

CRIMSON EXPLORATION INC.

Form 10-Q

November 10, 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 September 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 001-12108

CRIMSON EXPLORATION INC.

(Exact name of registrant as specified in its charter)

Delaware
(State or other jurisdiction of
incorporation)

20-3037840
(IRS Employer Identification
No.)

717 Texas Avenue, Suite 2900
Houston, Texas
(Address of principal executive offices)

77002
(Zip Code)

(713) 236-7400

(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 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

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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 definition 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 Smaller reporting company

(Do not check if smaller reporting company)

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

On November 5, 2010, there were 43,033,083 shares outstanding of the registrant’s Common Stock, par value \$0.001.

FORM 10-Q

CRIMSON EXPLORATION INC.

FOR THE QUARTER ENDED SEPTEMBER 30, 2010

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PART I. FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS

CRIMSON EXPLORATION INC. AND SUBSIDIARIES
CONSOLIDATED BALANCE SHEETS

ASSETS

	September 30, 2010 (unaudited)	December 31, 2009
CURRENT ASSETS		
Cash and cash equivalents	\$—	\$—
Accounts receivable, net of allowance of \$411,324 and \$411,324, respectively	15,835,972	14,773,246
Prepaid expenses	9,000	—
Derivative instruments	11,063,206	9,937,697
Total current assets	26,908,178	24,710,943
PROPERTY AND EQUIPMENT		
Oil and gas properties (successful efforts method of accounting)	597,364,843	559,565,531
Other property and equipment	3,375,348	3,679,515
Accumulated depreciation, depletion and amortization	(202,647,649)	(170,117,319)
Total property and equipment, net	398,092,542	393,127,727
NONCURRENT ASSETS		
Deposits	104,697	104,697
Debt issuance cost	2,892,264	4,347,298
Derivative instruments	1,688,931	2,513,369
Deferred tax asset, net	476,374	—
Total noncurrent assets	5,162,266	6,965,364
TOTAL ASSETS	\$430,162,986	\$424,804,034

LIABILITIES AND STOCKHOLDERS' EQUITY

CURRENT LIABILITIES		
Current portion of long-term debt	\$1,662	\$19,014
Accounts payable	33,290,306	20,263,343
Income taxes payable	—	250,931
Accrued liabilities	11,049,163	8,852,310
Asset retirement obligations	766,427	330,287
Derivative instruments	2,040,208	872,849
Deferred tax liability, net	2,824,145	2,897,300
Total current liabilities	49,971,911	33,486,034
NONCURRENT LIABILITIES		
Long-term debt, net of current portion	196,274,986	192,749,751
Asset retirement obligations	9,068,117	9,372,366
Derivative instruments	151,917	1,284,105
Deferred tax liability, net	—	4,471,023

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Other noncurrent liabilities	682,737	709,867
Total noncurrent liabilities	206,177,757	208,587,112
Total liabilities	256,149,668	242,073,146

COMMITMENTS AND CONTINGENCIES

STOCKHOLDERS' EQUITY

Common stock (par value \$0.001; 200,000,000 shares authorized; 38,785,570 and 38,516,658 shares issued and outstanding, respectively)	38,881	38,578
Additional paid-in capital	211,114,212	209,738,513
Retained deficit	(36,643,834)	(26,661,891)
Treasury stock (at cost, 95,146 and 61,546 shares, respectively)	(495,941)	(384,312)
Total stockholders' equity	174,013,318	182,730,888

TOTAL LIABILITIES AND STOCKHOLDERS' EQUITY	\$430,162,986	\$424,804,034
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The Notes to the Consolidated Financial Statements are an integral part of these statements.

CRIMSON EXPLORATION INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF OPERATIONS
(UNAUDITED)

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2010	2009	2010	2009
OPERATING REVENUES				
Natural gas sales	\$15,474,237	\$16,426,246	\$43,490,452	\$55,135,137
Crude oil sales	5,404,136	6,709,774	15,095,988	21,518,736
Natural gas liquids sales	3,529,359	3,616,522	9,577,462	9,089,086
Operating overhead and other income	128,175	147,862	434,807	508,249
Total operating revenues	24,535,907	26,900,404	68,598,709	86,251,208
OPERATING EXPENSES				
Lease operating expenses	3,583,572	3,879,621	11,420,069	13,517,664
Production and ad valorem taxes	1,399,292	1,563,460	4,580,119	6,060,579
Exploration expenses	1,311,678	687,613	1,994,794	2,873,255
Depreciation, depletion and amortization	12,035,848	13,400,031	32,973,530	41,599,314
General and administrative	4,501,413	3,836,194	13,897,108	13,381,282
(Gain) loss on sale of assets	(10,453)	—	420,366	18,925
Total operating expenses	22,821,350	23,366,919	65,285,986	77,451,019
INCOME FROM OPERATIONS	1,714,557	3,533,485	3,312,723	8,800,189
OTHER INCOME (EXPENSE)				
Interest expense	(5,785,042)	(6,633,642)	(16,387,881)	(16,349,300)
Other financing cost	(776,137)	(382,159)	(2,349,167)	(1,109,805)
Unrealized (loss) gain on derivative instruments	(1,258,326)	(9,929,947)	265,899	(17,237,909)
Total other income (expense)	(7,819,505)	(16,945,748)	(18,471,149)	(34,697,014)
LOSS BEFORE INCOME TAXES	(6,104,948)	(13,412,263)	(15,158,426)	(25,896,825)
Income tax benefit	2,285,040	4,826,137	5,176,483	9,080,238
NET LOSS	(3,819,908)	(8,586,126)	(9,981,943)	(16,816,587)
Dividends on preferred stock (Paid 2010 — \$0; 2009 — \$20,370)	—	(1,156,163)	—	(3,353,150)
NET LOSS AVAILABLE TO COMMON STOCKHOLDERS	\$(3,819,908)	\$(9,742,289)	\$(9,981,943)	\$(20,169,737)
NET LOSS PER SHARE				
Basic	\$(0.10)	\$(1.51)	\$(0.26)	\$(3.20)
Diluted	\$(0.10)	\$(1.51)	\$(0.26)	\$(3.20)
WEIGHTED AVERAGE SHARES OUTSTANDING				

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Basic	38,819,780	6,444,013	38,655,038	6,301,280
Diluted	38,819,780	6,444,013	38,655,038	6,301,280

The Notes to the Consolidated Financial Statements are an integral part of these statements.

CRIMSON EXPLORATION INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENT OF STOCKHOLDERS' EQUITY
FOR THE NINE MONTHS ENDED SEPTEMBER 30, 2010
(UNAUDITED)

	NUMBER OF SHARES		ADDITIONAL PAID-IN CAPITAL	RETAINED DEFICIT	TREASURY STOCK	TOTAL STOCKHOLDERS' EQUITY
	COMMON STOCK	COMMON STOCK				
BALANCE, DECEMBER 31, 2009	38,516,658	\$38,578	\$ 209,738,513	\$(26,661,891)	\$(384,312)	\$ 182,730,888
Current period net loss	—	—	—	(9,981,943)	—	(9,981,943)
Share-based compensation	287,749	288	1,353,056	—	—	1,353,344
Stock options exercised	14,763	15	35,416	—	—	35,431
Common stock issuance costs	—	—	(12,773)	—	—	(12,773)
Treasury stock	(33,600)	—	—	—	(111,629)	(111,629)
BALANCE, SEPTEMBER 30, 2010	38,785,570	\$38,881	\$ 211,114,212	\$(36,643,834)	\$(495,941)	\$ 174,013,318

The Notes to the Consolidated Financial Statements are an integral part of this statement.

CRIMSON EXPLORATION INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF CASH FLOWS
(UNAUDITED)

	Nine Months Ended September 30,	
	2010	2009
CASH FLOWS FROM OPERATING ACTIVITIES:		
Net loss	\$(9,981,943)	\$(16,816,587)
Adjustments to reconcile net loss to net cash provided by operating activities:		
Depreciation, depletion and amortization	32,973,530	41,599,314
Asset retirement obligations	(150,512)	(361,239)
Stock compensation expense	1,353,344	1,869,400
Amortization of debt issuance cost	2,049,205	945,313
Discount on notes payable	56,854	—
Deferred charges	—	1,324,907
Deferred income taxes	(5,020,552)	(9,595,940)
Dry holes, abandoned property, impaired assets	1,202,033	221,960
Loss on sale of assets	420,366	18,925
Unrealized (gain) loss on derivative instruments	(265,899)	17,237,909
Changes in operating assets and liabilities:		
(Increase) decrease in accounts receivable, net	(1,062,726)	8,675,339
(Increase) decrease in prepaid expenses	(9,000)	73,444
Increase (decrease) in accounts payable and accrued liabilities	14,945,755	(42,440,824)
Net cash provided by operating activities	36,510,455	2,751,921
CASH FLOWS FROM INVESTING ACTIVITIES:		
Capital expenditures	(38,903,315)	(16,545,051)
Acquisition of oil and gas properties	—	493,532
Sale of assets	(375,026)	24,327
Net cash used in investing activities	(39,278,341)	(16,027,192)
CASH FLOWS FROM FINANCING ACTIVITIES:		
Payments on debt	(69,259,844)	(76,578,082)
Proceeds from debt	72,710,872	91,373,659
Debt issuance expenditures	(594,171)	(1,387,195)
Common stock issuance costs	(12,773)	—
Proceeds from stock option exercises	35,431	—
Purchase of treasury stock	(111,629)	(133,111)
Net cash provided by financing activities	2,767,886	13,275,271
INCREASE IN CASH AND CASH EQUIVALENTS	—	—
CASH AND CASH EQUIVALENTS, Beginning of period	—	—
CASH AND CASH EQUIVALENTS, End of period	\$—	\$—

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Cash paid for interest	\$19,823,842	\$14,484,741
Cash paid for income taxes	\$95,000	\$539,671

The Notes to the Consolidated Financial Statements are an integral part of these statements.

CRIMSON EXPLORATION INC. AND SUBSIDIARIES
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
(UNAUDITED)

1. ORGANIZATION AND NATURE OF OPERATIONS

Crimson Exploration Inc., together with its subsidiaries, (“Crimson”, “we”, “our”, “us”) is an independent energy company engaged in the acquisition, exploitation, exploration and development of natural gas and crude oil properties. We have historically focused our operations in the onshore U.S. Gulf Coast and South Texas regions, which are generally characterized by high rates of return in known, prolific producing trends. We have recently expanded our strategic focus to include longer reserve life resource plays in East Texas and South Texas that we believe provide significant long-term reserve and production growth potential from multiple formations.

2. BASIS OF PRESENTATION

Presentation

The accompanying unaudited consolidated financial statements have been prepared in accordance with accounting principles generally accepted in the United States (“U.S.”) for interim financial information and with the instructions to Form 10-Q and Rule 8-03 of Regulation S-X. Accordingly, they do not include all of the information and notes required by U.S. generally accepted accounting principles (“GAAP”) for complete annual financial statements. The accompanying consolidated financial statements at September 30, 2010 (unaudited) and December 31, 2009 and for the three and nine months ended September 30, 2010 (unaudited) and 2009 (unaudited) contain all normally recurring adjustments considered necessary for a fair presentation of our financial position, results of operations and cash flows for such periods. Operating results for the three and nine months ended September 30, 2010 are not necessarily indicative of the results that may be expected for the year ending December 31, 2010. These consolidated financial statements should be read in conjunction with the consolidated financial statements and accompanying notes included in our Annual Report on Form 10-K for the year ended December 31, 2009.

The accompanying consolidated financial statements include Crimson Exploration Inc. and its wholly-owned subsidiaries: Crimson Exploration Operating, Inc., formed January 5, 2006 and LTW Pipeline Co., formed April 19, 1999 (inactive). All material intercompany transactions and balances are eliminated upon consolidation.

Use of Estimates in the Preparation of Financial Statements

The preparation of the consolidated financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the consolidated financial statements and the reported amounts of revenues and expenses during the reporting period. Significant estimates included in the consolidated financial statements are: (1) natural gas, crude oil and natural gas liquids revenues and reserves; (2) depreciation, depletion and amortization; (3) valuation allowances associated with income taxes and accounts receivables; (4) accrued assets and liabilities; (5) stock-based compensation; (6) asset retirement obligations and (7) valuation of derivative instruments. Although management believes these estimates are reasonable, changes in facts and circumstances or discovery of new information may result in revised estimates. Actual results could differ from those estimates.

3. FAIR VALUE MEASUREMENTS

Accounting guidance establishes a single authoritative definition of fair value based upon the assumptions market participants would use when pricing an asset or liability and creates a fair value hierarchy that prioritizes the information used to develop those assumptions. Additional disclosures are required, including disclosures of fair value measurements by level within the fair value hierarchy. We incorporate a credit risk assumption into the measurement of certain assets and liabilities.

Certain of our assets and liabilities are reported at fair value in our consolidated balance sheets. The following methods and assumptions were used to estimate the fair values for each class of financial instruments:

Cash and Cash Equivalents, Accounts Receivable and Accounts Payable. The carrying amounts approximate fair value due to the short-term nature or maturity of the instruments.

Derivative Instruments. Our derivative instruments consist of variable to fixed price commodity swaps, costless collars and interest rate swaps. The fair value measurement of our unrealized natural gas, crude oil and interest rate swaps and collars were obtained from financial institutions and such fair value was evaluated and determined to be reasonable, using our crude oil, natural gas and interest rate swap and collar agreements and future commodity and interest rate curves. See Note 4 – “Derivative Instruments” for further information.

Impairments. We review our oil and gas properties for impairment, at least annually, and quarterly if events and circumstances indicate a possible decline in the recoverability of the carrying value of such properties, such as a downward revision of the reserve estimates or lower commodity prices. We estimate the expected future cash flows from the properties and compare such future cash flows to the carrying amounts of the properties to determine if the carrying amounts are recoverable. The factors used to determine fair value include, but are not limited to, estimates of proved and probable reserves, future commodity prices, the timing of future production and capital expenditures and a discount rate commensurate with the risk reflective of the lives remaining for the respective oil and gas properties. Because these significant fair value inputs are typically not observable, we classify impairments of long-lived assets as a level 3 fair value measure. We had no asset impairments in the three and nine months ended September 30, 2010.

Debt. The fair value of floating-rate debt is estimated to be equivalent to the carrying amounts because the interest rates paid on such debt are set for periods of three months or less. See Note 6 - “Debt” for further information.

Fair value information for assets and (liabilities) that are measured at fair value was as follows at September 30, 2010:

	Total Carrying Value	Fair Value Measurements Using		
		Level 1	Level 2	Level 3
Derivatives				
Crude oil swaps and collars	\$(1,642,043)	\$—	\$(1,642,043)	\$—
Natural gas swaps and collars	14,730,612	—	14,730,612	—
Interest rate swaps	(2,528,557)	—	(2,528,557)	—
Total	\$10,560,012	\$—	\$10,560,012	\$—

Fair value information for assets and (liabilities) that are measured at fair value was as follows at December 31, 2009:

	Total Carrying Value	Fair Value Measurements Using		
		Level 1	Level 2	Level 3
Derivatives				
Crude oil swaps and collars	\$(1,332,084)	\$—	\$(1,332,084)	\$—
Natural gas swaps and collars	16,236,665	—	16,236,665	—
Interest rate swaps	(4,610,469)	—	(4,610,469)	—
Total	\$10,294,112	\$—	\$10,294,112	\$—

FASB guidance established a fair value hierarchy which prioritizes the inputs to valuation techniques used to measure fair value into three levels. The fair value hierarchy gives the highest priority to quoted market prices (unadjusted) in active markets for identical assets or liabilities (Level 1) and the lowest priority to unobservable inputs (Level 3). Level 2 inputs are inputs, other than quoted prices included within Level 1, which are observable for the asset or liability, either directly or indirectly. There were no transfers between fair value hierarchy levels in the first nine months of 2010.

4. DERIVATIVE INSTRUMENTS

At the end of each reporting period we record on our balance sheet the mark-to-market valuation of our derivative instruments. We recorded net assets for derivative instruments of approximately \$10.6 million and \$10.3 million at September 30, 2010 and December 31, 2009, respectively. The change in estimated fair value of the derivatives during the period is reported in other income (expense) as unrealized gain or loss on derivative instruments. Realized gain (loss) on derivative instruments is included in natural gas and crude oil sales for our commodity price hedges and in interest expense for our interest rate swaps.

The following table details the location and effect of the Company's derivative contracts on the Consolidated Statements of Operations for realized and unrealized gains and losses:

Contract Type	Location of Gain or (Loss) Recognized in Income	Amount of Gain or (Loss) Recognized in Income			
		Three months ended September 30,		Nine months ended September 30,	
		2010	2009	2010	2009
Natural gas contracts	Operating revenues	\$ 4,758,796	\$ 8,743,868	\$ 13,810,595	\$ 23,238,589
Crude oil contracts	Operating revenues	576,588	1,625,058	1,432,867	7,570,971
Interest rate contracts	Interest expense	(1,145,628)	(1,158,810)	(3,438,406)	(3,242,533)
	Realized gain	\$ 4,189,756	\$ 9,210,116	\$ 11,805,056	\$ 27,567,027
Natural gas contracts	Other income (expense)	\$ (389,793)	\$ (8,693,933)	\$ (1,506,052)	\$ (4,630,639)
		(1,680,336)	(891,655)	(309,959)	(13,058,373)

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Crude oil contracts	Other income (expense)				
Interest rate contracts	Other income (expense)	811,803	(344,359)	2,081,910	451,103
	Unrealized gain (loss)	\$(1,258,326)	\$(9,929,947)	\$ 265,899	\$(17,237,909)

In the past we have entered into, and may in the future enter into, certain derivative arrangements with respect to portions of our natural gas and crude oil production to reduce our sensitivity to potential commodity price declines, and with respect to portions of our debt, to reduce our sensitivity to potential

increases in interest rates. None of our derivative instruments are designated as cash flow hedges. We believe that these derivative arrangements, although not free of risk, allow us to achieve a more predictable cash flow and to reduce exposure to commodity price and interest rate fluctuations. However, derivative arrangements may limit the benefit of increases in commodity prices or limit the benefit of decreases in interest rates. Moreover, our derivative arrangements apply only to a portion of our production and our debt, and therefore, provide only partial protection against declines in commodity prices and increases in interest rates, respectively. We continuously reevaluate our hedging programs in light of changes in production, market conditions, commodity price forecasts, capital spending, interest rate forecasts and debt service requirements.

We use a mix of commodity swaps and costless collars and interest rate swaps to accomplish our hedging strategy. We have exposure to financial institutions in the form of derivative transactions in connection with our hedges. These transactions are with counterparties in the financial services industry, and specifically with members of our bank group. These transactions could expose us to credit risk in the event of default of our counterparties. In addition, if any lender under our credit agreement is unable to fund their commitment, our liquidity could be reduced by an amount up to the aggregate amount of such lender's commitment under our credit agreement. We believe our counterparty risk is low in part because of the offset option we have with each of our counterparties in our revolving credit agreement and various hedge contracts. See Note 3 — "Fair Value Measurements" for further information.

The following derivative contracts were in place at September 30, 2010:

Crude Oil		Volume/Month	Price/Unit	Fair Value
Oct 2010-Dec 2010 (2)	Swap	4,250 Bbls	\$72.32	\$ (112,931)
Oct 2010-Dec 2010 (2)	Collar	9,000 Bbls	\$65.28-\$70.60	(293,917)
Oct 2010-Dec 2010 (2)	Collar	7,667 Bbls ⁽¹⁾	\$110.00-\$181.25	662,682
Jan 2011-Dec 2011	Swap	3,300 Bbls	\$70.74	(555,783)
Jan 2011-Dec 2011	Collar	7,000 Bbls	\$64.50-\$69.50	(1,372,441)
Jan 2011-Mar 2011	Swap	2,000 Bbls	\$86.15	17,030
Apr 2011-Jun 2011	Swap	1,500 Bbls	\$86.78	10,381
Jul 2011-Sep 2011	Swap	500 Bbls	\$87.32	2,936
Natural Gas				
Oct 2010-Dec 2010 (2)	Swap	29,000 Mmbtu	\$7.88	342,464
Oct 2010-Dec 2010 (2)	Collar	351,000 Mmbtu	\$7.57-\$9.05	3,831,230
Oct 2010-Dec 2010 (2)	Collar	85,867 Mmbtu ⁽¹⁾	\$9.00-\$15.25	1,305,231
Jan 2011-Dec 2011	Collar	266,000 Mmbtu	\$7.32-\$8.70	9,251,687
Commodity price derivative instruments				13,088,569
Interest rate				
		Notional Amount	Fixed LIBOR Rate	
Oct 2010-Dec 2010 (2)	Swap	\$50,000,000	1.50%) (141,892
Oct 2010- May 2011 (2)	Swap	\$150,000,000	2.90%) (2,386,665
Interest rate derivative instruments				(2,528,557)

Total net fair value asset of derivative instruments \$ 10,560,012

- (1) Average volume per month for the remaining contract term
- (2) Remaining contract period

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5. ASSET RETIREMENT OBLIGATIONS

We estimate the fair values of asset retirement obligations ("AROs") based on historical experience of plug and abandonment costs by field, and assumptions and judgments regarding such factors as the existence of a legal obligation for an ARO, estimated probabilities, amounts and timing of settlements, the credit-adjusted risk-free rate to be used and inflation rates.

Asset Retirement Obligations Rollforward

Beginning January 1, 2010 liability	\$	9,702,653
Additions		43,119
Accretion expense		443,202
Revisions		—
Properties sold		(203,918)
Plugging and abandonment activity		(150,512)
Ending September 30, 2010 liability	\$	9,834,544

6. DEBT

We maintain a senior secured revolving credit facility with Wells Fargo Bank, National Association ("Wells Fargo Bank"), as agent (the "Senior Credit Agreement"), and the lender parties thereto that currently provides for a \$100 million borrowing base, based on our current proved crude oil and natural gas reserves. The borrowing base is subject to semi-annual redeterminations, although our lenders may elect to make one additional unscheduled redetermination between scheduled redetermination dates. We are currently working with our bank group on finalizing the November 2010 scheduled redetermination of our borrowing base and believe that it will be determined at an amount that is reasonably comparable with our current borrowing base. The Senior Credit Agreement's outstanding principal amounts, together with all accrued and unpaid interest, will be due and payable in full on January 8, 2012. As of September 30, 2010, we had an outstanding loan balance of \$44.5 million under our Senior Credit Agreement.

On June 9, 2010, we entered into a fifth amendment to our Senior Credit Agreement. This amendment provided, among other things, for an extension of the maturity date to January 8, 2012 and the redetermination of the borrowing base to \$100 million. Until we enter into additional hedging agreements that would add an incremental \$3 million in discounted present value to our reserve base, a maximum of \$95 million of the \$100 million borrowing base may be utilized.

We also maintain a second lien credit agreement dated May 8, 2007 (the "Second Lien Credit Agreement") with our lenders, including an affiliate of OCM GW Holdings, LLC ("Oaktree Holdings"), our largest stockholder. The Second Lien Credit Agreement provides for a maximum loan amount of \$150 million which we borrowed in a single draw at closing and is due and payable in full at maturity on May 8, 2012. As of September 30, 2010, we had an outstanding loan balance of \$150 million under our Second Lien Credit Agreement.

The Senior Credit Agreement and the Second Lien Credit Agreement (the "Credit Agreements") are secured by a lien on substantially all of our assets, as well as a security interest in the stock of our subsidiaries. The obligations under the Second Lien Credit Agreement are junior to those under the Senior Credit Agreement. Interest is payable on the Credit Agreements as individual borrowings mature and renew.

The Credit Agreements include usual and customary affirmative covenants for credit facilities of similar type and size, as well as customary negative covenants, including, among others, limitations on liens, hedging, mergers, asset sales or dispositions, payments of dividends, incurrence of additional indebtedness, certain leases and investments outside of the ordinary course of business. The Credit Agreements also contain certain financial and proved reserve covenants. See Note 10 of our Annual Report on Form 10-K for the year ended December 31, 2009 for a more detailed description of our Credit Agreements and the covenants under the Credit Agreements. At September 30, 2010, we were in compliance with all covenants under our Credit Agreements.

As consideration for Oaktree Holdings' agreement to deposit \$10 million in escrow on November 6, 2009, to collateralize a \$10 million unsecured promissory note between Crimson and Wells Fargo Bank, which was subsequently repaid on December 22, 2009, we issued an unsecured subordinated promissory note on November 6, 2009 for the principal amount of \$2 million to Oaktree Holdings, a related party. The indebtedness under the \$2 million promissory note bears interest at a per annum rate equal to 8% and matures on the later of (i) November 8, 2012 and (ii) the date nine months after payment in full in cash of all Obligations (as such term is defined under our Credit Agreements) and the termination of all commitments to extend credit under our Credit Agreements. The promissory note is subordinated in right of payment to the prior payment in full in cash of all obligations under our Credit Agreements. At September 30, 2010, the carrying fair value of this debt was calculated as \$1.8 million, net of discount, using the estimated market value interest rate at the time of issuance.

7. STOCKHOLDERS' EQUITY

In the nine months ended September 30, 2010, we issued approximately 0.3 million shares of unvested restricted Common Stock to certain employees under the 2005 Stock Incentive Plan. We issued 31,646 shares of unvested restricted Common Stock to two members of our board of directors as compensation pursuant to the Director Compensation Plan.

In the nine months ended September 30, 2010, approximately 0.3 million shares of previously issued restricted Common Stock vested, of which 33,600 shares were withheld by us to satisfy the employees' tax liability resulting from the vesting of these shares, as provided for in the restricted stock agreement, with the remaining shares being released to the employees and directors. We also had 74,256 unvested shares of restricted Common Stock forfeited due to employee terminations. We also issued 14,763 shares of Common Stock pursuant to employee stock option exercises in the nine months ended September 30, 2010.

8. INCOME TAXES

Income tax benefit for the three and nine months ended September 30, 2010 was \$2.3 million and \$5.2 million, respectively, compared to \$5.2 million and \$9.1 million, respectively, for the three and nine months ended September 30, 2009. The year-to-date income tax expense is based on our estimate of the effective tax rate expected to be applicable for the full year.

9. SUBSEQUENT EVENT

On October 26, 2010, we entered into a private placement transaction with America Capital Energy Corporation ("ACEC"), a private investor, whereby ACEC may purchase up to \$30.0 million of newly issued Common Stock at a purchase price of \$5.00 per share in a two step process. We completed the first step of the transaction and issued 4,250,000 shares of Common Stock, or 9.9% of the post-transaction outstanding shares, to ACEC for a total cash consideration of \$21.25 million, of which a \$3.0 million deposit was received at the end of September 2010. Because of its contingent nature, the

deposit was recorded in accounts payable at September 30, 2010. We also issued a 60-day option by which ACEC may acquire an additional 1,750,000 shares of Series I Convertible Preferred Stock, par value \$0.01 per share, a newly created series of preferred stock at \$5.00 per share, for additional consideration of \$8.75 million. If the preferred stock is issued upon exercise of the option, ACEC, as holder of preferred stock, would have the right to appoint a director to our board of directors. The preferred stock will automatically convert into an equal number of shares of Common Stock upon the earlier of (i) the exercise of the ACEC's right to appoint a director and (ii) December 31, 2010. If the option is exercised and the preferred shares are converted, ACEC will have been issued an aggregate of 6.0 million shares of common stock, or approximately 13.4% of the outstanding shares of Common Stock. We intend to use the net proceeds from the private placement for general corporate purposes, including the continued development of our significant inventory of drilling prospects.

10. RECENT ACCOUNTING PRONOUNCEMENTS

New Accounting Standards Adopted in 2010

In April 2010, the Financial Accounting Standards Board ("FASB") issued Accounting Standards Update ("ASU") No. 2010-14, Accounting for Extractive Industries—Oil and Gas (Topic 932): Amendments to Paragraph 932-10-S99-1 ("ASU 2010-14"). ASU 2010-14 incorporates updated text changes to Rule 4-10 of the Securities and Exchange Commission ("SEC") Regulation S-X into the FASB's Accounting Standards Codification ("ASC"). The amendments reflect changes to fossil fuel exploration and production definitions, and addresses issues associated with new technology implemented over the past several decades. Specifically, the additional text added to FASB ASC 932-10-S99-1 reflects changes previously included in SEC Final Rulemaking Release No. 33-8995, Modernization of Oil and Gas Reporting, which became effective on January 1, 2010. The adoption of this ASU did not have a material impact on our financial position, results of operations or cash flows.

In February 2010, the FASB issued ASU No. 2010-09, Subsequent Events (Topic 855): Amendments to Certain Recognition and Disclosure Requirements ("ASU 2010-09"). ASU 2010-09 amends Subtopic 855-10 to remove some contradictions between the requirements of U.S. GAAP and the SEC's filing rules. As a result, public companies will no longer have to disclose the date through which subsequent events have been evaluated. We adopted these amendments as of February 24, 2010, with the issuance of this ASU. The adoption of this ASU did not have a material impact on our financial position, results of operations or cash flows.

We adopted FASB ASU No. 2010-06, Fair Value Measurements and Disclosures (Topic 820): Improving Disclosures about Fair Value Measurements ("ASU 2010-06") on January 1, 2010. ASU 2010-06 requires, among other items, reporting entities to provide information about movements of assets among Levels 1 and 2 of the three-tier fair value hierarchy established by FASB ASC 820. The adoption of this ASU did not have a material impact on our financial position, results of operations or cash flows.

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

Forward-looking Statements

The following discussion should be read in conjunction with the consolidated financial statements and the notes thereto included in this Quarterly Report on Form 10-Q and with the consolidated financial statements, notes and management's discussion and analysis reported in our Annual Report on Form 10-K for the year ended December 31, 2009. Statements in this discussion may be forward-looking. These forward-looking statements involve risks and uncertainties.

These forward-looking statements include, but are not limited to, statements regarding:

- estimates of proved reserve quantities and net present values of those reserves;
 - reserve potential;
 - business strategy;
 - estimates of future commodity prices;
- amounts, timing and types of capital expenditures and operating expenses;
 - expansion and growth of our business and operations;
 - expansion and development trends of the oil and gas industry;
 - acquisitions of natural gas and crude oil properties;
 - production of natural gas and crude oil reserves;
 - exploration prospects;
 - wells to be drilled and drilling results;
 - operating results and working capital;
- results of borrowing base redeterminations under our revolving credit facility; and
 - future methods and types of financing.

We caution that a number of factors could cause future production, revenues and expenses to differ materially from our expectations. For a discussion on risk factors affecting our business, see the information in "ITEM 1A. Risk Factors" contained in our Annual Report on Form 10-K for the year ended December 31, 2009 and our Quarterly Report on Form 10-Q for the period ended June 30, 2010, as filed with the Securities and Exchange Commission.

Overview

We are an independent energy company engaged in the acquisition, exploitation, exploration and development of natural gas and crude oil properties. We have historically focused our operations in the onshore U.S. Gulf Coast and South Texas regions, which are generally characterized by high rates of return in known, prolific producing trends. We have recently expanded our strategic focus to include longer reserve life resource plays in East Texas and South Texas that we believe provide significant long-term reserve and production growth potential from multiple formations. Our gross revenues are derived from the following sources:

1. Natural gas, crude oil and natural gas liquids sales that are proceeds from the sale of natural gas, crude oil and natural gas liquids production. This represents over 99% of our gross revenues.
2. Operating overhead and other income that consists primarily of administrative fees received for operating natural gas and crude oil properties for other working interest owners and for marketing and transporting natural gas for those owners.

Results of Operations

The following is a discussion of our consolidated results of operations, financial condition and capital resources. You should read this discussion in conjunction with our consolidated financial statements and the notes thereto included in this Quarterly Report on Form 10-Q.

Comparative results of operations for the periods indicated are discussed below.

Three Months Ended September 30, 2010 Compared to Three Months Ended September 30, 2009

Revenues

Natural Gas, Crude Oil and Natural Gas Liquids Sales

	Three months ended September 30,			Percent Change	
	2010	2009	Change		
Product revenues:	(in millions, except percentages)				
Natural gas sales	\$ 15.5	\$ 16.4	\$ (0.9)	-5.5	%
Crude oil sales	5.4	6.7	(1.3)	-19.4	%
Natural gas liquids sales	3.5	3.6	(0.1)	-2.8	%
Product revenues	\$ 24.4	\$ 26.7	\$ (2.3)	-8.6	%

Revenues from the sale of natural gas, crude oil and natural gas liquids, net of the realized effects of our commodity price hedging instruments, were \$24.4 million for the third quarter 2010 compared to \$26.7 million for the third quarter 2009. The decrease in revenue was due to lower production and lower realized commodity prices.

Production

	Three months ended September 30,			Percent Change	
	2010	2009	Change		
Sales volumes:					
Natural gas (Mcf)	2,390,868	2,373,940	16,928	0.7	%
Crude oil (Bbl)	63,755	76,376	(12,621)	-16.5	%
Natural gas liquids (Bbl)	101,992	114,792	(12,800)	-11.2	%
Natural gas equivalents (Mcf)	3,385,350	3,520,948	(135,598)	-3.9	%

Quarterly production was approximately 3.4 Bcfe for the third quarter 2010 compared to approximately 3.5 Bcfe for the third quarter 2009 and 2.7 Bcfe for the second quarter of 2010. On a daily basis, we produced an average of 36,797 Mcfe for the 2010 third quarter compared to an average of 38,271 Mcfe for the 2009 quarter and 30,084 Mcfe per day for the second quarter of 2010. Included in the 2009 quarter was approximately 259,000 Mcfe from our Southwest Louisiana properties that were sold in December 2009. Higher normalized production volumes, exclusive of the sale of our Southwest Louisiana properties, are a result of production from new wells drilled and workovers completed in 2010.

Average Sales Prices

	Three months ended September 30,			Percent Change	
	2010	2009	Change		
Average sales prices (before hedging):					
Natural gas (Mcf)	\$4.48	\$3.24	\$1.24	38.3	%
Crude oil (Bbl)	75.72	66.57	9.15	13.7	%
Natural gas liquids (Bbl)	34.60	31.51	3.09	9.8	%
Natural gas equivalents (Mcfe)	5.63	4.65	0.98	21.1	%

	Three months ended September 30,			Percent Change	
	2010	2009	Change		
Average sales prices (after hedging):					
Natural gas (Mcf)	\$6.47	\$6.92	\$(0.45)	-6.5	%
Crude oil (Bbl)	84.76	87.85	(3.09)	-3.5	%
Natural gas liquids (Bbl)	34.60	31.51	3.10	9.8	%
Natural gas equivalents (Mcfe)	7.21	7.60	(0.39)	-5.1	%

Natural gas, crude oil and natural gas liquids prices are reported net of the realized effect of our hedging agreements. We realized gains of \$0.6 million on our crude oil hedges and \$4.8 million on our natural gas hedges in the third quarter 2010, compared to realized gains of \$1.6 million for crude oil hedges and \$8.8 million for natural gas hedges in the third quarter 2009, all of which were included in our natural gas and crude oil sales revenues on our Consolidated Statements of Operations.

Costs and Expenses

	Three months ended September 30,			Percent Change	
	2010	2009	Change		
Certain Operating Expenses:					
	(in millions, except percentages)				
Lease operating expenses	\$3.6	\$3.9	\$(0.3)	-7.7	%
Production and ad valorem taxes	1.4	1.6	(0.2)	-12.5	%
Exploration expenses	1.3	0.7	0.6	85.7	%
General and administrative(1)	4.0	3.5	0.5	14.3	%
Operating expenses	10.3	9.7	0.6	6.2	%
Depreciation, depletion & amortization	12.0	13.4	(1.4)	-10.4	%
Share-based compensation(1)	0.5	0.3	0.2	66.7	%
Certain operating expenses	\$22.8	\$23.4	\$(0.6)	-2.6	%

(1) Total general and administrative costs on the Consolidated Statements of Operations include share-based compensation.

	Three months ended September 30,			Percent Change	
	2010	2009	Change		
Selected Costs (\$ per Mcfe):	(in millions, except percentages)				
Lease operating expenses	\$1.06	\$1.10	\$(0.04)	-3.6	%
Production and ad valorem taxes	0.41	0.44	(0.03)	-6.8	%
Exploration expenses	0.39	0.20	0.19	95.0	%
General and administrative(1)	1.20	0.99	0.21	21.2	%
Operating expenses	3.06	2.73	0.33	12.1	%
Depreciation, depletion & amortization	3.56	3.81	(0.25)	-6.6	%
Share-based compensation(1)	0.13	0.10	0.03	30.0	%
Selected costs	\$6.75	\$6.64	\$0.11	1.7	%

(1) Total general and administrative costs on the Consolidated Statements of Operations include share-based compensation.

Lease Operating Expenses. Lease operating expenses for the third quarter 2010 were \$3.6 million, compared to \$3.9 million in the third quarter 2009, a slight increase over the \$3.2 million incurred in the third quarter 2009 after adjustment for the sale of the Southwest Louisiana properties in December 2009.

Production and Ad Valorem Tax Expenses. Production and ad valorem tax expenses for the third quarter 2010 were \$1.4 million, compared to \$1.6 million for the third quarter 2009, due to lower production, offset in part by higher sales prices in the third quarter of 2010.

Exploration Expenses. Exploration expenses were \$1.3 million in the third quarter 2010, compared to \$0.7 million for the third quarter 2009. Exploration expenses resulted primarily from lease expiration on certain conventional prospects in South Texas during the third quarter 2010, and from geological and geophysical costs in the third quarter 2009.

Depreciation, Depletion and Amortization (“DD&A”). DD&A expense for the third quarter 2010 was \$12 million compared to \$13.4 million for the third quarter 2009, a decrease primarily due to lower production.

General and Administrative (“G&A”) Expenses. Total G&A expenses were \$4.5 million for the third quarter 2010 compared to \$3.8 million for the third quarter 2009. Included in G&A expense is non-cash stock expense of \$0.5 million (\$0.13 per Mcfe) and \$0.3 million (\$0.10 per Mcfe) for the third quarters 2010 and 2009, respectively. G&A expenses for the third quarter 2010 were higher primarily due to higher estimated incentive compensation and higher legal fees.

Interest Expense. Interest expense was \$5.8 million for the third quarter 2010, compared to \$6.6 million for the third quarter 2009. Total interest expense decreased primarily due to the decrease in the outstanding debt on our revolving credit agreement, offset in part by the increase in the interest rate on our second lien agreement in May 2009.

Other Financing Costs. Other financing costs were \$0.8 million for the third quarter 2010, compared to \$0.4 million for the third quarter 2009. These expenses consist primarily of the amortization of deferred debt issuance costs associated with our credit facilities.

Unrealized Loss on Derivative Instruments. The non-cash unrealized loss on derivative instruments for the third quarter 2010 was \$1.3 million, compared to \$9.9 million for the third quarter 2009.

Unrealized gain or loss is the change in the fair value of our commodity price hedging contracts and our interest rate swaps during the period. Unrealized gain or loss will vary period to period, and will be a function of the hedges in place, the strike prices of those hedges and the forward curve pricing of the commodities and interest rates being hedged.

Income Taxes. Our net loss before taxes was \$6.1 million for the third quarter 2010, compared to \$13.4 million in the third quarter 2009. After adjusting for permanent tax differences, we recorded an income tax benefit of \$2.3 million for the third quarter 2010, compared to \$4.8 million for the third quarter 2009.

Dividends on Preferred Stock. Dividends on preferred stock were zero for the third quarter 2010, compared with \$1.2 million in the third quarter 2009. All of the Series G and Series H Preferred Stock, including accrued dividends, were converted to Common Stock in December 2009 in conjunction with our Common Stock offering. Dividends in the third quarter 2009 included approximately \$1.1 million on the Series G Preferred Stock and \$10,745 on the Series H Preferred Stock.

Nine months Ended September 30, 2010 Compared to Nine months Ended September 30, 2009

Revenues

Natural Gas, Crude Oil and Natural Gas Liquids Sales

	Nine months ended September 30,			Percent Change	
	2010	2009	Change		
Product revenues:	(in millions, except percentages)				
Natural gas sales	\$43.5	\$55.1	\$(11.6)	-21.1	%
Crude oil sales	15.1	21.5	(6.4)	-29.8	%
Natural gas liquids sales	9.6	9.1	0.5	5.5	%
Product revenues	\$68.2	\$85.7	\$(17.5)	-20.4	%

Revenues from the sale of crude oil, natural gas and natural gas liquids, net of the realized effects of our hedging instruments, were \$68.2 million for the first nine months of 2010 compared to \$85.7 million for the first nine months of 2009, a decrease due primarily to lower production, offset in part by higher realized commodity prices.

Production

	Nine months ended September 30,			Percent Change	
	2010	2009	Change		
Sales volumes:					
Natural gas (Mcf)	6,432,283	8,142,588	(1,710,305)	-21.0	%
Crude oil (Bbl)	178,825	264,170	(85,345)	-32.3	%
Natural gas liquids (Bbl)	243,859	334,303	(90,444)	-27.1	%
Natural gas equivalents (Mcf)	8,968,387	11,733,426	(2,765,039)	-23.6	%

Production was approximately 9.0 Bcfe for the first nine months of 2010 compared to 11.7 Bcfe for the first nine months of 2009. On a daily basis, we produced an average of 32,851 Mcfe in the first nine

months of 2010 compared to an average of 42,980 Mcfe in the first nine months of 2009. Production for the first nine months of 2009 included approximately 906,000 Mcfe from our Southwest Louisiana properties that were sold in December 2009.

Average Sales Prices

	Nine months ended September 30,			Percent Change	
	2010	2009	Change		
Average sales prices (before hedging):					
Natural gas (Mcf)	\$4.61	\$3.92	\$0.69	17.6	%
Crude oil (Bbl)	76.40	52.80	23.60	44.7	%
Natural gas liquids (Bbl)	39.27	27.19	12.08	44.4	%
Natural gas equivalents (Mcfe)	5.90	4.68	1.22	26.1	%

	Nine months ended September 30,			Percent Change	
	2010	2009	Change		
Average sales prices (after hedging):					
Natural gas (Mcf)	\$6.76	\$6.77	\$(0.01)	-0.1	%
Crude oil (Bbl)	84.42	81.46	2.96	3.6	%
Natural gas liquids (Bbl)	39.27	27.19	12.09	44.5	%
Natural gas equivalents (Mcfe)	7.60	7.31	0.29	4.0	%

Natural gas, crude oil and natural gas liquids prices are reported net of the realized effect of our hedging agreements. We realized gains of \$1.4 million on our crude oil hedges and \$13.8 million on our natural gas hedges in the first nine months of 2010, compared to realized gains of \$7.6 million on our crude oil hedges and \$23.2 million on our natural gas hedges in the first nine months of 2009, which were included in our natural gas and crude oil sales revenues on our Consolidated Statements of Operations.

Costs and Expenses

	Nine months ended September 30,			Percent Change	
	2010	2009	Change		
Certain Operating Expenses: (in millions, except percentages)					
Lease operating expenses	\$11.4	\$13.5	\$(2.1)	-15.6	%
Production and ad valorem taxes	4.6	6.1	(1.5)	-24.6	%
Exploration expenses	2.0	2.9	(0.9)	-31.0	%
General and administrative(1)	12.5	11.5	1.0	8.7	%
Operating expenses	30.5	34.0	(3.5)	-10.3	%
Depreciation, depletion & amortization	33.0	41.6	(8.6)	-20.7	%
Share-based compensation	1.4	1.9	(0.5)	-26.3	%
Certain operating expenses	\$64.9	\$77.5	\$(12.6)	-16.3	%

(1)

Total general and administrative costs include share-based compensation on the Consolidated Statements of Operations

Selected Costs (\$ per Mcfe):	Nine months ended September 30,			Percent Change	
	2010	2009	Change		
	(in millions, except percentages)				
Lease operating expenses	\$1.27	\$1.15	\$0.12	10.4	%
Production and ad valorem taxes					