

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

FORM 10-Q

(Mark One)

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

For the Quarterly Period Ended June 30, 2023

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 **000-06814**



(Exact Name of Registrant as Specified in its Charter)

Delaware	83-0205516	
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)	
1616 S. Voss Road , Suite 725 , Houston , Texas	77057	
(Address of principal executive offices)	(Zip Code)	
<u>(346) 509-8734</u> (Registrant's telephone number, including area code)		
Securities registered pursuant to Section 12(b) of the Act:		
Title of each class	Trading symbol(s)	Name of each exchange on which registered
Common stock, par value \$0.01	USEG	NASDAQ Stock Market LLC (Nasdaq Capital Market)

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

Indicate by check mark whether the registrant has submitted electronically every Interactive Data File required to be submitted pursuant to Rule 405 of Regulation S-T (\$232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit such files). YES  NO

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

Large accelerated filer   
Non-accelerated filer

Accelerated filer   
Smaller reporting company   
Emerging growth company

If an emerging growth company, indicate by check mark if the registrant has elected not to use the extended transition period for complying with any new or revised financial accounting standards provided pursuant to Section 13(a) of the Exchange Act.

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

The registrant had 25,506,570 shares of its common stock, par value \$0.01 per share, outstanding as of August 14, 2023.

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#### CAUTIONARY STATEMENT REGARDING FORWARD-LOOKING STATEMENTS

This Quarterly Report on Form 10-Q (this "Report" or "Form 10-Q"), including "Management's Discussion and Analysis of Financial Condition and Results of Operations," contains "forward-looking statements" within the meaning of the federal securities laws, including Section 27A of the Securities Act of 1933, as amended, Section 21E of the Securities Exchange Act of 1934, as amended (the "Exchange Act") and the Private Securities Litigation Reform Act of 1995. All statements other than statements of historical facts are forward-looking statements.

Examples of forward-looking statements in this Report include:

- planned capital expenditures for oil and natural gas exploration and environmental compliance;
- potential drilling locations and available spacing units, and possible changes in spacing rules;
- cash expected to be available for capital expenditures and to satisfy other obligations;
- recovered volumes and values of oil and natural gas approximating third-party estimates;
- anticipated changes in oil and natural gas production;
- drilling and completion activities and opportunities;
- timing of drilling additional wells and performing other exploration and development projects;
- expected spacing and the number of wells to be drilled with our oil and natural gas industry partners;
- when payout-based milestones or similar thresholds will be reached for the purposes of our agreements with our partners;
- expected working and net revenue interests, and costs of wells, relating to the drilling programs with our partners;
- actual decline rates for producing wells;
- future cash flows, expenses and borrowings;
- pursuit of potential acquisition opportunities;
- economic downturns, wars and increased inflation and interest rates, and possible recessions caused thereby;
- the effects of global pandemics on our operations, properties, the market for oil and gas, and the demand for oil and gas;
- our expected financial position;
- our expected future overhead reductions;
- our ability to become an operator of oil and natural gas properties;
- our ability to raise additional financing and acquire attractive oil and natural gas properties; and
- other plans and objectives for future operations.

These forward-looking statements are identified by their use of terms and phrases such as "may," "expect," "estimate," "project," "plan," "believe," "intend," "achievable," "anticipate," "will," "continue," "potential," "should," "could," "up to," and similar terms and phrases. Though we believe that the expectations reflected in these statements are reasonable, they involve certain assumptions, risks and uncertainties. Factors that could cause or contribute to such differences include, but are not limited to, those discussed in this Quarterly Report on Form 10-Q, and in particular, under and incorporated by reference in, "[Risk Factors](#)", below, the risks discussed in Part I, Item 1A, "[Risk Factors](#)" in our Annual Report on Form 10-K for the fiscal year ended December 31, 2022, and those discussed in other documents we file with the Securities and Exchange Commission (the "SEC" or the "Commission"). Given these risks and uncertainties, readers are cautioned not to place undue reliance on such forward-looking statements.

All subsequent written and oral forward-looking statements attributable to the Company, or persons acting on its behalf, are expressly qualified in their entirety by the cautionary statements above.

All forward-looking statements speak only at the date of the filing of this Report. We do not undertake any obligation to update or revise publicly any forward-looking statements except as required by law, including the securities laws of the United States and the rules and regulations of the SEC.

#### Part I. FINANCIAL INFORMATION

##### Item 1. Financial Statements

##### U.S. ENERGY CORP. AND SUBSIDIARIES UNAUDITED CONDENSED CONSOLIDATED BALANCE SHEETS (in thousands, except share and per share amounts)

ASSETS			
<b>Current assets:</b>			
Cash and equivalents	\$ 1,175	\$ 4,411	4,411
Oil and natural gas sales receivable	2,714	3,193	3,193
Marketable equity securities	91	107	107
Other current assets	973	558	558
Commodity derivative asset-current	8	-	-
Real estate assets held for sale, net of selling costs	175	175	175
<b>Total current assets</b>	<b>5,136</b>	<b>8,444</b>	<b>8,444</b>
<b>Oil and natural gas properties under full cost method:</b>			
Unevaluated properties	1,584	1,584	1,584
Evaluated properties	205,463	203,144	203,144
Less accumulated depreciation, depletion and amortization	(101,391)	(96,725)	(96,725)
<b>Net oil and natural gas properties</b>	<b>105,656</b>	<b>108,003</b>	<b>108,003</b>
Property and equipment, net	913	651	651
Right-of-use asset	773	868	868
Other assets	330	354	354
<b>Total assets</b>	<b>\$ 112,808</b>	<b>\$ 118,320</b>	<b>\$ 118,320</b>
LIABILITIES AND SHAREHOLDERS' EQUITY			
<b>Current liabilities:</b>			
Accounts payable and accrued liabilities	\$ 8,464	\$ 7,832	7,832
Accrued compensation and benefits	611	1,111	1,111
Commodity derivative liability-current	-	1,694	1,694
Asset retirement obligations-current	668	668	668
Current lease obligation	176	189	189
<b>Total current liabilities</b>	<b>9,919</b>	<b>11,494</b>	<b>11,494</b>
Credit facility	12,000	12,000	12,000
Asset retirement obligations- noncurrent	15,226	14,774	14,774
Long-term lease obligation, net of current portion	704	794	794
Deferred tax liability	610	898	898
Other noncurrent liabilities	6	6	6
<b>Total liabilities</b>	<b>38,465</b>	<b>39,966</b>	<b>39,966</b>
<b>Commitments and contingencies (Note 8)</b>			
<b>Shareholders' equity:</b>			
Common stock, \$ 0.01 par value; 245,000,000 shares authorized; 25,071,372 and 25,023,812 shares issued and outstanding at June 30, 2023 and December 31, 2022, respectively	251	250	250
Additional paid-in capital	217,632	216,690	216,690
Accumulated deficit	(143,540)	(138,586)	(138,586)
<b>Total shareholders' equity</b>	<b>74,343</b>	<b>78,354</b>	<b>78,354</b>
<b>Total liabilities and shareholders' equity</b>	<b>\$ 112,808</b>	<b>\$ 118,320</b>	<b>\$ 118,320</b>

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

**U.S. ENERGY CORP. AND SUBSIDIARIES**  
**UNAUDITED CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS**  
**FOR THE THREE AND SIX MONTHS ENDED JUNE 30, 2023 AND 2022**  
 (In thousands, except share and per share amounts)

	Three Months Ended June 30,		Six Months Ended June 30,	
	2023	2022	2023	2022
<b>Revenue:</b>				
Oil	\$ 7,028	\$ 11,334	\$ 14,124	\$ 19,167
Natural gas and liquids	950	2,146	2,127	3,185
Total revenue	7,978	13,480	16,251	22,352
<b>Operating expenses:</b>				
Lease operating expenses	3,877	4,646	8,400	7,382
Production taxes	538	913	1,058	1,485
Depreciation, depletion, accretion and amortization	2,896	2,571	5,313	4,457
General and administrative expenses	3,368	2,642	6,140	5,588
Total operating expenses	10,679	10,772	20,911	18,912
<b>Operating income (loss)</b>	<b>(2,701)</b>	<b>2,708</b>	<b>(4,660)</b>	<b>3,440</b>

<b>Other non-operating income (expense):</b>					
Commodity derivative gain (loss)	288	( 2,132)	1,208	( 8,969)	
Marketable equity securities loss	( 16)	( 121)	( 16)	( 40)	
Other expense, net	( 6)	( 5)	( 6)	( 6)	
Interest expense, net	( 289)	( 60)	( 558)	( 108)	
Total other non-operating income (expense)	( 23)	( 2,318)	628	( 9,123)	
Net income (loss) before income taxes	\$ ( 2,724)	\$ 390	\$ ( 4,032)	\$ ( 5,683)	
Income tax (expense) benefit	209	( 268)	270	2,421	
<b>Net income (loss)</b>	<b>\$ ( 2,515)</b>	<b>\$ 122</b>	<b>\$ ( 3,762)</b>	<b>\$ ( 3,262)</b>	
Basic weighted shares outstanding	25,186,797	24,923,812	25,182,704	24,323,859	
Diluted weighted shares outstanding	25,186,797	25,265,180	25,182,704	24,323,859	
Basic earnings (loss) per share	\$ ( 0.10)	\$ 0.00	\$ ( 0.15)	\$ ( 0.13)	
Diluted earnings (loss) per share	\$ ( 0.10)	\$ 0.00	\$ ( 0.15)	\$ ( 0.13)	

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

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**U.S. ENERGY CORP. AND SUBSIDIARIES**  
**UNAUDITED CONDENSED CONSOLIDATED STATEMENTS OF CHANGES**  
**IN SHAREHOLDERS' EQUITY**  
**FOR THE SIX MONTHS ENDED JUNE 30, 2023 AND 2022**  
(in thousands, except share amounts)

	<b>Common Stock</b>		<b>Additional Paid-in Capital</b>	<b>Accumulated Deficit</b>	<b>Total</b>
	<b>Shares</b>	<b>Amount</b>			
<b>Balances, December 31, 2021</b>	4,676,301	\$ 47	\$ 149,276	\$ ( 135,888)	\$ 13,435
Shares issued for acquired properties	19,905,736	\$ 199	\$ 64,495		\$ 64,694
Stock-based compensation	-	-	1,500		1,500
Shares issued upon vesting of restricted stock awards	373,500	4	( 4)	-	-
Shares withheld to settle tax withholding obligations for restricted stock awards	( 81,725)	( 1)	( 306)	-	( 307)
Exercise of warrants	50,000	-	213	-	213
Net loss	-	-	-	( 3,384)	( 3,384)
<b>Balances, March 31, 2022</b>	<b>24,923,812</b>	<b>\$ 249</b>	<b>\$ 215,174</b>	<b>\$ ( 139,272)</b>	<b>\$ 76,151</b>
Cash dividends, \$ 0.0225 per share	-	-	-	( 578)	( 578)
Stock-based compensation	-	-	609	-	609
Net income	-	-	-	122	122
<b>Balances, June 30, 2022</b>	<b>24,923,812</b>	<b>\$ 249</b>	<b>\$ 215,783</b>	<b>\$ ( 139,728)</b>	<b>\$ 76,304</b>
<b>Balances, December 31, 2022</b>	25,023,812	\$ 250	\$ 216,690	\$ ( 138,586)	\$ 78,354
Stock-based compensation	-	-	727	-	727
Shares issued upon vesting of restricted stock awards	273,000	3	( 3)	-	-
Shares withheld to settle tax withholding obligations for restricted stock awards	( 62,140)	( 1)	( 149)	-	( 150)
Cash dividends \$ 0.0225 per share	-	-	-	( 596)	( 596)
Net loss	-	-	-	( 1,247)	( 1,247)
<b>Balances, March 31, 2023</b>	<b>25,234,672</b>	<b>\$ 252</b>	<b>\$ 217,265</b>	<b>\$ ( 140,429)</b>	<b>\$ 77,088</b>
Stock-based compensation	-	-	607	-	607
Cash dividends, \$ 0.0225 per share	-	-	-	( 596)	( 596)
Share repurchases	( 163,300)	( 1)	( 240)	-	( 241)
Net loss	-	-	-	( 2,515)	( 2,515)
<b>Balances, June 30, 2023</b>	<b>25,071,372</b>	<b>\$ 251</b>	<b>\$ 217,632</b>	<b>\$ ( 143,540)</b>	<b>\$ 74,343</b>

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

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**U.S. ENERGY CORP. AND SUBSIDIARIES**  
**UNAUDITED CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS**  
**FOR THE SIX MONTHS ENDED JUNE 30, 2023 AND 2022**  
(in thousands)

	<b>2023</b>	<b>2022</b>
<b>Cash flows from operating activities:</b>		
Net loss	\$ ( 3,762)	\$ ( 3,262)
Adjustments to reconcile net loss to net cash used in operating activities:		
Depreciation, depletion, accretion, and amortization	5,313	4,457
Deferred income taxes	( 288)	( 2,460)
Total commodity derivative (gains) losses, net	( 1,208)	8,969
Commodity derivative settlements paid	( 494)	( 4,487)
Loss on marketable equity securities	16	40
Amortization of debt issuance costs	24	20
Stock-based compensation	1,334	2,109

Right of use asset amortization	95	75
Changes in operating assets and liabilities:		
Oil and natural gas sales receivable	479	( 5,198)
Other assets	240	( 192)
Accounts payable and accrued liabilities	314	4,315
Accrued compensation and benefits	( 500)	( 675)
Payments on operating lease liability	( 102)	( 49)
Payments on asset retirement obligations	( 52)	-
Net cash provided by operating activities	1,409	3,662
<b>Cash flows from investing activities:</b>		
Acquisition of proved properties	-	( 4,383)
Oil and natural gas capital expenditures	( 2,402)	( 1,131)
Expenditures for pending acquisitions	-	( 592)
Property and equipment expenditures	( 373)	( 295)
Proceeds from sale of oil and gas properties	-	1,231
Net cash used in investing activities	( 2,775)	( 5,170)
<b>Cash flows from financing activities:</b>		
Borrowings on credit facility	-	4,500
Repayment of debt	-	( 3,847)
Payment of fees for credit facility	-	( 174)
Repayments of insurance premium finance note payable	( 286)	( 236)
Exercise of warrant	-	195
Shares withheld to settle tax withholding obligations for restricted stock awards	( 151)	( 307)
Dividends paid	( 1,192)	( 578)
Repurchases of common stock	( 241)	-
Net cash used in financing activities	( 1,870)	( 447)
Net decrease in cash and equivalents	( 3,236)	( 1,955)
Cash and equivalents, beginning of period	4,411	4,422
Cash and equivalents, end of period	\$ 1,175	\$ 2,467

The accompanying notes are an integral part of these unaudited condensed consolidated financial statements. Please see *Note-15- Supplemental Disclosures of Cash Flow Information*.

**U.S. ENERGY CORP. AND SUBSIDIARIES**  
**NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**

**1. ORGANIZATION, OPERATIONS AND SIGNIFICANT ACCOUNTING POLICIES**

**Organization and Operations**

U.S. Energy Corp. (collectively with its wholly-owned subsidiaries, Energy One LLC ("Energy One") and New Horizon Resources LLC ("New Horizon Resources"), referred to as the "Company" in these Notes to Unaudited Condensed Consolidated Financial Statements) is incorporated in the State of Delaware. The Company's principal business activities are focused on the acquisition and development of onshore oil and natural gas properties in the United States, which the Company considers a single operating segment. Our principal properties and operations are in the Rockies region (Montana, Wyoming and North Dakota), the Mid-Continent (Oklahoma, Kansas and North and East Texas), and the West Texas, South Texas, and Gulf Coast regions.

**Basis of Presentation**

The accompanying unaudited condensed consolidated financial statements are presented in accordance with U.S. generally accepted accounting principles ("GAAP") and have been prepared by the Company pursuant to the rules and regulations of the Securities and Exchange Commission (the "SEC") regarding interim financial reporting. Accordingly, certain information and footnote disclosures required by GAAP for complete financial statements have been condensed or omitted in accordance with such rules and regulations. In the opinion of management, all adjustments (consisting of normal recurring adjustments) considered necessary for a fair presentation of the condensed consolidated financial statements have been included.

For further information, refer to the consolidated financial statements and footnotes thereto included in our Annual Report on Form 10-K for the year ended December 31, 2022, as filed with the SEC on April 13, 2023. Our financial condition as of June 30, 2023, and operating results for the three and six months ended June 30, 2023, are not necessarily indicative of the financial condition and results of operations that may be expected for any future interim period or for the year ending December 31, 2023.

**Use of Estimates**

The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Significant estimates include the fair value of oil and gas properties acquired, oil and natural gas reserves that are used in the calculation of depreciation, depletion, amortization, and impairment of the carrying value of evaluated oil and natural gas properties; realizability of unevaluated properties; production and commodity price estimates used to record accrued oil and natural gas sales receivables; future prices of commodities used in the valuation of commodity derivative contracts; and the cost and timing of future asset retirement obligations. The Company evaluates its estimates on an on-going basis and bases its estimates on historical experience and on various other assumptions the Company believes to be reasonable. Due to inherent uncertainties, including the future prices of oil and natural gas, these estimates could change in the near term and such changes could be material.

**Recently Adopted Accounting Standards**

On January 1, 2023, the Company adopted Accounting Standards Update ("ASU") 2016-13 to Topic 326, *Financial Instruments-Credit Losses*, as amended by other related ASUs that provided targeted improvements. The standard changes the impairment model for trade receivables and other financial assets measured at amortized cost. This ASU requires the use of a new forward-looking "expected loss" model compared to the previous "incurred loss" model, resulting in accelerated recognition of credit losses. This ASU primarily applies to the Company's accounts receivable balances, of which the majority are received within a short-term period of one to three months. The Company monitors the credit quality of its counterparties through review of collections, credit ratings, and other analyses. The Company develops its estimated allowance for credit losses primarily using an aging method and analyses of historical loss rates as well as consideration of current and future conditions that could impact its counterparties' credit quality and liquidity. The adoption and implementation of this ASU did not have a material impact on the Company's financial statements.

#### **Principles of Consolidation**

The accompanying financial statements have been prepared in conformity with GAAP and include the accounts of U.S. Energy Corp. and its wholly-owned subsidiaries Energy One and New Horizon Resources. U.S. Energy Corp. accounts for its share of oil and gas exploration and production activities, in which it has a direct working interest, by reporting its proportionate share of assets, liabilities, revenues, costs, and cash flows within the relevant lines on the balance sheets, statements of operations, and statements of cash flows. All inter-company balances and transactions have been eliminated in consolidation.

#### **2. ACQUISITIONS**

##### January 2022 Acquisition

On January 5, 2022 (the "Closing Date"), the Company closed the acquisitions (the "Acquisition") contemplated by three separate Purchase and Sale Agreements (the "Purchase Agreements" and the "Closing"), entered into by the Company on October 4, 2021, with each of (a) Lubbock Energy Partners LLC ("Lubbock"); (b) Banner Oil & Gas, LLC, Woodford Petroleum, LLC and Llano Energy LLC (collectively, "Banner"), and (c) Synergy Offshore LLC ("Synergy", and collectively with Lubbock and Banner, the "Sellers"). Pursuant to the Purchase Agreements, the Company acquired certain oil and gas properties from the Sellers, representing a diversified portfolio of primarily operated, producing, oil-weighted assets located across the Rockies, West Texas, Eagle Ford, and Mid-Continent. The acquisition also included certain wells, contracts, technical data, records, personal property and hydrocarbons associated with the acquired assets (collectively with the oil and gas properties acquired, the "Acquired Assets").

The Company accounted for the acquisition of the Acquired Assets as an asset acquisition. The purchase price for the Acquired Assets was (a) \$ 125,000 in cash and 6,568,828 shares of our common stock, as to Lubbock; (b) \$ 1,000,000 in cash, the assumption of \$ 3.3 million of debt, and 6,790,524 shares of common stock, as well as the novation of certain hedges which had a mark to market loss of approximately \$ 3.1 million as of the Closing Date, as to Banner; and (c) \$ 125,000 in cash and 6,546,384 shares of common stock, as to Synergy. The aggregate purchase price under all the Purchase Agreements was \$ 66.4 million, representing \$ 1.25 million in cash, the value of 19,905,736 shares of our common stock on the Closing Date of \$ 64.7 million and purchase price adjustments of \$ 0.5 million. In addition, we assumed various liabilities, including the repayment of \$ 3.3 million in debt, as well as a derivative liability from the novation of the hedges discussed above of \$ 3.1 million, suspense accounts and asset retirement obligations.

	<b>Amount</b>
	(in thousands)
<b>Amounts incurred as of the Closing Date:</b>	
Cash	\$ 1,250
Value of 19,905,736 shares issued	64,694
Purchase price adjustments	487
Transaction costs	1,267
<b>Total consideration paid</b>	<b>67,698</b>
 Debt assumed	
Commodity derivative liabilities assumed	3,347
Suspense accounts assumed	1,276
Employee obligations assumed	100
Asset retirement obligations assumed	9,614
Deferred tax liabilities	2,819
<b>Total liabilities assumed</b>	<b>20,308</b>
 Total consideration paid and liabilities assumed	
	\$ 88,006
 Allocation to acquired assets:	
Proved oil and gas properties <sup>(1)</sup>	87,672
Vehicles	165
Deposit account	169
 <b>Total allocation to acquired assets</b>	<b>\$ 88,006</b>

(1) Included in the above purchase price adjustments is settlement for oil in temporary storage in tank batteries at the leases. The Company does not separately account for oil in temporary storage until the oil is sold and title transfers to the purchaser. Consistent with the Company's accounting policy and reporting of similar transactions this amount was recorded within Evaluated Properties on the Company's condensed consolidated balance sheet.

##### Liberty County, Texas Acquisition

On May 3, 2022, the Company acquired certain operated oil and gas producing properties in Liberty County, Texas, adjacent to its existing assets in the area, for \$ 1.0 million in an all-cash transaction. The effective date of the transaction was April 1, 2022. The assets include approximately 1,022 acres, which are 100% held by production, a gas pipeline and associated infrastructure. In addition, the Company assumed suspense accounts of \$ 0.2 million and asset retirement obligations of \$ 0.5 million. The Company accounted for the acquisition as an asset acquisition.

##### East Texas Acquisition

On July 27, 2022, the Company closed a purchase and sale agreement for the acquisition of properties from ETXENERGY, LLC ("ETXENERGY"). The properties are located in Henderson and Anderson Counties, Texas (the "East Texas Assets"). The properties consist of approximately 16,600 net acres,

all of which are held by production and certain wells and gathering systems. The initial purchase price for the East Texas Assets was \$ 11.9 million in cash. The effective date of the acquisition of the East Texas Assets was June 1, 2022. The Company accounted for the acquisition as an asset acquisition.

	<b>Amount</b>
	(in thousands)
Amounts incurred as of the closing date:	
Cash	\$ 11,875
Purchase price adjustments	( 1,048)
Transaction costs	63
Total consideration paid	<u>10,890</u>
Suspense accounts assumed	380
Asset retirement obligations assumed	1,689
Total liabilities assumed	<u>2,069</u>
Total consideration paid and liabilities assumed	<u>\$ 12,959</u>
Allocation to acquired assets:	
Proved oil and gas properties	<u>\$ 12,959</u>

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### 3. REVENUE RECOGNITION

The Company's operated oil production is sold at the delivery point specified in the contract. The Company collects an agreed-upon index price, net of pricing differentials. The purchaser takes custody, title and risk of loss of the oil at the delivery point; therefore, control passes at the delivery point. The Company does not separately account for oil in temporary storage at the site of production prior to its transfer to the purchaser. The Company recognizes revenue at the net price received when control transfers to the purchaser. Natural gas and natural gas liquid ("NGL") are sold at the lease location, which is generally when control of the natural gas and NGL transfers to the purchaser, and revenue is recognized as the amount received from the purchaser.

The Company does not disclose the values of unsatisfied performance obligations under its contracts with customers as it applies the practical exemption in accordance with Accounting Standards Codification (ASC) 606. The exemption applies to variable consideration that is recognized as control of the product is transferred to the customer. Since each unit of product represents a separate performance obligation, future volumes are wholly unsatisfied, and disclosure of the transaction price allocated to the remaining performance obligations is not required.

The Company reports revenue as its proportionate share of the gross amount received from the purchasers before taking into account transportation costs. Production taxes are reported separately, and transportation costs are included in lease operating expense in the accompanying condensed consolidated statements of operations.

The Company's non-operated revenues are derived from its interest in the sales of oil and natural gas production. The sales of oil and natural gas are made under contracts that operators of the wells have negotiated with third-party customers. Oil and natural gas production is typically sold at delivery points to various purchasers under contract terms that are common in the oil and natural gas industry. Regardless of the contract type, the terms of these contracts compensate the well operators for the value of the oil and natural gas at specified prices, and then the well operators remit payment to the Company for its share in the value of the oil and natural gas sold. Variances between the Company's estimated revenue and actual payments are recorded in the month the payment is received; however, differences have been, and are expected to be, insignificant. Accordingly, the variable consideration is not constrained. As a non-operator of its oil and natural gas properties, the Company records its share of the revenues and expenses based upon the information provided by the operators within the revenue statements.

The Company disaggregates revenues from its share of revenue from the sale of oil and natural gas and liquids by region. The Company's revenues in its Rockies, West Texas, South Texas and Gulf Coast, and Mid-Continent regions for the three and six months ended June 30, 2023 and 2022, are presented in the following table:

	<b>Three Months Ended June 30,</b>		<b>Six Months Ended June 30,</b>	
	2023	2022	2023	2022
(in thousands)				
<b>Revenue:</b>				
<b>Rockies</b>				
Oil	\$ 2,470	\$ 4,587	\$ 4,808	\$ 7,978
Natural gas and liquids	128	343	216	536
Total	<u>\$ 2,598</u>	<u>\$ 4,930</u>	<u>\$ 5,024</u>	<u>\$ 8,514</u>
<b>West Texas, South Texas, and Gulf Coast</b>				
Oil	\$ 3,022	\$ 4,823	\$ 5,978	\$ 8,604
Natural gas and liquids	112	475	321	680
Total	<u>\$ 3,134</u>	<u>\$ 5,298</u>	<u>\$ 6,299</u>	<u>\$ 9,284</u>
<b>Mid-Continent</b>				
Oil	\$ 1,536	\$ 1,825	\$ 3,338	\$ 2,584
Natural gas and liquids	710	1,427	1,590	1,970
Total	<u>\$ 2,246</u>	<u>\$ 3,252</u>	<u>\$ 4,928</u>	<u>\$ 4,554</u>
<b>Combined Total</b>	<b><u>\$ 7,978</u></b>	<b><u>\$ 13,480</u></b>	<b><u>\$ 16,251</u></b>	<b><u>\$ 22,352</u></b>

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#### Significant concentrations of credit risk

The Company has exposure to credit risk in the event of non-payment of oil and natural gas receivables by purchasers of its operated oil and natural gas properties and the joint interest operators of the Company's non-operated oil and natural gas properties. The following table presents the purchasers that

accounted for 10% or more of the Company's total oil and natural gas revenue for at least one of the periods presented:

	Six Months Ended June 30,	
	2023	2022
Purchaser A	23%	23%
Purchaser B	18%	22%

#### 4. LEASES

The Company's operating lease right-of-use assets and lease liabilities are recognized at their discounted present value under the following captions in the condensed consolidated balance sheets at June 30, 2023 and December 31, 2022:

	June 30, 2023	December 31, 2022
	(in thousands)	
Right-of-use assets	\$ 773	\$ 868
Lease liabilities		
Current lease obligation	\$ 176	\$ 189
Long-term lease obligation	704	794
Total lease liabilities	\$ 880	\$ 983

The Company recognizes lease expense on a straight-line basis excluding short-term and variable lease payments, which are recognized as incurred. Short-term lease cost represents payments for office leases with original terms less than one year. Beginning in March 2020, the Company subleased its Denver, Colorado office and recognized sublease income as a reduction of rent expense. The term of the sublease was through the term of the Company's Denver office lease, which terminated on January 31, 2023. Following are the amounts recognized as components of rental expense for the three and six months ended June 30, 2023 and 2022:

	Three Months Ended June 30,		Six Months Ended June 30,	
	2023	2022	2023	2022
			(in thousands)	
Operating lease cost	\$ 49	\$ 69	\$ 114	\$ 100
Short-term lease cost	184	2	453	4
Sublease income	-	(17)	-	(33)
Total lease costs	\$ 233	\$ 54	\$ 567	\$ 71

The Company's Houston office operating lease does not contain implicit interest rates that can be readily determined; therefore, the Company used the incremental borrowing rates in effect at the time the Company entered into the leases.

	As of June 30,	
	2023	2022
	(in thousands)	
Weighted average lease term (years)	4.4	5.1
Weighted average discount rate	4.25%	4.60%

Maturity of operating lease liabilities with terms of one year or more as of June 30, 2023 are presented in the following table:

	June 30, 2023	
	(in thousands)	
2023	\$ 105	
2024	213	
2025	218	
2026	224	
2027	210	
Total lease payments	\$ 970	
Less: imputed interest	(90)	
Total lease liability	\$ 880	

#### 5. OIL AND NATURAL GAS PRODUCTION ACTIVITIES

##### Divestitures

During the six months ended June 30, 2023 there were no divestitures of oil and gas properties. During the six months ended June 30, 2022, the Company divested of the Wildhorse Waterflood Unit in Osage County, Oklahoma, which was part of the Acquired Assets acquired on January 5, 2022. Net proceeds from the sale of the Wildhorse Waterflood Unit were \$ 1.2 million. In addition, in December 2022, the Company sold its approximately 30 % interest in two non-operated wells in Zavala County, Texas and associated acreage of approximately 4,500 acres for \$ 1.1 million. The proceeds from divestitures are recorded as reductions in the full cost pool.

##### Ceiling Test and Impairment

The reserves used in the ceiling test incorporate assumptions regarding pricing and discount rates over which management has no influence in the determination of present value. In the calculation of the ceiling test as of June 30, 2023, the Company used \$ 82.82 per barrel for oil and \$ 4.76 per one million British Thermal Units (MMbtu) for natural gas (as further adjusted for property, specific gravity, quality, local markets and distance from markets) to compute the future cash flows of the Company's producing properties. The discount factor used was 10 %.

For the three and six months ended June 30, 2023, and 2022, the Company did not record ceiling test write downs of its oil and natural gas properties.

#### 6. DEBT

On January 5, 2022, the Company entered into a four-year credit agreement ("Credit Agreement") with Firstbank Southwest ("Firstbank") as administrative agent for one or more lenders (the "Lenders"), which provided for a revolving line of credit with an initial borrowing base of \$ 15 million, and

a maximum credit amount of \$ 100 million. Borrowings under the Credit Agreement are collateralized by a first priority, perfected lien and security interests on substantially all assets of the Company (subject to permitted liens and other customary exceptions). On July 26, 2022, the Company, in anticipation of the closing of the ETXENERGY East Texas acquisition entered into a letter agreement with FirstBank whereby it increased the borrowing base under the Credit Agreement from \$ 15 million to \$ 20 million.

Under the Credit Agreement, revolving loans may be borrowed, repaid and re-borrowed until January 5, 2026, when all outstanding amounts must be repaid. Interest on the outstanding amounts under the Credit Agreement will accrue at an interest rate equal to (a) the greatest of (i) the prime rate in effect on such day, and (b) the Federal Funds rate in effect on such day (as determined in the Credit Agreement) plus 0.50%, and an applicable margin that ranges between 0.25% to 1.25% depending on utilization of the amount of the borrowing base (the "Applicable Margin"). Interest expense recognized on the Credit Agreement and the weighted average interest rates for the three and six months ended June 30, 2023 and 2022 are presented in the following table:

	Three Months Ended June 30,		Six Months Ended June 30,	
	2023	2022	2023	2022
(in thousands)				
Interest expense	\$ 267	\$ 56	\$ 519	\$ 100
Weighted average interest rate	8.9%	4.7%	8.7%	4.5%

The Credit Agreement contains various restrictive covenants and compliance requirements, which include: (i) maintenance of certain financial ratios, as defined in the Credit Agreement tested quarterly, that limit the Company's ratio of total debt to EBITDAX (as defined in the Credit Agreement) to 3:1 and require its ratio of consolidated current assets to consolidated current liabilities (as each is described in the Credit Agreement) to remain at 1:1 or higher; (ii) restrictions on making restricted payments as defined in the Credit Agreement, including the payment of cash dividends and repurchases of equity interests (subject to certain limited rights to make restricted payments as long as no event of default has occurred, or would result from the restricted payment, certain financial ratios are met and the borrowing availability after giving pro forma effect to any borrowing to be made on the date of the restricted payment is greater than, or equal to, 20% of the then existing borrowing base); (iii) limits on the incurrence of additional indebtedness; (iv) a prohibition on the entry into commodity swap contracts exceeding a specified percentage of our expected production; and (v) restrictions on the disposition of assets. As of June 30, 2023, the borrowing base was \$ 20 million, and the Company was in compliance with all financial covenants related to the Credit Agreement.

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The amount outstanding on the Credit Agreement as of June 30, 2023 and December 31, 2022, was \$ 12.0 million.

### 7. COMMODITY DERIVATIVES

The Company's results of operations and cash flows are affected by changes in market prices for crude oil and natural gas. To manage a portion of its exposure to price volatility from producing crude oil and natural gas, the Company may enter into commodity derivative contracts to protect against price declines in future periods. The Company does not enter into derivative contracts for speculative purposes. The Company does not currently apply hedge accounting. Accordingly, changes in the fair value of the derivative contracts are recorded in the condensed consolidated statements of operations and are included as a non-cash adjustment to net income in the operating activities section in the condensed consolidated statement of cash flows.

On January 5, 2022, the Company and NextEra Energy Marketing LLC ("NextEra") entered into an International Swap Dealers Association, Inc. Master Agreement and Schedule (the "Master Agreement"), facilitating the Company to enter into derivative contracts to manage the risk associated with its business relating to commodity prices. The Company's obligations to NextEra under the Master Agreement are secured by liens and security interests which also secure the loans under the Credit Agreement on a pari passu and pro rata basis with the principal of such loans. The structure of the derivative contracts may include swaps, caps, floors, collars, locks, forwards and options.

The Company's entry into and the obligations of the Company under the Master Agreement were required conditions to the January 2022 acquisition closing, pursuant to which the Company was required to assume and novate certain hedges which had a mark to market loss of approximately \$ 3.1 million as of the Closing Date. In addition, on January 12, 2022, the Company entered into additional NYMEX WTI crude oil commodity derivative contracts with NextEra for 2022 and 2023 production. As of June 30, 2023, the Company had commodity derivative contracts outstanding through the fourth quarter of 2023 as summarized in the tables below:

Commodity/ Index/ Maturity Period	Collars			
	Quantity Crude oil (Bbls) <sup>(1)</sup>	Weighted Average Prices		
		Floors	Ceilings	
<b>NYMEX WTI</b>				
<i>Crude Oil 2023 Contracts:</i>				
Third quarter 2023	52,600	\$ 60.00	\$ 81.04	
Fourth quarter 2023	51,200	\$ 60.00	\$ 81.04	
<b>Total 2023</b>	<b>103,800</b>	<b>\$ 60.00</b>	<b>\$ 81.04</b>	

(1) "Bbl" refers to one stock tank barrel, or 42 U.S. gallons liquid volume, used in this report in reference to crude oil or other liquid hydrocarbons.

The following table details the fair value of commodity derivative contracts recorded in the accompanying balance sheets by category:

	June 30, 2023		December 31, 2022		
	(in thousands)				
<b>Derivative assets:</b>					
Current assets		\$ 8	\$ -	\$ -	
<b>Total derivative assets</b>	<b>\$ 8</b>	<b>\$ 8</b>	<b>\$ -</b>	<b>\$ -</b>	
<b>Derivative liabilities:</b>					
Current liabilities		\$ -	\$ 1,694	\$ -	
<b>Total derivative liabilities</b>	<b>\$ -</b>	<b>\$ -</b>	<b>\$ 1,694</b>	<b>\$ -</b>	

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As of June 30, 2023, all commodity derivative contracts held by the Company were subject to master netting arrangements with its counterparty. The

terms of the Company's derivative agreements provide for the offsetting of amounts payable or receivable between it and the counterparty for contracts that settle on the same date. The Company's agreements also provide that in the event of an early termination, the counterparty has the right to offset amounts owed or owing under that and any other agreement. The Company's accounting policy is to offset positions that settle on the same date with the same counterparty. See Note 13-Fair Value Measurements for disclosure of the fair value of derivative assets and liabilities on a gross and net basis.

The following table summarizes the commodity components of the derivative settlement gain (loss) as well as the components of the net derivative loss line-item presentation in the accompanying condensed consolidated statement of operations:

	Three Months Ended June 30,		Six Months Ended June 30,	
	2023	2022	2023	2022
(in thousands)				
Derivative settlement losses:				
Oil contracts	\$ (89)	\$ (2,590)	\$ (466)	\$ (4,137)
Gas contracts	-	(239)	(28)	(350)
Total derivative settlement losses	\$ (89)	\$ (2,829)	\$ (494)	\$ (4,487)
Total net derivative loss:				
Oil contracts	\$ 288	\$ (2,068)	\$ 1,148	\$ (8,364)
Gas contracts	-	(64)	60	(605)
Total net derivative gains (losses)	\$ 288	\$ (2,132)	\$ 1,208	\$ (8,969)

## 8. COMMITMENTS AND CONTINGENCIES

### Contingencies

The Company is subject to litigation and claims arising in the ordinary course of business. The Company accrues for such items when a liability is both probable and the amount can be reasonably estimated. In the opinion of management, the anticipated results of any pending litigation and claims are not expected to have a material effect on the results of operations, the financial position, or the cash flows of the Company.

## 9. SHAREHOLDERS' EQUITY

At June 30, 2023, the Company had 25,071,372 shares of common stock outstanding and 245,000,000 authorized. In addition, as of June 30, 2023, the Company had 5,000,000 authorized but unissued shares of preferred stock. During the three months ended June 30, 2023, the Company paid \$ 241 thousand to repurchase 163,300 shares of common stock as part of a share repurchase plan. On January 5, 2022, the Company issued 19,905,736 shares of common stock in connection with the acquisition of the Acquired Assets.

### Stock Options Plans

From time to time, the Company may grant stock options under its incentive plan covering shares of common stock to employees of the Company. Stock options, when exercised, are settled through the payment of the exercise price in exchange for new shares of stock underlying the option. These awards typically expire ten years from the grant date.

For the three and six months ended June 30, 2023 and 2022, there was no compensation expense related to stock options. As of June 30, 2022, all stock options had vested. No stock options were granted or exercised during the three or six months ended June 30, 2023 or 2022. Stock options for the purchase of 2,913 shares of common stock expired during the six months ended June 30, 2022. The stock options had de minimis intrinsic values for the periods reported. Presented below is information for stock options outstanding and exercisable as of June 30, 2023, and December 31, 2022:

	June 30, 2023		December 31, 2022	
	Shares	Price	Shares	Price
Stock options outstanding and exercisable	28,122	\$ 54.03	28,122	\$ 54.03

The following table summarizes information for stock options outstanding and for stock options exercisable at June 30, 2023:

Number of Shares	Options Outstanding			Options Exercisable		
	Exercise Price Range		Weighted Average Exercise Price	Remaining Contractual Term (years)	Number of Shares	Weighted Average Exercise Price
	Low	High				
16,500	\$ 7.20	\$ 11.60	\$ 10.00	4.3	16,500	\$ 10.00
10,622	90.00	124.80	106.20	0.8	10,622	106.20
1,000	226.20	226.20	226.20	1.2	1,000	226.20
28,122	\$ 7.20	\$ 226.20	\$ 54.03	2.9	28,122	\$ 54.03

### Restricted Stock

The Company grants restricted stock under its incentive plan covering shares of common stock to employees and directors of the Company. In January 2023, 796,434 restricted stock awards were granted to employees and directors from the 2021 Equity Incentive Plan and 2022 Equity Incentive Plan. In addition, in June 2023, per the terms of his employment agreement 100,000 restricted stock awards were issued to the Company's new Chief Financial Officer. The restricted stock awards are time-based awards and are amortized ratably over the requisite two-year service period. Restricted stock vests ratably on each anniversary following the grant date provided the grantee is employed on the vesting date. Forfeitures of restricted stock awards are recognized as they occur. Restricted stock granted to employees, when vested, may be settled through the net issuance of shares, reduced by the number of shares required to pay withholding taxes. Non-vested shares of restricted stock are not included in common shares outstanding until vesting has occurred.

The following table presents the changes in non-vested, time-based restricted stock awards to all employees and directors for the six months ended June 30, 2023:

	Shares	Weighted-Avg. Grant Date Fair Value per Share
Non-vested restricted stock as of December 31, 2022	687,000	3.79
Granted	896,434	2.21
Vested	(273,000)	3.78
Forfeited	(60,000)	2.30
Non-vested restricted stock as of June 30, 2023	<u>1,250,434</u>	<u>2.73</u>

For the three and six months ended June 30, 2023, the Company recognized \$ 0.6 million and \$ 1.3 million, respectively, of stock compensation expense related to restricted stock grants. For the three and six months ended June 30, 2022, the Company recognized \$ 0.6 million and \$ 2.1 million, respectively, of stock compensation expense related to restricted stock grants. Total compensation cost related to non-vested time-based awards not yet recognized in the Company's condensed consolidated statements of operations as of June 30, 2023 was \$ 1.5 million. This cost is expected to be recognized over a weighted average period of 1.9 years.

#### Dividends

During the three-month periods ended March 31 and June 30, 2023, the Company's board of directors approved the declaration and payment of quarterly cash dividends of \$ 0.0225 per share of common stock. For the six months ended June 30, 2023 and 2022, the Company paid dividends of \$ 1.2 million and \$ 0.6 million, respectively. As an update to the existing shareholder returns program, on August 9, 2023, the Board of Directors suspended the Company's dividend payment program, with the associated future capital resources being allocated towards the Company's share repurchase program and repayments of our credit facility's outstanding balance.

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#### Share Repurchase Program

On April 26, 2023, the Board of Directors of the Company authorized and approved a share repurchase program for up to \$ 5.0 million of the currently outstanding shares of the Company's common stock. Subject to any future extensions, the repurchase program is scheduled to expire the earlier of on June 30, 2024, or when a maximum of \$ 5.0 million of the Company's common stock has been repurchased, or when the program is discontinued by the Company.

Under the stock repurchase program, shares are repurchased from time to time in the open market or through negotiated transactions at prevailing market prices, or by other means in accordance with federal securities laws. Repurchases are made at management's discretion at prices management considers to be attractive and in the best interests of both the Company and its stockholders, subject to the availability of stock, general market conditions, the trading price of the stock, alternative uses for capital, and the Company's financial performance. The repurchase program is funded using the Company's working capital. The repurchased shares are cancelled and therefore will not be held in treasury or reissued.

During the three months ended June 30, 2023, the Company paid \$ 0.2 million for the repurchase of 163,300 shares at a weighted average price of \$ 1.48 per share.

#### **10. ASSET RETIREMENT OBLIGATIONS**

The Company has asset retirement obligations ("AROs") associated with the future plugging and abandonment of proved properties. Initially, the fair value of a liability for an ARO is recorded in the period in which the ARO is incurred with a corresponding increase in the carrying amount of the related asset. The liability is accreted to its present value each period and the capitalized cost is depleted over the life of the related asset. If the liability is settled for an amount other than the recorded amount, an adjustment to the full-cost pool is recognized. The Company had no assets that are restricted for the purpose of settling AROs.

The Company recorded \$ 9.6 million of ARO related to the assets acquired in the January 5, 2022 acquisition, \$ 0.5 million of ARO related to the assets acquired in the May 3, 2022 acquisition of Liberty County, Texas assets and \$ 1.7 million of ARO related to the assets acquired in the July 27, 2022 acquisition. See Note 2- Acquisitions.

In the fair value calculation for the ARO there are numerous assumptions and judgments, including the ultimate retirement cost, inflation factors, credit-adjusted risk-free discount rates, timing of retirement and changes in legal, regulatory, environmental, and political environments. To the extent future revisions to assumptions and judgments impact the present value of the existing ARO, a corresponding adjustment is made to the oil and natural gas property balance.

The following is a reconciliation of the changes in the Company's liabilities for asset retirement obligations as of June 30, 2023 and December 31, 2022:

	June 30, 2023	December 31, 2022
	(in thousands)	
Balance, beginning of year	\$ 15,442	\$ 1,461
Acquired or incurred	11	11,811
Cost and life revisions	(43)	1,825
Plugged	(52)	(407)
Sold	-	(189)
Accretion	536	941
Balance, end of period	<u>\$ 15,894</u>	<u>\$ 15,442</u>

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#### **11. INCOME TAXES**

The Company's tax provision or benefit from income taxes for interim periods is determined using an estimate of its annual effective tax rate, adjusted for discrete items, if any. Each quarter the Company updates its estimate of the annual effective tax rate and makes a year-to-date adjustment to the provision. The Company's effective tax rate was approximately 7 % and 45 % for the six months ended June 30, 2023 and 2022, respectively. The primary difference in the Company's effective tax rate and the statutory rate for the six months ended June 30, 2023 related to the movement in the valuation allowance against the Company's net deferred tax assets.

The Company's income tax benefit for the six months ended June 30, 2022 includes a discrete income tax benefit of \$ 2.4 million related to the release of a portion of the Company's previously established valuation allowance to offset deferred tax liabilities arising from the January 5, 2022 transaction.

Deferred taxes are recognized for the expected future tax consequences of temporary differences between the financial statement and tax basis of assets, liabilities, net operating losses and tax credit carry-forwards. We review our deferred tax assets ("DTAs") and valuation allowance on a quarterly basis. As part of our review, we consider positive and negative evidence, including cumulative results in recent years.

The Company recognizes, measures, and discloses uncertain tax positions whereby tax positions must meet a "more-likely-than-not" threshold to be recognized. During the three and six months ended June 30, 2023 and 2022, no adjustments were recognized for uncertain tax positions.

## 12. LOSS PER SHARE

Basic net loss per common share is calculated by dividing net loss attributable to common shareholders by the weighted-average number of common shares outstanding for the respective period. Diluted net loss per common share is calculated by dividing adjusted net loss by the diluted weighted average number of common shares outstanding, which includes the effect of potentially dilutive securities. Potentially dilutive securities for this calculation consist of stock options and unvested shares of restricted common stock, which are measured using the treasury stock method. When the Company recognizes a net loss, as was the case for the three and six months ended June 30, 2023 and the six months ended June 30, 2022, all potentially dilutive shares are anti-dilutive and are consequently excluded from the calculation of dilutive net loss per common share.

The following table sets forth the calculation of basic and diluted net income (loss) per share for the three and six months ended June 30, 2023 and 2022:

	Three Months Ended June 30,		Six Months Ended June 30,	
	2023	2022	2023	2022
(in thousands except per share data)				
Net income (loss)	\$ (2,515)	\$ 122	\$ (3,762)	\$ (3,262)
Basic weighted average common shares outstanding	25,187	24,924	25,183	24,324
Dilutive effect of potentially dilutive securities	-	341	-	-
Diluted weighted average common shares outstanding	25,187	25,265	25,183	24,324
Basic net income (loss) per share	\$ (0.10)	\$ 0.00	\$ (0.15)	\$ (0.13)
Diluted net income (loss) per share	\$ (0.10)	\$ 0.00	\$ (0.15)	\$ (0.13)

For the three and six months ended June 30, 2023 and 2022, potentially dilutive securities excluded from the calculation of weighted average shares because they were anti-dilutive are as follows:

	Three Months Ended June 30,		Six Months Ended June 30,	
	2023	2022	2023	2022
(in thousands)				
Stock options	28	30	28	30
Unvested shares of restricted stock	1,250	-	1,250	787
Total	1,278	30	1,278	817

## 13. FAIR VALUE MEASUREMENTS

The Company's 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 highest priority to quoted prices in active markets (Level 1) and the lowest priority to unobservable data (Level 3). In some cases, the inputs used to measure fair value might fall in different levels of the fair value hierarchy. The lowest level input that is significant to a fair value measurement in its entirety determines the applicable level in the fair value hierarchy. Assessing the significance of a particular input to the fair value measurement in its entirety requires judgment, considering factors specific to the asset or liability, and may affect the valuation of the assets and liabilities and their placement within the hierarchy level. The three levels of inputs that may be used to measure fair value are defined as:

Level 1 - Quoted prices for identical assets and liabilities traded in active exchange markets.

Level 2 - Observable inputs other than Level 1 that are 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, or other observable inputs that can be corroborated by observable market data.

Level 3 - Unobservable inputs supported by little or no market activity for financial instruments whose value is determined using pricing models, discounted cash flow methodologies, or similar techniques, as well as instruments for which the determination of fair value requires significant management judgment or estimation.

The Company has processes and controls in place to estimate fair value. The Company performs due diligence procedures over third-party pricing service providers in order to support their use in the valuation process. Where market information is not available to support internal valuations, independent reviews of the valuations are performed, and any material exposures are evaluated through a management review process.

While the Company believes its valuation methods are appropriate and consistent with other market participants, the use of different methodologies or assumptions to determine the fair value of certain financial instruments could result in a different estimate of fair value at the reporting date. The following is a description of the valuation methodologies used for complex financial instruments measured at fair value:

### Recurring Fair Value Measurements

#### Commodity Derivative Instruments

The Company measures the fair value of commodity derivative contracts using an income valuation technique based on the contract price of the underlying positions, crude oil and natural gas forward curves, discount rates, and Company or counterparty non-performance risk. The fixed-price swaps and collar derivative contracts are included in Level 2. The fair value of commodity derivative contracts and their presentation in our unaudited condensed consolidated balance sheet as of June 30, 2023 are presented below:

	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Total Fair Value	Effect of Netting	Net Fair Value Presented in the Unaudited Condensed Consolidated Balance Sheet
<b>Assets</b>						
<b>Current:</b>						
Commodity derivatives	\$ -	\$ 129	\$ -	\$ 129	\$ (121)	\$ 8
<b>Liabilities</b>						
<b>Current:</b>						
Commodity derivatives	\$ -	\$ (121)	\$ -	\$ (121)	\$ 121	\$ -
Net derivative instruments	\$ -	\$ 8	\$ -	\$ 8	\$ -	\$ 8
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### Marketable Equity Securities

We measure the fair value of marketable equity securities based on quoted market prices obtained from independent pricing services. The Company has an investment in the marketable equity securities of Anfield Energy ("Anfield"), which it acquired as consideration for sales of certain mining operations. Anfield is traded in an active market under the trading symbol AEC:TSXV and has been classified as Level 1.

	June 30, 2023	December 31, 2022
<b>Current assets:</b>		
<b>Marketable equity securities</b>		
Number of shares owned	2,421,180	2,421,180
Quoted market price	\$ 0.03771	\$ 0.04429
 Fair value of marketable equity securities	 \$ 91,293	 \$ 107,234

### Credit Facility

The Company's credit facility approximates fair value because the interest rate is variable and reflective of market rates.

### Other Financial Instruments

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

### Nonrecurring Fair Value Measurements

#### Asset Retirement Obligations

The Company measures the fair value of asset retirement obligations as of the date a well is acquired, the date a well begins drilling, or the date the Company revises its ARO assumptions. The Company's estimated asset retirement obligation is based on historical experience in plugging and abandoning wells, estimated economic lives, estimated plugging and abandonment costs and federal and state regulatory requirements, all unobservable inputs, and therefore, are designated as Level 3 within the valuation hierarchy. The liability is discounted using the credit-adjusted risk-free rate estimated at the time the liability is incurred or revised. The credit adjusted risk-free rate used to discount the Company's plugging and abandonment liabilities range from 7.30 % to 9.75 %. See Note 10-Asset Retirement Obligations.

#### Other Assets and Liabilities

The Company evaluates the fair value on a non-recurring basis of properties acquired in asset acquisitions using inputs that are not observable in the market and are therefore designated as Level 3 inputs within the fair value hierarchy. The Company evaluated the fair value of its January 2022 asset acquisition based on discounted future cash flows using estimated production at estimated prices based on NYMEX strip pricing adjusted for differentials, operating costs, production taxes and development costs, all discounted at 10 %. This evaluation resulted in an estimate of fair value of \$ 87.7 million. The Company has also valued asset acquisitions using a multiple of expected cash flows based on comparable transactions. For the asset acquisition of East Texas assets that was completed on July 27, 2022, the Company used a cash flow multiple of approximately 1.75 times estimated cash flows of \$ 7.3 million.

The Company evaluates the fair value on a non-recurring basis of its 13.84-acre land parcel in Riverton, Wyoming, which is currently listed for sale and classified as held for sale, when circumstances indicate that the value has been impaired. At June 30, 2023, the Company estimated the fair value of its real estate assets based on a market approach with comparison to recent comparable sales, all Level 3 inputs within the fair value hierarchy.

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## 14. OTHER CURRENT ASSETS AND ACCOUNTS PAYABLE AND ACCRUED LIABILITIES

### Other Current Assets

The following table presents the components of other current assets as of the dates indicated:

	June 30, 2023	December 31, 2022
	(in thousands)	
Prepaid expense	\$ 550	\$ 138
Joint interest billings receivable	352	332

Income tax receivable	33	50
Other	38	38
<b>Total other current assets</b>	<b>\$ 973</b>	<b>\$ 558</b>

#### Accounts Payable and Accrued Liabilities.

The following table presents the components of accounts payable and accrued liabilities as of the dates indicated:

	June 30, 2023	December 31, 2022
	(in thousands)	
Accounts payable	\$ 2,538	\$ 2,566
Operating expense and oil and gas property accruals	1,136	1,378
Revenue payables	3,983	3,503
Production taxes payable	370	319
Insurance premium financing	422	54
Other	15	12
<b>Total accounts payable and accrued expenses</b>	<b>\$ 8,464</b>	<b>\$ 7,832</b>

#### 15. SUPPLEMENTAL DISCLOSURES OF CASH FLOW INFORMATION

	Six Months Ended June 30,	
	2023	2022
	(in thousands)	
<b>Cash paid for interest</b>		
	\$ ( 558)	\$ ( 86)
<b>Investing activities:</b>		
Change in capital expenditure accruals	\$ 50	\$ 453
Change in accrual for acquisition costs	-	( 546)
Common stock issued for acquisition of properties	-	64,694
Assumption of commodity derivative liability in acquisition of properties	-	3,152
Assumption of debt in acquisition of properties	-	3,347
Assumption of suspense accounts in acquisition of properties	-	1,276
Addition of operating lease liability and right of use asset	-	953
Asset retirement obligations	( 32)	10,302
<b>Financing activities:</b>		
Financing of insurance premiums with note payable	\$ 654	\$ 588

#### 16. SUBSEQUENT EVENTS

Under the full-cost method of accounting, the net book value of proved oil and gas properties, less related deferred income taxes, may not exceed a calculated "ceiling." The ceiling limitation is the estimated after-tax future net cash flows from proved oil and gas reserves. Estimated future net cash flows are calculated using the unweighted arithmetic average of commodity prices in effect on the first day of each of the previous 12 months, adjusted for location and quality differentials, held flat for the life of the production (except where prices are defined by contractual arrangements), less estimated operating costs, production taxes and future development costs, all discounted at 10 percent per annum. Future cash outflows associated with settling accrued asset retirement obligations are excluded from the calculation.

As of June 30, 2023, no ceiling test write-down of our oil and gas assets was necessary. However, we expect to record a write-down of our oil and gas properties in the third quarter of 2023 due to lower commodity prices used in the calculation of the ceiling test as higher third quarter 2022 realized prices will be removed from the ceiling calculation and replaced with lower third quarter 2023 commodity prices. Depending on actual commodity prices, estimated price differentials, lease operating costs, revisions to reserve estimates, and the amount and timing of capital expenditures, the write-down could be approximately \$ 3 million to \$ 4 million in the third quarter of 2023. Additional write-downs could be incurred in the fourth quarter of 2023.

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

##### Introduction

This information should be read in conjunction with the interim unaudited financial statements and the notes thereto included in this Quarterly Report on Form 10-Q, and the audited financial statements and notes thereto and "[Management's Discussion and Analysis of Financial Condition and Results of Operations](#)" contained in our Annual Report on Form 10-K for the year ended December 31, 2022, filed with the Securities and Exchange Commission on April 13, 2023 (the "[Annual Report](#)").

Certain abbreviations and oil and gas industry terms used throughout this Report are described and defined in greater detail under "[Glossary of Oil and Natural Gas Terms](#)" on page 4 of our Annual Report.

Certain capitalized terms used below and otherwise defined below, have the meanings given to such terms in the footnotes to our unaudited condensed consolidated financial statements included above under "[Part I - Financial Information](#)" – "[Item 1. Financial Statements](#)".

In this Quarterly Report on Form 10-Q, we may rely on and refer to information regarding the industries in which we operate in general from market research reports, analyst reports and other publicly available information. Although we believe that this information is reliable, we cannot guarantee the accuracy and completeness of this information, we have not independently verified any of it, and we have not commissioned any such information.

See also "[Cautionary Statement About "Forward-Looking Statements"](#)" above.

Unless the context requires otherwise, references to the "[Company](#)," "[we](#)," "[us](#)," "[our](#)," "[U.S. Energy](#)," and "[U.S. Energy Corp.](#)" refer specifically to U.S. Energy Corp. and its consolidated subsidiaries.

In addition, unless the context otherwise requires and for the purposes of this report only:

- "Bbl" refers to one stock tank barrel, or 42 U.S. gallons liquid volume, used in this report in reference to crude oil or other liquid hydrocarbons;

- “BOE” refers to barrels of oil equivalent, determined using the ratio of one Bbl of crude oil, condensate or natural gas liquids, to six Mcf of natural gas;
- “Bopd” refers to barrels of oil day;
- “Mcf” refers to a thousand cubic feet of natural gas;
- “Mcfe” means 1,000 cubic feet equivalent, determined using the ratio of six Mcf of natural gas to one Bbl of crude oil, condensate or natural gas liquids;
- “NGL” refers to natural gas liquids;
- “Exchange Act” refers to the Securities Exchange Act of 1934, as amended;
- “SEC” or the “Commission” refers to the United States Securities and Exchange Commission;
- “Securities Act” refers to the Securities Act of 1933, as amended; and
- “WTI” means West Texas Intermediate.

### **Where You Can Find Other Information**

We file annual, quarterly, and current reports, proxy statements and other information with the SEC. The SEC maintains an Internet site that contains reports, proxy and information statements, and other information regarding issuers that file electronically with the SEC like us at <https://www.sec.gov> (our filings can be found at <https://www.sec.gov/cgi-bin/browse-edgar?action=getcompany&CIK=0000101594>) and on the “[Investors – SEC Filings](#)” page of our website at <https://usnrg.com>. Copies of documents filed by us with the SEC are also available from us without charge, upon oral or written request to our Secretary, who can be contacted at the address and telephone number set forth on the cover page of this Report.

### ***Summary of The Information Contained in Management’s Discussion and Analysis of Financial Condition and Results of Operations***

Our Management’s Discussion and Analysis of Financial Condition and Results of Operations (MD&A) is provided in addition to the accompanying unaudited condensed consolidated financial statements and notes to assist readers in understanding our results of operations, financial condition, and cash flows. MD&A is organized as follows:

- **General Overview.** A general overview of the Company and our operations.
- **Recent Developments.** Discussion of recent developments affecting the Company and our operations.
- **Plan of Operations and Strategy.** Discussion of our strategy moving forward and how we plan to seek to increase stockholder value.
- **Critical Accounting Policies and Estimates.** Accounting estimates that we believe are important to understanding the assumptions and judgments incorporated in our reported financial results and forecasts.
- **Results of Operations.** An analysis of our financial results comparing the three and six months ended June 30, 2023 and 2022.
- **Liquidity and Capital Resources.** A discussion of our financial condition, including descriptions of balance sheet information and cash flows.

### **General Overview**

U.S. Energy Corp. was incorporated in the State of Wyoming on January 26, 1966, and reincorporated to Delaware effective on August 3, 2022. We are an independent energy company focused on the acquisition and development of oil and natural gas producing properties in the continental United States. Our principal properties and operations are in the Rockies region (Montana, Wyoming and North Dakota), the Mid-Continent region (Oklahoma, Kansas and North and East Texas), and the West Texas, South Texas and Gulf Coast region.

We have historically explored for and produced oil and natural gas through a non-operator business model, however, during 2020 we acquired operated properties in North Dakota, New Mexico, Wyoming and the Texas Gulf Coast, and on January 5, 2022, we closed the acquisitions of certain oil and gas properties from three separate sellers, representing a diversified portfolio of primarily operated, producing, oil-weighted assets located across the Rockies, West Texas, South Texas and Mid-Continent regions.

Our business strategy is to enhance the value of our acquired operated assets through evaluation of selected properties with the goal of increasing production and reserves. We plan to deploy our capital in a conservative and strategic manner and pursue value-enhancing transactions. We also continuously evaluate strategic alternative opportunities that we believe will enhance stockholder value.

Global commodity and financial markets continue to be subject to heightened levels of uncertainty and volatility as a result of inflation, disruptions resulting from recent bank failures, and the ongoing conflict between Russia and Ukraine and associated economic and trade sanctions on Russia. These circumstances have driven commodity price volatility and have contributed to increased service provider costs as well as other costs and a rise in interest rates, and could have further industry-specific impacts that may require us to adjust our business plan.

### **Material Developments**

#### **Acquisitions**

On January 5, 2022, we closed the acquisitions of assets from three separate Purchase and Sale Agreements entered into by the Company on October 4, 2021, with (i) Lubbock Energy Partners LLC, (ii) Banner Oil & Gas, LLC, Woodford Petroleum, LLC and Llano Energy LLC (collectively, “Banner”), and (iii) Synergy Offshore LLC for approximately \$66.4 million. The acquisition had an effective date of January 1, 2022. The purchase price included payment of \$1.25 million in cash and issuance of 19,905,736 shares of our common stock, valued at \$64.7 million. In addition, we assumed Banner’s debt of approximately \$3.3 million and derivative positions, which were in a loss position of \$3.1 million. The assets acquired include certain oil and gas properties representing a diversified portfolio of primarily operated, producing, oil-weighted assets located across the Rockies, West Texas, South Texas, and Mid-Continent. The acquisition also included certain wells, contracts, technical data, records, personal property and hydrocarbons associated with the acquired assets.

On May 3, 2022, the Company acquired certain operated oil and gas producing properties in Liberty County, Texas, adjacent to its existing assets in the area, for \$1.0 million in an all-cash transaction. The effective date of the transaction was April 1, 2022. The assets include approximately 1,022 acres, which are 100% held by production, a gas pipeline and associated infrastructure. In addition, the Company assumed suspense accounts of \$0.2 million and asset retirement obligations of \$0.5 million. The Company accounted for the acquisition as an asset acquisition.

On June 29, 2022, the Company entered into a Purchase and Sale Agreement (the "PSA") with ETXENERGY, LLC (the "Seller"). Pursuant to the PSA, we agreed to acquire all of the Seller's rights to, and interest in, certain operated producing properties totaling approximately 16,600 net acres, located in Henderson and Anderson Counties, Texas, adjacent to the Company's existing assets in the area. Substantially all of the acreage is developed and/or held by production. The acquisition also included certain wells, pipelines, contracts, technical data, records, personal property and hydrocarbons associated with the Properties, including two pipeline gathering systems and related infrastructure (collectively with the oil and gas properties to be acquired, the "ETXEnergy Assets"). The PSA closed on July 27, 2022, at which time we acquired the ETXEnergy Assets in consideration for the purchase price of \$11.875 million in cash, less purchase price adjustments. The effective date of the acquisition was June 1, 2022.

On July 26, 2022, in anticipation of the closing of the PSA, we entered into a letter agreement with Firstbank whereby we increased our borrowing base under the Credit Agreement from \$15 million to \$20 million, and paid the administrative agent an upfront fee of \$32,500 in connection with such increase (the "Borrowing Base Increase").

#### Dividends

On February 23, 2023 and May 30, 2023, the Company paid a quarterly cash dividends of \$0.0225 per share of common stock outstanding to stockholders of record at the close of business on February 10, 2023 and May 19, 2023. Total dividends paid during the six months ended June 30, 2023 were \$1.2 million. The Board of Directors suspended the Company's dividend payment policy on August 9, 2023, with the associated capital resources going towards the Company's share repurchase program and repayments of our credit facility's outstanding balance.

#### Stock Repurchase Program

On April 26, 2023, the Board of Directors of the Company authorized and approved a share repurchase program for up to \$5.0 million of the currently outstanding shares of the Company's common stock. Subject to any future extensions, the repurchase program is scheduled to expire on the earlier of June 30, 2024, when a maximum of \$5.0 million of the Company's common stock has been repurchased, or when the program is discontinued by the Company.

Under the stock repurchase program, shares may be repurchased from time to time in the open market or through negotiated transactions at prevailing market prices, or by other means in accordance with federal securities laws. Repurchases will be made at management's discretion at prices management considers to be attractive and in the best interests of both the Company and its stockholders, subject to the availability of stock, general market conditions, the trading price of the stock, alternative uses for capital, and the Company's financial performance. The repurchase program will be funded using the Company's working capital.

During the three months ended June 30, 2023, the Company paid \$241 thousand for the repurchase of 163,300 shares at a weighted average price of \$1.48 per share.

#### Full-Cost Method Ceiling Test

As commodity prices have decreased in 2023 relative to 2022 prices, we expect to record a write-down of our oil and gas properties in the third quarter of 2023 due to lower commodity prices being used in the calculation of the full-cost method ceiling test. Depending on actual commodity prices, estimated price differentials, lease operating costs, revisions to reserve estimates, and the amount and timing of capital expenditures, the write-down could be approximately \$3 million to \$4 million in the third quarter of 2023. Additional write-downs could be incurred in the fourth quarter of 2023.

#### **Plan of Operations and Strategy**

Continuing through the second half of 2023 and beyond, we intend to seek additional opportunities in the oil and natural gas sector, including but not limited to further acquisition of assets, participation with current and new industry partners in their exploration and development projects, acquisition of existing companies, and the purchase of oil and natural gas producing assets. In addition, we plan to grow production by performing workovers on operated idle wells acquired in 2022 to return them to production.

Key elements of our business strategy include:

- *Deploy our Capital in a Conservative and Strategic Manner and Review Opportunities to Bolster our Liquidity* . In the current industry environment, maintaining liquidity is critical. Therefore, we plan to be highly selective in the projects we evaluate and plan to review opportunities to bolster our liquidity and financial position through various means.
- *Evaluate and Pursue Value-Enhancing Transactions* . We continuously evaluate strategic alternative opportunities that we believe will enhance shareholder value.

#### **Critical Accounting Policies and Estimates**

The preparation of our unaudited condensed consolidated financial statements in conformity with generally accepted accounting principles in the United States ("GAAP") requires us to make assumptions and estimates that affect the reported amounts of assets, liabilities, revenues and expenses, as well as the disclosure of contingent assets and liabilities at the date of our financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results may differ from these estimates under different assumptions or conditions. A summary of our significant accounting policies is detailed in *Part II, Item 7 – Management's Discussion and Analysis of Financial Condition and Results of Operations* of our 2022 Annual Report on Form 10-K filed with the SEC on April 13, 2023.

#### **Recently Adopted Accounting Standards**

On January 1, 2023, the Company adopted Accounting Standards Update ("ASU") 2016-13 to Topic 326, *Financial Instruments-Credit Losses*. See Note 1 in the accompanying notes to unaudited condensed consolidated financial statements included in Part 1, Item 1 for additional discussion of the impact of the adoption of this ASU on our financial statements and disclosures.

#### **Results of Operations**

For the three months ended June 30, 2023, we recorded a net loss of \$2.5 million, which was primarily due to lower revenues as a result of lower commodity prices, which resulted in reduced revenues on our production during the period. For the three months ended June 30, 2022, we recorded net income of \$0.1 million. In the following sections we discuss our revenue, operating expenses and non-operating income and expenses for the three months ended June 30, 2023, compared to the three months ended June 30, 2022.

**Revenue.** Presented below is a comparison of our oil and gas sales, production quantities and average sales prices for the three months ended June 30, 2023 and 2022:

	Three months ended June 30,		Change			
	2023		2022		Amount	
	(in thousands except average prices and production quantities)				Percent	
<b>Revenue:</b>						
Oil	\$ 7,028	\$ 11,334	\$ (4,306)		(38)%	
Natural gas and liquids	\$ 950	\$ 2,146	\$ (1,196)		(56)%	
<b>Total</b>	<b>\$ 7,978</b>	<b>\$ 13,480</b>	<b>\$ (5,502)</b>		<b>(41)%</b>	
<b>Production quantities:</b>						
Oil (Bbls)	114,900	107,845	7,055		7%	
Natural gas and liquids (Mcfe)	380,419	326,308	54,111		17%	
BOE	178,303	162,230	16,073		10%	
BOE/Day	1,959	1,783	176		10%	
<b>Average sales prices:</b>						
Oil (Bbls)	\$ 61.17	\$ 105.09	\$ (43.92)		(42)%	
Natural gas and liquids (Mcfe)	\$ 2.50	\$ 6.58	\$ (4.08)		(62)%	
BOE	\$ 44.74	\$ 83.09	\$ (38.35)		(46)%	

The decrease in our oil and gas revenue of \$5.5 million for the three months ended June 30, 2023, as compared to the three months ended June 30, 2022, was primarily due to a decrease in commodity pricing of 46% on a per BOE basis, which was partially offset by an increase of 10% in production quantities on a per BOE basis. For the three months ended June 30, 2023, we produced 178,303 BOE, or an average of 1,959 BOE per day, as compared to 162,230 BOE or an average of 1,783 BOE per day during the comparable period in 2022. The increase in our production quantities relates to production from properties in East Texas that we acquired in July 2022. The production mix remained relatively consistent between periods. During the three months ended June 30, 2023, our production was 64% oil and 36% natural gas and liquids compared to 66% oil and 34% natural gas and liquids produced during the three months ended June 30, 2022.

**Oil and Gas Production Costs.** Presented below is a comparison of our oil and gas production costs for the three months ended June 30, 2023 and 2022:

	Three months ended June 30,		Change		
	2023		2022		Amount
	(in thousands)				Percent
Lease operating expense	\$ 3,877	\$ 4,646	\$ (769)		(17)%
Production taxes	\$ 538	\$ 913	\$ (375)		(41)%
<b>Total</b>	<b>\$ 4,415</b>	<b>\$ 5,559</b>	<b>\$ (1,144)</b>		<b>(21)%</b>
Lease operating expense per BOE	\$ 21.75	\$ 28.61	\$ (6.87)		(24)%

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For the three months ended June 30, 2023, lease operating expenses were \$3.9 million or \$21.75 per BOE, a decrease of \$0.8 million when compared to the \$4.6 million or \$28.61 per BOE for the three months ended June 30, 2022. The decrease in lease operating expense was due to a reduction in well workover activity in 2023 when compared to 2022. The decrease on a per BOE basis is the result of increased efficiency from the integration of assets acquired in 2022.

For the three months ended June 30, 2023, production taxes were \$538 thousand, a decrease of \$375 thousand, or 41%, compared to the comparable period of 2022. This decrease was primarily attributable to the decrease in revenues of 41% related to the decreases in commodity pricing as discussed above.

**Depreciation, Depletion and Amortization.** Our depreciation, depletion and amortization ("DD&A") was \$2.9 million and \$2.6 million for the three months ended June 30, 2023 and 2022, respectively. Our depletion rate was \$14.39 per BOE and \$14.20 per BOE for the three months ended June 30, 2023 and 2022, respectively. Our DD&A rate can fluctuate because of acquisitions, changes in drilling and completion costs, impairments, divestitures, changes in the mix of our production, the underlying proved reserve volumes and estimated future development costs.

**General and Administrative Expenses.** Presented below is a comparison of our general and administrative expenses for the three months ended June 30, 2023 and 2022:

	Three months ended June 30,		Change		
	2023		2022		Amount
	(in thousands)				Percent
Compensation and benefits	\$ 1,330	\$ 1,189	\$ 141		12%
Stock-based compensation	607	609	(2)		-%
Professional fees, insurance and other	1,431	844	597		70%
<b>Total</b>	<b>\$ 3,368</b>	<b>\$ 2,642</b>	<b>\$ 726</b>		<b>27%</b>

General and administrative expenses increased by \$0.7 million during the three-month period ended June 30, 2023, as compared to the prior year period. The increase was primarily attributable to an increase in professional fees related to the 2022 audit, additional contract accounting personnel costs and Delaware franchise taxes.

**Non-Operating Income (Expense).** Presented below is a comparison of our non-operating income (expense) for the three months ended June 30, 2023 and 2022:

	Three months ended June 30,		Change	
	2023	2022	Amount	Percent
Commodity derivative gain (loss), net	\$ 288	\$ (2,132)	\$ 2,420	114%
Marketable equity securities gain (loss)	(16)	(121)	105	87%
Other income (expense), net	(6)	(5)	(1)	(20)%
Interest, net	(289)	(60)	(229)	(382)%
<b>Total non-operating income (expense)</b>	<b>\$ (23)</b>	<b>\$ (2,318)</b>	<b>\$ 2,295</b>	<b>99%</b>

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Commodity derivative gain (loss), net, is the result of changes in derivative fair values associated with fluctuations in forward price curves for the commodities underlying our outstanding derivative contracts and the monthly cash settlements of our derivative positions during the period. For the three months ended June 30, 2023, we recognized gains on commodity derivative contracts of \$0.3 million, primarily as the result of a reduction in the mark-to-market liability of our outstanding commodity derivative contracts due to lower commodity prices. See Note 7 *Commodity Derivatives* in the notes to the unaudited condensed consolidated financial statements.

The loss on marketable equity securities represents the change in fair value of our investment in Anfield Energy.

Interest, net represents the interest on our credit facility with Firstbank Southwest. The increase in interest expense, net represents an increase in the amount borrowed on the credit facility as well as an increase in the interest rate. As of June 30, 2023, we had borrowed \$12.0 million on the credit facility as compared to \$4.0 million borrowed as of June 30, 2022. The average interest rate increased to 8.9% for the three months ended June 30, 2023, as compared to 4.7% for the three months ended June 30, 2022. See Note 6 *Debt* in the notes to the unaudited condensed consolidated financial statements.

#### Comparison of our Statements of Operations for the Six Months Ended June 30, 2023 and 2022

For the six months ended June 30, 2023, we recorded a net loss of \$3.8 million, which was primarily due to a loss from operations of \$4.7 million. This loss was partially offset by gains on our commodity derivative contracts of \$1.2 million during the period. Our operating loss is due to lower commodity prices and higher costs for services and materials experienced during the period. For the six months ended June 30, 2022, we recorded a net loss of \$3.3 million.

**Revenue.** Presented below is a comparison of our oil and gas sales, production quantities and average sales prices for the six months ended June 30, 2023 and 2022:

	Six months ended June 30,		Change	
	2023	2022	Amount	Percent
(in thousands except average prices and production quantities)				
<b>Revenue:</b>				
Oil	\$ 14,124	\$ 19,167	\$ (5,033)	(26)%
Natural gas and liquids	2,127	3,185	(1,058)	(33)%
<b>Total</b>	<b>\$ 16,251</b>	<b>\$ 22,352</b>	<b>\$ (6,101)</b>	<b>(27)%</b>
<b>Production quantities:</b>				
Oil (Bbls)	206,211	198,666	7,545	4%
Natural gas and liquids (Mcfe)	764,451	505,651	258,800	51%
BOE	333,620	282,942	50,678	18%
BOE/Day	1,843	1,563	280	18%
<b>Average sales prices:</b>				
Oil (Bbls)	\$ 68.49	\$ 96.48	\$ (27.99)	(29)%
Natural gas and liquids (Mcfe)	\$ 2.78	\$ 6.30	\$ (3.52)	(56)%
BOE	\$ 48.71	\$ 79.00	\$ (30.29)	(38)%

The decrease in our oil and gas revenue of \$6.1 million for the six months ended June 30, 2023 as compared to the six months ended June 30, 2022, was due primarily to a decrease in commodity prices. Our realized price for oil was down 29% and the realized price received for natural gas and liquids was down 56% from the prior year period. Partially offsetting the decrease in revenues from declines in commodity prices was an increase in the volumes we produced during the period. For the six months ended June 30, 2023, we produced 333,620 BOE, or an average of 1,843 BOE per day, as compared to 282,942 BOE or 1,563 BOE per day, during the comparable period in 2022. Our oil production was up 4% and our natural gas and liquids production was up 51% compared to the prior year period. The increase in the volumes of natural gas and liquids produced is primarily due to the acquisition of our East Texas assets in July 2022 with relatively more natural gas production. See Note 2 – *Acquisitions*. The production mix shifted to become slightly less oil weighted in 2023 when compared to 2022. Our BOE production mix was 62% oil and 38% natural gas and liquids during the six months ended June 30, 2023 compared to 70% oil and 30% natural gas and liquids in the comparable period of 2022.

**Oil and Gas Production Costs.** Presented below is a comparison of our oil and gas production costs for the six months ended June 30, 2023 and 2022:

	Six months ended June 30,		Change	
	2023	2022	Amount	Percent
(in thousands)				
Lease operating expense	\$ 8,400	\$ 7,382	\$ 1,018	14%
Production taxes	\$ 1,058	\$ 1,485	\$ (427)	(29)%
<b>Total</b>	<b>\$ 9,458</b>	<b>\$ 8,867</b>	<b>\$ 591</b>	<b>7%</b>
Lease operating expense per BOE	\$ 25.18	\$ 26.09	\$ (0.91)	(3)%

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For the six months ended June 30, 2023, lease operating expenses were \$8.4 million or \$25.18 per BOE, an increase of \$1.0 million when compared to

the \$7.4 million or \$26.09 per BOE for the six months ended June 30, 2022. Lease operating expense per BOE decreased as a result of increased efficiency from the integration of assets acquired in 2022. However, overall lease operating expense increased due to the increase in production period over period. For the six months ended June 30, 2023, production taxes were \$1.1 million, a decrease of 0.4 million, or 29%, compared to the comparable period of 2022. This decrease was primarily attributable to the decrease in oil and natural gas and liquids revenues of 27% related to the decreases in commodity prices discussed above.

*Depreciation, Depletion and Amortization.* Our DD&A rate for the six months ended June 30, 2023, was \$13.99 per BOE, compared to \$13.97 per BOE for the six months ended June 30, 2022. Our DD&A rate can fluctuate because of acquisitions, changes in drilling and completion costs, impairments, divestitures, changes in the mix of our production, the underlying proved reserve volumes and estimated future development costs to develop reserves.

*General and Administrative Expenses.* Presented below is a comparison of our general and administrative expenses for the six months ended June 30, 2023 and 2022:

	Six months ended June 30,		Change	
	2023	2022	Amount	Percent
(in thousands)				
Compensation and benefits	\$ 2,517	\$ 1,818	\$ 699	38%
Stock-based compensation	1,334	2,109	(775)	(37)%
Professional fees, insurance and other	2,289	1,661	628	38%
<b>Total</b>	<b>\$ 6,140</b>	<b>\$ 5,588</b>	<b>\$ 552</b>	<b>10%</b>

General and administrative expenses increased by \$0.6 million during the six-month period ended June 30, 2023, as compared to the prior year period. The increase was primarily attributable to an increase in compensation and benefits of \$0.7 million due to the addition of seven employees added in the last half of 2022 and the first half of 2023. Professional fees, insurance and other expenses increased \$0.6 million, primarily due to increased consulting, accounting, legal and insurance expenses related to the acquisition of properties in January 2022. Stock-based compensation decreased \$0.8 million due to the amortization of stock-based compensation awards granted to employees and directors in January 2022, which were in connection with new directors and officers appointed in connection with the January 2022 acquisition.

*Non-Operating Income (Expense).* Presented below is a comparison of our non-operating income (expense) for the three months ended June 2023 and 2022:

	Six months ended June 30,		Change	
	2023	2022	Amount	Percent
(in thousands)				
Commodity derivative gain (loss), net	\$ 1,208	\$ (8,969)	\$ 10,177	113%
Marketable equity securities gain (loss)	(16)	(40)	24	60%
Other income (expense), net	(6)	(6)	-	-%
Interest, net	(558)	(108)	(450)	(417)%
<b>Total non-operating income (expense)</b>	<b>\$ 628</b>	<b>\$ (9,123)</b>	<b>\$ 9,751</b>	<b>107%</b>

Commodity derivative gain (loss), net is the result of changes in derivative fair values associated with fluctuations in forward price curves for the commodities underlying our outstanding derivative contracts and the monthly cash settlements of our derivative positions during the period. For the six months ended June 30, 2023, we recognized gains on commodity derivative contracts of \$1.2 million for contracts that we assumed in the acquisition, as well as, contracts we added during the period. See Note 7 *Commodity Derivatives* in the notes to the condensed consolidated financial statements.

Loss on marketable equity securities represents the change in fair value of our investment in Anfield Energy. For the six months ended June 30, 2023, we recognized an unrealized loss on marketable equity securities of \$16 thousand as compared to a loss of \$40 thousand for the comparable period of 2022.

Interest, net, represents the interest related to our credit facility with Firstbank Southwest. We had \$12.0 million borrowed on the credit facility at June 30, 2023 compared to \$4.0 million borrowed on the facility at June 30, 2022. During the six months ended June 30, 2023, the interest rate on the Credit Facility increased to an average of 8.7% compared to the average rate during the six months ended June 30, 2022 of 4.5%. See Note 6-*Debt* in the notes to the condensed consolidated financial statements.

#### Liquidity and Capital Resources

Based on the current commodity price environment, we believe we have sufficient liquidity and capital resources to execute our business plan while continuing to meet our current financial obligations. We continue to manage our commitments in order to maintain flexibility with regard to our activity level and capital expenditures.

We do not anticipate operating any drill rigs within the next 12 months or performing any developmental or exploratory drilling except on a limited basis in some of our non-operated properties. We will incur approximate \$0.2 million on lease commitments and approximately \$1.0 million on interest expense assuming no material changes to interest rates over the next 12 months. Our capital budget is typically comprised of return to production workovers, repairs and maintenance, plugging and abandonment costs, and similar activities to support our asset base. We view some of these investments as discretionary for which we can control both the timing and amount of these expenditures. Other activities, such as some repairs and maintenance and plugging activities, may be required from time to time by regulatory bodies. While we do not have an approved budget for 2024, we anticipate any such expenditures would be sourced primarily by operating cash flows. In the event that our operating cash flows are not sufficient to fund these expenditures, we have access to our credit facility and equity markets if such a need arises.

#### Sources of Cash

For the six months ended June 30, 2023, we funded our capital expenditures with cash on hand and cash flows from operating activities. If during the second half of 2023, cash flows are not sufficient to fund our capital expenditures and operations, we may also use borrowings under our credit facility or raise funds through new equity offerings or from other sources of financing and re-evaluate our capital spend program as economic conditions warrant. Additionally, we may enter into carrying cost and sharing arrangements with third parties for certain development programs. All of our sources of liquidity can be affected by the changes in economic conditions, rising interest rate, changes in debt and equity markets, force majeure events, fluctuations in commodity prices, operating costs, tax law changes, and volumes produced, all of which would affect us and our industry.

We have no control over the market prices for oil and gas, although we may be able to influence the amount of our realized revenues from oil and gas through the use of commodity derivative contracts as part of our commodity price risk management program. Commodity derivative contracts may limit the prices we receive from our oil and gas sales if oil and gas prices rise substantially over the price established by the commodity derivative contract. See Note 7- *Commodity Derivatives* in Part I, Item 1 of this report for additional information about our oil and gas commodity derivative contracts currently in place and the timing of the settlement of those contracts.

## Credit Agreement

On January 5, 2022, we entered into a four-year credit agreement with Firstbank Southwest as administrative agent, which provides for a revolving line of credit with a borrowing base of \$20 million, and a maximum credit amount of \$100 million (the "Credit Agreement"). Under the Credit Agreement, revolving loans may be borrowed, repaid and re-borrowed until January 5, 2026, when all outstanding amounts must be repaid. The Credit Agreement contains customary indemnification requirements, representations and warranties and customary affirmative and negative covenants applicable to the Company and its subsidiaries. In addition, the Credit Agreement contains financial covenants, tested quarterly, that limit our ratio of total debt to EBITDAX (as defined in the Credit Agreement) to 3:1 and require our ratio of consolidated current assets to consolidated current liabilities (as each is described in the Credit Agreement) to remain at 1:1 or higher. We were in compliance with all financial covenants as of June 30, 2023. Please refer to *Note 6 - Debt* in Part I, Item 1 of this report for additional discussion.

The borrowing base is redetermined semi-annually on or about April 1 and October 1 of each year during the four-year term of the Credit agreement. At the April 2023 redetermination we reaffirmed the borrowing base. The next borrowing base redetermination date is scheduled for October 1, 2023. Our borrowing base can be adjusted as a result of changes in commodity prices, acquisitions or divestitures of proved properties, or financing activities, all as provided for in the Credit Agreement.

Cash flows provided by our operating activities, proceeds received from divestitures of properties, capital markets activities, and our capital expenditures, including acquisitions, all impact the amount we borrow under our revolving Credit Agreement. The amount outstanding on the Credit Agreement as of June 30, 2023, was \$12.0 million.

## Uses of Cash

We use cash for the acquisition and development of oil and gas properties and for the payment of operating and general and administrative costs, settlements of commodity derivative contracts, debt obligations including interest, share repurchases, and dividends. Expenditures for the acquisition and development of oil and gas properties are the primary use of our capital resources. During the six months ended June 30, 2023, we spent approximately \$2.4 million on capital expenditures.

The amount and allocation of our future capital expenditures will depend upon a number of factors, including our cash flows from operating, investing, and financing activities, our ability to execute our development program, and the number and size of acquisitions that we complete. In addition, the impact of oil and gas, prices on investment opportunities, the availability of capital, tax law changes, and the timing and results of our development activities may lead to changes in funding requirements for future development. We periodically review our capital expenditure budget to assess if changes are necessary based on current and projected cash flows, acquisition and divestiture activities, and other factors. Our 2023 capital program is expected to be approximately \$5.0 million. We will continue to monitor the economic environment through the remainder of the year and adjust our activity level as warranted.

## Cash Flows

The following table summarizes our cash flows for the six months ended June 30, 2023 and 2022:

	Six months ended June 30,		Change
	2023	2022	
(in thousands)			
Net cash provided by (used in):			
Operating activities	\$ 1,409	\$ 3,662	\$ (2,253)
Investing activities	(2,775)	(5,170)	2,395
Financing activities	(1,870)	(447)	(1,423)

**Operating Activities.** Cash provided by operating activities for the six months ended June 30, 2023 was \$1.4 million as compared to cash provided by operating activities of \$3.7 million for the comparable period in 2022. The decrease in cash provided by operating activities is mainly attributable to a reduction in cash receipts for revenues as a result of a decrease in the prices we received for our oil and natural gas production and an increase in lease operating expenses. The increase in lease operating expense is primarily due to higher production volumes, as lease operating expense on a BOE basis decreased period over period. These reductions in operating cash flows were partially offset by decreases in cash paid to settle commodity derivative contracts.

**Investing Activities.** Cash used in investing activities for the six months ended June 30, 2023, was \$2.8 million as compared to \$5.2 million for the comparable period in 2022. The primary use of cash in our investing activities for the six months ended June 30, 2023, was the capital expenditures related to returning idle wells to production and improvements to our gathering system in East Texas.

**Financing Activities.** Cash used in financing activities for the six months ended June 30, 2023, was \$1.9 million as compared to \$0.4 million for the comparable period in 2022. The cash used in financing activities during the six months ended June 30, 2023, was primarily attributable to cash dividends paid of \$1.2 million, cash paid to settle taxes on the vesting of share-based compensation awards of \$0.2 million, cash paid for the repurchase of shares of 0.2 million and principal payments on our insurance premium finance note payable of \$0.3 million. Cash used in financing activities during the six months ended June 30, 2022, represented cash dividends paid of \$0.6 million, cash paid to settle taxes on the vesting share-based compensation awards of \$0.3 million, and payments of principal on our insurance premium finance note of \$0.2 million, which were partially offset by borrowings, net of repayments and fees under our credit facility of \$0.5 million and proceeds received on the exercise of stock warrants of \$0.2 million.

## Item 3. Quantitative and Qualitative Disclosures About Market Risk

Pursuant to Item 305(e) of Regulation S-K (§ 229.305(e)), the Company is not required to provide the information required by this Item as it is a "smaller reporting company," as defined by Rule 229.10(f)(1).

## Item 4. Controls and Procedures

### Conclusion Regarding the Effectiveness of Disclosure Controls and Procedures

We are required to maintain disclosure controls and procedures (as defined by Rules 13a-15(e) and 15d-15(e) under the Exchange Act) that are designed to ensure that information required to be disclosed by the Company in reports that it files or submits under the Exchange Act is (i) recorded, processed, summarized and reported within the time periods specified in the SEC rules and forms and (ii) accumulated and communicated to the Company's management, including its principal executive officer and principal financial officer, as appropriate to allow timely decisions regarding required disclosure.

As of June 30, 2023, our management, including our Chief Executive Officer and Chief Financial Officer, carried out an evaluation of the effectiveness of the design and operation of our disclosure controls and procedures as defined in Rules 13a-15(e) and 15d-15(e) of the Exchange Act. Based on the results of the evaluation, the Chief Executive Officer and Chief Financial Officer concluded that our disclosure controls were not effective as of June 30, 2023 to ensure that information required to be disclosed by us in reports that we file or submit under the Exchange Act is recorded, processed, summarized and reported within the time periods specified in SEC rules and forms and is accumulated and communicated to our management, including our Chief Executive Officer and Chief Financial Officer, as appropriate to allow timely decisions regarding required disclosures. Such determination was made in part on material weaknesses in our internal control over financial reporting as of December 31, 2022, as discussed below.

A material weakness is a deficiency, or a combination of deficiencies, in internal control over financial reporting, such that there is a reasonable possibility that a material misstatement of the Company's annual or interim financial statements will not be prevented or detected on a timely basis. As previously reported in our Annual Report on Form 10-K for the year ended December 31, 2022, filed with the SEC on April 13, 2023, in connection with our assessment of the effectiveness of our internal control over financial reporting at the end of our last fiscal year, management identified the following material weaknesses in our internal control over financial reporting as of December 31, 2022 and is in the process of remediating such material weaknesses as of June 30, 2023:

- Third party information technology general controls ("ITGCs") related to our accounting system were not designed appropriately and reliance could not be placed on the processing integrity of the accounting system.

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- Certain control activities with a review component were not implemented and operating effectively for a sufficient portion of the period and did not include sufficient evidence of review procedures performed or formal approval by the reviewer.
- Certain business process controls were not implemented for a sufficient portion of the period and did not include sufficient evidence of operation.

#### **Limitations on Effectiveness of Controls and Procedures**

In designing and evaluating the disclosure controls and procedures, management recognizes that any controls and procedures, no matter how well designed and operated, can provide only reasonable assurance of achieving the desired control objectives. In addition, the design of disclosure controls and procedures must reflect the fact that there are resource constraints and that management is required to apply its judgment in evaluating the benefits of possible controls and procedures relative to their costs.

#### **Changes in Internal Control over Financial Reporting**

Except as disclosed below there were no changes in our internal control over financial reporting during the six months ended June 30, 2023, that have materially affected or are reasonably likely to materially affect, our internal control over financial reporting.

During the quarter ended June 30, 2023, we contracted for an interim Corporate Controller and on July 24, 2023, we hired a Corporate Controller to supervise the day-to-day accounting function. In addition, we have made efforts to improve the documentation of review for control activities with a review component to include review notes and documented approval by the reviewer. In addition, we have begun evaluating accounting systems for conversion. The accounting system we select will have ITGCs that are designed effectively by the software provider and independently tested.

## **PART II – OTHER INFORMATION**

#### **Item 1. Legal Proceedings**

From time to time, we may become party to litigation or other legal proceedings that we consider to be a part of the ordinary course of our business. We are not currently involved in any legal proceedings that we believe could reasonably be expected to have a material adverse effect on our business, prospects, financial condition or results of operations. We may become involved in material legal proceedings in the future.

#### **Item 1A. Risk Factors.**

There have been no material changes from the risk factors previously disclosed in the Company's Annual Report on Form 10-K for the year ended December 31, 2022, as filed with the SEC on April 13, 2023, under the heading "[Item 1A. Risk Factors](#)", except as discussed below, and investors should review the risks provided in the Annual Report, prior to making an investment in the Company. The business, financial condition and operating results of the Company can be affected by a number of factors, whether currently known or unknown, including but not limited to those described in the Annual Report, under "[Item 1A. Risk Factors](#)", and below, any one or more of which could, directly or indirectly, cause the Company's actual financial condition and operating results to vary materially from past, or from anticipated future, financial condition and operating results. Any of these factors, in whole or in part, could materially and adversely affect the Company's business, financial condition, operating results and stock price.

#### ***Our stock repurchases are discretionary and even if effected, they may not achieve the desired objectives.***

On April 26, 2023, the Board of Directors of the Company authorized and approved a share repurchase program for up to \$5.0 million of the currently outstanding shares of the Company's common stock. Subject to any future extensions, the repurchase program is scheduled to expire on June 30, 2024. Under the stock repurchase program, shares may be repurchased from time to time in the open market or through negotiated transactions at prevailing market rates, or by other means in accordance with federal securities laws. Repurchases will be made at management's discretion at prices management considers to be attractive and in the best interests of both the Company and its stockholders, subject to the availability of stock, general market conditions, the trading price of the stock, alternative uses for capital, and the Company's financial performance. During the three months ended June 30, 2023, the Company paid \$241 thousand for the repurchase of 163,300 shares at a weighted average price of \$1.48 per share in open market transactions. The program does not obligate the Company to acquire a minimum amount of shares.

There can be no assurance that any repurchases pursuant to our stock repurchase program will enhance stockholder value because the market price of our common stock may decline below the levels at which we repurchase such shares. The amounts and timing of the repurchases may also be influenced by general market conditions, regulatory developments (including recent legislative actions which, subject to certain conditions, may impose an excise tax of 1% on our stock repurchases) and the prevailing price and trading volumes of our common stock. If our financial condition deteriorates or we decide to use our cash for other purposes, we may suspend repurchase activity at any time.

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#### ***Our Board of Directors has determined to suspend our quarterly cash dividend.***

On April 13, 2022, August 5, 2022, November 7, 2022, February 9, 2023 and May 18, 2023, the Company's Board of Directors approved the declaration and payment of quarterly cash dividends of \$0.0225 per share of common stock. Our Board of Directors, at its sole discretion, determines the amount of

the quarterly dividends to be distributed to our shareholders, if any, based on consideration of a number of factors including, but not limited to, our results of operations, cash flow and capital requirements, economic conditions, tax considerations, borrowing capacity and other factors, including future acquisitions and divestitures. Consequently, our dividend levels may fluctuate. On August 9, 2023, the Board of Directors determined it appropriate to suspend dividend payments, with the associated future capital resources being allocated towards the Company's share repurchase program and repayments of the outstanding balance on our credit facility. The Board of Directors may or may not reinstate future dividend payments in the future, the amount and frequency of which will be determined at the sole discretion of the Board. To the extent that the dividend is not reinstated in the future, only appreciation of the price of our common stock, which may not occur, will provide a return to our stockholders.

***We may enter into strategic transactions in the future which may result in a material change in our operations and/or a change of control.***

In the future, we or our majority stockholders, may enter into transactions with, or undertake transactions with, parties seeking to merge and/or acquire us and/or our operations. While neither we, nor our majority stockholders have entered into any such agreements or understandings to date, in the event that we or our majority stockholders do enter into such a transaction or transactions in the future, it could result in a change in our business focus, the acquisition of significant amounts of our outstanding common stock, or a change in our majority stockholders. We and our majority stockholders have not entered into any agreements relating to any strategic transaction involving the Company as of the date of this filing and may never enter into such agreement(s) in the future. Any future strategic transaction involving the Company or its operations may have a material effect on our operations, cash flows, results of operations, prospects, plan of operations, the listing of our common stock on the Nasdaq Capital Market, our officers, directors and majority stockholders, and the value of our securities.

***We have written down, and may in the future be forced to further write-down, material portions of our assets due to low oil and natural gas prices.***

The full cost method of accounting is used for oil and gas acquisition, exploration, development and production activities. Under the full cost method, all costs associated with the acquisition, exploration, and development of oil and natural gas properties are capitalized and accumulated in a country-wide cost center. This includes any internal costs that are directly related to development and exploration activities, but does not include any costs related to production, general corporate overhead, or similar activities. Proceeds received from disposals are credited against accumulated cost, except when the sale represents a significant disposal of reserves, in which case a gain or loss is recognized. The sum of net capitalized costs and estimated future development and dismantlement costs for each cost center is depleted on the equivalent unit-of-production method, based on proved oil and natural gas reserves. Excluded from amounts subject to depreciation, depletion, and amortization are costs associated with unevaluated properties.

Under the full cost method, net capitalized costs are limited to the lower of (a) unamortized cost reduced by the related net deferred tax liability and asset retirement obligations, and (b) the cost center ceiling. The cost center ceiling is defined as the sum of (i) estimated future net revenue, discounted at 10% per annum, from proved reserves, based on unescalated costs, adjusted for contract provisions, any financial derivatives qualifying as accounting hedges and asset retirement obligations, and unescalated oil and natural gas prices during the period, (ii) the cost of properties not being amortized, and (iii) the lower of cost or market value of unproved properties included in the cost being amortized, less income tax effects related to tax assets directly attributable to the natural gas and crude oil properties. If the net book value reduced by the related net deferred income tax liability and asset retirement obligations exceeds the cost center ceiling limitation, a non-cash impairment charge is required in the period in which the impairment occurs.

We perform a quarterly ceiling test for our only oil and natural gas cost center, which is the United States. During 2022 we did not record a ceiling test write-down. The ceiling test incorporates assumptions regarding pricing and discount rates over which we have no influence in the determination of present value. In arriving at the ceiling test for the year ended December 31, 2022, we used an average price applicable to our properties of \$93.67 per barrel for oil and \$6.36 per Mcfe for natural gas, based on average prices per barrel of oil and per Mcfe of natural gas at the first day of each month of the 12-month period prior to the end of the reporting period, to compute the future cash flows of each of the producing properties at that date.

Through the period ended June 30, 2023, no ceiling test write-down of our oil and gas assets was necessary. However, we expect to record a write-down of our oil and gas properties in the third quarter of 2023 due to lower commodity prices used in the calculation of the ceiling test as higher third quarter 2022 realized prices will be removed from the ceiling calculation and replaced with lower third quarter 2023 commodity prices. Depending on actual commodity prices, estimated price differentials, lease operating costs, revisions to reserve estimates, and the amount and timing of capital expenditures, the write-down could be approximately \$3 million to \$4 million in the third quarter of 2023. Additional write-downs could be incurred in the fourth quarter of 2023.

Material future write-downs or impairments of our oil and gas properties may have a material adverse effect on our assets and/or our financial condition, either of which may cause the value of our securities to decline in value.

**Item 2. Unregistered Sales of Equity Securities and Use of Proceeds.**

***Sales of Unregistered Securities***

There have been no sales of unregistered securities during the quarter ended June 30, 2023, and from the period from July 1, 2023, to the filing date of this Report.

***Purchases of Equity Securities by the Issuer and Affiliated Purchasers***

The following table sets forth share repurchase activity for the respective periods:

Period	Total Number of Shares Purchased	Average Price Paid Per Share	Announced Plans or Programs <sup>(1)</sup>	Approximate Dollar Value of Shares that May Yet Be Purchased Under the Plans or Programs <sup>(1)</sup>
April 1 – April 30, 2023	—	\$ —	—	\$ —
May 1 - May 31, 2023	65,400	\$ 1.42	65,400	\$ 4,907,348
June 1 – June 30, 2023	97,900	\$ 1.51	97,900	\$ 4,759,207
Total	163,300	\$ —	163,300	\$ 4,759,207

<sup>(1)</sup> On April 26, 2023, the Board of Directors of the Company authorized and approved a share repurchase program for up to \$5.0 million of the currently outstanding shares of the Company's common stock. Subject to any future extensions, the repurchase program is scheduled to expire on June 30, 2024, when a maximum of \$5.0 million of the Company's common stock has been repurchased, or when the program is discontinued by the Company. Under the stock repurchase program, shares may be repurchased from time to time in the open market or through negotiated transactions at prevailing market rates, or by other means in accordance with federal securities laws. Repurchases are made at management's discretion at prices management considers to be attractive and in the best interests of both the Company and its stockholders, subject to the availability of stock, general market conditions, the trading price of the stock, alternative uses for capital, and the Company's financial performance. The repurchase program is funded using the Company's working capital. The program does not obligate the Company to acquire a minimum amount of shares.

**Item 3. Defaults Upon Senior Securities.**

Not applicable.

**Item 4. Mine Safety Disclosures.**

Not applicable.

**Item 5. Other Information.**

The Current Report on Form 8-K filed by the Company with the SEC on June 5, 2023, mistakenly discussed the grant to Mr. Mark Zajac, the then newly appointed Chief Financial Officer (CFO) and Principal Financial and Accounting Officer of the Company, of 100,000 restricted stock units of the Company (the "RSUs") under the Company's 2022 Equity Incentive Plan, with such RSUs vesting to Mr. Zajac at the rate of 1/2 of such RSUs on each of June 1, 2024 and 2025, provided he is still employed by the Company on such dates.

The Board actually approved the grant of 100,000 shares of Restricted Stock to Mr. Zajac, instead of RSUs, which shares of Restricted Stock had identical vesting terms as the RSUs discussed above and the references to RSUs in the Form 8-K were in error.

On August 9, 2023, the Board of Directors determined that it was appropriate to suspend dividend payments moving forward, with the associated future capital resources being allocated towards the Company's share repurchase program and repayments of the outstanding balance on our credit facility. The Board of Directors may or may not reinstate future dividend payments in the future, the amount and frequency of which will be determined at the sole discretion of the Board. To the extent that the dividend is not reinstated in the future, only appreciation of the price of our common stock, which may not occur, will provide a return to our stockholders.

**Item 6. Exhibits**

Exhibit No.	Description	Form	File No.	Exhibit	Filing Date	Filed / Furnished Herewith
10.1†	<a href="#">Offer Letter dated June 1, 2023, by and between U.S. Energy Corp. and Mark Zajac</a>	8-K	000-06814	10.2	6/16/2023	
10.2†	<a href="#">Form of U.S. Energy Corp. Form of Restricted Stock Grant Agreement (2022 Equity Incentive Plan) (1)</a>	S-8	333-267267	4.3	9/2/2022	
10.3†	<a href="#">Separation and Release Agreement, dated July 31, 2023, by and between U.S. Energy Corp. and Donald A. Kessel</a>	8-K	000-06814	10.1	8/01/2023	
16.1	<a href="#">Letter from Plante &amp; Moran, PLLC, dated June 15, 2023</a>	8-K	000-06814	16.1	6/16/2023	
31.1*	<a href="#">Certification of Chief Executive Officer pursuant to Section 302 of the Sarbanes – Oxley Act of 2002</a>					X
31.2*	<a href="#">Certification of Chief Financial Officer pursuant to Section 302 of the Sarbanes – Oxley Act of 2002</a>					X
32.1♦	<a href="#">Certification of Chief Executive Officer under Rule 13a-14(b)</a>					X
32.2♦	<a href="#">Certification of Chief Financial Officer under Rule 13a-14(b)</a>					X
101.INS	Inline XBRL Instance Document - the instance document does not appear in the Interactive Data File because its XBRL tags are embedded within the Inline XBRL document					X
101.SCH*	Inline XBRL Schema Document					X
101.CAL*	Inline XBRL Calculation Linkbase Document					X
101.DEF*	Inline XBRL Definition Linkbase Document					X
101.LAB*	Inline XBRL Label Linkbase Document					X
101.PRE*	Inline XBRL Presentation Linkbase Document					X
104*	Inline XBRL for the cover page of this Quarterly Report on Form 10-Q, included in the Exhibit 101 Inline XBRL Document Set					X

\* Filed herewith.

† Exhibit constitutes a management contract or compensatory plan or agreement.

♦ Furnished herewith.

**SIGNATURES**

Pursuant to the requirements of Section 13 or 15(d) of the Securities Exchange Act of 1934, the Registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

U.S. ENERGY CORP.

Date: August 14, 2023

By: /s/ Ryan L. Smith

RYAN L. SMITH,  
Chief Executive Officer (Principal Executive Officer)

Date: August 14, 2023

By: /s/ Mark L. Zajac



## CERTIFICATION

I, Ryan L. Smith, certify that:

1. I have reviewed this Quarterly Report on Form 10-Q of U.S. Energy Corp.;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant, as of, and for, the periods presented in this report;
4. I am responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:
  - (a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
  - (b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
  - (c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
  - (d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
5. I have disclosed, based on my most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):
  - (a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
  - (b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: August 14, 2023

By: */s/ Ryan L. Smith*  
**Ryan L. Smith**  
**Chief Executive Officer**  
**(Principal Executive Officer)**

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**CERTIFICATION**

I, Mark L. Zajac, certify that:

1. I have reviewed this Quarterly Report on Form 10-Q of U.S. Energy Corp.;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant, as of, and for, the periods presented in this report;
4. I am responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:
  - (a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
  - (b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
  - (c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
  - (d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
5. I have disclosed, based on my most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):
  - (a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
  - (b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: August 14, 2023

By: /s/ Mark L. Zajac

**Mark L. Zajac**  
**Chief Financial Officer**  
**(Principal Financial and Accounting Officer)**

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**CERTIFICATION PURSUANT TO  
18 U.S.C. SECTION 1350, AS ADOPTED PURSUANT TO  
SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002**

In connection with the Quarterly Report on Form 10-Q of U.S. Energy Corp. (the "Company") for the period ended June 30, 2023 as filed with the Securities and Exchange Commission on the date hereof (the "Report"), I Ryan L. Smith, certify, pursuant to 18 U.S.C. § 1350, as adopted pursuant to § 906 of the Sarbanes-Oxley Act of 2002, to my knowledge, that:

- (1) The Report fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934; and
- (2) The information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company, at the dates and for the periods indicated.

Date: August 14, 2023

By: /s/ Ryan L. Smith

**Ryan L. Smith  
Chief Executive Officer  
(Principal Executive Officer)**

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**CERTIFICATION PURSUANT TO  
18 U.S.C. SECTION 1350, AS ADOPTED PURSUANT TO  
SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002**

In connection with the Quarterly Report on Form 10-Q of U.S. Energy Corp. (the "Company") for the period ended June 30, 2023 as filed with the Securities and Exchange Commission on the date hereof (the "Report"), I, Mark L. Zajac, certify, pursuant to 18 U.S.C. § 1350, as adopted pursuant to § 906 of the Sarbanes-Oxley Act of 2002, to my knowledge, that:

- (1) The Report fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934; and
- (2) The information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company, at the dates and for the periods indicated.

Date: August 14, 2023

By: */s/ Mark L. Zajac*

**Mark L. Zajac  
Chief Financial Officer  
(Principal Financial and Accounting Officer)**

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