LINN ENERGY, LLC
Form 10-Q
August 07, 2014

UNITED STATES SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549
Form 10-Q

x QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the Quarterly Period Ended June 30, 2014

OR

¨ TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
for the transition period from _______________ to _______________

Commission File Number: 000-51719

LINN ENERGY, LLC
(Exact name of registrant as specified in its charter)

Delaware (State or other jurisdiction of incorporation or organization)	65-1177591 (IRS Employer Identification No.)
600 Travis, Suite 5100 Houston, Texas (Address of principal executive offices)	77002 (Zip Code)

(281) 840-4000
(Registrant’s telephone number, including area code)

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

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

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See the definitions of “large accelerated filer,” “accelerated filer,” and “smaller reporting company” in Rule 12b-2 of the Exchange Act.
Large accelerated filer x Accelerated filer ¨ Non-accelerated filer ¨ Smaller reporting company ¨
Indicate by check mark whether registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). Yes ¨ No x
As of July 31, 2014, there were 331,729,246 units outstanding.

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GLOSSARY OF TERMS

As commonly used in the oil and natural gas industry and as used in this Quarterly Report on Form 10-Q, the following terms have the following meanings:

Bbl. One stock tank barrel or 42 United States gallons liquid volume.
Bcf. One billion cubic feet.
Bcfe. One billion cubic feet equivalent, determined using a ratio of six Mcf of natural gas to one Bbl of oil, condensate or natural gas liquids.
Btu. One British thermal unit, which is the heat required to raise the temperature of a one-pound mass of water from 58.5 degrees to 59.5 degrees Fahrenheit.
MBbls. One thousand barrels of oil or other liquid hydrocarbons.
MBbls/d. MBbls per day.
Mcf. One thousand cubic feet.
Mcfe. One thousand cubic feet equivalent, determined using the ratio of six Mcf of natural gas to one Bbl of oil, condensate or natural gas liquids.
MMBbls. One million barrels of oil or other liquid hydrocarbons.
MMBtu. One million British thermal units.
MMcf. One million cubic feet.
MMcf/d. MMcf per day.
MMcfe. One million cubic feet equivalent, determined using a ratio of six Mcf of natural gas to one Bbl of oil, condensate or natural gas liquids.
MMcfe/d. MMcfe per day.
MMMBtu. One billion British thermal units.
NGL. Natural gas liquids, which are the hydrocarbon liquids contained within natural gas.

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PART I – FINANCIAL INFORMATION
Item 1. Financial Statements
LINN ENERGY, LLC
CONDENSED CONSOLIDATED BALANCE SHEETS
(Unaudited)

	June 30, 2014	December 31, 2013
	(in thousands, except unit amounts)	
ASSETS		
Current assets:		
Cash and cash equivalents	$38,339	$52,171
Accounts receivable – trade, net	549,589	488,202
Derivative instruments	91,611	176,130
Other current assets	107,882	99,437
Total current assets	787,421	815,940
Noncurrent assets:		
Oil and natural gas properties (successful efforts method)	18,684,209	17,888,559
Less accumulated depletion and amortization	(4,051,761)	(3,546,284)
	14,632,448	14,342,275
Other property and equipment	676,294	647,882
Less accumulated depreciation	(135,316)	(110,939)
	540,978	536,943
Derivative instruments	175,537	682,002
Other noncurrent assets	132,280	127,804
	307,817	809,806
Total noncurrent assets	15,481,243	15,689,024
Total assets	$16,268,664	$16,504,964
LIABILITIES AND UNITHOLDERS' CAPITAL		
Current liabilities:		
Accounts payable and accrued expenses	$860,171	$849,624
Derivative instruments	59,907	28,176
Other accrued liabilities	138,378	163,375
Current portion of long-term debt	—	211,558
Total current liabilities	1,058,456	1,252,733
Noncurrent liabilities:		
Credit facilities	3,418,175	2,733,175
Term loan	500,000	500,000
Senior notes, net	5,726,176	5,725,483
Derivative instruments	8,827	4,649
Other noncurrent liabilities	395,907	397,497
Total noncurrent liabilities	10,049,085	9,360,804
Commitments and contingencies (Note 10)		

Unitholders' capital:		
331,667,975 units and 329,661,161 units issued and outstanding at June 30, 2014, and December 31, 2013, respectively	5,854,727	6,291,824
Accumulated deficit	(693,604)	(400,397)
	5,161,123	5,891,427
Total liabilities and unitholders' capital	$16,268,664	$16,504,964

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

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LINN ENERGY, LLC
CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS
(Unaudited)

	Three Months Ended June 30,		Six Months Ended June 30,	
	2014	2013	2014	2013
	(in thousands, except per unit amounts)			
Revenues and other:				
Oil, natural gas and natural gas liquids sales	$967,850	$488,207	$1,906,727	$950,939
Gains (losses) on oil and natural gas derivatives	(408,788)	326,733	(650,281)	218,363
Marketing revenues	30,273	17,222	60,819	27,074
Other revenues	7,616	6,663	13,273	11,509
	596,951	838,825	1,330,538	1,207,885
Expenses:				
Lease operating expenses	184,901	83,584	378,934	172,305
Transportation expenses	44,854	29,298	90,484	56,481
Marketing expenses	23,274	9,360	44,346	16,734
General and administrative expenses	66,906	46,305	146,134	104,871
Exploration costs	1,551	818	2,642	3,044
Depreciation, depletion and amortization	274,435	198,629	542,236	396,070
Impairment of long-lived assets	—	(14,851)	—	42,202
Taxes, other than income taxes	68,531	32,397	134,244	72,068
(Gains) losses on sale of assets and other, net	5,467	(959)	8,053	2,213
	669,919	384,581	1,347,073	865,988
Other income and (expenses):				
Interest expense, net of amounts capitalized	(134,300)	(103,847)	(268,113)	(204,206)
Loss on extinguishment of debt	—	(4,187)	—	(4,187)
Other, net	(2,549)	(2,182)	(4,852)	(3,825)
	(136,849)	(110,216)	(272,965)	(212,218)
Income (loss) before income taxes	(209,817)	344,028	(289,500)	129,679
Income tax expense (benefit)	(1,947)	(1,129)	3,707	6,407
Net income (loss)	$(207,870)	$345,157	$(293,207)	$123,272
Net income (loss) per unit:				
Basic	$(0.64)	$1.47	$(0.91)	$0.52
Diluted	$(0.64)	$1.46	$(0.91)	$0.52
Weighted average units outstanding:				
Basic	328,844	233,448	328,588	233,313
Diluted	328,844	233,910	328,588	233,800
Distributions declared per unit	$0.725	$0.725	$1.45	$1.45

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

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LINN ENERGY, LLC
CONDENSED CONSOLIDATED STATEMENT OF UNITHOLDERS' CAPITAL
(Unaudited)

	Units	Unitholders' Capital	Accumulated Deficit	Total Unitholders' Capital
	(in thousands)			
December 31, 2013	329,661	$6,291,824	$(400,397)	$5,891,427
Issuance of units	2,007	7,887	—	7,887
Distributions to unitholders		(480,583)	—	(480,583)
Unit-based compensation expenses		32,583	—	32,583
Excess tax benefit from unit-based compensation		3,016	—	3,016
Net loss		—	(293,207)	(293,207)
June 30, 2014	331,668	$5,854,727	$(693,604)	$5,161,123

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

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LINN ENERGY, LLC
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
(Unaudited)

	Six Months Ended June 30, 2014	2013
	(in thousands)	
Cash flow from operating activities:		
Net income (loss)	$(293,207)	$123,272
Adjustments to reconcile net income (loss) to net cash provided by operating activities:		
Depreciation, depletion and amortization	542,236	396,070
Impairment of long-lived assets	—	42,202
Unit-based compensation expenses	32,583	19,575
Loss on extinguishment of debt	—	4,187
Amortization and write-off of deferred financing fees	6,202	10,905
Losses on sale of assets and other, net	3,506	16,814
Deferred income taxes	3,475	5,725
Derivatives activities:		
Total (gains) losses	650,281	(218,363)
Cash settlements	(23,123)	144,502
Changes in assets and liabilities:		
(Increase) decrease in accounts receivable – trade, net	(61,891)	36,174
(Increase) decrease in other assets	(6,947)	2,260
Increase (decrease) in accounts payable and accrued expenses	113,582	(5,319)
Decrease in other liabilities	(51,062)	(16,648)
Net cash provided by operating activities	915,635	561,356
Cash flow from investing activities:		
Acquisition of oil and natural gas properties and joint-venture funding	(25,891)	(64,381)
Development of oil and natural gas properties	(805,617)	(495,899)
Purchases of other property and equipment	(31,411)	(55,147)
Proceeds from sale of properties and equipment and other	(11,730)	210,899
Net cash used in investing activities	(874,649)	(404,528)
Cash flow from financing activities:		
Proceeds from borrowings	1,095,000	775,000
Repayments of debt	(616,124)	(560,737)
Distributions to unitholders	(480,583)	(341,117)
Financing fees and other, net	(56,127)	(30,656)
Excess tax benefit from unit-based compensation	3,016	591
Net cash used in financing activities	(54,818)	(156,919)
Net decrease in cash and cash equivalents	(13,832)	(91)
Cash and cash equivalents:		
Beginning	52,171	1,243
Ending	$38,339	$1,152

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

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LINN ENERGY, LLC
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(Unaudited)

Note 1 – Basis of Presentation

Nature of Business

Linn Energy, LLC ("LINN Energy" or the "Company") is an independent oil and natural gas company. LINN Energy's mission is to acquire, develop and maximize cash flow from a growing portfolio of long-life oil and natural gas assets. The Company's properties are located in the United States ("U.S."), in the Mid-Continent, the Rockies, the Permian Basin, California, the Hugoton Basin, Michigan, Illinois and east Texas.

Principles of Consolidation and Reporting

The information reported herein reflects all normal recurring adjustments that are, in the opinion of management, necessary for the fair presentation of the results for the interim periods. Certain information and note disclosures normally included in annual financial statements prepared in accordance with U.S. generally accepted accounting principles ("GAAP") have been condensed or omitted under Securities and Exchange Commission ("SEC") rules and regulations; as such, this report should be read in conjunction with the financial statements and notes in the Company's Annual Report on Form 10-K for the year ended December 31, 2013. The results reported in these unaudited condensed consolidated financial statements should not necessarily be taken as indicative of results that may be expected for the entire year.

The condensed consolidated financial statements include the accounts of the Company and its wholly owned subsidiaries. All significant intercompany transactions and balances have been eliminated upon consolidation. Investments in noncontrolled entities over which the Company exercises significant influence are accounted for under the equity method. The Company's other investment is accounted for at cost.

The condensed consolidated financial statements for previous periods include certain reclassifications that were made to conform to current presentation. Such reclassifications have no impact on previously reported net income (loss), unitholders' capital or cash flows.

Use of Estimates

The preparation of the accompanying condensed consolidated financial statements in conformity with GAAP requires management of the Company to make estimates and assumptions about future events. These estimates and the underlying assumptions affect the amount of assets and liabilities reported, disclosures about contingent assets and liabilities, and reported amounts of revenues and expenses. The estimates that are particularly significant to the financial statements include estimates of the Company's reserves of oil, natural gas and natural gas liquids ("NGL"), future cash flows from oil and natural gas properties, depreciation, depletion and amortization, asset retirement obligations, certain revenues and operating expenses, fair values of commodity derivatives and fair values of assets acquired and liabilities assumed. As fair value is a market-based measurement, it is determined based on the assumptions that market participants would use. These estimates and assumptions are based on management's best estimates and judgment. Management evaluates its estimates and assumptions on an ongoing basis using historical experience and other factors, including the current economic environment, which management believes to be reasonable under the circumstances. Such estimates and assumptions are adjusted when facts and circumstances dictate. As future events and their effects cannot be determined with precision, actual results could differ from these estimates. Any changes in estimates resulting from continuing changes in the economic environment will be reflected in the financial statements in future periods.

Recently Issued Accounting Standards

In May 2014, the Financial Accounting Standards Board issued an Accounting Standards Update ("ASU") that is intended to improve and converge the financial reporting requirements for revenue from contracts with customers. The ASU will be applied either retrospectively or as a cumulative-effect adjustment as of the date of adoption and is effective for fiscal years beginning after December 15, 2016, and interim periods within those years (early adoption prohibited). The Company is currently evaluating the impact, if any, of the adoption of this ASU on its consolidated financial statements and related disclosures.

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LINN ENERGY, LLC
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS – Continued
(Unaudited)

Note 2 – Acquisitions, Joint-Venture Funding and Divestitures

For the six months ended June 30, 2014, the Company paid approximately $25 million, including interest, towards the future funding commitment related to the joint-venture agreement it entered into with an affiliate of Anadarko Petroleum Corporation (“Anadarko”) in April 2012. As of February 2014, the Company had fully funded the total commitment of $400 million.

During the six months ended June 30, 2014, the Company completed small acquisitions of oil and natural gas properties located in its various operating regions. The Company, in the aggregate, paid approximately $1 million in total consideration for these properties.

Properties Exchange – Pending

On May 20, 2014, the Company, through two of its wholly owned subsidiaries, entered into a definitive agreement to trade a portion of its Permian Basin properties to Exxon Mobil Corporation and its affiliates, including its wholly owned subsidiary XTO Energy Inc., for operating interests in the Hugoton Basin. The Company anticipates the transaction will close in the third quarter of 2014, subject to closing conditions. There can be no assurance that all of the conditions to closing will be satisfied.

Acquisitions and Divestiture – Pending

On June 27, 2014, the Company, through one of its wholly owned subsidiaries, entered into a definitive purchase and sale agreement to acquire certain oil and natural gas properties and related assets located primarily in the Rockies, Mid-Continent, east Texas, north Louisiana and south Texas from affiliates of Devon Energy Corporation for a contract price of $2.3 billion. The Company anticipates the acquisition will close in the third quarter of 2014, subject to closing conditions, and has secured $2.3 billion of committed interim financing for the acquisition, subject to final documentation. There can be no assurance that all of the conditions to closing will be satisfied.

On July 18, 2014, the Company, through one of its wholly owned subsidiaries, entered into a definitive purchase and sale agreement to acquire certain oil and natural gas properties located in the Hugoton Basin from Pioneer Natural Resources Company for a contract price of $340 million, including a deposit of $34 million paid in July 2014. The Company anticipates the acquisition will close in the third quarter of 2014, subject to closing conditions, and will be financed with borrowings under the LINN Credit Facility, as defined in Note 6. There can be no assurance that all of the conditions to closing will be satisfied.

On July 24, 2014, the Company, through one of its wholly owned subsidiaries, entered into a definitive purchase and sale agreement to sell its interests in certain non-producing oil and natural gas properties located in the Mid-Continent region for a purchase price of approximately $90 million, subject to closing adjustments. The sale is anticipated to close in the fourth quarter of 2014, subject to closing conditions. There can be no assurance that all of the conditions to closing will be satisfied. The Company plans to use the net proceeds from the sale to repay borrowings under the LINN Credit Facility.

Acquisitions – 2013

Berry Acquisition

On December 16, 2013, the Company completed the transactions contemplated by the merger agreement between the Company, LinnCo, LLC (“LinnCo”), an affiliate of LINN Energy, and Berry Petroleum Company, now Berry Petroleum Company, LLC (“Berry”), under which LinnCo acquired all of the outstanding common shares of Berry and the contribution agreement between LinnCo and the Company, under which LinnCo contributed Berry to the Company in exchange for LINN Energy units. Under the merger agreement, as amended, Berry’s shareholders received 1.68 LinnCo common shares for each Berry common share they owned, totaling 93,756,674 LinnCo common shares. Under the contribution agreement, LinnCo contributed Berry to LINN Energy in exchange for 93,756,674 newly issued LINN Energy units, after which Berry became an indirect wholly owned subsidiary of LINN Energy. The transaction has a value of approximately $4.6 billion, including the assumption of approximately $2.3 billion of Berry’s debt and net of cash acquired of approximately $451 million.

This acquisition was accounted for under the acquisition method of accounting. Accordingly, the Company conducted assessments of net assets acquired and recognized amounts for identifiable assets acquired and liabilities assumed at their estimated fair values on the acquisition date, while transaction and integration costs associated with the acquisitions were

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expensed as incurred. The initial accounting for the business combination is not complete and adjustments to provisional amounts, or recognition of additional assets acquired or liabilities assumed, may occur as more detailed analyses are completed and additional information is obtained about the facts and circumstances that existed as of the acquisition date. The results of operations of the acquisition have been included in the condensed consolidated financial statements since the acquisition date.

The following unaudited pro forma financial information presents a summary of the Company's consolidated results of operations for the three months and six months ended June 30, 2013, assuming the Berry acquisition had been completed as of January 1, 2013, including adjustments to reflect the values assigned to the net assets acquired:

	Three Months Ended June 30, 2013	Six Months Ended June 30, 2013
	(in thousands, except per unit amounts)	
Total revenues and other	$1,161,137	$1,806,346
Total operating expenses	$586,909	$1,256,821
Net income	$441,935	$284,615
Net income per unit:		
Basic	$1.34	$0.86
Diluted	$1.34	$0.86

The pro forma condensed combined statements of operations includes adjustments to:

- Reflect the results of Berry.
- Reflect incremental depreciation, depletion and amortization expense, using the units-of-production method, related to oil and natural gas properties acquired and using an estimated useful life of 20 years for other property and equipment.
- Reflect a reduction in interest expense related to the amortization of the adjustment to fair value of Berry's debt using the effective interest method.
- Exclude transaction costs included in the historical statements of operations for the three months and six months ended June 30, 2013, as they reflect nonrecurring charges not expected to have a continuing impact on the combined results.
- Reflect approximately 93.8 million LINN Energy units assumed to be issued in conjunction with the transaction on January 1, 2013.

Divestiture – 2013

On May 31, 2013, the Company, through one of its wholly owned subsidiaries, together with the Company's partners, Panther Energy, LLC and Red Willow Mid-Continent, LLC, completed the sale of its interests in certain oil and natural gas properties located in the Mid-Continent region ("Panther Operated Cleveland Properties") to Midstates Petroleum Company, Inc. At March 31, 2013, the carrying value of the Panther Operated Cleveland Properties was reduced to fair value less costs to sell resulting in an impairment charge of approximately $57 million and the properties were classified as "assets held for sale." On May 31, 2013, upon the completion of the sale, the Company recorded an adjustment of approximately $15 million to reduce the initial impairment charge recorded in March 2013 resulting in a total impairment charge of approximately $42 million for the six months ended June 30, 2013. The charge is included in "impairment of long-lived assets" on the condensed consolidated statement of operations. Proceeds received for the Company's portion of its interests in the properties were approximately $219 million, net of costs to sell of approximately $2 million.

Note 3 – Unitholders' Capital

Distributions

Under the Company's limited liability company agreement, unitholders are entitled to receive a distribution of available cash, which includes cash on hand plus borrowings less any reserves established by the Company's Board of Directors to provide for the proper conduct of the Company's business (including reserves for future capital expenditures, including drilling, acquisitions and anticipated future credit needs) or to fund distributions over the next four quarters. Distributions paid by the Company are presented on the condensed consolidated statement of unitholders' capital and the condensed consolidated statements of cash flows. On July 1, 2014, the Company's Board of Directors declared a cash distribution of $0.725 per unit with respect to the second quarter of 2014, to be paid in three equal installments of $0.2416 per unit. The first monthly distribution with respect to the second quarter of 2014, totaling approximately $80 million, was paid on July 16, 2014, to unitholders of record as of the close of business on July 11, 2014.

Note 4 – Oil and Natural Gas Properties

Oil and Natural Gas Capitalized Costs

Aggregate capitalized costs related to oil, natural gas and NGL production activities with applicable accumulated depletion and amortization are presented below:

	June 30, 2014	December 31, 2013
	(in thousands)	
Proved properties:		
Leasehold acquisition	$12,329,359	$12,277,089
Development	4,468,702	3,660,277
Unproved properties	1,886,148	1,951,193
	18,684,209	17,888,559
Less accumulated depletion and amortization	(4,051,761)	(3,546,284)
	$14,632,448	$14,342,275

Note 5 – Unit-Based Compensation

During the six months ended June 30, 2014, the Company granted 1,447,577 restricted units and 214,875 phantom units to employees, primarily as part of its annual review of its employees' compensation, including executives, with an aggregate fair value of approximately $56 million. The restricted units and phantom units vest over three years. The Company also granted 212,524 performance units (the maximum number of units available to be earned) to certain executive officers, with an aggregate fair value of approximately $5 million. The initial 2014 performance unit awards vest 50% in two years and 50% in three years from the award date. A summary of unit-based compensation expenses included on the condensed consolidated statements of operations is presented below:

	Three Months Ended June 30,		Six Months Ended June 30,	
	2014	2013	2014	2013
	(in thousands)			
General and administrative expenses	$9,496	$7,136	$27,719	$17,001
Lease operating expenses	1,587	1,177	4,864	2,574
Total unit-based compensation expenses	$11,083	$8,313	$32,583	$19,575
Income tax benefit	$4,095	$3,072	$12,039	$7,233

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LINN ENERGY, LLC
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS – Continued
(Unaudited)

Note 6 – Debt
The following summarizes the Company's outstanding debt:

	June 30, 2014	December 31, 2013
	(in thousands, except percentages)	
LINN credit facility (1)	$2,245,000	$1,560,000
Berry credit facility (2)	1,173,175	1,173,175
Term loan (3)	500,000	500,000
10.25% Berry senior notes due June 2014	—	205,257
6.50% senior notes due May 2019	750,000	750,000
6.25% senior notes due November 2019	1,800,000	1,800,000
8.625% senior notes due April 2020	1,300,000	1,300,000
6.75% Berry senior notes due November 2020	299,970	300,000
7.75% senior notes due February 2021	1,000,000	1,000,000
6.375% Berry senior notes due September 2022	599,163	600,000
Net unamortized discounts and premiums	(22,957)	(18,216)
Total debt, net	9,644,351	9,170,216
Less current maturities	—	(211,558)
Total long-term debt, net	$9,644,351	$8,958,658