GeoMet, Inc.
Form 10-Q
July 27, 2010

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, 2010

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 000-52155

GeoMet, Inc.

(Exact name of registrant as specified in its charter)

Delaware	**76-0662382**
(State or other jurisdiction of incorporation or organization)	**(I.R.S. Employer Identification Number)**

909 Fannin, Suite 1850

Houston, Texas 77010

(713) 659-3855

(Address of principal executive offices and telephone number, including area code)

N/A

(Former name, former address and former fiscal year, if changed since last report)

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. x Yes ¨ No

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). ¨ Yes ¨ 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	¨	Accelerated filer	¨
Non-accelerated filer	x (Do not check if a smaller reporting company)	Smaller reporting company	¨

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

As of July 21, 2010, there were 39,462,762 shares issued and outstanding of GeoMet, Inc. s common stock, par value $0.001 per share.

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Part I. Financial Information

Item 1. Financial Statements

GEOMET, INC. AND SUBSIDIARIES

Consolidated Balance Sheets

(Unaudited)

	June 30, 2010	December 31, 2009
ASSETS		
Current Assets:		
Cash and cash equivalents	$ 493,701	$ 973,720
Accounts receivable, both amounts net of allowance of $60,848	2,477,084	2,909,293
Inventory	1,533,639	2,131,901
Derivative asset	6,075,383	2,563,898
Other current assets	1,274,080	475,025
Total current assets	11,853,887	9,053,837
Gas properties utilizing the full cost method of accounting:		
Proved gas properties	466,336,932	461,003,091
Other property and equipment	3,341,182	3,480,202
Total property and equipment	469,678,114	464,483,293
Less accumulated depreciation, depletion, amortization and impairment of gas properties	(369,147,640)	(365,784,964)
Property and equipment net	100,530,474	98,698,329
Other noncurrent assets:		
Derivative asset	1,917,335	761,192
Deferred income taxes	49,711,842	51,804,971
Other	244,507	609,972
Total other noncurrent assets	51,873,684	53,176,135
TOTAL ASSETS	$ 164,258,045	$ 160,928,301
LIABILITIES AND STOCKHOLDERS EQUITY		
Current Liabilities:		
Accounts payable	$ 4,967,011	$ 5,169,174
Accrued liabilities	4,016,250	2,808,227
Deferred income taxes	1,549,919	157,256
Derivative liability	266,189	724,253
Asset retirement liability	104,739	108,111
Current portion of long-term debt	129,050	121,792
Total current liabilities	11,033,158	9,088,813

Long-term debt	116,406,256	119,996,163
Asset retirement liability	5,127,043	4,862,278
Other long-term accrued liabilities	57,017	73,308
TOTAL LIABILITIES	132,623,474	134,020,562
Commitments and contingencies (Note 11)		
Stockholders Equity:		
Preferred stock, $0.001 par value authorized 10,000,000, none issued		
Common stock, $0.001 par value authorized 125,000,000 shares; issued and outstanding 39,457,612 and 39,460,060 at June 30, 2010 and December 31, 2009, respectively	39,294	39,294
Treasury stock 10,432 shares at June 30, 2010 and December 31, 2009	(94,424)	(94,424)
Paid-in capital	189,860,397	189,681,816
Accumulated other comprehensive loss	(1,479,744)	(1,768,521)
Retained deficit	(156,445,860)	(160,710,889)
Less notes receivable	(245,092)	(239,537)
Total stockholders equity	31,634,571	26,907,739
TOTAL LIABILITIES AND STOCKHOLDERS EQUITY	$ 164,258,045	$ 160,928,301

See accompanying Notes to Consolidated Financial Statements (Unaudited)

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GEOMET, INC. AND SUBSIDIARIES

Consolidated Statements of Operations

(Unaudited)

	Three Months Ended June 30, 2010	Three Months Ended June 30, 2009	Six Months Ended June 30, 2010	Six Months Ended June 30, 2009
Revenues:				
Gas sales	$ 7,661,353	$ 6,837,910	$ 17,545,039	$ 16,290,419
Operating fees	70,703	76,923	144,995	174,934
Total revenues	7,732,056	6,914,833	17,690,034	16,465,353
Expenses:				
Lease operating expense	2,812,883	3,348,170	5,920,254	7,917,487
Compression and transportation expense	1,075,392	1,364,841	2,079,839	2,814,965
Production taxes	288,039	240,593	496,268	607,655
Depreciation, depletion and amortization	1,450,238	1,981,707	3,095,603	5,018,438
Impairment of gas properties		27,582,106		167,294,577
General and administrative	1,314,840	2,180,889	2,792,565	5,153,501
Terminated transaction costs	1,402,534		1,402,534	
Realized gains on derivative contracts	(2,210,850)	(2,733,816)	(3,670,978)	(5,457,120)
Unrealized losses (gains) from the change in market value of open derivative contracts	2,974,026	2,144,115	(4,668,016)	1,958,232
Total operating expenses	9,107,102	36,108,605	7,448,069	185,307,735
Operating (loss) income	(1,375,046)	(29,193,772)	10,241,965	(168,842,382)
Other income (expense):				
Interest income	5,057	5,674	30,861	15,634
Interest expense (net of amounts capitalized)	(1,423,476)	(1,418,402)	(2,667,636)	(2,401,447)
Other	625	8,750	(16,702)	7,732
Total other income (expense):	(1,417,794)	(1,403,978)	(2,653,477)	(2,378,081)
(Loss) income before income taxes	(2,792,840)	(30,597,750)	7,588,488	(171,220,463)
Income tax benefit (expense)	1,030,717	11,211,554	(3,323,459)	64,108,463
Net (loss) income	$ (1,762,123)	$ (19,386,196)	$ 4,265,029	$ (107,112,000)
Earnings per share:				
Net (loss) income				
Basic	$ (0.04)	$ (0.50)	$ 0.11	$ (2.75)
Diluted	$ (0.04)	$ (0.50)	$ 0.11	$ (2.75)
Weighted average number of common shares:				
Basic	39,240,545	39,122,570	39,199,990	39,024,353
Diluted	39,240,545	39,122,570	39,290,788	39,024,353

See accompanying Notes to Consolidated Financial Statements (Unaudited)

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GEOMET, INC. AND SUBSIDIARIES

Consolidated Statements of Comprehensive (Loss) Income

(Unaudited)

	Three Months Ended June 30, 2010	Three Months Ended June 30, 2009	Six Months Ended June 30, 2010	Six Months Ended June 30, 2009
Net (loss) income	$ (1,762,123)	$ (19,386,196)	$ 4,265,029	$ (107,112,000)
(Loss) gain on foreign currency translation adjustment	(2,899)	85,871	5,934	181,264
Gain on interest rate swap	115,891	32,138	282,844	31,199
Other comprehensive (loss) income	$ (1,649,131)	$ (19,268,187)	$ 4,553,807	$ (106,899,537)

See accompanying Notes to Consolidated Financial Statements (Unaudited)

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GEOMET, INC. AND SUBSIDIARIES

Consolidated Statements of Cash Flows

(Unaudited)

	Six Months Ended June 30, 2010	2009
Cash flows provided by operating activities:		
Net income (loss)	$ 4,265,029	$ (107,112,000)
Adjustments to reconcile net income (loss) to net cash flows provided by operating activities:		
Depreciation, depletion and amortization	3,095,603	5,018,438
Impairment of gas properties		167,294,577
Amortization of debt issuance costs	189,028	102,481
Terminated transaction costs	666,306	
Deferred income tax expense (benefit)	3,310,959	(64,120,962)
Unrealized (gains) losses from the change in market value of open derivative contracts	(4,668,016)	1,958,232
Stock-based compensation	79,569	501,114
Loss on sale of other assets	23,685	31,076
Accretion expense	241,395	212,640
Changes in operating assets and liabilities:		
Accounts receivable	434,118	2,881,388
Inventory	600,555	(182,207)
Other current assets	322,224	349,625
Accounts payable	(1,292,025)	(3,903,241)
Other accrued liabilities	1,206,121	211,538
Net cash provided by operating activities	8,474,551	3,242,699
Cash flows used in investing activities:		
Capital expenditures	(4,167,601)	(9,264,458)
Proceeds from sale of other property and equipment	31,838	19,165
Other assets	75,285	(56,593)
Net cash used in investing activities	(4,060,478)	(9,301,886)
Cash flows (used in) provided by financing activities:		
Proceeds from exercise of stock options	46,327	
Proceeds from revolver borrowings	10,500,000	28,550,000
Payments on revolver	(14,000,000)	(23,300,000)
Deferred financing costs	(703,245)	
Deferred financing costs related to terminated transactions	(666,306)	
Purchase of treasury stock		(613)
Payments on other debt	(82,650)	(75,990)
Net cash (used in) provided by financing activities	(4,905,874)	5,173,397
Effect of exchange rate changes on cash	11,782	9,888
Decrease in cash and cash equivalents	(480,019)	(875,902)
Cash and cash equivalents at beginning of period	973,720	2,096,561
Cash and cash equivalents at end of period	$ 493,701	$ 1,220,659
Significant noncash investing activities:		
Accrued capital expenditures	$ 1,650,768	$ 382,668

See accompanying Notes to Consolidated Financial Statements (Unaudited)

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GEOMET, INC. AND SUBSIDIARIES

Notes to Consolidated Financial Statements

(Unaudited)

Note 1 Organization and Our Business

GeoMet, Inc. (GeoMet, Company, we, or our) (formerly GeoMet Resources, Inc.) was incorporated under the laws of the state of Delaware on November 9, 2000. We are an independent natural gas producer primarily involved in the exploration, development and production of natural gas from coal seams (coalbed methane) and non-conventional shallow gas. Our principal operations and producing properties are located in Alabama, West Virginia, Virginia and Canada.

The accompanying unaudited consolidated financial statements include our accounts and those of our wholly owned subsidiaries. All significant intercompany transactions and balances have been eliminated in consolidation. The unaudited consolidated financial statements reflect, in the opinion of our management, all adjustments, consisting only of normal and recurring adjustments, necessary to present fairly the financial position as of, and results of operations for, the interim periods presented. These unaudited consolidated financial statements have been prepared in accordance with the guidelines of interim reporting; therefore, they do not include all disclosures required for our year-end audited consolidated financial statements prepared in conformity with accounting principles generally accepted in the United States of America (GAAP). Interim period results are not necessarily indicative of results of operations or cash flows for the full year. These unaudited consolidated financial statements included herein should be read in conjunction with the audited consolidated financial statements for the fiscal year ended December 31, 2009 and the accompanying notes included in our Annual Report on Form 10-K, which we filed with the Securities and Exchange Commission (the SEC) on March 31, 2010.

Note 2 Recent Pronouncements

In January 2010, the FASB issued Update No. 2010-06 Fair Value Measurements and Disclosures (Topic 820): Improving Disclosures about Fair Value Measurements. This Update provides amendments to Subtopic 820-10 that require new disclosures for transfers in and out of Levels 1 and 2. This Update also clarifies existing disclosures for level of disaggregation, as well as valuation techniques and inputs used to measure fair value for both recurring and nonrecurring fair value measurements. The new disclosures and clarifications of existing disclosures are effective for interim and annual reporting periods beginning after December 15, 2009. See additional disclosure provided in Note 6 Derivative Instruments and Hedging Activities.

Note 3 (Loss) Income Per Share

(Loss) Income Per Share of Common Stock Basic (loss) income per share is calculated by dividing net (loss) income by the weighted average number of shares of common stock outstanding during the period. Fully diluted (loss) income per share assumes the conversion of all potentially dilutive securities and is calculated by dividing net (loss) income by the sum of the weighted average number of shares of common stock outstanding plus potentially dilutive securities. Dilutive (loss) income per share considers the impact of potentially dilutive securities except in periods in which there is a loss because the inclusion of the potential common shares would have an anti-dilutive effect. A reconciliation of the numerator and denominator is as follows:

	Three Months Ended June 30,		Six Months Ended June 30,	
	2010	2009	2010	2009
Net (loss) income per share:				
Basic-net (loss) income per share	$ (0.04)	$ (0.50)	$ 0.11	$ (2.75)
Diluted-net (loss) income per share	$ (0.04)	$ (0.50)	$ 0.11	$ (2.75)
Numerator:				
Net (loss) income available to common stockholders	$ (1,762,123)	$ (19,386,196)	$ 4,265,029	$ (107,112,000)
Denominator:				

Weighted average shares outstanding-basic	39,240,545	39,122,570	39,199,990	39,024,353
Add potentially dilutive securities:				
Stock options			90,798	
Dilutive securities	39,240,545	39,122,570	39,290,788	39,024,353

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GEOMET, INC. AND SUBSIDIARIES

Notes to Consolidated Financial Statements (Continued)

(Unaudited)

Diluted net loss per share for the three months ended June 30, 2010 excluded the effect of outstanding options to purchase 2,206,132 shares and 161,728 shares of restricted stock because we reported a net loss, which caused options to be anti-dilutive. Diluted net income per share for the six months ended June 30, 2010 excluded the effect of outstanding options to purchase 1,661,626 shares because the strike prices of the options were above the average market price of our common stock for the period and would have therefore been anti-dilutive. Diluted net loss per share for the three and six months ended June 30, 2009 excluded the effect of outstanding options to purchase 2,444,333 shares and 329,410 shares of restricted stock because we reported a net loss, which caused options to be anti-dilutive.

Note 4 Gas Properties

The method of accounting for gas properties determines what costs are capitalized and how these costs are ultimately matched with revenues and expenses. We use the full cost method of accounting for gas properties as prescribed by the SEC. Under this method, all direct costs and certain indirect costs associated with the acquisition, exploration, and development of our gas properties are capitalized and segregated into United States of America (U.S.) and Canadian cost centers. The Canadian cost center was fully impaired in 2009.

Gas properties are depleted using the units-of-production method. The depletion expense is significantly affected by the unamortized historical and future development costs and the estimated proved gas reserves. Depletion for the three months ended June 30, 2010 and 2009 was $0.72 and $0.96 per Mcf, respectively. Depletion for the six months ended June 30, 2010 and 2009 was $0.78 and $1.24 per Mcf, respectively.

Estimation of proved gas reserves relies on professional judgment and use of factors that cannot be precisely determined. Subsequent proved reserve estimates materially different from those reported would change the depletion expense recognized during future reporting periods. No gains or losses are recognized upon the sale or disposition of gas properties unless the sale or disposition represents a significant quantity of gas reserves, which would have a significant impact on the depreciation, depletion and amortization rate.

Under full cost accounting rules, total capitalized costs are limited to a ceiling equal to the present value of estimated future net revenues, discounted at 10% per annum, plus cost of properties not being amortized plus the lower of cost or fair value of unevaluated properties less income tax effects (the ceiling limitation). We perform a quarterly ceiling test to evaluate whether the net book value of our full cost pool exceeds the ceiling limitation. The ceiling test is performed separately for our U.S. and Canadian cost centers. If capitalized costs (net of accumulated depreciation, depletion and amortization) less related deferred taxes are greater than the discounted future net revenues or ceiling limitation, a write-down or impairment of the full cost pool is required. A write-down of the carrying value of the full cost pool is a non-cash charge that reduces earnings and impacts stockholders equity in the period of occurrence and typically results in lower depreciation, depletion and amortization expense in future periods. Once incurred, a write-down is not reversible at a later date.

The ceiling test is calculated using the unweighted arithmetic average of the natural gas price on the first day of each month within the 12-month period prior to the end of the reporting period, unless prices are defined by contractual arrangements, excluding escalations based on future conditions, as allowed by the guidelines of the SEC. In addition, subsequent to the adoption of Accounting Standards Codification (ASC) 410-20-25, formerly Financial Accounting Standard Board (FASB) Statement No. 143, Accounting for Asset Retirement Obligations, the future cash outflows associated with settling asset retirement obligations were not included in the computation of the discounted present value of future net revenues for the purposes of the ceiling test calculation.

No impairments were recorded during the three and six months ended June 30, 2010.

At June 30, 2009, the carrying value of the Company s gas properties in the U.S. and Canada exceeded the full cost ceiling limitation based upon the natural gas prices per Mcf in effect as of the balance sheet date, adjusted for location differentials, which were approximately $4.00 and $3.57, respectively. For the three months ended June 30, 2009, impairments recorded to gas properties were:

	United States	Canada	Total
Impairment of gas properties	$ 27,082,174	$ 499,932	$ 27,582,106
Deferred income tax benefit	(10,345,392)		(10,345,392)
Impairment of gas properties, net of tax	$ 16,736,782	$ 499,932	$ 17,236,714

For the six months ended June 30, 2009, impairments recorded to gas properties were:

	United States	Canada	Total
Impairment of gas properties	$ 165,453,805	$ 1,840,772	$ 167,294,577
Deferred income tax benefit	(63,203,421)		(63,203,421)
Impairment of gas properties, net of tax	$ 102,250,384	$ 1,840,772	$ 104,091,156

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GEOMET, INC. AND SUBSIDIARIES

Notes to Consolidated Financial Statements (Continued)

(Unaudited)

Note 5 Asset Retirement Liability

We record an asset retirement obligation (ARO) on the consolidated balance sheets and capitalize the asset retirement costs in gas properties in the period in which the retirement obligation is incurred. The amount of the ARO and the costs capitalized are equal to the estimated future costs to satisfy the obligation using current prices that are escalated by an assumed inflation factor up to the estimated settlement date, which is then discounted back to the date we incurred the abandonment obligation using an assumed interest rate. Once the ARO is recorded, it is then accreted to its estimated future value using the same assumed interest rate. The following table details the changes to our asset retirement liability for the six months ended June 30, 2010:

Current portion of liability at January 1, 2010	$ 108,111
Add: Long-term asset retirement liability at January 1, 2010	4,862,278
Asset retirement liability at January 1, 2010	4,970,389
Liabilities incurred	20,017
Liabilities settled	(3,792)
Accretion	241,395
Foreign currency translation	3,773
Asset retirement liability at June 30, 2010	5,231,782
Less: Current portion of liability	(104,739)
Long-term asset retirement liability	$ 5,127,043

Note 6 Derivative Instruments and Hedging Activities

The energy markets have historically been volatile, and there can be no assurance that future natural gas prices will not be subject to wide fluctuations. In an effort to reduce the effects of the volatility of the price of natural gas on our operations, management has adopted a policy of hedging natural gas prices from time to time primarily using derivative instruments in the form of three-way collars, traditional collars and swaps. While the use of these hedging arrangements limits the downside risk of adverse price movements, it also limits future gains from favorable movements. Our price risk management policy strictly prohibits the use of derivatives for speculative positions.

We enter into hedging transactions, generally for forward periods up to two years or more, which increase the probability of achieving our targeted level of cash flows. We generally limit the amount of these hedges during any period to no more than 50% to 70% of the then expected gas production for such future periods. Swaps exchange floating price risk in the future for a fixed price at the time of the hedge. Costless collars set both a maximum ceiling (a sold ceiling) and a minimum floor (a bought floor) future price. Three-way costless collars are similar to regular costless collars except that, in order to increase the ceiling price, we agree to limit the amount of the floor price protection (through a sold floor) to a predetermined amount, generally between $2.00 and $3.00 per MMBtu below the bought floor. We have accounted for these transactions using the mark-to-market accounting method. Generally, we incur accounting losses on derivatives during periods where prices are rising and gains during periods where prices are falling which may cause significant fluctuations in our consolidated balance sheets and consolidated statements of operations.

Commodity Price Risk and Related Hedging Activities

At June 30, 2010, we had the following natural gas collar positions:

Period	Volume (MMBtu)	Sold Ceiling	Bought Floor	Sold Floor	Fair Value
July through October 2010	492,000	$ 6.80	$ 5.50	$ 3.50	$ 429,186
July through October 2010	492,000	$ 6.35	$ 5.50		436,893
November 2010 through March 2011	604,000	$ 7.45	$ 6.50		815,931
	1,588,000				$ 1,682,010

At December 31, 2009, we had the following natural gas collar positions:

Period	Volume (MMBtu)	Sold Ceiling	Bought Floor	Sold Floor	Fair Value
January 2010 through March 2010	540,000	$ 11.20	$ 9.50	$ 7.00	$ 1,326,724
January 2010 through March 2010	360,000	$ 6.65	$ 5.50	$ 3.50	65,098
April through October 2010	856,000	$ 6.80	$ 5.50	$ 3.50	172,072
April through October 2010	856,000	$ 6.35	$ 5.50		116,559
November 2010 through March 2011	604,000	$ 7.45	$ 6.50		160,745
	3,216,000				$ 1,841,198

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GEOMET, INC. AND SUBSIDIARIES

Notes to Consolidated Financial Statements (Continued)

(Unaudited)

At June 30, 2010, we had the following natural gas swap positions:

Period	Volume (MMBtu)	Price	Fair Value
July through October 2010	492,000	$ 5.70	$ 499,183
July through October 2010	369,000	$ 6.30	595,472
November 2010 through March 2011	604,000	$ 6.67	839,421
November 2010 through March 2011	906,000	$ 7.27	1,795,809
April 2011 through October 2011	856,000	$ 6.37	980,013
April 2011 through October 2011	856,000	$ 5.37	131,075
April 2011 through October 2011	856,000	$ 5.43	185,981
November 2011 through March 2012	608,000	$ 7.12	741,714
November 2011 through March 2012	608,000	$ 6.12	143,656
April 2012 through October 2012	856,000	$ 5.73	205,565
November 2012 through March 2013	604,000	$ 6.42	192,819
	7,615,000		$ 6,310,708

At December 31, 2009, we had the following natural gas swap positions:

Period	Volume (MMBtu)	Price	Fair Value
April through October 2010	856,000	$ 5.70	$ 5,341
April through October 2010	642,000	$ 6.30	