date of issuance and interest is payable semi-annually on May 15 and November 15. Approximately \$7.6 million in costs associated with the issuance of the



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**PDC ENERGY, INC.**

**NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**

**March 31, 2019**

*(unaudited)*

2026 Senior Notes were capitalized as debt issuance costs and are being amortized as interest expense over the life of the notes using the effective interest method.

Our wholly-owned subsidiary PDC Permian, Inc. guarantees our obligations under the 2021 Convertible Notes, the 2026 Senior Notes and the 2024 Senior Notes (collectively, the "Notes"). Accordingly, condensed consolidating financial information for PDC and PDC Permian, Inc. is presented in the footnote titled *Subsidiary Guarantor*.

As of March 31, 2019, we were in compliance with all covenants related to the Notes.

### **Revolving Credit Facility**

In May 2018, we entered into a Fourth Amended and Restated Credit Agreement (the "Restated Credit Agreement"). Among other things, the Restated Credit Agreement provides for a maximum credit amount of \$2.5 billion and, as of March 31, 2019, a borrowing base of \$1.3 billion. The amount we may borrow under the Restated Credit Agreement is subject to certain limitations under our Notes.

The revolving credit facility is available for working capital requirements, capital investments, acquisitions, to support letters of credit and for general corporate purposes. The borrowing base is based on, among other things, the loan value assigned to the proved reserves attributable to our crude oil and natural gas interests. The borrowing base is subject to a semi-annual redetermination on November 1 and May 1 based upon quantification of our reserves at June 30 and December 31, and is also subject to a redetermination upon the occurrence of certain events. Substantially all of our crude oil and natural gas properties, excluding our share of properties held by the limited partnerships that we sponsor, have been mortgaged or pledged as security for our revolving credit facility.

The outstanding principal amount under the revolving credit facility accrues interest at a varying interest rate that fluctuates with an alternate base rate (equal to the greatest of the administrative agent's prime rate, the federal funds rate plus a premium and the rate for dollar deposits in the London interbank market ("LIBOR") for one month, plus a premium) or, at our election, a rate equal to LIBOR for certain time periods. Additionally, commitment fees, interest margin and other bank fees, charged as a component of interest, vary with our utilization of the facility. As of March 31, 2019, the applicable interest margin is 0.25 percent for the alternate base rate option or 1.25 percent for the LIBOR option, and the unused commitment fee is 0.375 percent. Principal payments are generally not required until the revolving credit facility expires in May 2023, unless the borrowing base falls below the outstanding balance.

The revolving credit facility contains covenants customary for agreements of this type, with the most restrictive being certain financial tests on a quarterly basis. The financial tests, as defined per the revolving credit facility, include requirements to: (a) maintain a minimum current ratio of 1.0:1.0 and (b) not exceed a maximum leverage ratio of 4.0:1.0. As of March 31, 2019, we were in compliance with all the revolving credit facility covenants.

As of March 31, 2019 and December 31, 2018, debt issuance costs related to our revolving credit facility were \$10.9 million and \$11.5 million, respectively, and are included in other assets on the condensed consolidated balance sheets. As of March 31, 2019, the weighted-average interest rate on the outstanding balance on our revolving credit facility, exclusive of fees on the unused commitment, was 4.5 percent.

### **NOTE 9 - LEASES**

On January 1, 2019, we adopted the New Lease Standard issued by the FASB. We determine if an arrangement is representative of a lease under the New Lease Standard at contract inception. ROU assets represent our right to use the underlying assets for the lease term and the corresponding lease liabilities represent our obligations to make lease payments arising from the leases. Operating and finance lease ROU assets and liabilities are recognized at the commencement date based on the present value of the expected lease payments over the lease term. As most of our leases do not provide an implicit interest rate, we utilize our incremental borrowing rate based on information available at the commencement date in determining the present value of lease payments. Subsequent measurement, as well as presentation of expenses and cash flows, will depend upon the classification of the lease as either a finance or operating lease. Terms of our leases include options to extend or terminate the lease only when we can ascertain that it is reasonably certain we will exercise that option.

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We have operating leases for office space and compressors and finance leases for vehicles. Our leases have remaining lease terms ranging from one to five years. The vehicle leases include options to renew for up to four years. Lease payments associated with vehicle leases also include a contractually stated residual value guarantee.

The following table presents the components of lease costs:

<b>Lease Costs</b>	<b>Three Months Ended March 31, 2019 (in thousands)</b>
Operating lease costs	\$ 1,348
Finance lease costs:	
Amortization of ROU assets	\$ 483
Interest on lease liabilities	60
Total finance lease costs	543
Short-term lease costs	61,030
Total lease costs	\$ 62,921

Our operating lease costs are recorded in lease operating expenses or general and administrative expense and our finance lease costs are recorded in DD&A expense and interest expense on our condensed consolidated statements of operations. Our short-term lease costs include amounts that are capitalized as part of the cost of another asset and are recorded as properties and equipment in our condensed consolidated balance sheets or amounts recognized as expense in our condensed consolidated statements of operations.

The following table presents leases and the balance sheet classification as of:

<b>Leases</b>	<b>Condensed Consolidated Balance Sheet Line Item</b>	<b>March 31, 2019 (in thousands)</b>
Operating Leases:		
Operating lease ROU assets	Other assets	\$ 19,535
Operating lease obligation - short-term	Other accrued expense	\$ 4,958
Operating lease obligation - long-term	Other liabilities	17,055
Total operating lease liabilities		\$ 22,013
Finance Leases:		
Finance lease ROU assets	Properties and equipment, net	\$ 4,748
Finance lease obligation - short-term	Other accrued expense	\$ 1,687
Finance lease obligation - long-term	Other liabilities	3,008
Total finance lease liabilities		\$ 4,695
Weighted-average remaining lease term (years)		
Operating leases		3.22

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Finance leases	4.53	
Weighted-average discount rate		
Operating leases	5.0	%
Finance leases	5.0	%

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Maturity of lease liabilities by year and in the aggregate, under operating and financing leases with terms of one year or more, consist of the following:

	<b>Operating</b>	<b>Finance</b>	<b>Total</b>
	<b>Leases</b>	<b>Leases</b>	
	<i>(in thousands)</i>		
2019	\$4,378	\$1,431	\$5,809
2020	5,910	1,716	7,626
2021	5,782	1,101	6,883
2022	4,851	528	5,379
2023	1,394	321	1,715
Thereafter	2,291	6	2,297
Total lease payments	24,606	5,103	29,709
Less interest and discount	(2,593 )	(408 )	(3,001 )
Present value of lease liabilities	\$22,013	\$4,695	\$26,708

**NOTE 10 - ASSET RETIREMENT OBLIGATIONS**

The following table presents the changes in carrying amounts of the asset retirement obligations associated with our working interests in crude oil and natural gas properties:

	<b>Amount</b>
	<i>(in thousands)</i>
Balance at December 31, 2018	\$ 115,021
Obligations incurred with development activities	2,807
Accretion expense	1,584
Revisions in estimated cash flows	3,200
Obligations discharged with asset retirements and divestiture	(6,703 )
Balance at March 31, 2019	115,909
Liabilities held-for-sale	(4,614 )
Current portion	(28,798 )
Long-term portion	\$ 82,497

Our estimated asset retirement obligations liability is based on historical experience in plugging and abandoning wells, estimated economic lives and estimated plugging, abandonment and surface reclamation costs considering federal and state regulatory requirements in effect at that time. The liability is discounted using the credit-adjusted risk-free rate estimated at the time the liability is incurred or revised. To the extent future revisions to these assumptions impact the present value of the existing asset retirement obligations liability, a corresponding adjustment is made to the properties and equipment balance. Changes in the liability due to the passage of time are recognized as an increase in the carrying amount of the liability and as accretion expense. Short-term asset retirement obligations are included in other accrued expenses on the condensed consolidated balance sheets.

**NOTE 11 - COMMITMENTS AND CONTINGENCIES**

**Firm Transportation and Processing Agreements.** We enter into contracts that provide firm transportation and processing on pipeline systems through which we transport or sell crude oil and natural gas. Satisfaction of the volume requirements includes volumes produced by us, purchased from third parties and produced by our affiliated partnerships and other third-party working, royalty and overriding royalty interest owners whose volumes we market on their behalf. Our condensed consolidated statements of operations reflect our share of these firm transportation and processing costs. These contracts require us to pay these transportation and processing charges whether or not the required volumes are delivered.

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The following table presents gross volume information related to our long-term firm transportation, sales and processing agreements for pipeline capacity and water delivery and disposal commitments:

Area	For the Twelve Months Ending March 31,					Total	Expiration Date
	2020	2021	2022	2023	2024 and Through Expiration		
Natural gas (MMcf)							
Wattenberg Field	26,772	31,025	31,025	31,025	85,290	205,137	April 30, 2026
Delaware Basin	47,150	33,410	16,097	—	—	96,657	December 31, 2021
Gas Marketing	7,136	7,117	6,966	2,830	—	24,049	August 31, 2022
Total	81,058	71,552	54,088	33,855	85,290	325,843	
Crude oil (MBbls)							
Wattenberg Field	9,740	6,227	5,475	5,475	450	27,367	April 30, 2023
Delaware Basin	8,227	8,580	8,030	8,030	6,050	38,917	December 31, 2023
Total	17,967	14,807	13,505	13,505	6,500	66,284	
Water (MBbls)							
Wattenberg Field	3,886	6,207	6,207	6,206	10,899	33,405	December 31, 2024
Delaware Basin	3,660	3,650	3,650	3,650	870	15,480	June 26, 2023
Total	7,546	9,857	9,857	9,856	11,769	48,885	
Dollar commitment (in thousands)	\$ 104,504	\$ 80,633	\$ 73,851	\$ 68,882	\$ 94,836	\$ 422,706	

*Wattenberg Field.* We have entered into two facilities expansion agreements with our primary midstream provider to expand and improve its natural gas gathering pipelines and processing facilities. The midstream provider completed and turned on line the first of the two 200 MMcfd cryogenic plants in August 2018. The second plant is currently scheduled to be completed by the end of the second quarter of 2019. We are bound to the volume requirements in these agreements on the first day of the calendar month following the actual in-service date of the relevant plant. Both agreements require baseline volume commitments, consisting of our gross wellhead volume delivered in November 2016 to this midstream provider, and incremental wellhead volume commitments of 51.5 MMcfd and 33.5 MMcfd for the first and second agreements, respectively, for seven years. We may be required to pay shortfall fees for any volumes under the 51.5 MMcfd and 33.5 MMcfd incremental commitments. Any shortfall in these volume commitments may be offset by other producers' volumes sold to the midstream provider that are greater than a certain total baseline volume. We are also required for the first three years of the contracts to guarantee a certain target profit margin to the midstream provider on these incremental volumes. Payments made to date for such quantities have not been significant.

*Delaware Basin.* In May 2018, we entered into a firm sales agreement that is effective from June 2018 through December 2023 with an integrated marketing company for our crude oil production in the Delaware Basin. Contracted volumes are currently 17,200 barrels of crude oil per day and increase over time to 26,400 barrels of crude oil per day. These agreements are expected to provide price diversification through realization of export market pricing via a

Corpus Christi terminal and exposure to Brent-weighted prices.

*Crude Oil, Natural Gas and NGLs Sales.* For the three months ended March 31, 2019 and 2018, amounts related to long-term transportation volumes in the table above were \$10.9 million and \$2.6 million, respectively, and were netted against our crude oil and natural gas sales in our condensed consolidated statements of operations.

**Litigation and Legal Items.** We are involved in various legal proceedings. We review the status of these proceedings on an ongoing basis and, from time to time, may settle or otherwise resolve these matters on terms and conditions that management believes are in our best interests. We have provided the necessary estimated accruals in the accompanying balance sheets where deemed appropriate for litigation and legal related items that are ongoing and not yet concluded. Although the results cannot be known with certainty, we currently believe that the ultimate results of such proceedings will not have a



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material adverse effect on our financial position, results of operations or liquidity.

*Action Regarding Partnerships.* In December 2017, we received an action entitled *Dufresne, et al. v. PDC Energy, et al.*, filed in the United States District Court for the District of Colorado (the "Dufresne Case"). The original complaint stated that it was a derivative action brought by a number of limited partner investors seeking to assert claims on behalf of our two affiliated partnerships, Rockies Region 2006 LP and Rockies Region 2007 LP (collectively, the "Partnerships"), against PDC and includes claims for breach of fiduciary duty and breach of contract. The plaintiffs also included claims against two of our senior officers and three independent members of our Board of Directors for allegedly aiding and abetting PDC's breach of fiduciary duty. The lawsuit accuses PDC, as the managing general partner of the Partnerships, of, among other things, failing to maximize the productivity of the Partnerships' crude oil and natural gas wells and improperly assigning the Partnerships only interests in the wells, as opposed to leasehold interests in surrounding acreage. In late April 2018, the plaintiffs filed an amendment to their complaint, which alleges additional facts and purports to add direct class action claims in addition to the original derivative claims. We filed a motion to dismiss this amended complaint and the claims against the individuals named as defendants on July 31, 2018. On February 19, 2019, the court granted the motion to dismiss, in part. It dismissed all claims against the individuals named as defendants. It also held that that the plaintiffs were time-barred from using the failure to assign acreage assignments to support their claims for breach of fiduciary duty against PDC. We filed an answer to the remaining claims on March 5, 2019. We understand that this action is stayed as a result of the partnership bankruptcy proceedings described in *Partnership Bankruptcy Filings* below. We are currently unable to estimate any potential damages resulting from this lawsuit.

*Partnership Bankruptcy Filings.* On October 30, 2018, the Partnerships filed petitions under Chapter 11 of the Bankruptcy Code (the "Chapter 11 Proceedings") in the United States Bankruptcy Court for the Northern District of Texas, Dallas Division (the "Bankruptcy Court"). The Partnerships intend to enter into a transaction with us, pursuant to which they will sell substantially all of their assets to us through a Chapter 11 plan of liquidation (the "Chapter 11 Plan") and provide a release of any claims, including those asserted in the Dufresne Case. The Partnerships remain in possession of their assets and continue to operate their businesses as debtors-in-possession under the jurisdiction of the Bankruptcy Court and in accordance with the applicable provisions of the Bankruptcy Code and the orders of the Bankruptcy Court. In addition, a third-party (the "Responsible Party") has been designated for the Partnerships. The Responsible Party is expected to oversee all actions for the Partnerships in connection with the Chapter 11 Proceedings, including actions relating to the anticipated transactions with us and seeking approval of the Chapter 11 Plan. In late November and early December 2018, the plaintiffs in the Dufresne Case filed several pleadings in the Bankruptcy Court, including one to dismiss the bankruptcy on grounds that PDC had no authority to hire the Responsible Party, the Responsible Party had no authority to cause the Partnerships to file bankruptcy, and the bankruptcy was filed solely for the purpose of gaining a litigation advantage in the Dufresne Case. The plaintiffs in the Dufresne Case also objected to the retention of the Responsible Party. PDC, the Partnerships and the plaintiffs in the Dufresne Case agreed to mediate their disputes. As a result, on December 17, 2018 the Bankruptcy Court entered an agreed order staying the bankruptcy motions and abating the Dufresne Case to allow the parties to mediate their disputes. The mediation was conducted in late February 2019, but the parties did not reach a settlement. As a result, on March 21, 2019, the Bankruptcy Court entered an agreed scheduling order with respect to the motion to dismiss and objection to the retention of the Responsible Party, with a hearing scheduled for June 2019. We do not believe that the Partnership's Chapter 11 Proceedings will have a material adverse effect on our financial position, results of operations or liquidity, but we cannot predict the outcome of such proceedings.

*Environmental.* Due to the nature of the natural gas and oil industry, we are exposed to environmental risks. We have various policies and procedures to minimize and mitigate the risks from environmental contamination. We conduct periodic reviews and simulated drills to identify changes in our environmental risk profile. Liabilities are recorded when environmental damages resulting from past events are probable and the costs can be reasonably estimated. Except as discussed herein, we are not aware of any material environmental claims existing as of March 31, 2019 which have not been provided for or would otherwise have a material impact on our financial statements; however, there can be no assurance that current regulatory requirements will not change or that unknown potential past non-compliance with environmental laws or other environmental liabilities will not be discovered on our properties. Accrued environmental liabilities are recorded in other accrued expenses on the condensed consolidated balance sheets. The liability ultimately incurred with respect to a matter may exceed the related accrual.

*Clean Air Act Agreement and Related Consent Decree.* In June 2017, following our receipt of a 2015 Clean Air Act information request from the Environmental Protection Agency ("EPA") and a 2015 compliance advisory from the Colorado Department of Public Health and Environment's ("CDPHE") Air Pollution Control Division, the U.S. Department of Justice, on

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behalf of the EPA and the state of Colorado, filed a complaint against us in the U.S. District Court for the District of Colorado, claiming that we failed to operate and maintain certain condensate collection facilities at 65 facilities so as to minimize leakage of volatile organic compounds in compliance with applicable law.

In October 2017, we entered into a consent decree to resolve the lawsuit and the compliance advisory. Pursuant to the consent decree, we agreed to implement a variety of operational enhancements and mitigation and similar projects, including vapor control system modifications and verification, increased inspection and monitoring and installation of tank pressure monitors. The three primary elements of the consent decree are: (i) fine/supplemental environmental projects (\$1.5 million cash fine, plus \$1 million in supplemental environmental projects) of which the cash fines and the full cost of supplemental environmental projects were paid in the first and third quarters of 2018, respectively, (ii) injunctive relief with an estimated cost of approximately \$18 million, primarily representing capital enhancements to our operations and (iii) mitigation with an estimated cost of \$1.7 million. We continue to incur costs associated with these activities. If we fail to comply fully with the requirements of the consent decree with respect to those matters, we could be subject to additional liability. We do not believe that the expenditures resulting from the settlement will have a material adverse effect on our consolidated financial statements.

We are in the process of implementing the consent decree program. Over the course of its execution, we have identified certain immaterial deficiencies in our implementation of the program. We report these immaterial deficiencies to the appropriate authorities and remediate them promptly. We do not believe that the penalties and expenditures associated with the consent decree, including any sanctions associated with these deficiencies, will have a material effect on our financial condition or results of operations, but they may exceed \$100,000.

In addition, in December 2018, we were named as a nominal defendant in a derivative action filed in the Delaware chancery court. The complaint, which seeks unspecified monetary damages and various forms of equitable relief, alleges that certain current and former members of our Board of Directors violated their fiduciary duties, committed waste and were unjustly enriched by, among other things, failing to implement adequate environmental safeguards in connection with the issues that gave rise to the Department of Justice lawsuit and consent decree. We believe that this lawsuit is without merit but cannot predict its outcome.

Further, we could be the subject of other enforcement actions by regulatory authorities in the future relating to our past, present or future operations.

## **NOTE 12 - COMMON STOCK**

### **Stock-Based Compensation Plans**

*2018 Equity Incentive Plan.* In May 2018, our stockholders approved a long-term equity compensation plan for our employees and non-employee directors (the "2018 Plan"). The 2018 Plan provides for a reserve of 1,800,000 shares of our common stock that may be issued pursuant to awards under the 2018 Plan and a term that expires in March 2028. Shares issued may be either authorized but unissued shares, treasury shares or any combination. Additionally, the 2018 Plan permits the reuse or reissuance of shares of common stock which were canceled, expired, forfeited or paid out in the form of cash. However, shares tendered or withheld to satisfy the exercise price of options or tax withholding obligations, and shares covering the portion of exercised stock-settled stock appreciation rights ("SARs") (regardless of the number of shares actually delivered), count against the share limit. Awards may be issued in the form of options, SARs, restricted stock, restricted stock units ("RSUs"), performance stock units ("PSUs") and other

stock-based awards. Awards may vest over periods of continued service or the satisfaction of performance conditions set at the discretion of the Compensation Committee of our Board of Directors (the "Compensation Committee"), with a minimum one-year vesting period applicable to most awards. With regard to SARs and options, awards have a maximum exercisable period of ten years. We began issuing shares from the 2018 Plan during the three months ended March 31, 2019. As of March 31, 2019, there were 1,772,088 shares available for grant under the 2018 plan.

*2010 Long-Term Equity Compensation Plan.* Our Amended and Restated 2010 Long-Term Equity Compensation Plan, which was most recently approved by stockholders in 2013 (as the same has been amended and restated from time to time, the "2010 Plan"), remains outstanding and we may continue to use the 2010 Plan to grant awards. As of March 31, 2019, there were 37,703 shares available for grant under the 2010 Plan.

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The following table provides a summary of the impact of our outstanding stock-based compensation plans on the results of operations for the periods presented:

	<b>Three Months Ended March 31, 2019    2018</b>	
	<i>(in thousands)</i>	
Stock-based compensation expense	\$4,683	\$5,261
Income tax benefit	(1,120 )	(1,261 )
Stock-based compensation expense, net of tax	\$3,563	\$4,000

Restricted Stock Units

*Time-Based Awards.* The fair value of the time-based RSUs is amortized ratably over the requisite service period, primarily three years. The time-based RSUs generally vest ratably on each anniversary following the grant date provided that a participant is continuously employed.

The following table presents the changes in non-vested time-based RSUs to all employees, including executive officers, for the three months ended March 31, 2019:

	<b>Shares</b>	<b>Weighted-Average Grant Date Fair Value per Share</b>
Non-vested at December 31, 2018	618,407	\$ 54.16
Granted	189,137	38.59
Vested	(93,685 )	54.64
Forfeited	(12,186 )	48.38
Non-vested at March 31, 2019	701,673	50.00

The following table presents the weighted-average grant date fair value per share and related information as of/for the periods presented:

	<b>Three Months Ended March 31, 2019    2018</b>	
	<i>(in thousands, except per share data)</i>	
Total intrinsic value of time-based awards vested	\$3,311	\$3,530
Total intrinsic value of time-based awards non-vested	28,544	26,297
Market price per share as of March 31	40.68	49.03

Weighted-average grant date fair value per share      38.59   50.94

Total compensation cost related to non-vested time-based awards and not yet recognized in our condensed consolidated statements of operations as of March 31, 2019 was \$23.8 million. This cost is expected to be recognized over a weighted-average period of 1.9 years.

Performance Stock Units

*Market-Based Awards.* The fair value of the market-based PSUs is amortized ratably over the requisite service period, primarily three years. The market-based shares vest if the participant is continuously employed throughout the performance period and the market-based performance measure is achieved, with a maximum vesting period of three years. All compensation cost related to the market-based awards will be recognized if the requisite service period is fulfilled, even if the market condition is not achieved.

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The Compensation Committee awarded a total of 139,197 market-based PSUs to our executive officers during the three months ended March 31, 2019. In addition to continuous employment, the vesting of these PSUs is contingent on our total stockholder return ("TSR"), which is essentially our stock price change including any dividends over a three-year period ending on December 31, 2021, as compared to the TSR of a group of peer companies over the same period. The PSUs will result in a payout between zero and 200 percent of the target PSUs awarded. The weighted-average grant date fair value per PSU granted was computed using the Monte Carlo pricing model using the following assumptions:

	<b>Three Months Ended March 31, 2019</b>		<b>2018</b>	
Expected term of award (in years)	3		3	
Risk-free interest rate	2.5 %		2.4 %	
Expected volatility	41.4 %		42.3 %	

The expected term of the awards was based on the requisite service period. The risk-free interest rate was based on the U.S. Treasury yields in effect at the time of grant and extrapolated to approximate the life of the award. The expected volatility was based on our historical volatility.

The following table presents the change in non-vested market-based awards during the three months ended March 31, 2019:

	<b>Shares</b>	<b>Weighted-Average Grant Date Fair Value per Share</b>
Non-vested at December 31, 2018	102,914	\$ 74.88
Granted	139,197	56.68
Non-vested at March 31, 2019	242,111	64.42

The following table presents the weighted-average grant date fair value per share and related information as of/for the periods presented:

	<b>Three Months Ended March 31, 2019</b>		<b>2018</b>	
	<i>(in thousands, except per share data)</i>			
Total intrinsic value of market-based awards non-vested	\$9,849		\$6,815	
Market price per common share as of March 31,	40.68		49.03	
Weighted-average grant date fair value per share	56.68		69.98	

Total compensation cost related to non-vested market-based awards not yet recognized in our condensed consolidated statements of operations as of March 31, 2019 was \$11.6 million. This cost is expected to be recognized over a weighted-average period of 2.2 years.

Stock Appreciation Rights

The SARs vest ratably over a three-year period and may generally be exercised at any point after vesting through ten years from the date of issuance. Pursuant to the terms of the awards, upon exercise, the executive officers will receive, in shares of common stock, the excess of the market price of the award on the date of exercise over the market price of the award on the date of issuance. No SARs were awarded or expired during the three months ended March 31, 2019.

Total compensation cost related to non-vested SARs granted and not yet recognized in our condensed consolidated statements of operations as of March 31, 2019 was \$0.4 million. The cost is expected to be recognized over a weighted-average period of 0.8 years.



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## **Preferred Stock**

We are authorized to issue 50,000,000 shares of preferred stock, par value \$0.01 per share, which may be issued in one or more series, with such rights, preferences, privileges and restrictions as shall be fixed by our Board of Directors from time to time. Through March 31, 2019, no shares of preferred stock have been issued.

## **Stock Repurchase Program**

In April 2019, our Board of Directors approved a stock repurchase program (the “Program”) to acquire up to \$200 million of our outstanding common stock, depending on market conditions. The Program is expected to begin in the third quarter of 2019 with a target completion date of December 31, 2020. Repurchases under the Program can be made in open markets at our discretion and in compliance with safe harbor provisions, or in privately negotiated transactions. The Program does not require any specific number of shares to be acquired, and can be modified or discontinued by the Board of Directors at any time.

## **NOTE 13 - INCOME TAXES**

We compute our quarterly tax provision using the effective tax rate method by applying the anticipated annual effective rate to our year-to-date income or loss, except for discrete items. Income tax on discrete items is computed and recorded in the period in which the specific transaction occurs. Consequently, based upon the mix and timing of our actual annual earnings compared to annual projections, our effective tax rate may vary quarterly and may make quarterly comparisons not meaningful.

The effective income tax rates differ from the statutory federal tax rate, primarily due to state taxes, stock-based compensation, nondeductible officers’ compensation, nondeductible lobbying expenses, and federal tax credits. The effective income tax rate for the three months ended March 31, 2019 includes discrete income tax provision items of \$0.5 million relating to the tax detriment on stock-based compensation, which resulted in a 0.3 percent decrease to our effective income tax rate. We anticipate the potential for increased periodic volatility in future effective tax rates from the impact of stock-based compensation tax deductions as they are treated as discrete tax items.

The effective income tax rate for the three months ended March 31, 2019 was a 23.7 percent benefit on loss, compared to a 25.8 percent benefit on loss for the three months ended March 31, 2018.

As of March 31, 2019, there is no liability for unrecognized income tax benefits. As of the date of this report, we are current with our income tax filings in all applicable state jurisdictions and are not currently under any state income tax examinations. The IRS partially accepted our 2017 tax return. The 2017 tax return is in the IRS CAP Program post-filing review process, with no significant tax adjustments currently proposed. We are currently participating in the CAP Program for the review of our 2018 and 2019 tax years. Participation in the CAP Program has enabled us to have minimal uncertain tax benefits associated with our federal tax return filings.

## **NOTE 14 - EARNINGS PER SHARE**

Basic earnings per share is computed by dividing net earnings by the weighted-average number of common shares outstanding for the period. Diluted earnings per share is similarly computed, except that the denominator includes the

effect, using the treasury stock method, of unvested restricted stock, outstanding SARs, convertible notes and shares held pursuant to our non-employee director deferred compensation plan, if including such potential shares of common stock is dilutive.

The following table presents our weighted-average basic and diluted shares outstanding:

	<b>Three Months Ended March 31, 2019 2018</b>	
	<i>(in thousands)</i>	
Weighted-average common shares outstanding - basic	66,182	65,957
Weighted-average common shares and equivalents outstanding - diluted	66,182	65,957

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We reported a net loss for the three months ended March 31, 2019 and 2018. As a result, our basic and diluted weighted-average common shares outstanding were the same for those periods because the effect of the common share equivalents was anti-dilutive.

The following table presents the weighted-average common share equivalents excluded from the calculation of diluted earnings per share due to their anti-dilutive effect:

**Three  
Months  
Ended  
March  
31,  
2019**