

Midstates Petroleum Company, Inc.  
Form S-1  
January 18, 2017

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As filed with the Securities and Exchange Commission on January 18, 2017

No. 333-

**SECURITIES AND EXCHANGE COMMISSION**  
Washington, D.C. 20549

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**FORM S-1**  
REGISTRATION STATEMENT  
UNDER  
THE SECURITIES ACT OF 1933

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**Midstates Petroleum Company, Inc.**

(Exact name of registrant as specified in its charter)

**Delaware**  
(State or other jurisdiction of  
incorporation or organization)

**1311**  
(Primary Standard Industrial  
Classification Code Number)  
**321 South Boston, Suite 1000**  
**Tulsa, Oklahoma 74103**  
**(918) 947-8550**

**45-3691816**  
(I.R.S. Employer  
Identification No.)

(Address, including zip code, and telephone number, including area code, of registrant's principal executive offices)

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**Scott C. Weatherholt**  
**Vice President General Counsel & Corporate Secretary**  
**Vice President Land**

**Midstates Petroleum Company, Inc.**  
**321 South Boston, Suite 1000**  
**Tulsa, Oklahoma 74103**  
**(918) 947-8550**

(Name, address, including zip code, and telephone number, including area code, of agent for service)

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**Copies of all communications, including communications sent to agent for service, should be sent to:**

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Matthew R. Pacey  
 Kirkland & Ellis LLP  
 600 Travis Street, Suite 3300  
 Houston, Texas 77002  
 713-835-3600

**Approximate date of commencement of proposed sale to the public:  
 From time to time after this Registration Statement becomes effective.**

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If any of the securities being registered on this Form are to be offered on a delayed or continuous basis pursuant to Rule 415 under the Securities Act of 1933, check the following box:

If this Form is filed to register additional securities for an offering pursuant to Rule 462(b) under the Securities Act, please check the following box and list the Securities Act registration statement number of the earlier effective registration statement for the same offering.

If this Form is a post-effective amendment filed pursuant to Rule 462(c) under the Securities Act, check the following box and list the Securities Act registration statement number of the earlier effective registration statement for the same offering.

If this Form is a post-effective amendment filed pursuant to Rule 462(d) under the Securities Act, check the following box and list the Securities Act registration statement number of the earlier effective registration statement for the same offering.

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. (Check one):

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

**CALCULATION OF REGISTRATION FEE**

Title of Each Class of Securities to be Registered	Amount to be Registered	Proposed Maximum Offering Price Per Unit(1)	Proposed Maximum Aggregate Offering Price(1)	Amount of Registration Fee
Shares of common stock, par value \$0.01 per share	13,473,639	\$20.97	\$282,542,209.83	\$32,746.64
Shares of common stock, par value \$0.01 per share, underlying warrants	996,654	\$20.97	\$20,899,834.38	\$2,422.29

(1) Estimated solely for the purpose of calculating the registration fee, based on the average of the high and low sales prices for our common stock as quoted on the NYSE MKT on January 17, 2017, in accordance with Rule 457(c) under the Securities Act of 1933, as amended.

The registrant hereby amends this Registration Statement on such date or dates as may be necessary to delay its effective date until the registrant shall file a further amendment which specifically states that this Registration Statement shall thereafter become effective in accordance with Section 8(a) of the Securities Act of 1933 or until this Registration Statement shall become effective on such date as the Commission, acting pursuant to said Section 8(a), may determine.



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**The information in this prospectus is not complete and may be changed. The securities described herein may not be sold until the registration statement filed with the Securities and Exchange Commission is effective. This prospectus is not an offer to sell such securities, and it is not soliciting an offer to buy such securities, in any state or jurisdiction where such offer or sale is not permitted.**

**Subject to Completion, dated January 18, 2017**

**PROSPECTUS**

## **Midstates Petroleum Company, Inc.**

### **14,470,293 Shares of Common Stock**

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This prospectus relates to the resale of an aggregate of 14,470,293 shares of our common stock, which may be offered for sale from time to time by the selling stockholders named in this prospectus. The number of shares the selling stockholders may sell consists of 13,473,639 shares of common stock that are currently issued and outstanding and 996,654 shares of common stock that they may receive if they exercise their warrants. The selling stockholders acquired all of the shares of common stock and warrants covered by this prospectus in a distribution pursuant to Section 1145 under the United States Bankruptcy Code in connection with our plan of reorganization that became effective on October 21, 2016. We are registering the offer and sale of the shares of common stock to satisfy registration rights we have granted to the selling stockholders.

We are not selling any shares of common stock under this prospectus and will not receive any proceeds from the sale of common stock by the selling stockholders. The shares of common stock to which this prospectus relates may be offered and sold from time to time directly by the selling stockholders or alternatively through underwriters, broker-dealers or agents. The shares of common stock may be sold in one or more transactions, at fixed prices, at prevailing market prices at the time of sale or at negotiated prices. The selling stockholders will be responsible for any underwriting fees, discounts and commissions due to underwriters, brokers-dealers or agents. Please see the section titled "Plan of Distribution" of this prospectus for a more complete description of how the offered common stock may be sold.

You should carefully read this prospectus and any prospectus supplement before you invest. You also should read the documents we have referred you to in the "Where You Can Find More Information" and the "Incorporation by Reference" sections of this prospectus for information about us and our financial statements.

Our common stock is listed on the NYSE MKT under the symbol "MPO." On January 17, 2017, the last reported sale price of our common stock on the NYSE MKT was \$21.39 per share.

**Investing in our common stock involves risks. See "Risk Factors" on page 3 of this prospectus.**

Neither the Securities and Exchange Commission nor any state securities commission has approved or disapproved of these securities or passed upon the adequacy or accuracy of this prospectus. Any representation to the contrary is a criminal offense.

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The date of this Prospectus is \_\_\_\_\_, 2017.

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Neither we nor the selling stockholders have authorized any dealer, salesman or other person to provide you with information other than the information contained in or incorporated by reference into this prospectus. This prospectus does not constitute, and may not be used in connection with, an offer to sell, or a solicitation of an offer to buy, the common stock offered by this prospectus by any person in any jurisdiction in which it is unlawful for such person to make such an offer or solicitation. You should not assume that the information contained in this prospectus is accurate as of any date other than the date on the front cover of the prospectus, or that the information contained in any document incorporated by reference into this prospectus is accurate as of any date other than the date of the document incorporated by reference, regardless of the time of delivery of this prospectus or any sale of a security. Our business, financial condition, results of operations and prospects may have changed since those dates.

This prospectus contains forward-looking statements that are subject to a number of risks and uncertainties, many of which are beyond our control. See "Risk Factors" and "Cautionary Statement Regarding Forward-Looking Statements."

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**CAUTIONARY STATEMENT REGARDING FORWARD-LOOKING STATEMENTS**

The information in this prospectus includes "forward-looking statements." All statements, other than statements of historical fact included in this prospectus, regarding our strategy, future operations, financial position, estimated revenues and losses, projected costs, prospects, plans and objectives of management are forward-looking statements. When used in this prospectus, the words "could," "believe," "anticipate," "intend," "estimate," "expect," "project" and similar expressions are intended to identify forward-looking statements, although not all forward-looking statements contain such identifying words. These forward-looking statements are based on management's current expectations and assumptions about future events and are based on currently available information as to the outcome and timing of future events. When considering forward-looking statements, you should keep in mind the risk factors and other cautionary statements described under the heading "Risk Factors" included in this prospectus.

Forward-looking statements may include statements about our:

business strategy, including our business strategy post-emergence from bankruptcy;

estimated future net reserves from future production of our oil and natural gas reserves and present value thereof;

the amount of oil and natural gas recoverable from our oil and natural gas properties;

technology;

financial condition, revenues, cash flows and expenses;

levels of indebtedness, liquidity and compliance with debt covenants;

financial strategy, budget, projections and operating results;

oil and natural gas realized prices;

timing and amount of future production of oil and natural gas;

availability of drilling and production equipment;

availability of oilfield labor;

availability of third party natural gas gathering and processing capacity;

the amount, nature and timing of capital expenditures, including future development costs;

availability and terms of capital;

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drilling of wells, including our identified drilling locations;

successful results from our identified drilling locations;

marketing of oil and natural gas;

the integration and benefits of asset and property acquisitions or the effects of asset and property acquisitions or dispositions on our cash position and levels of indebtedness;

infrastructure for salt water disposal and electricity;

current and future ability to dispose of produced salt water;

sources of electricity utilized in operations and the related infrastructures;

costs of developing our properties and conducting other operations;

general economic conditions;

effectiveness of our risk management activities;

environmental liabilities;

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counterparty credit risk;

the outcome of pending and future litigation;

governmental regulation and taxation of the oil and natural gas industry;

developments in oil-producing and natural gas-producing countries;

new capital structure and the adoption of fresh start accounting, including the risk that assumptions and factors used in estimating enterprise value vary significantly from the current estimates in connection with the application of fresh start accounting;

uncertainty regarding our future operating results; and

plans, objectives, expectations and intentions that are not historical.

We caution you that these forward-looking statements are subject to all of the risks and uncertainties, most of which are difficult to predict and many of which are beyond our control, incident to the exploration for and development, production, gathering and sale of oil and natural gas. These risks include, but are not limited to, commodity price volatility, inflation, lack of availability of drilling and production equipment and services, environmental risks, drilling and other operating risks, regulatory changes, the uncertainty inherent in estimating reserves and in projecting future rates of production, cash flow and access to capital, the timing of development expenditures and the other risks described under "Risk Factors" in this prospectus.

Reserve engineering is a process of estimating underground accumulations of oil and natural gas that cannot be measured in an exact way. The accuracy of any reserve estimate depends on the quality of available data, the interpretation of such data and price and cost assumptions made by reserve engineers. In addition, the results of drilling, testing and production activities may justify revisions of estimates that were made previously. If significant, such revisions may change the schedule of any future production and development drilling. Accordingly, reserve estimates may differ significantly from the quantities of oil and natural gas that are ultimately recovered.

Should one or more of the risks or uncertainties described in this prospectus occur, or should underlying assumptions prove incorrect, our actual results and plans could differ materially from those expressed in any forward-looking statements.

All forward-looking statements, expressed or implied, included in this prospectus are expressly qualified in their entirety by this cautionary statement. This cautionary statement should also be considered in connection with any subsequent written or oral forward-looking statements that we or persons acting on our behalf may issue.

Except as otherwise required by applicable law, we disclaim any duty to update any forward-looking statements, all of which are expressly qualified by the statements in this section, to reflect events or circumstances after the date of this prospectus.

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**PROSPECTUS SUMMARY**

*This summary description about us and our business highlights selected information contained elsewhere in this prospectus or incorporated by reference into this prospectus. It does not contain all the information you should consider before investing in our securities. Important information is incorporated by reference into this prospectus. To understand this offering fully, you should read carefully the entire prospectus, including "Risk Factors," together with the additional information described under "Incorporation By Reference."*

*Unless otherwise stated or the context otherwise requires, references in this prospectus to "our company," "we," "us," "our" and "ours" refer to Midstates Petroleum Company, Inc. and its subsidiary.*

**Our Company**

We are an independent exploration and production company focused on the application of modern drilling and completion techniques to oil-prone resources in the United States. Our operations are primarily focused on exploration and production activities in the Mississippian Lime and the Anadarko Basin.

**Chapter 11 Plan of Reorganization**

On April 30, 2016 (the "Petition Date"), we filed voluntary petitions for reorganization under Chapter 11 of the United States Bankruptcy Code (the "Bankruptcy Code") in the United States Bankruptcy Court for the Southern District of Texas (the "Bankruptcy Court"). Our Chapter 11 cases (the "Chapter 11 Cases") were jointly administered under the case styled *In re Midstates Petroleum Company, Inc., et al., Case No. 16-32237*.

On September 28, 2016, the Bankruptcy Court entered the *Findings of Fact, Conclusions of Law, and Order Confirming Debtors' First Amended Joint Chapter 11 Plan of Reorganization of Midstates Petroleum Company, Inc. and its Debtor Affiliate* (the "Confirmation Order"), which approved and confirmed the First Amended Joint Chapter 11 Plan of Reorganization of Midstates Petroleum Company, Inc. and its Debtor Affiliate as filed on the same date (the "Plan").

On October 21, 2016 (the "Effective Date"), we satisfied the conditions to effectiveness set forth in the Confirmation Order and in the Plan, the Plan became effective in accordance with its terms and we emerged from the Chapter 11 Cases.

**Principal Executive Offices**

Our principal executive offices are located at 321 South Boston, Suite 1000, Tulsa, Oklahoma 74103, and our telephone number at that address is (918) 947-8550. Information contained on our website, [www.midstatespetroleum.com](http://www.midstatespetroleum.com), does not constitute a part of this prospectus.

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**The Offering**

Common Stock Offered by the Selling Stockholders:	14,470,293 shares, including 996,654 shares of common stock issuable upon exercise of warrants.
Common Stock Outstanding:	24,994,867 shares of common stock outstanding as of January 17, 2017.
Use of Proceeds:	We will not receive any of the proceeds from the sale of any shares of common stock by the selling stockholders.
NYSE MKT Symbol for Common Stock:	"MPO"
Risk Factors:	Investing in our common stock involves a high degree of risk. See "Risk Factors" and the risk factors set forth in the documents incorporated by reference herein for a discussion of factors you should carefully consider before deciding to invest in our common stock.

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**RISK FACTORS**

Investing in our common stock involves a high degree of risk. Before deciding whether to purchase shares of our common stock, you should carefully consider the risks and uncertainties described under "Risk Factors" in the Annual Report on Form 10-K for the fiscal year ended December 31, 2015, any subsequent Quarterly Report on Form 10-Q and our other filings with the SEC, all of which are incorporated by reference herein. If any of these risks actually occur, our business, financial condition and results of operations could be materially and adversely affected and we may not be able to achieve our goals, the value of our securities could decline and you could lose some or all of your investment. Additional risks not presently known to us or that we currently deem immaterial may also impair our business operations.

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**USE OF PROCEEDS**

The common stock to be offered and sold using this prospectus will be offered and sold by the selling stockholders named in this prospectus. See "Principal and Selling Stockholders." Accordingly, we will not receive any proceeds from the sale of shares of our common stock in this offering.

Table of Contents**MARKET PRICE OF OUR COMMON STOCK**

Our new common stock is quoted on the NYSE MKT under the symbol "MPO" and has been trading since October 24, 2016. No prior established public trading market existed for our new common stock prior to this date. The following table sets forth the per share range of high and low bid information for our common stock as reported on the NYSE MKT for the periods presented.

<b>Quarter Ended:</b>	<b>High</b>	<b>Low</b>
December 31, 2016 (beginning on October 24, 2016)	\$ 22.65	\$ 17.01
March 31, 2017 (through January 17, 2017)	\$ 21.85	\$ 20.10

On January 17, 2017, the last sale price of our common stock as reported on the NYSE MKT was \$21.39 per share. As of January 17, 2017, we had one holder of record of our common stock, based on information provided by our transfer agent.

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**PRINCIPAL AND SELLING STOCKHOLDERS**

The following table sets forth as of January 17, 2017 information regarding the beneficial ownership of our common stock and shows the number of shares of common stock and the percentage owned by:

each member of our board of directors and each of our named executive officers;

all of the executive officers and members of the board of directors as a group; and

each person known to beneficially own more than 5% of our common stock, each of whom is a selling stockholder.

On October 21, 2016, we entered into an agreement containing registration rights with the selling stockholders pursuant to which we were obligated to prepare and file a registration statement to permit the resale of certain common stock held by the selling stockholders from time to time as permitted by Rule 415 promulgated under the Securities Act of 1933, as amended, or the Securities Act. We are registering the common stock described in this prospectus pursuant to this agreement. The following table also sets forth the maximum number of shares of our common stock to be sold by the selling stockholders, the name of each selling stockholder, the nature of any position, office, or other material relationship which the selling stockholder has had, within the past three years, with us or with any of our predecessors or affiliates, and the number of shares and percentage of our common stock to be owned by such stockholders after completion of the offering, assuming the sale of all shares of common stock offered hereby.

Additionally, the selling stockholders may have sold or transferred some or all of their shares of our common stock in transactions exempt from the registration requirements of the Securities Act since the date on which the information in the table was provided to us. Other information about the selling stockholders may also change over time.

Except as otherwise indicated, each selling stockholder has sole voting and dispositive power with respect to such shares.

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All information with respect to beneficial ownership has been furnished by the respective 5% or more stockholders, selling stockholders, directors or named executive officers, as the case may be. We have not sought to verify such information.

	Shares of Common Stock Beneficially Owned Prior to the Offering(1)		Number of Shares of Common Stock Being Offered Hereby	Shares of Common Stock Beneficially Owned After Completion of the Offering(2)	
	Number	Percentage		Number	Percentage
<b>Selling shareholders:</b>					
Avenue Capital funds(3)	3,494,914	13.98%	3,494,914	0	*
Centerbridge funds(4)	4,582,301(5)	18.33%	4,582,301	0	*
Fir Tree funds(6)	6,393,078	25.58%	6,393,078	0	*
<b>Other 5% shareholders:</b>					
Man Group plc(7)	1,421,123	5.69%			
<b>Directors and named executive officers:</b>					
Alan J. Carr	13,451(8)	*			
Frederic F. Brace	131,873(9)	*			
Patrice Douglas	9,001(10)	*			
Neal P. Goldman	9,001(11)	*			
Todd R. Snyder	9,001(12)	*			
Michael S. Reddin	9,001(13)	*			
Bruce H. Vincent	9,001(14)	*			
Nelson M. Haight	95,328(15)	*			
Mitchell G. Elkins	101,653(16)	*			
Scott C. Weatherholt	47,678(17)	*			
Amelia K. Harding	37,347(18)	*			
All directors and executive officers as a group (12 persons)	472,335	1.84%			

\*

Less than 1%

(1)

The amounts and percentages of common stock beneficially owned are reported on the bases of regulations of the SEC governing the determination of beneficial ownership of securities. Under the rules of the SEC, a person is deemed to be a "beneficial owner" of a security if that person has or shares voting power, which includes the power to vote or direct the voting of such security, or investment power, which includes the power to dispose of or to direct the disposition of such security. Under these rules, more than one person may be deemed to be a beneficial owner of the same securities, and a person may be deemed to be a beneficial owner of securities as to which such person has no economic interest. The number of shares beneficially owned by a person includes shares of common stock underlying warrants, stock options, convertible preferred stock, and any other derivative securities to acquire common stock held by that person that are currently exercisable or convertible within 60 days after the date of this prospectus. The shares issuable under any such securities are treated as outstanding for computing the percentage ownership of the person holding these securities, but are not treated as outstanding for the purposes of computing the percentage ownership of any other person.

(2)

Assumes the exercise of all warrants and the sale of all shares held by the selling stockholders covered by this prospectus and assumes the selling stockholders do not acquire beneficial ownership of any additional shares of our common stock. The selling stockholders are not obligated to sell any of the shares of our common stock covered by this prospectus. Also assumes no sale by us of shares of our common stock under this registration statement.

(3)

Comprised of 3,494,914 shares of common stock held directly by Avenue Energy Opportunities Fund, L.P. ("Avenue Energy Opportunities Fund"). Avenue Energy Opportunities Partners, LLC is the general partner of Avenue Energy Opportunities Fund. GL Energy Opportunities Partners, LLC is the managing member of Avenue Energy Opportunities Partners, LLC. Avenue Capital Management II, L.P. is the investment adviser to Avenue Energy Opportunities Fund, L.P. Avenue Capital Management II

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GenPar, LLC is the general partner of Avenue Capital Management II, L.P. Marc Lasry is the managing member of GL Energy Opportunities Partners, LLC and Avenue Capital Management II GenPar, LLC. Each of the foregoing individuals and entities share the power to vote common stock held by Avenue Energy Opportunities Fund.



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The principal address of the foregoing individuals and entities is 399 Park Avenue, 6th Floor, New York, NY 10022.

- (4) Includes 1,204,284 shares of common stock (including 243,053 shares of common stock issuable upon exercise of warrants) held by Centerbridge Credit Partners, L.P. ("Onshore Fund"), 1,068,913 shares of common stock (including 314,836 shares of common stock issuable upon exercise of warrants) held directly by Centerbridge Special Credit Partners II AIV III, L.P. ("SC II AIV III"), 500,970 shares of common stock (including 77,838 shares of common stock issuable upon exercise of warrants) held directly by Centerbridge Credit Partners Offshore Intermediate III, L.P. ("Offshore Int III") and 1,808,134 shares of common stock (including 360,927 shares of common stock issuable upon exercise of warrants) held directly by Centerbridge Credit Partners TE Intermediate I, L.P. ("TE Int I").
- Centerbridge Credit Partners General Partner, L.P. ("Credit GP") is the general partner of Onshore Fund and TE Int I. Centerbridge Credit Partners Offshore General Partner, L.P. ("Credit Offshore GP") is the general partner of Offshore Int III. Centerbridge Credit Cayman GP Ltd. ("Credit Cayman GP") is the general partner of Credit GP and Credit Offshore GP. Centerbridge Special Credit Partners General Partner II, L.P. ("SC II GP") is the general partner of SC II AIV III. CSCP II Cayman GP Ltd. ("SC II Cayman GP") is the general partner of SC II GP. Credit GP and Credit Cayman GP share the power to vote and invest the common stock held by Onshore Fund and TE Int I. Credit Offshore GP and Credit Cayman GP share the power to vote and invest the common stock held by Offshore Int III. SC II Cayman GP and SC II GP share the power to vote and invest the common stock held by SC II AIV III. Mark T. Gallogly and Jeffrey H. Aronson, indirectly, through various intermediate entities, control each of Onshore Fund, TE Int I, Offshore Int III and SC II AIV III. Each of Credit GP, Credit Offshore GP, Credit Cayman GP, SC II GP, SC II Cayman GP, Mr. Gallogly and Mr. Aronson disclaims beneficial ownership of such securities. The principal address of the foregoing individuals and entities is 375 Park Avenue, 12th Floor, New York, NY 10152.
- (5) Includes shares issuable upon exercise of warrants.
- (6) Comprised of 1,065,256 shares of common stock held directly by Fir Tree Capital Opportunity (LN) Master Fund, L.P., 3,852,002 shares of common stock held directly by Fir Tree Value (LN) Master Fund, L.P., 109,494 shares of common stock held directly by FT SOF IV Holdings, LLC, 127,358 shares of common stock held directly by FT SOF V Holdings, LLC and 1,238,968 shares of common stock held directly by FT SOF VII AIV Holdings I, LLC. Fir Tree Inc., is the investment manager for the foregoing entities, has the shared power to vote or direct the voting, and to dispose or direct the disposition of, the shares of our common stock beneficially owned by each of the foregoing entities. The principal address of these entities is 55 West 46th Street, 29th Floor, New York, NY 10036.
- (7) The principal address of this entity is Riverbank House, 2 Swan Lane, London EC4R 3AD, United Kingdom.
- (8) Includes 13,351 restricted stock units ("RSUs").
- (9) Includes 131,773 RSUs.
- (10) Includes 8,901 RSUs.
- (11) Includes 8,901 RSUs.
- (12) Includes 8,901 RSUs.
- (13) Includes 8,901 RSUs.
- (14) Includes 8,901 RSUs.
- (15)

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Includes 95,228 RSUs.

(16)

Includes 101,553 RSUs.

(17)

Includes 47,578 RSUs.

(18)

Includes 37,247 RSUs.

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**CERTAIN RELATIONSHIPS AND RELATED PARTY TRANSACTIONS**

In the ordinary course of our business, we may enter into transactions with our directors, officers and 5% or greater shareholders.

**Registration Rights Agreement**

On the Effective Date, we entered into a registration rights agreement (the "Registration Rights Agreement") with certain of the pre-emergence creditors that received shares of our common stock (the "Common Stock") on the Effective Date (the "Holders"), as provided in the Plan. The Registration Rights Agreement provides resale registration rights for the Holders' Registrable Securities (as defined in the Registration Rights Agreement).

Pursuant to the Registration Rights Agreement, we are required to file a Shelf Registration Statement (as defined in the Registration Rights Agreement) with respect to the Registrable Securities within 90 days of the Effective Date. We are required to maintain the effectiveness of any such registration statement until the Registrable Securities covered by the registration statement are no longer Registrable Securities.

Additionally, holders have customary demand, underwritten offering and piggyback registration rights, subject to the limitations set forth in the Registration Rights Agreement. Under their demand registration rights, Qualified Holders (as defined in the Registration Rights Agreement) may request us to register all or a portion of their Registrable Securities, including on a delayed or continuous basis under Rule 415 of the Securities Act, provided that such offering is expected to yield aggregate gross proceeds of at least \$25 million and we are not otherwise in violation of our obligation to file a Shelf Registration Statement. Under their underwritten offering registration rights, Holders also have certain rights to demand that we effectuate the distribution of any or all of their Registrable Securities by means of an underwritten offering pursuant to an effective registration statement. We shall not be obligated to effect more than four underwritten offerings in any twelve-month period and the aggregate proceeds expected to be received from the sale of the Registrable Securities requested to be sold in such underwritten offering, in the good faith judgment of the managing underwriters, must be at least \$25 million. We are not obligated to file a registration statement pursuant to a demand notice or conduct an underwritten offering pursuant to a demand notice within 90 days of either a demand registration or an underwritten offering. The Registration Rights Agreement also provides customary piggyback registration rights.

These registration rights are subject to certain conditions and limitations, including the right of the underwriters to limit the number of shares to be included in a registration statement and our right to delay or withdraw a registration statement under certain circumstances. We will generally pay all registration expenses in connection with our obligations under the Registration Rights Agreement, regardless of whether a registration statement is filed or becomes effective. The registration rights granted in the Registration Rights Agreement are subject to customary indemnification and contribution provisions, as well as customary restrictions such as blackout periods and, if an underwritten offering is contemplated, limitations on the number of shares to be included in the underwritten offering that may be imposed by the managing underwriter.

The obligations to register shares under the Registration Rights Agreement will terminate with respect to us and each Holder on the first date upon which the Holder no longer owns any Registrable Securities.

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**DESCRIPTION OF CAPITAL STOCK**

**Authorized Capitalization**

The Company's authorized capital stock consists of 300,000,000 shares, which include 250,000,000 shares of common stock and 50,000,000 shares of preferred stock, par value \$0.01 per share.

**Common Stock**

Except as provided by law or in a preferred stock designation, holders of common stock are entitled to one vote for each share held of record on all matters submitted to a vote of the stockholders, will have the exclusive right to vote for the election of directors and do not have cumulative voting rights. Except as otherwise required by law, holders of common stock are not entitled to vote on any amendment to the Second Amended and Restated Certificate of Incorporation (the "Certificate of Incorporation") (including any certificate of designations relating to any series of preferred stock) that relates solely to the terms of any outstanding series of preferred stock if the holders of such affected series are entitled, either separately or together with the holders of one or more other such series, to vote thereon pursuant to the Certificate of Incorporation (including any certificate of designations relating to any series of preferred stock) or pursuant to the Delaware General Corporation Law (the "DGCL"). Subject to prior rights and preferences that may be applicable to any outstanding shares or series of preferred stock, holders of common stock are entitled to receive ratably in proportion to the shares of common stock held by them such dividends (payable in cash, stock or otherwise), if any, as may be declared from time to time by our board of directors out of funds legally available for dividend payments. All outstanding shares of common stock are fully paid and non-assessable, and the shares of common stock that will be issued under this prospectus will be fully paid and non-assessable. The holders of common stock have no preferences or rights of conversion, exchange, pre-emption or other subscription rights. There are no redemption or sinking fund provisions applicable to the common stock. In the event of any voluntary or involuntary liquidation, dissolution or winding-up of our affairs, holders of common stock will be entitled to share ratably in our assets in proportion to the shares of common stock held by them that are remaining after payment or provision for payment of all of our debts and obligations and after distribution in full of preferential amounts to be distributed to holders of outstanding shares of preferred stock, if any.

**Preferred Stock**

Our Certificate of Incorporation authorizes our board of directors, subject to any limitations prescribed by law, without further stockholder approval, to establish and to issue from time to time one or more classes or series of preferred stock, par value \$0.01 per share, covering up to an aggregate of 50,000,000 shares of preferred stock. Each class or series of preferred stock will cover the number of shares and will have the powers, preferences, rights, qualifications, limitations and restrictions determined by the board of directors, which may include, among others, dividend rights, liquidation preferences, voting rights, conversion rights, preemptive rights and redemption rights. Except as provided by law or in a preferred stock designation, the holders of preferred stock will not be entitled to vote at or receive notice of any meeting of stockholders.

**Anti-Takeover Effects of Provisions of our Amended and Restated Certificate of Incorporation, our Amended and Restated Bylaws and Delaware Law**

Some provisions of Delaware law, and our Certificate of Incorporation and our Amended and Restated Bylaws (the "Bylaws") described below, will contain provisions that could make the following transactions more difficult: acquisitions of us by means of a tender offer, a proxy contest or otherwise; or removal of our incumbent officers and directors. These provisions may also have the effect of preventing changes in our management. It is possible that these provisions could make it more difficult

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to accomplish or could deter transactions that stockholders may otherwise consider to be in their best interest or in our best interests, including transactions that might result in a premium over the market price for our shares.

These provisions, summarized below, are expected to discourage coercive takeover practices and inadequate takeover bids. These provisions are also designed to encourage persons seeking to acquire control of us to first negotiate with us. We believe that the benefits of increased protection and our potential ability to negotiate with the proponent of an unfriendly or unsolicited proposal to acquire or restructure us outweigh the disadvantages of discouraging these proposals because, among other things, negotiation of these proposals could result in an improvement of their terms.

**Delaware Law**

We are not subject to the provisions of Section 203 of the DGCL, regulating corporate takeovers. In general, Section 203 prohibits a publicly held Delaware corporation from engaging in a "business combination" with an "interested stockholder" for a three-year period following the time that such stockholder becomes an interested stockholder, unless the business combination is approved in a prescribed manner. A "business combination" includes, among other things, a merger, asset or stock sale, or other transaction resulting in a financial benefit to the interested stockholder. An "interested stockholder" is a person who, together with affiliates and associates, owns, or did own within three years prior to the determination of interested stockholder status, 15% or more of the corporation's outstanding voting stock. Under Section 203, a business combination between a corporation and an interested stockholder is prohibited unless it satisfies one of the following conditions:

the transaction is approved by the board of directors before the date the interested stockholder attained that status;

upon consummation of the transaction that resulted in the stockholder becoming an interested stockholder, the interested stockholder owned at least 85% of the voting stock of the corporation outstanding at the time the transaction commenced, excluding for purposes of determining the voting stock outstanding, shares owned by persons who are directors and also officers, and employee stock plans, in some instances; or

on or after such time, the business combination is approved by the board of directors and authorized at a meeting of stockholders by at least two-thirds of the outstanding voting stock that is not owned by the interested stockholder.

A Delaware corporation may "opt out" of Section 203 with an express provision in its original certificate of incorporation or an express provision in its certificate of incorporation or Bylaws resulting from amendments approved by the holders of at least a majority of the corporation's outstanding voting shares. We elected to "opt out" of the provisions of Section 203.

**Amended and Restated Certificate of Incorporation and Amended and Restated Bylaws**

Provisions of our Certificate of Incorporation and amended and restated Bylaws may delay or discourage transactions involving an actual or potential change in control or change in our management, including transactions in which stockholders might otherwise receive a premium for their shares, or transactions that our stockholders might otherwise deem to be in their best interests. Therefore, these provisions could adversely affect the price of our common stock.

Among other things, our Certificate of Incorporation and Bylaws:

permit our board of directors to issue up to 50,000,000 shares of preferred stock, with any rights, preferences and privileges as they may designate;

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provide that the authorized number of directors may be changed only by resolution of the board of directors;

provide that all vacancies, including newly created directorships, may, except as otherwise required by law, be filled by the affirmative vote of a majority of directors then in office, even if less than a quorum (prior to such time, vacancies may also be filled by the affirmative vote of the holders of a majority of our then outstanding common stock);

provide that our amended and restated Bylaws may only be amended by the affirmative vote of the holders of a majority of our then outstanding common stock or by resolution adopted by a majority of the directors); and

provide that special meetings of our stockholders may only be called by the board of directors, the chief executive officer or the chairman of the board or the board of directors;

eliminate the personal liability of our directors for monetary damages resulting from breaches of their fiduciary duty to the extent permitted by the DGCL and indemnify our directors and officers to the fullest extent permitted by Section 145 of the DGCL;

Interest on the line of credit and discounting charges on accounts receivable advances was accrued at a rate of 2% per annum over the prime rate as published by the Wall Street Journal and at no time shall the effective rate be less than 5.25% per annum. During the three month periods ended June 30, 2014 and 2013, the Company incurred interest expense of \$1,576 and \$736, respectively on amounts borrowed against the line of credit. The credit facility is secured with all assets of the Company as well as related-party debt subordination agreements totaling \$2,500,000 from Ram Light Management, Ltd. in the amount of \$1,683,247 and Starlight Marketing Development, Ltd. in the amount of \$816,753. There is a 1% commission fee of the gross invoice amount on all domestic accounts receivable pledged. For the three months ended June 30, 2014 and 2013, the Company incurred commission fees on pledged receivables in the amount of \$14,506 and \$23,020, respectively. There was an outstanding amount of \$64,776 due on the line of credit as of June 30, 2014. There were no amounts outstanding on the line of credit as of the year ended March 31, 2014.

#### **PNC BANK NATIONAL ASSOCIATION**

On July 14, 2014, the Company executed a three-year revolving credit facility (the “Revolving Credit Facility”) with PNC Bank, National Association (“PNC”) that replaced the existing line of credit agreement with Crestmark. The Revolving Credit Facility has a three year term expiring on July 14, 2017. The outstanding loan balance cannot exceed \$15,000,000 during peak selling season between August 1 and December 31 and is reduced to a maximum of \$7,500,000 between January 1 and July 31. Usage under the Revolving Credit Facility shall not exceed the sum of the following (the “Borrowing Base”):

Up to 85% of the company’s eligible domestic and Canadian accounts receivable aged less than 60 days past due (not to exceed 90 days from invoice date, cross aged on the basis of 50% or more past due with certain specific accounts qualifying for up to 120 days from invoice date not to exceed 30 days from the due date; plus

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Up to the lesser of (a) 50% of the cost of eligible inventory or (b) 75% of net orderly liquidation value percentage of eligible inventory (annual inventory appraisals required); minus  
An all-time \$500,000 block; minus  
Applicable reserves including a dilution reserve equal to 125% of the Company's advertising and return accrual reserves. Dilution reserve not to exceed availability generated from eligible accounts receivable.

The Revolving Credit Facility includes the following sub-limits:

Letters of Credit to be issued limited to \$3,000,000.

Inventory availability limited to \$4,000,000.

Mandatory pay-down to \$1,000,000 (excluding letters of credit) for any 30 consecutive days between February 1 and April 30.

The Revolving Credit Facility must comply with the following quarterly financial covenants to avoid default:

Fixed charge coverage ratio test of 1.1:1 times measured on a rolling four quarter basis, defined as EBITDA less non-financed capital expenditures, cash dividends and distributions paid and cash taxes paid divided by the sum of interest and principal on all indebtedness.

Capital expenditures limited to \$150,000 per year.

Interest on the Revolving Line of Credit will initially be accrued at 2% per annum over PNC's announced prime rate with an option for the Company to elect the 1, 2 or 3 month fully absorbed PNC LIBOR Rate plus 3.5% per annum with a default rate of 2% over the applicable rate. There will be an unused facility fee equal to .375% per annum on the unused portion of the Revolving Credit Facility which will be calculated on the basis of a 360 day year for the actual number of days elapsed and will be payable quarterly in arrears.

The Revolving Line of Credit is secured by first priority security interests in all of the named borrowers' tangible and intangible assets as well as first priority security interests of 100% of member or ownership interests of any of its domestic existing or newly formed subsidiaries and first priority lien on up to 65% of the borrowers' domestic subsidiary's existing or subsequently formed or acquired foreign subsidiaries. The Revolving Credit Facility is also secured by a related-party debt subordination agreement with Starlight Marketing Development, Ltd. in the amount of \$2,500,000. Costs associated with securing the Revolving Credit Facility of approximately \$200,000 will be deferred and amortized over the term of the agreement.

As a condition of the Revolving Credit Facility, a portion of the Company's related-party debt with Ram Light Management, Ltd. in the amount of \$1,100,000 was converted to a note payable with Ram Light Management, Ltd. ("Ram Light Note"). The Ram Light Note bears interest at 6% per annum with quarterly payments of \$150,000 (including principle and interest) payable beginning December 31, 2014. The first scheduled principal and interest payment of \$150,000 will only be permitted upon receipt of the Company's December 31, 2014 quarterly compliance certificate; the Company having met the mandatory pay-down of the Revolving Credit Facility to \$1,000,000 and average excess availability for the prior 30 days (after subtraction of third party trade payables 30 days or more past due) of no less than \$1,000,000 after giving effect to the payment.

#### **NOTE 8 – LONG-TERM CAPITAL LEASE**

On April 13, 2013, the company entered into a long-term capital leasing arrangement with Wells Fargo Equipment Finance ("Wells Fargo") to finance the lease of two used forklift vehicles in the amount of \$36,388. The lease requires monthly payments in the amount of \$1,082 per month over a total lease term of 36 months which commenced on May 19, 2013. The agreement has an effective interest rate of 4.5% and the company has the option to purchase the equipment at the end of the lease term for one dollar. As of June 30, 2014 and March 31, 2014, the outstanding amount due to Wells Fargo was \$22,813 and \$25,782, respectively.

As of June 30, 2014 and March 31, 2014, the Company had obligations under the capital lease repayable as follows:



	June 30, 2014 (unaudited)	March 31, 2014 (audited)
Total minimum lease payments		
Within one year	\$ 12,984	\$ 12,984
After one year but within 3 years	10,820	14,066
	23,804	27,050
Interest payments relating to future periods	(991 )	(1,268 )
Present Value of minimum lease payments	\$ 22,813	\$ 25,782

For the three month periods ended June 30, 2014 and June 30, 2013 the amount of interest related to the capital lease was \$277 and \$268, respectively.

#### **NOTE 9 - OBLIGATIONS TO CUSTOMERS FOR RETURNS AND ALLOWANCES**

Due to the seasonality of the business and length of time customers are given to return defective product, it is not uncommon for customers to accumulate credits from the Company's sales and allowance programs that are in excess of unpaid invoices in accounts receivable. All credit balances in customers' accounts receivable are reclassified to "obligations to customers for returns and allowances" in current liabilities on the consolidated balance sheet. Client requests for payment of a credit balance are reclassified from obligations to customers for returns and allowances to accounts payable on the condensed consolidated balance sheets. When new invoices are processed prior to settlement of the credit balance and the client accepts settlement of open credits with new invoices, then the excess of new invoices over credits are netted in accounts receivable. As of June 30, 2014 and March 31, 2014 obligations to customers for returns and allowances reclassified from accounts receivable were \$495,426 and \$469,838, respectively. As of June 30, 2014 there were no customers requesting payment of their credit balance and as such there were no amounts reclassified from obligations to customers for returns and allowances to accounts payable.

#### **NOTE 10 - COMMITMENTS AND CONTINGENCIES**

##### **LEGAL MATTERS**

Management is currently not aware of any legal proceedings.

##### **OPERATING LEASES**

The Company has entered into various operating lease agreements for office and warehouse facilities in Fort Lauderdale, Florida, Ontario, California and Macau expiring at varying dates. Rent expense for the three month periods ended June 30, 2014 and 2013 was \$163,470 and \$155,231, respectively.

In addition, the Company maintains various warehouse equipment and computer equipment operating leases. Future minimum lease payments under property and equipment leases with terms exceeding one year as of June 30, 2014 are as follows:

Property Leases	
For period ending June 30	
2015	\$ 524,024
2016	543,714
2017	519,258
2018	490,722
2019	524,272
2020 and beyond	611,650
	\$ 3,213,640

#### **NOTE 11 - SHAREHOLDERS' EQUITY**

##### **COMMON STOCK ISSUANCES**

During the three months ended June 30, 2014, the Company did not issue any shares of its common stock.

##### **STOCK OPTIONS**

On June 1, 2001, the Board of Directors approved the 2001 Stock Option Plan ("Plan"), which replaced the 1994 Stock Option Plan, as amended. The Plan was developed to provide a means whereby directors and selected employees, officers, consultants, and advisors of the Company were granted incentive or non-qualified stock options to purchase common stock of the Company. As of June 30, 2014, the Plan had expired and no shares were available to be issued. As of June 30, 2014, there were 1,196,000 options still outstanding and exercisable under the Plan. This does not include an additional 700,000 options issued after the expiration date of the Plan to directors and key employees as compensation that were not issued from the Plan.

There were no stock options issued during the three months ended June 30, 2014.

#### **NOTE 12 - GEOGRAPHICAL INFORMATION**

All sales to customers outside of the United States for the three months ended June 30, 2014 were made by the Macau Subsidiary. Sales by geographic region for the periods presented are as follows:

	FOR THE THREE MONTHS ENDED	
	June 30,	
	2014	2013
North America	\$ 2,290,253	\$ 1,413,567
Europe	254,706	-
	\$ 2,544,959	\$ 1,413,567

The geographic area of sales was based primarily on the location where the product is delivered.

**NOTE 13 – DUE TO RELATED PARTIES, NET**

As of June 30, 2014 and March 31, 2014, the Company had amounts due to related parties in the amounts of \$5,529,929 and \$4,925,982 respectively, consisting primarily of non-interest bearing trade payables due to Starlight affiliates. As of June 30, 2014 and March 31, 2014 the Company had amounts due from related parties in the amounts of \$328,927 and \$367,520 respectively, consisting primarily of non-interest bearing trade receivables due from Starlight affiliates.

#### **NOTE 14 – RELATED PARTY TRANSACTIONS**

During the three months ended June 30, 2014 and June 30, 2013 the Company sold \$316,594 and \$226,665, respectively to Starlight Electronics Company, Ltd at a discounted price, similar to prices granted to major direct import customers shipped internationally with freight prepaid. The average gross profit margin on sales to Starlight Electronics for the three months ended June 30, 2014 and June 30, 2013 was 16.6% and 8.3%, respectively. The product was drop shipped to Cosmo Communications of Canada (“Cosmo”), the Company’s primary distributor of its products to Canada. During the three months ended June 30, 2014 and June 30, 2013 the Company sold an additional \$101,161 and \$282,188, respectively of product to Cosmo from its California warehouse facility. These amounts were included as a component of cost of goods sold in the accompanying condensed consolidated statements of operations.

The Company purchased products and services from Starlight R&D, Ltd, (“SLRD”) a subsidiary of Starlight International Holding Ltd. The purchases from SLRD for the three month periods ended June 30, 2014 and 2013 were \$24,769 and \$42,105, respectively. The Company purchased products from Starfair Electronics Co., Ltd, (“SFE”) a subsidiary of Starlight International Holding Ltd. The purchases from SFE for the three month periods ended June 30, 2014 and 2013 were \$0 and \$76,703, respectively. The Company purchased products from Starlight Consumer Electronics USA, Inc., (“SCE”) a subsidiary of Starlight International Holding Ltd. The purchases from SCE for the three month periods ended June 30, 2014 and 2013 were \$1,598,200 and \$0, respectively. These amounts were included as a component of cost of goods sold in the accompanying condensed consolidated statements of operations.

Effective April 1, 2014, SMC-L entered into a service and logistics agreement with SCE, Cosmo USA, Inc. (“Cosmo USA”) and Starlight Electronics USA, Inc. (“Starlight Electronics USA”) to provide logistics, fulfillment, and warehousing services for SCE, Cosmo USA and Starlight Electronic USA’s domestic sales. For these services, SCE, Cosmo USA and Starlight Electronics USA have agreed to reimburse the Company for actual warehouse space occupied by these companies at \$8 per pallet and for logistics services performed based on an agreed to fee schedule specified in the agreement. The Company received \$43,285 and \$0 in service fees from these affiliates during the three months ended June 30, 2014 and June 30, 2013, respectively. The agreement expires on March 31, 2015 and is estimated to yield approximately \$180,000 in reimbursements for the fiscal year ending March 31, 2015.

Effective April 1, 2013, SMC-L entered into a service and logistics agreement with SCE, Cosmo USA and Starlight Electronics USA, to provide logistics, fulfillment, and warehousing services for SCE, Cosmo USA and Starlight Electronic USA’s domestic sales. For these services, SCE, Cosmo USA and Starlight Electronics USA agreed to reimburse the Company for actual warehouse space occupied by these companies at \$0.50 per square foot and for logistics services performed based on an agreed to

fee schedule specified in the agreement. The Company received \$0 and \$82,500 in service fees from these affiliates during the three months ended June 30, 2014 and June 30, 2013, respectively. This agreement expired on March 31, 2014.

**NOTE 15 – WARRANTY PROVISIONS**

A return program for defective goods is negotiated with each of our wholesale customers on a year-to-year basis. Customers are either allowed to return defective goods within a specified period of time after shipment (between 6 and 9 months) or granted a “defective allowance” consisting of a fixed percentage (between 1% and 5%) off of invoice price in lieu of returning defective products. The Company records liabilities for its return goods programs and defective goods allowance program at the time of sale for the estimated costs that may be incurred. The liability for defective goods is included in warranty provisions on the condensed consolidated balance sheets.

Changes in the Company’s obligations for return and allowance programs are presented in the following table:

	Three Months Ended	
	June 30, 2014	June 30, 2013
Estimated return and allowance liabilities at beginning of period	\$235,172	\$215,471
Costs accrued for new estimated returns and allowances	54,002	48,741
Return and allowance obligations honored	(132,350)	(129,942)
Estimated return and allowance liabilities at end of period	\$156,824	\$134,270

**NOTE 16 – SUBSEQUENT EVENTS**

On July 14, 2014, the Company executed a three-year revolving credit facility with PNC Bank, National Association that replaced the existing line of credit agreement with Crestmark (See Note 7 – LINE OF CREDIT).

**ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS**

**FORWARD-LOOKING STATEMENTS**

The following discussion should be read in conjunction with the condensed consolidated financial statements and notes included elsewhere in this quarterly report. This document contains certain forward-looking statements including, among others, anticipated trends in our financial condition and results of operations and our business strategy. (See Part II, Item 1A, "Risk Factors "). These forward-looking statements are based largely on our current expectations and are subject to a number of risks and uncertainties. Actual results could differ materially from these forward-looking statements.

Statements included in this quarterly report that do not relate to present or historical conditions are called “forward-looking statements.” Such forward-looking statements involve known and unknown risks and uncertainties and other factors that could cause actual results or outcomes to differ materially from those expressed in, or implied by, the forward-looking statements. Forward-looking statements may include, without limitation, statements relating to our plans, strategies, objectives, expectations and intentions. Words such as “believes,” “forecasts,” “intends,” “possible,” “estimates,” “anticipates,” “expects,” “plans,” “should,” “could,” “will,” and similar expressions are intended to identify forward-looking statements. Our ability to predict or project future results or the effect of events on our operating results is inherently uncertain. Forward-looking statements should not be read as a guarantee of future performance or results, and will not necessarily be accurate indications of the times at, or by which, such performance or results will be achieved.

Important factors to consider in evaluating such forward-looking statements include, but are not limited to: (i) changes in external factors or in our internal budgeting process which might impact trends in our results of operations; (ii) unanticipated working capital or other cash requirements; (iii) changes in our business strategy or an inability to execute our strategy due to unanticipated changes in the industries in which we operate; and (iv) the effects of adverse general economic conditions, both within the United States and globally, (v) vendor price increases and decreased margins due to competitive pricing during the economic downturn (vi) various competitive market factors that may prevent us from competing successfully in the marketplace and (vii) other factors described in the risk factors section of our Annual Report on Form 10-K, this Quarterly Report on 10-Q, or in our other filings made with the SEC.

Readers are cautioned not to place undue reliance on these forward-looking statements, which reflect management's opinions only as of the date hereof. We undertake no obligation to revise or publicly release the results of any revision to these forward-looking statements.

## **OVERVIEW**

The Singing Machine Company, Inc., a Delaware corporation, (the “Singing Machine,” “we,” “us,” “our” or “the Company”) and our subsidiaries are primarily engaged in the design, marketing, and sale of consumer karaoke audio systems, accessories and musical recordings. The Company’s products are sold directly to distributors and retail customers. Our electronic karaoke machines and audio software products are marketed under The Singing Machine(R) and SoundX® trademarks.

Our products are sold throughout North America and Europe, primarily through major mass merchandisers and warehouse clubs, on-line retailers and to a lesser extent department stores, lifestyle merchants, direct mail catalogs and showrooms, music and record stores, and specialty stores.



Representative customers include Amazon, Best Buy, BJ's Wholesale, Costco, Sam's Club, Target, Toys R Us, and Wal-Mart. Our business has historically been subject to seasonal fluctuations causing our revenues to vary from quarter to quarter and between the same periods in different fiscal years. Our products are manufactured for the most part based on the purchase indications of our customers. We are uncertain of how significantly our business would be harmed by a prolonged economic recession, but we anticipate that continued contraction of consumer spending would negatively affect our revenues and profit margins.

## **RESULTS OF OPERATIONS**

The following table sets forth, for the periods indicated, certain items related to our consolidated statements of operations as a percentage of net sales for the three months ended June 30, 2014 and 2013.

**The Singing Machine Company, Inc. and Subsidiaries****CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS**

	For Three Months Ended			
	June 30, 2014		June 30, 2013	
Net Sales	100.0	%	100.0	%
Cost of Goods Sold	79.7	%	78.7	%
Gross Profit	20.3	%	21.3	%
Operating Expenses				
Selling expenses	13.6	%	19.9	%
General and administrative expenses	36.4	%	60.8	%
Depreciation and amortization	1.2	%	1.9	%
Total Operating Expenses	51.2	%	82.6	%
Loss from Operations	-30.9	%	-61.3	%
Other Expenses				
Interest expense	-0.1	%	-0.1	%
Loss before income tax benefit	-31.0	%	-61.4	%
Income tax benefit	11.4	%	23.1	%
Net Income	-19.6	%	-38.3	%

**QUARTER ENDED JUNE 30, 2014 COMPARED TO THE QUARTER ENDED JUNE 30, 2013****NET SALES**

Net sales for the quarter ended June 30, 2014 increased to \$2,544,959 from \$1,413,567, an increase of \$1,131,192 as compared to the same period ended June 30, 2013. This increase was primarily due to an increase in direct import sales to distributors in Mexico and the UK of approximately \$348,000 and an increase in sales to three major retail customers whose existing inventory required replenishment due to strong Christmas holiday sell-through in order to meet expected spring and summer sales

expectations.

## **GROSS PROFIT**

Gross profit for the quarter ended June 30, 2014 increased to \$515,891 from \$301,424 an increase of \$214,467 as compared to the same period in the prior year. This increase was primarily due to the increased sales to two direct import distributors and three major retail customers in the quarter as compared to the same quarter in the prior year.

As a percentage of revenues, gross profit margin for the three months ended June 30, 2014 was 20.3% compared to 21.3% for the three months ended June 30, 2013. This 1.0% decrease in gross profit margin points was primarily due to the sale of direct import goods to distributors in Mexico and the United Kingdom which yielded lower gross profit margins of 8.9% adversely affecting the overall gross margin percentage by approximately 2.3%. The decrease in gross profit points from sales to distributors was offset by a more favorable mix of products sold to domestic customers for the quarter ended June 30, 2014 compared to June 30, 2013 and accounted for most of the remaining difference in gross profit margin.

## **OPERATING EXPENSES**

For the quarter ended June 30, 2014, total operating expenses increased to \$1,303,469. This represents an increase in total operating expenses of \$135,606 from the quarter ended June 30, 2013 which were \$1,167,863. Selling expenses increased by \$64,493 as there was an increase in advertising allowance expense and sales commission expenses of approximately \$99,000 and \$20,000, respectively which was commensurate with the increase in sales. These costs were offset by a decrease in marketing expenses of approximately \$44,000 due to lowered expenditures associated with the test marketing of the Home™ product line during the previous season and a decrease in prior year one-time royalty expense of approximately \$32,000. The remaining variance was due to an increase of approximately \$21,000 in other variable selling expenses which were higher due to the increase in sales volume.

General and administrative expenses increased \$69,100 to \$928,871 for the three months ended June 30, 2014 compared to \$859,771 for the same period ended June 30, 2013. Due to declining domestic sales by related parties, our warehouse and logistics services support to related parties decreased significantly during the period and as a result we were reimbursed approximately \$38,000 less for these services compared to the same quarter in the prior year. The remaining variance in general and administrative expense is primarily due to employee stock option compensation of approximately \$30,000 associated with stock options issued to key employees on July 1, 2013 and expensed over a one-year vesting period.

### **LOSS FROM OPERATIONS**

Loss from operations decreased \$78,661 this quarter to \$787,578 for the three months ended June 30, 2014 compared to a loss from operations of \$866,439 for the same period ended June 30, 2013. An increase in gross profit margin contributed approximately \$214,000 to the decreased loss due to increased sales as explained in Net Sales and Gross Profit above and was offset by an increase in selling, general and administration expenses of approximately \$135,000 as discussed in Operating Expenses above.

### **INCOME TAXES**

The Company recorded an income tax benefit of approximately \$290,000 due to the loss from operations during the three months ended June 30, 2014 which generated an additional current deferred tax asset of approximately \$290,000 as of June 30, 2014. The income tax benefit was based on management's best estimate of the Company's full year effective tax rate of approximately 37%. Due to the seasonality of the business, the Company is expected to fully reverse this increase in deferred tax asset during the fiscal year ending March 31, 2015. For the three months ended June 30, 2013, the Company recorded an income tax benefit of approximately \$326,000 due to the loss from operations which generated an additional current deferred tax asset of approximately \$326,000 as of June 30, 2013.

### **NET LOSS**

For the three months ended June 30, 2014 net loss decreased to \$499,529 compared to a net loss of \$541,066 for the same period a year ago. The decrease in net loss was primarily due to the same reasons discussed in loss from operations and income taxes.

## LIQUIDITY AND CAPITAL RESOURCES

As of June 30, 2014, Singing Machine had cash on hand of \$502,872 of which \$138,042 was restricted as collateral for a stand-by letter of credit as compared to cash on hand of \$408,755 of which \$137,967 was restricted as collateral for a stand-by letter of credit on June 30, 2013. We had working capital of \$875,800 as of June 30, 2014.

Net cash used in operating activities was \$1,037,701 for the three months ended June 30, 2014, as compared to \$1,120,168 used in operating activities the same period a year ago. During the three month period ending June 30, 2014 there was a loss before income tax benefit of approximately \$790,000 due primarily to increased gross profit margin offset by increased selling and administrative expenses as explained in Net Sales, Gross Profit and Operating Expenses above. The Company also increased its accounts payable and net due to related parties by approximately \$5,500,000 which was offset by an increase in inventory of approximately \$5,700,000 during the three month period ended June 30, 2014 in anticipation of upcoming seasonal customer sales.

Net cash used in operating activities was \$1,120,168 for the three months ended June 30, 2013. During the three month period ending June 30, 2013 there was a net loss of approximately \$541,000 due primarily to lower gross profit margin on the mix of products sold, increased selling and administrative expenses associated with the planned launch of a new product line and a decrease in the amount of warehouse expense reimbursements from related parties. The Company also reduced its net due to related parties by approximately \$593,000 during the three month period ended June 30, 2013.

Net cash used by investing activities for the three months ended June 30, 2014 was \$33,013 as compared to \$260,144 used by investing activities for the same period ended a year ago. This decrease in investment activity was due to a decrease in investment of tooling and molds for new products during the three month period ended June 30, 2014 as compared to the three months ended June 30, 2013 when the company invested in tooling and molds for new products of approximately \$138,000 as well as forklift trucks, furniture and warehouse racking for the new California warehouse facility totaling approximately \$122,000. In addition, during the three month period ended June 30, 2013, we deposited approximately \$138,000 in a restricted certificate of deposit with Wells Fargo Bank as collateral for a stand-by letter of credit issued to Majestic Realty (new California warehouse's landlord) as a security deposit required by the property lease.

Net cash used by investing activities for the three months ended June 30, 2013 was \$260,144. This increase in investment activity was due to additional investment during the three month period ended June 30, 2013.

Net cash provided by financing activities for the three month period ended June 30, 2014 was \$81,445 compared to cash used in financing activities of \$1,896 for the same period ended a year ago. Financing activities for the three month period ended June 30, 2014 included net borrowings from the existing line of credit of \$84,414 offset by payments on long-term-capital lease of \$2,969. Financing activities for the three month period ended June 30, 2013 consisted of payments on long-term-capital lease of \$1,896.

Forward-looking liquidity and capital resources: As previously announced, SMC on July 14, 2014 entered into a 3-year Revolving Credit Facility with PNC Bank which provides for a near-tripling of our credit availability and at more attractive pricing than the previous factoring arrangement with Crestmark Bank. In addition to our current bank financing, the Starlight Group (“Group”) has expressed their willingness and ability to provide extended payment terms to us for key vendor payments primarily by extending longer payment terms for goods they manufacture for us. We do not believe we will require any bridge financing from the Group for the fiscal year ending March 31, 2015, however we will continue to take advantage of extended terms for trade payables with the Group throughout the year. During the three months ended June 30, 2014, our related party debt increased by approximately \$643,000 primarily due to increases in related-party inventory purchases in anticipation of the upcoming peak season selling period. Taking into account internally generated funds and credit facilities available to the Group we have concluded that our parent will have sufficient working capital to provide extended trade payable terms to us for at least the next 12 months.

Our average monthly general and administrative expenses are approximately \$310,000. We expect that we will require approximately \$930,000 for working capital during the next three-month period.

During the next 12 month period, we plan on financing our operation needs by:

- Collecting our existing accounts receivable;
- Selling existing inventory;
- Vendor financing;
- Borrowing from the Revolving Credit facility;
- Extended payment terms from our majority shareholder;
- Fees for fulfillment, delivery and returns services from related and non-related parties.

Our sources of cash for working capital in the long term, 12 months and beyond are essentially the same as our sources during the short term. As of July 14, 2014, we have secured an asset based lending facility with PNC Bank N.A. which provides for a maximum loan amount of \$15,000,000 during peak selling season and reduces to \$7,500,000 during the off-peak season. We believe this credit facility will be adequate to maintain and grow our business during the three-year term of the agreement. If we are unable to comply with the financial covenants defined in the financing agreement and default on the credit facility, it may have a material adverse effect on our ability to meet our financial obligations and to continue as a going concern.

## **INVENTORY SELL THROUGH**

We monitor the inventory levels and sell through activity of our major customers to properly anticipate defective returns and maintain the appropriate level of inventory. We believe that our warranty provision reflects the proper amount of reserves to cover potential defective sales returns based on historical return ratios and information available from the customers.

## **SEASONAL AND QUARTERLY RESULTS**

Historically, our operations have been seasonal, with the highest net sales occurring in our second and third fiscal quarters (reflecting increased orders for systems and music merchandise during the Christmas holiday season) and to a lesser extent the first and fourth quarters of the fiscal year. Sales in our second and third fiscal quarters, combined, accounted for approximately 88.1% and 90.0% of net sales in fiscal 2014 and 2013, respectively.

Our results of operations may also fluctuate from quarter to quarter as a result of the amount and timing of orders placed and shipped to customers, as well as other factors. The fulfillment of orders can therefore significantly affect results of operations on a quarter-to-quarter basis.

We are currently developing and considering selling products other than those within the karaoke category during the slow season to fulfill the revenue shortfall.

## **INFLATION**

Inflation has not had a significant impact on our operations. We generally have adjusted our prices to track changes in the Consumer Price Index since prices we charge are generally not fixed by long-term contracts.

## **OFF-BALANCE SHEET ARRANGEMENTS**

We do not have any off balance sheet arrangements that are reasonably likely to have a current or future effect on our financial condition, revenues, results of operations, liquidity or capital expenditures.



## **CRITICAL ACCOUNTING POLICIES**

We prepared our condensed consolidated financial statements in accordance with accounting principles generally accepted in the United States of America. As such, management is required to make certain estimates, judgments and assumptions that it believes are reasonable based on the information available. These estimates and assumptions affect the reported amounts of assets and liabilities at the date of the condensed consolidated financial statements and the reported amounts of revenues and expenses for the periods presented. The significant accounting policies which management believes are the most critical to aid in fully understanding and evaluating our reported financial results include: accounts receivable allowance for doubtful accounts, reserves on inventory, deferred tax assets and our Macau income tax exemption.

**COLLECTIBILITY OF ACCOUNTS RECEIVABLE.** Our allowance for doubtful accounts is based on management's estimates of the creditworthiness of our customers, current economic conditions and historical information, and, in the opinion of management, is believed to be an amount sufficient to respond to normal business conditions. Management sets 100% reserves for customers in bankruptcy and other reserves based upon historical collection experience. Should business conditions deteriorate or any major customer default on its obligations to the Company, this allowance may need to be significantly increased, which would have a negative impact on operations.

**RESERVES ON INVENTORIES.** We establish a reserve on inventory based on the expected net realizable value of inventory on an item-by-item basis when it is apparent that the expected realizable value of an inventory item falls below its original cost. A charge to cost of sales results when the estimated net realizable value of specific inventory items declines below cost. Management regularly reviews the Company's investment in inventories for such declines in value.

**INCOME TAXES.** Significant management judgment is required in developing our provision for income taxes, including the determination of foreign tax liabilities, deferred tax assets and liabilities and any valuation allowances that might be required against the deferred tax assets. Management evaluates its ability to realize its deferred tax assets on a quarterly basis and adjusts its valuation allowance when it believes that it is more likely than not that the asset will not be realized.

We operate within multiple taxing jurisdictions and are subject to audit in those jurisdictions. Because of the complex issues involved, any claims can require an extended period to resolve. In management's opinion, adequate provisions for potential income taxes in the jurisdiction have been made.

**USE OF OTHER ESTIMATES.** We make other estimates in the ordinary course of business relating to sales returns and allowances, warranty reserves, and reserves for promotional incentives. Historically, past changes to these estimates have not had a material impact on our financial condition. However, circumstances could change which may alter future expectations.

## **RECENT ACCOUNTING PRONOUNCEMENTS**

In May 2014, the Financial Accounting Standards Board issued Accounting Standards Update (“ASU”) 2014-09 which outlines a single comprehensive model for companies to use when accounting for revenue arising from contracts with customers. The core principle of the revenue recognition model is that an entity recognizes revenue to depict the transfer of goods and services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. In order to achieve this core principle a company must apply the following steps in determining revenue recognition:

- Identify the contract(s) with a customer.
- Identify the performance obligations in the contract.
- Determine the transaction price.
- Allocate the transaction price to the performance obligations in the contract.
- Recognize revenue when (or as) the entity satisfies a performance obligation.

The amendments in this ASU are effective for annual reporting periods beginning after December 15, 2016 including interim periods within that reporting period with early application not allowed. Management is currently assessing whether the implementation of ASU 2014-09 will have any material effect on the company’s consolidated financial statements.

In June 2014, the FASB issued ASU 2014-12, *Accounting for Share-Based Payments When the Terms of an Award Provide That a Performance Target Could Be Achieved after the Requisite Service Period*. The ASU clarifies that entities should treat performance targets that can be met after the requisite service period of a share-based payment award as performance conditions that affect vesting. An entity would not record compensation expense (measured as of the grant date without taking into account the effect of the performance target) related to an award for which transfer to the employee is contingent on the entity’s satisfaction of a performance target until it becomes probable that the performance target will be met. The ASU is effective for all entities for reporting periods beginning

after December 15, 2015. Management does not believe the implementation of ASU 2014-12 will have any material effect on the company's consolidated financial statements.

**ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK**

Not required for small reporting companies.

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#### ITEM 4. CONTROLS AND PROCEDURES

(a) ***Evaluation of Disclosure Controls and Procedures.*** As of the end of the period covered by this report, we conducted an evaluation, under the supervision and with the participation of our chief executive officer and chief financial officer of our disclosure controls and procedures (as defined in Rule 13a-15(e) and Rule 15d-15(e) of the Exchange Act). Based upon this evaluation, our chief executive officer and chief financial officer concluded that our disclosure controls and procedures were not effective to ensure that information required to be disclosed by us in the reports that we file or submit under the Exchange Act is recorded, processed, summarized and reported, within the time periods specified in the Commission's rules and forms and is accumulated and communicated to the Company's management, including its Chief Executive Officer and Chief Financial Officer, as appropriate, to allow timely decisions regarding required disclosure. Based upon this evaluation, our Chief Executive Officer and Chief Financial Officer concluded that our disclosure controls and procedures were not effective, as a result of a material weakness as identified in (b) below.

(b) ***Changes in Internal Controls.*** In our Annual Report for Fiscal 2014, we concluded that our internal control over financial reporting was not effective and identified a material weakness due to a deficiency in controls over matching and recording of invoices for inventory goods received. The Company's procedures were inadequate to ensure that invoices for goods received were properly matched to a receiving log and recorded or accrued in accounts payable. Since the filing of the Annual Report for Fiscal 2014, the CFO has initiated remediation of this material weakness by implementing the following procedures during the quarter ended June 30, 2014:

- Prepared checklist of items to be identified during the reconciliation and review process.
  - Reconciliation of an independently prepared monthly invoice log to invoices recorded or accrued in accounts payable.
  - Cross referencing invoice logs to the detailed shipped container log to identify and resolve any discrepancies.
  - Ensure that all invoices related to received and in-transit goods are timely recorded.
- We will continue to monitor the remediation process and procedures implemented to ensure that the identified material weakness has been fully addressed.

There were no other changes in the Company's internal controls over financial reporting during the quarter ended June 30, 2014 that materially affected, or were reasonably likely to materially affect, the Company's internal control over financial reporting, other than the remediation measures described above.

#### PART II - OTHER INFORMATION

**ITEM 1. LEGAL PROCEEDINGS**

Management is currently not aware of any legal proceedings.

**ITEM 1A. RISK FACTORS**

Not applicable for smaller reporting companies

**ITEM 2. UNREGISTERED SALES OF EQUITY SECURITIES AND USE OF PROCEEDS**

None

**ITEM 3. DEFAULTS UPON SENIOR SECURITIES**

We are not currently in default upon any of our senior securities.

**ITEM 4. MINE SAFETY DISCLOSURES**

None.

**ITEM 5. OTHER INFORMATION**

None.

**ITEM 6. EXHIBITS**

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31.1 Certification of Gary Atkinson, Chief Executive Officer pursuant to Rule 13a-14(a) of the Securities Exchange Act of 1934, as amended.\*

31.2 Certification of Lionel Marquis, Chief Financial Officer pursuant to Rule 13a-14(a) of the Securities Exchange Act of 1934, as amended.\*

32.1 Certifying Statement of the Chief Executive Officer pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act.\*

32.2 Certifying Statement of the Chief Financial Officer pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act.\*

\* Filed herewith

**SIGNATURES**

Pursuant to the requirements of the Securities and Exchange Act of 1934, the Registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

**THE SINGING MACHINE COMPANY, INC.**

Date: August 14, 2014 By: */s/ Gary Atkinson*  
Gary Atkinson  
Chief Executive Officer

*/s/ Lionel Marquis*  
Lionel Marquis  
Chief Financial Officer