

PDC ENERGY, INC.
Form 10-Q
October 31, 2013
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UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

FORM 10-Q

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

For the quarterly period ended September 30, 2013

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 000-07246
PDC ENERGY, INC.
(Exact name of registrant as specified in its charter)

Nevada
(State of incorporation)
1775 Sherman Street, Suite 3000
Denver, Colorado 80203
(Address of principal executive offices) (Zip code)

95-2636730
(I.R.S. Employer Identification No.)

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 T No £

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

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

Large accelerated filer x

Accelerated filer o

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Non-accelerated filer

(Do not check if a smaller reporting company)

Smaller reporting company

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

Indicate the number of shares outstanding of each of the issuer's classes of common stock, as of the latest practicable date: 35,653,050 shares of the Company's Common Stock (\$0.01 par value) were outstanding as of October 18, 2013.

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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") and Section 21E of the Securities Exchange Act of 1934 ("Exchange Act") regarding our business, financial condition, results of operations and prospects. All statements other than statements of historical facts included in and incorporated by reference into this report are "forward-looking statements" within the meaning of the safe harbor provisions of the United States ("U.S.") Private Securities Litigation Reform Act of 1995. Words such as expects, anticipates, intends, plans, believes, seeks, estimates and similar expressions or variations of such words are intended to identify forward-looking statements herein. These statements relate to, among other things: estimated crude oil, natural gas and natural gas liquids ("NGLs") reserves; future production (including the components of such production), sales, expenses, cash flows and liquidity; that our evaluation method is appropriate and consistent with those used by other market participants; anticipated capital projects, expenditures and opportunities; future exploration, drilling and development activities; our drilling programs; expected timing of additional rigs in the Wattenberg Field; availability of additional midstream facilities and services, timing of that availability and related benefits to us; impact of recent flooding in the Wattenberg Field; availability of sufficient funding for the remainder of our 2013 and 2014 capital program and sources of that funding, including our partnership repurchase obligation; expected use of the net proceeds from our August 2013 equity offering; expected use of proceeds from the potential sale of the upper Devonian assets; the impact of high line pressures and the expected impact of the O'Connor (formerly known as LaSalle) gas plant; our compliance with debt covenants; PDCM's compliance with its debt covenants and transactions to maintain compliance and/or reduce its indebtedness; potential future transactions; the borrowing base under our credit facility; our expected funding source for payments under our 3.25% Convertible Senior Notes due 2016; impact of litigation on our results of operations and financial position; effectiveness of our derivative program in providing a degree of price stability; that we do not expect to pay dividends in the foreseeable future; and our future strategies, plans and objectives.

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. Consequently, forward-looking statements are inherently subject to risks and uncertainties, including known and unknown risks and uncertainties incidental to the exploration for, and the acquisition, development, production and marketing of, crude oil, natural gas and NGLs, and actual outcomes may differ materially from the results and outcomes discussed in the forward-looking statements.

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

- changes in production volumes and worldwide demand, including economic conditions that might impact demand;
- volatility of commodity prices for crude oil, natural gas and NGLs;
- the impact of governmental policies and/or regulations, including changes in environmental and other laws, the interpretation and enforcement related to those laws and regulations, liabilities arising thereunder and the costs to comply with those laws and regulations;
- potential declines in the value of our crude oil and natural gas 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 to be greater than expected;
- timing and extent of our success in discovering, acquiring, developing and producing reserves;
- our ability to secure leases, drilling rigs, supplies and services at reasonable prices;
- timing of the connection of our Utica Basin wells to gathering, processing, fractionation and transportation infrastructure;

- timing and receipt of necessary regulatory permits;
- risks incidental to the drilling and operation of crude oil and natural gas wells;
- our future cash flows, liquidity and financial condition;
- competition within the oil and gas industry;
- availability and cost of capital;
- reductions in the borrowing base under our revolving credit facility;
- availability of sufficient pipeline, gathering and other transportation facilities and related infrastructure to process and transport our production, particularly in the Wattenberg Field and Utica Shale, and the impact of these facilities on the prices we receive for our production;
- our success in marketing crude oil, natural gas and NGLs;
- effect of crude oil and natural gas derivatives 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 expenditures;
- purchase price or other adjustments relating to asset acquisitions or dispositions that may be unfavorable to us;
- 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, 2012 ("2012

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Form 10-K"), filed with the U.S. Securities and Exchange Commission ("SEC") on February 27, 2013, and in our Current Report on Form 8-K filed on June 28, 2013, 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 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 and PDC Mountaineer, LLC ("PDCM"), a joint venture currently owned 50% each by PDC and Lime Rock Partners, LP, formed for the purpose of exploring and developing the Marcellus Shale formation in the Appalachian Basin. Unless the context otherwise requires, references in this report to "Appalachian Basin" refers to our operations in the Utica Shale in Ohio and Marcellus Shale in West Virginia and Pennsylvania, including PDC's proportionate share of our affiliated partnerships' and PDCM's assets, results of operations, cash flows and operating activities. See Note 1, Nature of Operations and Basis of Presentation, to our condensed consolidated financial statements included elsewhere in this report for a description of our consolidated subsidiaries.

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ITEM 1. FINANCIAL STATEMENTS

PDC ENERGY, INC.

Condensed Consolidated Balance Sheets

(unaudited; in thousands, except share and per share data)

| | September 30, 2013 | December 31, 2012 |
|--|--------------------|-------------------|
| Assets | | |
| Current assets: | | |
| Cash and cash equivalents | \$298,488 | \$2,457 |
| Restricted cash | 3,950 | 3,942 |
| Accounts receivable, net | 56,181 | 64,880 |
| Accounts receivable affiliates | 4,784 | 4,842 |
| Fair value of derivatives | 9,660 | 52,042 |
| Deferred income taxes | 22,238 | 36,151 |
| Prepaid expenses and other current assets | 9,073 | 7,635 |
| Total current assets | 404,374 | 171,949 |
| Properties and equipment, net | 1,539,701 | 1,616,706 |
| Assets held for sale | 29,034 | — |
| Fair value of derivatives | 5,922 | 6,883 |
| Other assets | 31,932 | 31,310 |
| Total Assets | \$2,010,963 | \$1,826,848 |
| Liabilities and Shareholders' Equity | | |
| Liabilities | | |
| Current liabilities: | | |
| Accounts payable | \$93,520 | \$82,716 |
| Accounts payable affiliates | 44 | 5,296 |
| Production tax liability | 23,867 | 25,899 |
| Fair value of derivatives | 14,623 | 18,439 |
| Funds held for distribution | 29,753 | 34,228 |
| Current portion of long-term debt | -104,050 | — |
| Accrued interest payable | 19,874 | 11,056 |
| Other accrued expenses | 25,720 | 25,715 |
| Total current liabilities | 311,451 | 203,349 |
| Long-term debt | 549,750 | 676,579 |
| Deferred income taxes | 112,800 | 148,427 |
| Asset retirement obligation | 35,654 | 61,563 |
| Fair value of derivatives | 6,573 | 10,137 |
| Liabilities held for sale | 22,788 | — |
| Other liabilities | 20,849 | 23,612 |
| Total liabilities | 1,059,865 | 1,123,667 |
| Commitments and contingent liabilities | | |
| Shareholders' equity | | |
| Preferred shares - par value \$0.01 per share, 50,000,000 shares authorized, none issued | — | — |

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| | | | |
|---|-------------|-------------|---|
| Common shares - par value \$0.01 per share, 100,000,000 authorized, 35,657,872 and 30,294,224 issued as of September 30, 2013 and December 31, 2012, respectively | 357 | 303 | |
| Additional paid-in capital | 670,990 | 387,494 | |
| Retained earnings | 280,068 | 315,568 | |
| Treasury shares - at cost, 7,114 and 5,059 as of September 30, 2013 and December 31, 2012, respectively | (317 |) (184 |) |
| Total shareholders' equity | 951,098 | 703,181 | |
| Total Liabilities and Shareholders' Equity | \$2,010,963 | \$1,826,848 | |

See accompanying Notes to Condensed Consolidated Financial Statements

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PDC ENERGY, INC.

Condensed Consolidated Statements of Operations
(unaudited; in thousands, except per share data)

| | Three Months Ended September | | Nine Months Ended September | |
|--|------------------------------|-------------|-----------------------------|-------------|
| | 30, | | 30, | |
| | 2013 | 2012 | 2013 | 2012 |
| Revenues: | | | | |
| Crude oil, natural gas and NGLs sales | \$82,136 | \$52,291 | \$239,112 | \$170,588 |
| Sales from natural gas marketing | 16,946 | 11,178 | 48,695 | 31,172 |
| Commodity price risk management gain (loss), net | (23,638) |) (31,943 |) (21,269 |) 18,287 |
| Well operations, pipeline income and other | 1,672 | 1,194 | 3,709 | 3,419 |
| Total revenues | 77,116 | 32,720 | 270,247 | 223,466 |
| Costs, expenses and other: | | | | |
| Production costs | 19,057 | 15,797 | 51,091 | 41,106 |
| Cost of natural gas marketing | 17,127 | 11,260 | 48,928 | 30,841 |
| Exploration expense | 2,030 | 1,773 | 5,156 | 6,019 |
| Impairment of crude oil and natural gas properties | 4,472 | 388 | 52,433 | 1,332 |
| General and administrative expense | 16,080 | 13,710 | 46,978 | 42,796 |
| Depreciation, depletion, and amortization | 30,870 | 22,121 | 86,619 | 73,872 |
| Accretion of asset retirement obligations | 1,186 | 1,101 | 3,506 | 2,560 |
| Gain on sale of properties and equipment | (712) |) (1,508 |) (759 |) (3,908) |
| Total cost, expenses and other | 90,110 | 64,642 | 293,952 | 194,618 |
| Income (loss) from operations | (12,994) |) (31,922 |) (23,705 |) 28,848 |
| Interest expense | (12,509) |) (11,360 |) (38,955 |) (31,857) |
| Interest income | 130 | 3 | 133 | 5 |
| Loss from continuing operations before income taxes | (25,373) |) (43,279 |) (62,527 |) (3,004) |
| Provision for income taxes | 10,155 | 15,268 | 22,856 | 935 |
| Loss from continuing operations | (15,218) |) (28,011 |) (39,671 |) (2,069) |
| Income (loss) from discontinued operations, net of tax | (782) |) (4,632 |) 4,171 | (2,468) |
| Net loss | \$(16,000) |) \$(32,643 |) \$(35,500) |) \$(4,537) |
| Earnings per share: | | | | |
| Basic | | | | |
| Loss from continuing operations | \$(0.46) |) \$(0.93 |) \$(1.26 |) \$(0.08) |
| Income (loss) from discontinued operations | (0.02) |) (0.15 |) 0.13 | (0.09) |
| Net loss | \$(0.48) |) \$(1.08 |) \$(1.13 |) \$(0.17) |
| Diluted | | | | |
| Loss from continuing operations | \$(0.46) |) \$(0.93 |) \$(1.26 |) \$(0.08) |
| Income (loss) from discontinued operations | (0.02) |) (0.15 |) 0.13 | (0.09) |
| Net loss | \$(0.48) |) \$(1.08 |) \$(1.13 |) \$(0.17) |
| Weighted-average common shares outstanding: | | | | |
| Basic | 33,413 | 30,214 | 31,350 | 26,819 |
| Diluted | 33,413 | 30,214 | 31,350 | 26,819 |

See accompanying Notes to Condensed Consolidated Financial Statements

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PDC ENERGY, INC.

Condensed Consolidated Statements of Cash Flows
(unaudited; in thousands)

| | Nine Months Ended September 30, | |
|--|---------------------------------|------------|
| | 2013 | 2012 |
| Cash flows from operating activities: | | |
| Net loss | \$(35,500 |) \$(4,537 |
| Adjustments to net loss to reconcile to net cash from operating activities: | | |
| Unrealized loss on derivatives, net | 32,057 | 20,917 |
| Depreciation, depletion and amortization | 88,877 | 106,745 |
| Impairment of crude oil and natural gas properties | 52,436 | 1,418 |
| Exploratory dry hole costs | — | 1,043 |
| Accretion of asset retirement obligation | 3,667 | 2,839 |
| Stock-based compensation | 9,991 | 6,126 |
| (Gain) loss on sale of properties and equipment | 1,571 | (23,828 |
| Amortization of debt discount and issuance costs | 5,093 | 5,082 |
| Deferred income taxes | (21,714 |) (7,090 |
| Other | (1,017 |) 4,674 |
| Changes in assets and liabilities | (15,918 |) 13,786 |
| Net cash from operating activities | 119,543 | 127,175 |
| Cash flows from investing activities: | | |
| Capital expenditures | (256,096 |) (271,769 |
| Acquisition of oil and gas properties | — | (309,285 |
| Proceeds from acquisition adjustments | 7,579 | 11,969 |
| Proceeds from sale of properties and equipment | 178,987 | 192,040 |
| Increase in restricted cash | — | (17,497 |
| Net cash from investing activities | (69,530 |) (394,542 |
| Cash flows from financing activities: | | |
| Proceeds from revolving credit facility | 252,500 | 591,250 |
| Repayment of revolving credit facility | (278,000 |) (492,250 |
| Proceeds from sale of common stock, net of issuance costs | 275,847 | 164,496 |
| Other | (4,329 |) (1,460 |
| Net cash from financing activities | 246,018 | 262,036 |
| Net change in cash and cash equivalents | 296,031 | (5,331 |
| Cash and cash equivalents, beginning of period | 2,457 | 8,238 |
| Cash and cash equivalents, end of period | \$298,488 | \$2,907 |
| Supplemental cash flow information: | | |
| Cash payments for: | | |
| Interest, net of capitalized interest | \$26,408 | \$30,868 |
| Income taxes | 525 | 1,830 |
| Non-cash investing activities: | | |
| Change in accounts payable related to purchases of properties and equipment | \$24,308 | \$(9,514 |
| Change in asset retirement obligation, with a corresponding change to crude oil and natural gas properties, net of disposals | 337 | 11,871 |

See accompanying Notes to Condensed Consolidated Financial Statements

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PDC ENERGY, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

SEPTEMBER 30, 2013

(Unaudited)

NOTE 1 - NATURE OF OPERATIONS AND BASIS OF PRESENTATION

PDC Energy, Inc. ("PDC," "PDC Energy," "we," "us" or "the Company") is a domestic independent crude oil, natural gas and NGL company engaged in the exploration for and the acquisition, development, production and marketing of crude oil, natural gas and NGLs. PDC is focused operationally on the liquid-rich Wattenberg Field in the DJ Basin and, in the Appalachian Basin, on the liquid-rich Utica Shale and the dry-gas Marcellus Shale formations. As of September 30, 2013, we owned an interest in approximately 6,250 gross wells. We are engaged in two business segments: (1) Oil and Gas Exploration and Production and (2) Gas Marketing.

The accompanying unaudited condensed consolidated financial statements include the accounts of PDC, our wholly owned subsidiaries, and our proportionate share of PDC Mountaineer, LLC ("PDCM") and our 21 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 only normal recurring adjustments) necessary for a fair presentation 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 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 2012 Form 10-K. Our results of operations and cash flows for the three and nine months ended September 30, 2013 are not necessarily indicative of the results to be expected for the full year or any other future period.

Certain reclassifications have been made to prior period financial statements to conform to the current year presentation. These reclassifications had no impact on previously reported cash flows, net income, earnings per share or shareholders' equity.

NOTE 2 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Recently Adopted Accounting Standard

On January 1, 2013, we adopted changes issued by the Financial Accounting Standards Board ("FASB") regarding the disclosure of offsetting assets and liabilities. These changes require an entity to disclose both gross and net information about both instruments and transactions eligible for offset in the statement of financial position and instruments and transactions subject to an enforceable master netting arrangement or similar agreement. The enhanced disclosures enable users of an entity's financial statements to understand and evaluate the effect or potential effect of master netting arrangements on the entity's financial position, including the effect or potential effect of rights of setoff associated with certain financial instruments and derivative instruments. Adoption of these changes had no impact on the condensed consolidated financial statements, except for additional disclosures.

Recently Issued Accounting Standard

Income Taxes. On July 18, 2013, the FASB issued an update to accounting for income taxes. The update provides clarification on the presentation of an unrecognized tax benefit when a net operating loss carryforward, a similar tax loss or a tax credit carryforward exists. The update is effective for public entities for fiscal years, and interim periods within those years, beginning after December 15, 2013. Early adoption is permitted. We are currently evaluating the impact of adopting this update on our financial statements, but do not believe it will have a material impact.

NOTE 3 - FAIR VALUE OF FINANCIAL INSTRUMENTS

Derivative 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. In these cases, 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.

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PDC ENERGY, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS - Continued

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.

We measure the fair value of our derivative instruments based on 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, the determination that the source of the inputs is valid, the 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. While we use common industry practices to develop our valuation techniques and believe our valuation method is appropriate and consistent with those used by other market participants, changes in our pricing methodologies or the underlying assumptions could result in significantly different fair values.

Our fixed-price swaps, basis swaps and physical purchases are included in Level 2 and our crude oil and natural gas collars, natural gas calls and physical sales are included in 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:

| | September 30, 2013 | | | December 31, 2012 | | |
|---------------------------------------|---|--|-----------|---|--|-----------|
| | Significant Other Observable Inputs (Level 2) (in thousands) | Significant Unobservable Inputs (Level 3) | Total | Significant Other Observable Inputs (Level 2) | Significant Unobservable Inputs (Level 3) | Total |
| Assets: | | | | | | |
| Commodity-based derivative contracts | \$ 12,328 | \$ 3,060 | \$ 15,388 | \$ 42,788 | \$ 15,734 | \$ 58,522 |
| Basis protection derivative contracts | 182 | 12 | 194 | 387 | 16 | 403 |
| Total assets | 12,510 | 3,072 | 15,582 | 43,175 | 15,750 | 58,925 |
| Liabilities: | | | | | | |
| Commodity-based derivative contracts | 17,293 | 2,340 | 19,633 | 9,839 | 2,081 | 11,920 |
| Basis protection derivative contracts | 1,563 | — | 1,563 | 16,656 | — | 16,656 |
| Total liabilities | 18,856 | 2,340 | 21,196 | 26,495 | 2,081 | 28,576 |
| Net asset (liability) | \$(6,346) |) \$ 732 | \$(5,614) |) \$ 16,680 | \$ 13,669 | \$ 30,349 |

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PDC ENERGY, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS - Continued

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

| | Three Months Ended September 30, 2013 | | Nine Months Ended September 30, 2013 | |
|---|---|------------|--|-----------|
| | 2012 | | 2012 | |
| | (in thousands) | | | |
| Fair value, net asset, beginning of period | \$3,904 | \$28,600 | \$13,669 | \$22,107 |
| Changes in fair value included in statement of operations line item: | | | | |
| Commodity price risk management gain (loss), net | (3,111 |) (9,055 |) (3,008 |) 6,098 |
| Sales from natural gas marketing | 11 | (4 |) 16 | 35 |
| Changes in fair value included in balance sheet line item: | | | | |
| Accounts payable affiliates (1) | — | (93 |) — | (240 |
| Settlements included in statement of operations line items: | | | | |
| Commodity price risk management gain (loss), net | (66 |) (3,900 |) (5,545 |) (12,357 |
| Sales from natural gas marketing | (6 |) (10 |) (34 |) (105 |
| Income (loss) from discontinued operations, net of tax | — | — | (4,366 |) — |
| Fair value, net asset end of period | \$732 | \$15,538 | \$732 | \$15,538 |
| Changes in unrealized gains (losses) relating to assets (liabilities) still held as of period-end, included in statement of operations line item: | | | | |
| Commodity price risk management gain (loss), net | \$(3,333 |) \$(8,169 |) \$(5,362 |) \$2,577 |
| Sales from natural gas marketing | (5 |) (13 |) 4 | (1 |
| Total | \$(3,338 |) \$(8,182 |) \$(5,358 |) \$2,576 |

(1) Represents the change in fair value related to derivative instruments entered into by us and designated to our affiliated partnerships.

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.

Non-Derivative Financial Assets and Liabilities

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

The portion of our debt related to our revolving credit facility, as well as our proportionate share of PDCM's credit facility and second lien term loan, 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, as of

September 30, 2013, we estimate the fair value of our 3.25% convertible senior notes due 2016 to be \$176.4 million, or 153.4% of par value, and our 7.75% senior notes due 2022 to be \$528.8 million, or 105.7% of par value. We determined these valuations based upon measurements of trading activity and broker and/or dealer quotes which are published market prices, and therefore are Level 2 inputs.

Concentration of Risk

Derivative Counterparties. Our derivative arrangements expose us to credit risk of nonperformance by our counterparties. We primarily use financial institutions who are also lenders under our revolving credit facility as counterparties to our derivative contracts. To date, we have had no counterparty default losses relating to our derivative arrangements. 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 counterparties on the fair value of our derivative instruments was not significant at September 30, 2013, taking into account the estimated likelihood of nonperformance.

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PDC ENERGY, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS - Continued

The following table presents the counterparties that expose us to credit risk as of September 30, 2013 with regard to our derivative assets:

| Counterparty Name | Fair Value of Derivative Assets As of September 30, 2013 (in thousands) |
|--|--|
| JPMorgan Chase Bank, N.A. (1) | \$4,163 |
| Wells Fargo Bank, N.A. (1) | 3,830 |
| Natixis (1) | 1,637 |
| Bank of Montreal (1) | 1,885 |
| BNP Paribas (1) | 1,285 |
| Other lenders in our revolving credit facility | 2,624 |
| Various (2) | 158 |
| Total | \$15,582 |

(1)Major lender in our revolving credit facility. See Note 7, Long-Term Debt.

(2)Represents a total of 20 counterparties.

NOTE 4 - 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 utilize the following economic hedging strategies for each of our business segments.

For crude oil and natural gas sales, we enter into derivative contracts to protect against price declines in future periods. While we structure these derivatives to reduce our exposure to changes in price associated with the derivative commodity, they also limit the benefit we might otherwise have received from price increases in the physical market.

For natural gas marketing, we enter into fixed-price physical purchase and sale agreements that qualify as derivative contracts. In order to offset the fixed-price physical derivatives in our natural gas marketing, we enter into financial derivative instruments that have the effect of locking in the prices we will receive or pay for the same volumes and period, offsetting the physical derivative.

We believe our derivative instruments continue to be effective in achieving the risk management objectives for which they were intended. As of September 30, 2013, we had derivative instruments, which were comprised of commodity floors, collars and swaps, basis protection swaps and physical sales and purchases, in place for a portion of our anticipated production through 2017 for a total of 51,305 BBTu of natural gas and 7,735 MBbls of crude oil. The majority of our derivative contracts are entered into at no cost to us as we hedge our anticipated production at the then-prevailing commodity market prices.

We have elected not to designate any of our derivative instruments as hedges and therefore do not qualify for use of hedge accounting. Accordingly, changes in the fair value of our derivative instruments are recorded in the statements of operations, with the exception of changes in fair value related to those derivatives we designated to our affiliated partnerships. Changes in the fair value of derivative instruments related to our Oil and Gas Exploration and

Production segment are recorded in commodity price risk management, net. Changes in the fair value of derivative instruments related to our Gas Marketing segment are recorded in sales from and cost of natural gas marketing. Changes in the fair value of the derivative instruments designated to our affiliated partnerships are recorded on the condensed consolidated balance sheets in accounts payable affiliates and accounts receivable affiliates. As positions designated to our affiliated partnerships settle, the realized gains and losses are netted for distribution. Net realized gains are paid to the partnerships and net realized losses are deducted from the partnerships' cash distributions from production. The affiliated partnerships bear their designated share of counterparty risk. As of September 30, 2013, our affiliated partnerships had no outstanding derivative instruments.

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PDC ENERGY, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS - Continued

The following table presents the location and fair value amounts of our derivative instruments on the condensed consolidated balance sheets as of September 30, 2013 and December 31, 2012:

| Derivatives instruments: | Balance sheet line item | Fair Value September 30, 2013 (in thousands) | December 31, 2012 |
|--|----------------------------|---|----------------------|
| Derivative assets: | | | |
| Current | | | |
| Commodity contracts | | | |
| Related to crude oil and natural gas sales | Fair value of derivatives | \$9,067 | \$47,016 |
| Related to affiliated partnerships (1) | Fair value of derivatives | — | 4,707 |
| Related to natural gas marketing | Fair value of derivatives | 444 | 302 |
| Basis protection contracts | | | |
| Related to crude oil and natural gas sales | Fair value of derivatives | 133 | — |
| Related to natural gas marketing | Fair value of derivatives | 16 | 17 |
| | | 9,660 | 52,042 |
| Non Current | | | |
| Commodity contracts | | | |
| Related to crude oil and natural gas sales | Fair value of derivatives | 5,792 | 6,671 |
| Related to natural gas marketing | Fair value of derivatives | 85 | 203 |
| Basis protection contracts | | | |
| Related to crude oil and natural gas sales | Fair value of derivatives | 44 | — |
| Related to natural gas marketing | Fair value of derivatives | 1 | 9 |
| | | 5,922 | 6,883 |
| Total derivative assets | | \$15,582 | \$58,925 |
| Derivative liabilities: Current | | | |
| Commodity contracts | | | |
| Related to crude oil and natural gas sales | Fair value of derivatives | \$12,880 | \$1,744 |
| Related to natural gas marketing | Fair value of derivatives | 310 | 226 |
| Basis protection contracts | | | |
| Related to crude oil and natural gas sales | Fair value of derivatives | 1,433 | 14,329 |
| Related to affiliated partnerships (2) | Fair value of derivatives | — | 2,140 |
| | | 14,623 | 18,439 |

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| | | | |
|--|---------------------------|----------|----------|
| Non Current | | | |
| Commodity contracts | | | |
| Related to crude oil and natural gas sales | Fair value of derivatives | 6,403 | 9,969 |
| Related to natural gas marketing | Fair value of derivatives | 40 | 168 |
| Basis protection contracts | | | |
| Related to crude oil and natural gas sales | Fair value of derivatives | 130 | — |
| | | 6,573 | 10,137 |
| Total derivative liabilities | | \$21,196 | \$28,576 |

Represents derivative positions designated to our affiliated partnerships. Accordingly, our accompanying (1)December 31, 2012 condensed consolidated balance sheet includes a corresponding payable to our affiliated partnerships representing their proportionate share of the derivative assets.

Represents derivative positions designated to our affiliated partnerships. Accordingly, our accompanying (2)December 31, 2012 condensed consolidated balance sheet includes a corresponding receivable from our affiliated partnerships representing their proportionate share of the derivative liabilities.

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PDC ENERGY, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS - Continued

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

| Statement of operations line item | 2013 | | | 2012 | | |
|--|--|---|--------------|--|---|--------------|
| | Reclassification of Realized Gains (Losses) Included in Prior Periods Unrealized (in thousands) | Realized and Unrealized Gains (Losses) For the Current Period | Total | Reclassification of Realized Gains (Losses) Included in Prior Periods Unrealized | Realized and Unrealized Gains (Losses) For the Current Period | Total |
| Three Months Ended September 30, | | | | | | |
| Commodity price risk management gain (loss), net | | | | | | |
| Realized gains (losses) | \$2,936 | \$ (4,461) | \$ (1,525) | \$15,010 | \$ (1,915) | \$13,095 |
| Unrealized losses | (2,936) | (19,177) | (22,113) | (15,010) | (30,028) | (45,038) |
| Total commodity price risk management gain (loss), net | \$— | \$ (23,638) | \$ (23,638) | \$— | \$ (31,943) | \$ (31,943) |
| Sales from natural gas marketing | | | | | | |
| Realized gains (losses) | \$249 | \$ (9) | \$240 | \$386 | \$15 | \$401 |
| Unrealized losses | (249) | (62) | (311) | (386) | (404) | (790) |
| Total sales from natural gas marketing | \$— | \$ (71) | \$ (71) | \$— | \$ (389) | \$ (389) |
| Cost of natural gas marketing | | | | | | |
| Realized gains (losses) | \$(196) | \$8 | \$(188) | \$(364) | \$ (20) | \$(384) |
| Unrealized gains | 196 | 82 | 278 | 364 | 467 | 831 |
| Total cost of natural gas marketing | \$— | \$90 | \$90 | \$— | \$447 | \$447 |
| Nine Months Ended September 30, | | | | | | |
| Commodity price risk management gain (loss), net | | | | | | |
| Realized gains (losses) | \$25,273 | \$ (14,426) | \$10,847 | \$22,813 | \$16,387 | \$39,200 |
| Unrealized gains (losses) | (25,273) | (6,843) | (32,116) | (22,813) | 1,900 | (20,913) |
| Total commodity price risk management gain (loss), net | \$— | \$ (21,269) | \$ (21,269) | \$— | \$18,287 | \$18,287 |
| Sales from natural gas marketing | | | | | | |
| Realized gains | \$206 | \$61 | \$267 | \$1,358 | \$588 | \$1,946 |
| Unrealized gains (losses) | (206) | 546 | 340 | (1,358) | (428) | (1,786) |
| Total sales from natural gas marketing | \$— | \$607 | \$607 | \$— | \$160 | \$160 |
| Cost of natural gas marketing | | | | | | |
| Realized gains (losses) | \$(133) | \$8 | \$(125) | \$(1,195) | \$ (652) | \$(1,847) |
| Unrealized gains (losses) | 133 | (414) | (281) | 1,195 | 587 | 1,782 |
| Total cost of natural gas marketing | \$— | \$ (406) | \$ (406) | \$— | \$ (65) | \$ (65) |

All of our financial derivative agreements contain master netting provisions that provide for the net settlement of all contracts through a single payment in the event of early termination. Our fixed-price physical purchase and sale agreements that qualify as derivative contracts are not subject to master netting provisions and are not significant. We have elected not to offset the fair value positions recorded on our condensed consolidated balance sheets.

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PDC ENERGY, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS - Continued

The following table reflects the impact of netting agreements on gross derivative assets and liabilities as of September 30, 2013 and December 31, 2012:

| As of | Derivatives instruments, recorded in condensed consolidated balance sheet, gross (in thousands) | Effect of master netting agreements | Derivative instruments, net |
|---------------------------------------|--|--|--------------------------------|
| As of September 30, 2013 | | | |
| Asset derivatives: | | | |
| Derivative instruments, at fair value | \$15,582 | \$(11,739 |) \$3,843 |
| Liability derivatives: | | | |
| Derivative instruments, at fair value | \$21,196 | \$(11,739 |) \$9,457 |
| As of December 31, 2012 | | | |
| Asset derivatives: | | | |
| Derivative instruments, at fair value | \$58,925 | \$(11,437 |) \$47,488 |
| Liability derivatives: | | | |
| Derivative instruments, at fair value | \$28,576 | \$(11,437 |) \$17,139 |

NOTE 5 - PROPERTIES AND EQUIPMENT

The following table presents the components of properties and equipment, net of accumulated depreciation, depletion and amortization:

| | September 30, 2013 (in thousands) | December 31, 2012 |
|--|--------------------------------------|-------------------|
| Properties and equipment, net: | | |
| Crude oil and natural gas properties | | |
| Proved | \$1,533,430 | \$2,075,924 |
| Unproved | 315,233 | 319,327 |
| Total crude oil and natural gas properties | 1,848,663 | 2,395,251 |
| Pipelines and related facilities | 15,749 | 47,786 |
| Equipment and other | 28,780 | 34,858 |
| Land and buildings | 13,612 | 14,935 |
| Construction in progress | 146,921 | 67,217 |
| Gross properties and equipment | 2,053,725 | 2,560,047 |
| Accumulated depreciation, depletion and amortization | (514,024 |) (943,341 |
| Properties and equipment, net | \$1,539,701 | \$1,616,706 |

The above decrease in property and equipment, net, includes decreases in crude oil and natural gas properties, pipelines and related facilities and equipment and other in the amount of \$780.0 million and accumulated depreciation, depletion and amortization in the amount of \$566.4 million attributable to the divestiture of our Piceance Basin, NECO and certain other non-core Colorado properties in June 2013 and the classification of our shallow upper Devonian (non-Marcellus Shale) Appalachian Basin crude oil and natural gas properties as held for sale in the condensed consolidated balance sheet as of September 30, 2013. See Note 12, Assets Held for Sale, Divestitures and Discontinued Operations, for additional information regarding these properties.

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PDC ENERGY, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS - Continued

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

| | Three Months Ended September 30, | | Nine Months Ended September 30, | |
|---|-------------------------------------|-------|------------------------------------|---------|
| | 2013 | 2012 | 2013 | 2012 |
| | (in thousands) | | | |
| Continuing operations: | | | | |
| Impairment of proved properties | \$3,750 | \$— | \$48,750 | \$— |
| Impairment of individually significant unproved properties | 154 | 154 | 979 | 462 |
| Amortization of individually insignificant unproved properties | 568 | 234 | 2,704 | 870 |
| Total continuing operations | 4,472 | 388 | 52,433 | 1,332 |
| Discontinued operations: | | | | |
| Amortization of individually insignificant unproved properties | — | 7 | 3 | 86 |
| Total discontinued operations | — | 7 | 3 | 86 |
| Total impairment of crude oil and natural gas properties | \$4,472 | \$395 | \$52,436 | \$1,418 |

In the first quarter of 2013, we recognized an impairment charge of approximately \$45.0 million related to all of our shallow upper Devonian (non-Marcellus Shale) Appalachian Basin producing properties located in West Virginia and Pennsylvania owned directly by us, as well as through our proportionate share of PDCM and our affiliated partnerships. The impairment charge represented the excess of the carrying value of the assets over the estimated fair value, less cost to sell. The fair value of the assets was determined based upon estimated future cash flows from unrelated third-party bids, a Level 3 input. Pursuant to a purchase and sale agreement dated October 8, 2013 with an unrelated third-party, we determined that the carrying value of the above-mentioned properties exceeded the transaction sales price, a Level 3 input, less costs to sell. As a result, we recognized an additional impairment charge of approximately \$3.8 million in the third quarter of 2013 to reduce the carrying value of the net assets to reflect the current net sales price. The impairment charge was included in the statement of operations line item impairment of crude oil and natural gas properties. See Note 12, Assets Held for Sale, Divestitures and Discontinued Operations, and Note 15, Subsequent Events, for additional information regarding the potential sale of these properties. We expect this sale to close in the fourth quarter of 2013. However, there can be no assurance we will be successful in closing this divestiture.

NOTE 6 - INCOME TAXES

We evaluate our estimated annual effective income tax rate on a quarterly basis based on current and forecasted operating results and tax laws. The estimated annual effective tax rate is adjusted quarterly based upon actual results and updated operating forecasts. Consequently, based upon the mix and timing of our actual earnings compared to annual projections, our effective tax rate may vary quarterly and may make quarterly comparisons not meaningful. A tax expense or benefit unrelated to the current year income or loss is recognized in its entirety as a discrete item of tax in the period identified. The quarterly income tax provision is generally comprised of tax expense on income or tax benefit on loss at the most recent estimated annual effective tax rate, adjusted for the effect of discrete items.

The effective tax rate for continuing operations for the three and nine months ended September 30, 2013 was a 40.0% and 36.6%, respectively, benefit on loss compared to a 35.3% and 31.1% benefit on loss for the three and nine months ended September 30, 2012, respectively. The effective tax rates for the three and nine months ended September 30, 2013 differ from the statutory rate primarily due to net permanent additions, largely nondeductible officers' compensation, partially offset by percentage depletion deductions. The effective tax rates for the three and nine months ended September 30, 2012 differ from the statutory rate primarily due to net permanent deductions, largely percentage depletion, partially offset by nondeductible officer's compensation. There were no significant discrete items recorded during the three and nine months ended September 30, 2013 or 2012.

As of September 30, 2013, we had a gross liability for unrecognized tax benefits of \$0.2 million, unchanged from the amount recorded at December 31, 2012. If recognized, this liability would affect our effective tax rate. This liability is reflected in other accrued expenses on our accompanying condensed consolidated balance sheets. We expect our remaining liability for uncertain tax positions to decrease in the next twelve months due to the expiration of the statute of limitations.

As of the date of this report, we are current with our income tax filings in all applicable state jurisdictions. We have received notice from the State of Colorado that our 2008 through current state income tax returns have been selected for audit.

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PDC ENERGY, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS - Continued

NOTE 7 - LONG-TERM DEBT

Long-term debt consists of the following:

| | September 30, 2013 (in thousands) | December 31, 2012 |
|--|--------------------------------------|-------------------|
| Senior notes: | | |
| 3.25% Convertible senior notes due 2016: | | |
| Principal amount | \$115,000 | \$115,000 |
| Unamortized discount | (10,950 |) (13,671 |
| 3.25% Convertible senior notes due 2016, net of discount | 104,050 | 101,329 |
| 7.75% Senior notes due 2022 | 500,000 | 500,000 |
| Total senior notes | 604,050 | 601,329 |
| Credit facilities: | | |
| Corporate | — | 49,000 |
| PDCM | 34,750 | 26,250 |
| Total credit facilities | 34,750 | 75,250 |
| PDCM second lien term loan | 15,000 | — |
| Total debt | 653,800 | 676,579 |
| Less: Current portion of long-term debt | 104,050 | — |
| Long-term debt | \$549,750 | \$676,579 |

Senior Notes

3.25% Convertible Senior Notes Due 2016. In November 2010, we issued \$115 million aggregate principal amount 3.25% convertible senior notes due May 15, 2016 (the "Convertible Notes") in a private placement to qualified institutional investors. Interest on the Convertible Notes is payable semi-annually in arrears on each May 15 and November 15. We allocated the gross proceeds of the Convertible Notes between the liability and equity components of the debt. The initial \$94.3 million liability component was determined based upon the fair value of similar debt instruments with similar terms, excluding the conversion feature, and priced on the same day we issued the Convertible Notes. The original issue discount and capitalized debt issuance costs are being amortized to interest expense over the life of the notes using an effective interest rate of 7.4%.

Upon conversion, the Convertible Notes may be settled, at our election, in shares of our common stock, cash or a combination of cash and shares of our common stock. We have initially elected a net-settlement method to satisfy our conversion obligation, which allows us to settle the principal amount of the Convertible Notes in cash and to settle the excess conversion value in shares, as well as cash in lieu of fractional shares.

The Convertible Notes became convertible at the option of holders beginning October 1, 2013. The conversion right was triggered on September 20, 2013, when the closing sale price of our common stock on the NASDAQ Global Select Market exceeded \$55.12 (130% of the applicable conversion price) for the 20th trading day in the 30 consecutive trading days ending on September 30, 2013. In the event a holder elects to convert its note, we expect to fund any cash settlement of any such conversion from working capital and/or borrowings under our revolving credit facility. As a result of the Convertible Notes becoming convertible, we have included the carrying value of the Convertible Notes, net of discount, in the current portion of long-term debt on our condensed consolidated balance sheet as of September 30, 2013. We will reassess the convertibility of the Convertible Notes, and the related balance sheet classification, on a quarterly basis. In the event that a holder exercises the right to convert its note, we will

write-off a ratable portion of the remaining debt issuance costs and unamortized discount to interest expense. Based on a September 30, 2013 stock price of \$59.54, the “if-converted” value of the Convertible Notes exceeded the principal amount by approximately \$46.5 million.

7.75% Senior Notes Due 2022. In October 2012, we issued \$500 million aggregate principal amount 7.75% senior notes due October 15, 2022 (the “2022 Senior Notes”) in a private placement to qualified institutional investors. Interest on the 2022 Senior Notes is payable semi-annually in arrears on each April 15 and October 15. The indenture governing the notes contains customary restrictive incurrence covenants. Capitalized debt issuance costs are being amortized as interest expense over the life of the notes using the effective interest method.

As of September 30, 2013, we were in compliance with all covenants related to the Convertible Notes and the 2022 Senior Notes, and expect to remain in compliance throughout the next twelve-month period.

In connection with the issuance of the 2022 Senior Notes, we entered into a registration rights agreement with the initial purchasers in which we agreed to file a registration statement with the SEC related to an offer to exchange the notes for substantially identical registered notes and to use commercially reasonable efforts to cause the exchange offer to be completed on or prior to September 28, 2013. The registration statement was declared effective by the SEC in July 2013 and the exchange offer was completed in August 2013.

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PDC ENERGY, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS - Continued

Credit Facilities

Revolving Credit Facility. In May 2013, we entered into a Third Amended and Restated Credit Agreement with JPMorgan Chase Bank, N.A. as administrative agent and other lenders party thereto. This agreement amends and restates the credit agreement dated November 2010 and expires in May 2018. The revolving credit facility is available for working capital requirements, capital expenditures, acquisitions, general corporate purposes and to support letters of credit. The revolving credit facility provides for a maximum of \$1 billion in allowable borrowing capacity, subject to the borrowing base. As of September 30, 2013, the borrowing base was \$450 million. The borrowing base is based on, among other things, the loan value assigned to the proved reserves attributable to our and our subsidiaries' crude oil and natural gas interests, excluding proved reserves attributable to PDCM and our 21 affiliated partnerships. The borrowing base is subject to a semi-annual size redetermination 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. The revolving credit facility is secured by a pledge of the stock of certain of our subsidiaries, mortgages of certain producing crude oil and natural gas properties and substantially all of our and such subsidiaries' other assets. Neither PDCM nor our affiliated partnerships are guarantors of the revolving credit facility. As of September 30, 2013, we had no outstanding draws on our revolving credit facility compared to \$49.0 million at a weighted-average interest rate of 2.3% as of December 31, 2012.

The revolving credit facility contains covenants customary for agreements of this type, with the most restrictive being certain financial tests and requirements to maintain certain financial ratios on a quarterly basis. The financial tests and ratios, as defined per the revolving credit facility, include requirements to maintain a minimum current ratio of 1.00 to 1.00 and to not exceed a maximum leverage ratio of 4.25 to 1.00. As of September 30, 2013, we were in compliance with all the revolving credit facility covenants and expect to remain in compliance throughout the next twelve-month period.

As of September 30, 2013, Riley Natural Gas, a wholly owned subsidiary of PDC, had an approximately \$11.8 million irrevocable standby letter of credit in favor of a third-party transportation service provider to secure firm transportation of the natural gas produced by third-party producers for whom we market production in the Appalachian Basin. In addition, PDC had an approximately \$6.7 million irrevocable standby letter of credit to secure firm transportation of natural gas that we produce. The letters of credit reduce the amount of available funds under our revolving credit facility by an equal amount. The letters of credit expire on September 17, 2014. As of September 30, 2013, the available funds under our revolving credit facility, including a reduction for the \$18.5 million irrevocable standby letters of credit in effect, was \$431.5 million.

In October 2013, pursuant to an agreement our \$6.7 million irrevocable standby letter of credit will be novated to the buyer of PDCM's shallow upper Devonian properties upon the closing of the transaction. See Note 15, Subsequent Events, for additional information regarding the potential sale. We expect this sale to close in the fourth quarter of 2013. However, there can be no assurance we will be successful in closing this divestiture.

PDCM Credit Facility. PDCM has a credit facility dated April 2010, as amended in May 2013, with a borrowing base of \$80 million, of which our proportionate share is \$40 million. The maximum allowable facility amount is \$400 million. No principal payments are required until the credit agreement expires in April 2017, or in the event that the borrowing base falls below the outstanding balance. The credit facility is subject to and secured by PDCM's properties, including our proportionate share of such properties. The borrowing base is subject to size redetermination semi-annually based upon a valuation of PDCM's reserves at June 30 and December 31. Either PDCM or the lenders may request a redetermination upon the occurrence of certain events. The credit facility will be utilized by PDCM for

the exploration and development of its Marcellus Shale assets.

The credit facility contains covenants customary for agreements of this type, with the most restrictive being certain financial tests and financial ratios that must be met on a quarterly basis. The financial tests and ratios, as defined by the credit facility, include requirements to maintain a minimum current ratio of 1.0 to 1.0, not to exceed a debt to EBITDAX ratio of 4.25 to 1.0 (declining to 4.0 to 1.0 on July 1, 2014) and to maintain a minimum interest coverage ratio of 2.5 to 1.0. As of September 30, 2013, our proportionate share of PDCM's outstanding credit facility balance was \$34.8 million compared to \$26.3 million as of December 31, 2012. The weighted-average borrowing rate on PDCM's credit facility was 3.6% per annum as of September 30, 2013, compared to 3.5% as of December 31, 2012.

As of September 30, 2013, PDCM was not in compliance with the minimum current ratio and debt to EBITDAX ratio covenants under the PDCM credit facility. In October 2013, PDCM received a waiver from Wells Fargo regarding the covenant violation. PDCM expects to maintain compliance with all PDCM credit facility covenants throughout the next twelve-month period.

PDCM Second Lien Term Loan

In July 2013, PDCM entered into a Second Lien Credit Agreement ("Term Loan Agreement") with Wells Fargo Energy Capital as administrative agent and a syndicate of other lenders party thereto. The aggregate commitment under the Term Loan Agreement is \$30 million, of which our proportionate share is \$15 million. The aggregate commitment may increase periodically up to a maximum of \$75 million, as PDCM's assets grow and the covenants under the Term Loan Agreement allow. The Term Loan matures on October 31, 2017. Amounts borrowed accrue interest, at PDCM's discretion, at either an alternative base rate plus a margin of 6% per annum or an adjusted LIBOR for the interest period in effect plus a margin of 7% per annum. As of September 30, 2013, amounts borrowed and outstanding on the Term Loan were \$30.0 million, of which our proportionate share is \$15.0 million. The weighted-average borrowing rate on the Term Loan was 8.5% per annum as of September 30, 2013.

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PDC ENERGY, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS - Continued

The Term Loan Agreement contains financial covenants that must be met on a quarterly basis, including requirements to maintain a minimum current ratio of 1.0 to 1.0, not to exceed a debt to EBITDAX ratio of 4.5 to 1.0, to maintain a minimum interest coverage ratio of 2.25 to 1.0 and not to exceed a present value of future net revenues to total debt ratio of 1.50 to 1.00. As of September 30, 2013, PDCM was not in compliance with the minimum current ratio and the debt to EBITDAX ratio covenants under the Term Loan Agreement. In October 2013, PDCM received a waiver from Wells Fargo regarding the covenant violation. PDCM expects to maintain compliance with all Term Loan Agreement covenants throughout the next twelve-month period.

NOTE 8 - ASSET RETIREMENT OBLIGATIONS

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

| | Amount (in thousands) |
|--|--------------------------|
| Balance at December 31, 2012 | \$62,563 |
| Obligations incurred with development activities | 337 |
| Accretion expense | 3,667 |
| Revisions in estimated cash flows | 251 |
| Obligations discharged with divestitures of properties and asset retirements | (7,376) |
| Balance at September 30, 2013 | 59,442 |
| Less: Liabilities held for sale (1) | 22,788 |
| Less: Current portion | 1,000 |
| Long-term portion | \$35,654 |

 Represents asset retirement obligations related to our assets held for sale. See Note 12, Assets Held for Sale, (1)Divestitures and Discontinued Operations and Note 15, Subsequent Events, for additional information regarding the potential sale of these properties.

NOTE 9 - COMMITMENTS AND CONTINGENCIES

Firm Transportation Agreements. We enter into contracts that provide firm transportation, sales and processing services on pipeline systems through which we transport or sell natural gas. Volumes produced by us, PDCM, our affiliated partnerships and other third-party working interest owners can be used to satisfy volume requirements, as can volumes purchased from third parties. We record in our financial statements only our share of costs based upon our working interest in the wells. These contracts require us to pay these transportation and processing charges whether the required volumes are delivered or not. With the exception of contracts entered into by PDCM, the costs of any volume shortfalls are borne by PDC.

The following table presents gross volume information, including our proportionate share of PDCM, related to our long-term firm transportation, sales and processing agreements for pipeline capacity:

| Area | For the Twelve Months Ending September 30, | | | | | 2018 and Through Expiration | Total | Expiration Date |
|------|--|------|------|------|--|-----------------------------------|-------|--------------------|
| | 2014 | 2015 | 2016 | 2017 | | | | |
| | | | | | | | | |

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|-------------------------------------|---------|----------|----------|----------|----------|----------|------------------|
| Volume (MMcf) | | | | | | | |
| West Virginia | 21,428 | 22,868 | 24,874 | 24,862 | 149,603 | 243,635 | January 31, 2026 |
| Utica Shale | 2,282 | 2,738 | 2,738 | 2,738 | 15,966 | 26,462 | July 22, 2023 |
| Total | 23,710 | 25,606 | 27,612 | 27,600 | 165,569 | 270,097 | |
| Dollar commitment (in thousands) | \$9,601 | \$10,056 | \$10,462 | \$10,294 | \$47,785 | \$88,198 | |

In March 2013, we entered into long-term agreements with a subsidiary of MarkWest Energy Partners, LP to provide midstream services, including gas gathering, processing, fractionation and marketing, to support our Utica Shale operations in Guernsey County in Southeast Ohio. The primary term of the agreements commenced in July 2013 when our natural gas began to flow into the gathering system. The gas processing agreement includes minimum volume commitments as shown in the table above, with certain fees assessed for any shortfall.

In June 2013, we closed a transaction pursuant to which our Piceance Basin and NECO firm gathering commitments were assumed by the buyer of certain of our oil and natural gas properties. See Note 12, Assets Held for Sale, Divestitures, and Discontinued Operations, for additional information regarding the sale of our non-core Colorado assets.

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PDC ENERGY, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS - Continued

In October 2013, pursuant to a purchase and sale agreement an existing agreement for firm transportation services of approximately 34,572 MMcf, representing a dollar commitment of \$16.5 million, in the Appalachian Basin will be novated to the buyer of PDCM's shallow upper Devonian crude oil and natural gas properties, thereby relieving the Company of all obligations or liabilities arising under the agreement. See Note 15, Subsequent Events, for additional information regarding the potential sale. We expect this sale to close in the fourth quarter of 2013. However, there can be no assurance we will be successful in closing this divestiture.

Litigation. The Company is involved in various legal proceedings that it considers normal to its business. The Company reviews 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 the best interests of the Company. There is no assurance that settlements can be reached on acceptable terms or that adverse judgments, if any, in the remaining litigation will not exceed the amounts reserved. Although the results cannot be known with certainty, we currently believe that the ultimate results of such proceedings will not have a material adverse effect on our financial position, results of operations or liquidity.

Alleged Class Action Filed Regarding 2010 and 2011 Partnership Purchases

On December 21, 2011 the Company and its wholly-owned merger subsidiary were served with an alleged class action on behalf of certain former partnership unit holders, related to its partnership repurchases completed by mergers in 2010 and 2011. The action was filed in U.S. District Court for the Central District of California and is titled *Schulein v. Petroleum Development Corp.* The complaint primarily alleges that the disclosures in the proxy statements issued in connection with the mergers were inadequate, and a state law breach of fiduciary duty. On June 15, 2012, the Court denied the Company's motion to dismiss and approved a litigation schedule including a jury trial in May 2014. We have not recorded a liability for claims pending because we believe we have good legal defenses to the asserted claims and because the plaintiffs have not specified damages and it is not possible for management to reasonably estimate what, if any, monetary damages could result from this claim.

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 avoid environmental contamination and mitigate the risks from environmental contamination. We conduct periodic reviews 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. As of September 30, 2013 and December 31, 2012, we had accrued environmental liabilities in the amount of \$5.6 million and \$8.4 million, respectively, included in other accrued expenses on the condensed consolidated balance sheets. We are not aware of any environmental claims existing as of September 30, 2013 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 unknown past non-compliance with environmental laws will not be discovered on our properties.

Partnership Repurchase Provision. Substantially all of our drilling programs contain a repurchase provision pursuant to which investing partners may request that we purchase their partnership units at any time beginning with the third anniversary of the first cash distribution. The provision provides that we are obligated to purchase an aggregate of 10% of the initial subscriptions per calendar year (at a minimum price of four times the most recent 12 months' cash distributions from production), if repurchase is requested by investors, subject to our financial ability to do so. As of September 30, 2013, the maximum annual repurchase obligation, based upon the minimum price described above, was approximately \$4.2 million. We believe we have adequate liquidity to meet this potential obligation. For the quarter ended September 30, 2013, amounts paid for the repurchase of partnership units pursuant to this provision were immaterial.

Employment Agreements with Executive Officers. Each of our senior executive officers may be entitled to a severance payment and certain other benefits upon the termination of the officer's employment pursuant to the officer's employment agreement and/or the Company's executive severance compensation plan. The nature and amount of such benefits would vary based upon, among other things, whether the termination followed a change of control of the Company.

NOTE 10 - COMMON STOCK

Sale of Equity Securities

In August 2013, we completed a public offering of 5,175,000 shares of our common stock, par value \$0.01 per share, at a price to us of \$53.37 per share, resulting in total shares outstanding of 35,650,758 as of September 30, 2013. Net proceeds of the offering were approximately \$275.8 million, after deducting offering expenses and underwriting discounts, of which \$51,750 is included in common shares-par value and approximately \$275.8 million is included in additional paid-in capital on the condensed consolidated balance sheet. The shares were issued pursuant to an effective shelf registration statement on Form S-3 filed with the SEC in January 2012.

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PDC ENERGY, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS - Continued

Stock-Based Compensation Plans

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:

| | Three Months Ended September 30, 2013 | | Nine Months Ended September 30, 2013 | |
|--------------------------------------|---|---------|--|---------|
| | 2012 | 2012 | 2012 | 2012 |
| | (in thousands) | | | |
| Stock-based compensation expense | \$3,040 | \$2,225 | \$9,991 | \$6,126 |
| Income tax benefit | (1,161) | (847) | (3,816) | (2,333) |
| Net stock-based compensation expense | \$1,879 | \$1,378 | \$6,175 | \$3,793 |

Stock Appreciation Rights ("SARs")

The SARs vest ratably over a three-year period and may be exercised at any point after vesting through 10 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.

In January 2013, the Compensation Committee awarded 87,078 SARs to our executive officers. The fair value of each SAR award was estimated on the date of grant using a Black-Scholes pricing model using the following assumptions:

| | Grant-Year | |
|--|------------|---------|
| | 2013 | 2012 |
| Expected term of award | 6 years | 6 years |
| Risk-free interest rate | 1.0 | % 1.1 |
| Expected volatility | 65.5 | % 64.3 |
| Weighted-average grant date fair value per share | \$21.96 | \$17.61 |

The expected life of the award was estimated using historical stock option exercise behavior data. The risk-free interest rate was based on the U.S. Treasury yields approximating the expected life of the award in effect at the time of grant. Expected volatilities were based on our historical volatility. We do not expect to pay or declare dividends in the foreseeable future.

The following table presents the changes in our SARs:

| | | Nine Months Ended September 30, 2013 | | | 2012 | | |
|----------------------|---------------------------------------|--|--|----------------------|---------------------------------------|---|--|
| Number of SARs | Weighted-Average Exercise Price | Average Remaining Contractual Term (in years) | Aggregate Intrinsic Value (in thousands) | Number of SARs | Weighted-Average Exercise Price | Average Remaining Contractual Term (in years) | Aggregate Intrinsic Value (in thousands) |

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| | | | | | | | | |
|--|---------|----------|-----|--------|---------|----------|-----|--------|
| Outstanding beginning of year, January 1, | 118,832 | \$ 30.80 | 8.4 | \$ 486 | 50,471 | \$ 31.61 | 8.6 | \$ 341 |
| Awarded | 87,078 | 37.18 | — | — | 68,361 | 30.19 | 9.3 | — |
| Outstanding at September 30, | 205,910 | 33.50 | 8.4 | 5,363 | 118,832 | 30.80 | 8.7 | 328 |
| Vested and expected to vest at September 30, | 198,163 | 33.41 | 8.4 | 5,178 | 113,426 | 30.77 | 8.7 | 319 |
| Exercisable at September 30, | 67,069 | 29.99 | 7.3 | 1,982 | 27,458 | 28.84 | 7.8 | 153 |

Total compensation cost related to SARs granted, net of estimated forfeitures, and not yet recognized in our statement of operations as of September 30, 2013 was \$2.0 million. The cost is expected to be recognized over a weighted-average period of 2.0 years.

Restricted Stock Awards

Time-Based Awards. The fair value of the time-based restricted shares is amortized ratably over the requisite service period, primarily three or four years. The time-based shares vest ratably on each annual anniversary following the grant date if the participant is continuously employed.

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PDC ENERGY, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS - Continued

In January 2013, the Compensation Committee awarded a total of 103,050 time-based restricted shares to our executive officers that vest ratably over a three-year period ending on January 16, 2016.

The following table presents the changes in non-vested time-based awards for the nine months ended September 30, 2013:

| | Shares | Weighted-Average Grant-Date Fair Value |
|----------------------------------|----------|--|
| Non-vested at December 31, 2012 | 646,490 | \$27.93 |
| Granted | 292,548 | 44.56 |
| Vested | (265,312 |) 27.53 |
| Forfeited | (22,507 |) 31.29 |
| Non-vested at September 30, 2013 | 651,219 | 35.45 |

| | As of/Year Ended September 30, | |
|---|---------------------------------------|---------|
| | 2013 | 2012 |
| | (in thousands, except per share data) | |
| Total intrinsic value of time-based awards vested | \$12,562 | \$4,818 |
| Total intrinsic value of time-based awards non-vested | 38,774 | 21,996 |
| Market price per common share as of September 30, | 59.54 | 31.63 |
| Weighted-average grant date fair value per share | 44.56 | 26.48 |

Total compensation cost related to non-vested time-based awards, net of estimated forfeitures, and not yet recognized in our statements of operations as of September 30, 2013 was \$16.8 million. This cost is expected to be recognized over a weighted-average period of 2.1 years.

Market-Based Awards. The fair value of the market-based restricted shares 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 to five 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.

In January 2013, the Compensation Committee awarded a total of 41,570 market-based restricted shares to our executive officers. In addition to continuous employment, the vesting of these shares is contingent on the Company's total shareholder return ("TSR"), which is essentially the Company's stock price change including any dividends, as compared to the TSR of a set group of 16 peer companies. The shares are measured over a three-year period ending on December 31, 2015 and can result in a payout between 0% and 200% of the total shares awarded. The weighted-average grant date fair value per market-based share for these awards granted was computed using the Monte Carlo pricing model using the following assumptions:

| | Nine Months Ended September 30, | |
|------------------------|---------------------------------|---------|
| | 2013 | 2012 |
| Expected term of award | 3 years | 3 years |

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| | | | |
|--|---------|---------|---|
| Risk-free interest rate | 0.4 | % 0.3 | % |
| Expected volatility | 56.6 | % 65.3 | % |
| Weighted-average grant date fair value per share | \$49.04 | \$36.54 | |

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. We do not expect to pay or declare dividends in the foreseeable future.

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PDC ENERGY, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS - Continued

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 | | Nine Months Ended | |
|---|--------------------|------|-------------------|------|
| | September 30, | | September 30, | |
| | 2013 | 2012 | 2013 | 2012 |
| | (in thousands) | | | |
| Weighted-average common share equivalents excluded from diluted earnings per share due to their anti-dilutive effect: | | | | |
| Restricted stock | 805 | 777 | 857 | 688 |
| SARs | 83 | 119 | 65 | 115 |
| Stock options | 7 | 7 | 7 | 7 |
| Non-employee director deferred compensation | 4 | 3 | 4 | 3 |
| Convertible senior notes | 671 | — | 387 | — |
| Total anti-dilutive common share equivalents | 1,570 | 906 | 1,320 | 813 |

In November 2010, we issued our Convertible Notes, which give the holders the right to convert the aggregate principal amount into 2.7 million shares of our common stock at a conversion price of \$42.40 per share. The Convertible Notes could be included in the dilutive earnings per share calculation using the treasury stock method if the average market share price exceeds the \$42.40 conversion price during the period presented. Shares issuable upon conversion of the Convertible Notes were excluded from the diluted earnings per share calculation for the three and nine months ended September 30, 2013 as the effect would be anti-dilutive to our earnings per share. Shares issuable upon conversion of the Convertible Notes were excluded from the diluted earnings per share calculation for the three and nine months ended September 30, 2012 as the conversion price was greater than the average market price of our common stock during the period.

NOTE 12 - ASSETS HELD FOR SALE, DIVESTITURES AND DISCONTINUED OPERATIONS

Piceance Basin and NECO. In February 2013, we entered into a purchase and sale agreement with certain affiliates of Caerus Oil and Gas LLC (“Caerus”), pursuant to which we agreed to sell to Caerus our Piceance Basin, NECO and certain other non-core Colorado oil and gas properties, leasehold mineral interests and related assets. Additionally, certain firm transportation obligations and natural gas hedging positions were assumed by Caerus. On June 18, 2013, this divestiture was completed with total consideration of approximately \$177.6 million, subject to customary post-closing adjustments, with an additional \$17.0 million paid to our non-affiliated investor partners in our affiliated partnerships. The sale resulted in a pre-tax loss of \$2.3 million. The proceeds from the asset divestiture were used to pay down our revolving credit facility and to fund a portion of our 2013 capital budget. Following the sale to Caerus, we do not have significant continuing involvement in the operations of, or cash flows from, the Piceance Basin and NECO oil and gas properties. Accordingly, the results of operations related to these assets have been separately reported as discontinued operations in the condensed consolidated statement of operations for all periods presented. The sale of our other non-core Colorado oil and gas properties did not meet the requirements to be accounted for as discontinued operations.

Appalachian Basin. In early 2013, we developed a plan to market all of our shallow upper Devonian (non-Marcellus Shale) Appalachian Basin crude oil and natural gas properties located in West Virginia and Pennsylvania owned

directly by us, as well as through our proportionate share of PDCM and our affiliated partnerships. The properties consist of approximately 3,500 gross shallow producing wells, related facilities and associated shallow leasehold acreage, limited to the upper Devonian and shallower formations. The Company will retain all zones, formations and intervals below the upper Devonian formation including the Marcellus Shale, Utica Shale and Huron Shale. We classified the related assets owned directly by us, as well as through our proportionate share of PDCM and our affiliated partnerships, as held for sale in the condensed consolidated balance sheet as of September 30, 2013. The divestiture of these assets does not meet the requirements to be accounted for as discontinued operations. In October 2013, PDCM executed a purchase and sale agreement with an unrelated third-party for the sale of these properties. The aggregate consideration is subject to customary terms and post-closing adjustments. See Note 15, Subsequent Events, for additional information on the potential sale. We expect this sale to close in the fourth quarter of 2013. However, there can be no assurance we will be successful in closing this divestiture.

Permian Basin. In December 2011, we executed a purchase and sale agreement with COG Operating LLC (“COG”), a wholly owned subsidiary of Concho Resources Inc., an unrelated third-party, for the sale of our core Permian Basin assets for a sale price of \$173.9 million, subject to customary terms and adjustments. In February 2012, the divestiture closed with total proceeds received of \$189.2 million after closing adjustments. Following the sale to COG, we do not have significant continuing involvement in the operations of, or cash flows from, these assets. Accordingly, the results of operations related to the Permian assets have been separately reported as discontinued operations in the condensed consolidated statement of operations for the nine months ended September 30, 2012.

Selected financial information related to divested and discontinued operations. The tables below set forth selected financial information related to net assets held for sale and operating results related to discontinued operations. Net assets held for sale represents the Appalachian Basin assets that are expected to be sold, net of liabilities that are expected to be assumed by the purchaser.

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PDC ENERGY, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS - Continued

The following table presents balance sheet data related to our pro rata share of these assets held for sale as of September 30, 2013:

| Balance Sheet | Net Assets Held for Sale (in thousands) |
|--|---|
| Assets | |
| Properties and equipment | \$ 130,835 |
| Accumulated depreciation, depletion and amortization | (101,801) |
| Total Assets | 29,034 |
| Liabilities | |
| Asset retirement obligation | 22,788 |
| Net Assets | \$6,246 |

The following table presents statement of operations data related to our discontinued operations for the Piceance Basin, NECO and Permian Basin divestiture:

| Statements of Operations - Discontinued Operations | Three Months Ended September 30, | | Nine Months Ended September 30, | |
|--|----------------------------------|------------|---------------------------------|------------|
| | 2013 | 2012 | 2013 | 2012 |
| | (in thousands) | | | |
| Revenues | | | | |
| Crude oil, natural gas and NGLs sales | \$(58) | \$7,624 | \$20,398 | \$25,972 |
| Sales from natural gas marketing | 1,789 | 392 | 2,825 | 1,149 |
| Well operations, pipeline income and other | 31 | 446 | 890 | 1,476 |
| Total revenues | 1,762 | 8,462 | 24,113 | 28,597 |
| Costs, expenses and other | | | | |
| Production costs | 18 | 4,959 | 7,975 | 17,743 |
| Cost of natural gas marketing | 1,679 | 338 | 2,673 | 1,010 |
| Depreciation, depletion and amortization | — | 10,362 | 2,258 | 32,873 |
| Other | 77 | 298 | 2,531 | 949 |
| (Gain) loss on sale of properties and equipment | 1,254 | — | 2,330 | (19,920) |
| Total costs, expenses and other | 3,028 | 15,957 | 17,767 | 32,655 |
| Income (loss) from discontinued operations | (1,266) | (7,495) | 6,346) | (4,058) |
| Provision for income taxes | 484 | 2,863 | (2,175) | 1,590 |
| Income (loss) from discontinued operations, net of tax | \$(782) | \$(4,632) | \$4,171) | \$(2,468) |

While the reclassification of revenues and expenses related to discontinued operations for the prior period had no impact upon previously reported net earnings, the statement of operations table presents the revenues and expenses that were reclassified from the specified statement of operations line items to discontinued operations.

NOTE 13 - TRANSACTIONS WITH AFFILIATES AND OTHER RELATED PARTIES

PDCM and Affiliated Partnerships. Our Gas Marketing segment markets the natural gas produced by PDCM and our affiliated partnerships in the Eastern operating region.

Amounts due from/to the affiliated partnerships have historically been primarily related to derivative positions and, to a lesser extent, unbilled well lease operating expenses, and costs resulting from audit and tax preparation services. Previously, we had entered into derivative instruments on behalf of our affiliated partnerships for a percentage of their estimated production. In June 2013, all remaining derivative positions designated to our affiliated partnerships were liquidated prior to settlement. As a result, there were no amounts due from/to our affiliated partnerships related to derivative positions as of September 30, 2013.

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PDC ENERGY, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS - Continued

The following table presents amounts included in our condensed consolidated statements of operations related to the marketing of natural gas on behalf of PDCM and our affiliated partnerships:

| Statement of Operations | Three Months Ended September 30, | | Nine Months Ended September 30, | |
|----------------------------------|----------------------------------|---------|---------------------------------|---------|
| | 2013 | 2012 | 2013 | 2012 |
| | (in thousands) | | | |
| PDCM: | | | | |
| Sales from natural gas marketing | \$4,774 | \$2,894 | \$12,742 | \$7,459 |
| Cost of natural gas marketing | 4,680 | 2,838 | 12,492 | 7,313 |
| Affiliated Partnerships: | | | | |
| Sales from natural gas marketing | 348 | 145 | 931 | 368 |
| Cost of natural gas marketing | 341 | 142 | 913 | 360 |

We provide certain well operating and administrative services for PDCM. Amounts billed to PDCM for these services were \$3.6 million and \$10.4 million in the three and nine months ended September 30, 2013, respectively, compared to \$3.0 million and \$9.2 million in the three and nine months ended September 30, 2012. Our statements of operations include only our proportionate share of these billings. The following table presents the statement of operations line item in which our proportionate share is recorded and the amount for each of the periods presented:

| Statement of Operations Line Item | Three Months Ended September 30, | | Nine Months Ended September 30, | |
|------------------------------------|----------------------------------|---------|---------------------------------|---------|
| | 2013 | 2012 | 2013 | 2012 |
| | (in thousands) | | | |
| Production costs | \$1,068 | \$1,022 | \$3,121 | \$3,080 |
| Exploration expense | 127 | 110 | 366 | 357 |
| General and administrative expense | 584 | 370 | 1,716 | 1,168 |

NOTE 14 - BUSINESS SEGMENTS

We separate our operating activities into two segments: (1) Oil and Gas Exploration and Production and (2) Gas Marketing. All material inter-company accounts and transactions between segments have been eliminated.

Oil and Gas Exploration and Production. Our Oil and Gas Exploration and Production segment includes all of our crude oil and natural gas properties. The segment represents revenues and expenses from the production and sale of crude oil, natural gas and NGLs. Segment revenue includes crude oil, natural gas and NGLs sales, commodity price risk management, net and well operation and pipeline income. Segment income (loss) consists of segment revenue less production cost, exploration expense, impairment of crude oil and natural gas properties, direct general and administrative expense and depreciation, depletion and amortization expense.

Gas Marketing. Our Gas Marketing segment purchases, aggregates and resells natural gas produced by us and others. Segment income (loss) primarily represents sales from natural gas marketing and direct interest income, less costs of natural gas marketing and direct general and administrative expense.

Unallocated amounts. Unallocated income includes corporate general administrative expense, corporate depreciation, depletion and amortization expense, interest income and interest expense.

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PDC ENERGY, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS - Continued

The following tables present our segment information:

| | Three Months Ended September 30, | | Nine Months Ended September 30, | |
|--|----------------------------------|--------------|---------------------------------|-------------|
| | 2013 | 2012 | 2013 | 2012 |
| | (in thousands) | | | |
| Segment revenues: | | | | |
| Oil and gas exploration and production | \$60,170 | \$21,542 | \$221,552 | \$192,294 |
| Gas marketing | 16,946 | 11,178 | 48,695 | 31,172 |
| Total revenues | \$77,116 | \$32,720 | \$270,247 | \$223,466 |
| Segment loss before income taxes: | | | | |
| Oil and gas exploration and production | \$4,573 | \$(16,266) |) \$27,243 |) \$76,852 |
| Gas marketing | (181) |) (82) |) (233) |) 331 |
| Unallocated | (29,765) |) (26,931) |) (89,537) |) (80,187) |
| Loss before income taxes | \$(25,373) |) \$(43,279) |) \$(62,527) |) \$(3,004) |

| | September 30, 2013 | December 31, 2012 |
|--|--------------------|-------------------|
| | (in thousands) | |
| Segment assets: | | |
| Oil and gas exploration and production | \$1,874,679 | \$1,723,011 |
| Gas marketing | 35,532 | 11,090 |
| Unallocated | 71,718 | 92,747 |
| Assets held for sale | 29,034 | — |
| Total assets | \$2,010,963 | \$1,826,848 |

Assets held for sale as of September 30, 2013 relate to our oil and gas exploration and production segment. We do not expect the divestiture of these assets to have a material impact on our financial condition and results of operations.

NOTE 15 - SUBSEQUENT EVENTS

On October 8, 2013, PDCM executed a purchase and sale agreement with an unrelated third-party pursuant to which PDCM agreed to sell its shallow upper Devonian (non-Marcellus Shale) Appalachian Basin crude oil and natural gas properties for aggregate consideration of approximately \$18.8 million, of which our proportionate share is \$6.2 million, after pre-closing adjustments. The properties consist of approximately 3,500 gross shallow producing wells, related facilities and associated shallow leasehold acreage, limited to the upper Devonian and shallower formations. The aggregate cash consideration is subject to customary terms and post-closing adjustments and by certain firm transportation obligations that will be assumed by the buyer. Concurrent with the closing of the transaction, our \$6.7 million irrevocable standby letter of credit and related obligations will be novated to the buyer. We expect this sale to close in the fourth quarter of 2013. However, there can be no assurance we will be successful in closing this divestiture.

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PDC ENERGY, INC.

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

The following discussion and analysis, as well as other sections in this report, should be read in conjunction with our condensed consolidated financial statements and related notes included elsewhere in this report. Further, we encourage you to revisit the Special Note Regarding Forward-Looking Statements.

EXECUTIVE SUMMARY

Financial Overview

Crude oil, natural gas and NGLs sales from continuing operations increased during the three and nine months ended September 30, 2013 by \$29.8 million, or 57.1%, and \$68.5 million, or 40.2%, respectively, compared to the three and nine months ended September 30, 2012. The growth in crude oil, natural gas and NGLs sales was the result of a significant increase in production and higher crude oil and natural gas prices. Our crude oil, natural gas and NGLs production from continuing operations during the three and nine months ended September 30, 2013 averaged 18.6 Mboe per day and 18.4 Mboe per day, respectively, an increase of approximately 29.2% and 26.9%, respectively, compared to the three and nine months ended September 30, 2012. The increases in production are primarily attributable to our successful horizontal Niobrara and Codell drilling program in the Wattenberg Field and, to a lesser extent, certain assets acquired from affiliates of Merit Energy (the "Merit Acquisition") in June 2012. Crude oil production from continuing operations increased 39.9% and 33.2% during the three and nine months ended September 30, 2013, respectively, while NGLs production from continuing operations increased 18.7% and 21.5%, respectively. Our liquids percentage of total production from continuing operations was 49.6% and 52.7% during the three and nine months ended September 30, 2013, respectively, compared to 48.4% and 51.5%, respectively, during the same prior year periods. Natural gas production from continuing operations increased 27.0% and 23.4% during the three and nine months ended September 30, 2013, respectively, compared to the same periods in 2012.

Available liquidity as of September 30, 2013 was \$735.3 million, including \$5.5 million through PDCM, compared to \$398.6 million, including \$14.1 million related to PDCM, as of December 31, 2012. Available liquidity is comprised of cash, cash equivalents and funds available under revolving credit facilities. In August 2013, we completed a public offering of 5,175,000 shares of our common stock, par value \$0.01 per share, at a price to us of \$53.37 per share, for net proceeds of approximately \$275.8 million, after deducting offering expenses and underwriting discounts. We expect to use the net proceeds from the offering to fund a portion of an expanded capital program for the remainder of 2013 and 2014 and for general corporate purposes. Our expanded capital program is expected to include the addition of a fourth drilling rig in the Wattenberg Field in the fourth quarter of 2013, as well as the potential for a second rig in the Utica Shale and a fifth rig in the Wattenberg Field in 2014. We may also use a portion of the proceeds to acquire additional Utica Shale acreage. We believe we have sufficient liquidity to allow us to execute our expanded drilling program through 2014.

Operational Overview

Drilling Activities. We continued to execute our strategic goal of increasing production while maintaining our production mix of crude oil and NGLs by focusing our drilling operations primarily in the liquid-rich Wattenberg Field in Colorado and the emerging Utica Shale play in Ohio. We have fully transitioned to multi-well pad drilling to optimize costs and enhance horizontal drilling efficiencies.

In our Western operating region, we currently have three drilling rigs operating in the Wattenberg Field. We are currently test-drilling increased density of 16 horizontal wells per section. During the nine months ended September 30, 2013, we spud 47 horizontal wells in the Wattenberg Field, 25 of which were completed, and participated in 27 gross, 6.6 net, horizontal non-operated drilling projects.

In our Eastern operating region, we spud five horizontal Utica exploratory wells during the nine months ended September 30, 2013, two of which were completed and connected to a gathering line. We also spud four horizontal Utica development wells, all of which were in various stages of completion as of September 30, 2013. In the Marcellus Shale, PDCM spud 11 horizontal wells during the nine months ended September 30, 2013, seven of which were completed and turned-in-line as of September 30, 2013.

Colorado Flooding. In September 2013, we experienced wide spread flooding in our Wattenberg Field operations in Weld County, Colorado, that resulted in a shut-in of approximately 200 vertical wells. As of September 30, 2013, approximately \$0.9 million was recorded in accrued environmental liabilities representing the estimated costs, based on initial assessments, to perform remediation operations. Assessment of the full impact of the flooding is on-going and we expect to incur approximately \$3 million to \$5 million in additional costs during the fourth quarter of 2013 and the first quarter of 2014 to repair and replace damaged well equipment and bring the vertical wells back on-line.

Crude Oil and Natural Gas Properties Divestitures. In February 2013, we entered into a purchase and sale agreement with certain affiliates of Caerus Oil and Gas LLC ("Caerus"), pursuant to which we agreed to sell to Caerus our Piceance Basin, NECO and certain other non-core Colorado oil and gas properties, leasehold mineral interests and related assets. This divestiture was completed in June 2013 with total consideration of approximately \$177.6 million, subject to customary post-closing adjustments, with an additional \$17.0 million paid to our non-affiliated investor partners in our affiliated partnerships. The sale resulted in a pre-tax loss of \$2.3 million. The proceeds from the asset disposal were used to pay down our revolving credit facility and to fund a portion of our 2013 capital budget. Following the sale to Caerus, we do not have significant continuing involvement in the operations of, or cash flows from, the Piceance Basin and NECO oil and gas properties. Accordingly, the results of operations related to these assets have been separately reported as discontinued operations in the condensed consolidated statement of operations for all periods presented.

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PDC ENERGY, INC.

On October 8, 2013, PDCM executed a purchase and sale agreement with an unrelated third-party pursuant to which PDCM agreed to sell its shallow upper Devonian (non-Marcellus Shale) Appalachian Basin crude oil and natural gas properties for aggregate consideration of approximately \$18.8 million, of which our proportionate share is \$6.2 million, after pre-closing adjustments. The properties consist of approximately 3,500 gross shallow producing wells, related facilities and associated shallow leasehold acreage, limited to the upper Devonian and shallower formations. The aggregate cash consideration is subject to customary terms and post-closing adjustments and by certain firm transportation obligations that will be assumed by the buyer. Concurrent with the closing of this transaction, our \$6.7 million irrevocable standby letter of credit and related obligations will be novated to the buyer. We expect this sale to close in the fourth quarter of 2013. However, there can be no assurance we will be successful in closing this divestiture.

Non-U.S. GAAP Financial Measures

We use "adjusted cash flows from operations," "adjusted net income (loss)" and "adjusted EBITDA," non-U.S. GAAP financial measures, for internal management reporting, when evaluating period-to-period changes and providing public guidance on possible future results. These measures are not measures of financial performance under U.S. GAAP and should be considered in addition to, not as a substitute for, net income (loss) or cash flows from operations, investing or financing activities, and should not be viewed as a liquidity measure or indicator of cash flows reported in accordance with U.S. GAAP. The non-U.S. GAAP financial measures that we use may not be comparable to similarly titled measures reported by other companies. Also, in the future, we may disclose different non-U.S. GAAP financial measures in order to help our investors more meaningfully evaluate and compare our future results of operations to our previously reported results of operations. We strongly encourage investors to review our financial statements and publicly filed reports in their entirety and to not rely on any single financial measure. See Reconciliation of Non-U.S. GAAP Financial Measures for a detailed description of these measures, as well as a reconciliation of each to the most comparable U.S. GAAP measure.

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PDC ENERGY, INC.

Results of Operations

Summary Operating Results

The following table presents selected information regarding our operating results from continuing operations:

| | Three Months Ended September 30, | | | Nine Months Ended September 30, | | |
|-------------------|---|-------|-------------------|---------------------------------|------|-------------------|
| | 2013 | 2012 | Percentage Change | 2013 | 2012 | Percentage Change |
| | (dollars in millions, except per unit data) | | | | | |
| Production (1) | | | | | | |
| Crude oil (MBbls) | 601.5 | 430.0 | 39.9 | % 1,887.5 | | |