Sanchez Energy Corp
Form S-1/A
October 06, 2011

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As filed with the Securities and Exchange Commission on October 6, 2011

**Registration No. 333-176613**

# UNITED STATES

# SECURITIES AND EXCHANGE COMMISSION

**Washington, D.C. 20549**

# Amendment No.1

# to

# FORM S-1

**REGISTRATION STATEMENT**

**UNDER THE SECURITIES ACT OF 1933**

# SANCHEZ ENERGY CORPORATION

(Exact name of registrant as specified in its charter)

| | | |
|---|---|---|
| **Delaware** | **1311** | **45-3090102** |
| (State or other jurisdiction of incorporation or organization) | (Primary Standard Industrial Classification Code Number) | (IRS Employer Identification Number) |

**1111 Bagby Street**

**Suite 1600**

**Houston, Texas 77002**

**(713) 783-8000**

(Address, including zip code, and telephone number, including

area code, of registrant s principal executive offices)

**Antonio R. Sanchez, III**

**1111 Bagby Street**

**Suite 1600**

**Houston, Texas 77002**

**(713) 783-8000**

(Name, address, including zip code, and telephone number, including area code, of agent for service)

**Copies to:**

| | |
|---|---|
| **David P. Elder**<br>**Patrick J. Hurley**<br>**Akin Gump Strauss Hauer & Feld LLP**<br>**1111 Louisiana Street, 44th Floor**<br>**Houston, Texas 77002**<br>**(713) 220-5881** | **Robert G. Reedy**<br>**E. James Cowen**<br>**Porter Hedges LLP**<br>**1000 Main Street, 36th Floor**<br>**Houston, Texas 77002**<br>**(713) 226-6674** |

**Approximate date of commencement of proposed sale to the public:**

As soon as practicable after this registration statement becomes effective.

If any of the securities being registered on this Form are to be offered on a delayed or continuous basis pursuant to Rule 415 under the Securities Act of 1933, check the following box. ¨

If this Form is filed to register additional securities for an offering pursuant to Rule 462(b) under the Securities Act, check the following box and list the Securities Act registration statement number of the earlier effective registration statement for the same offering. ¨

If this Form is a post-effective amendment filed pursuant to Rule 462(c) under the Securities Act, check the following box and list the Securities Act registration statement number of the earlier effective registration statement for the same offering. ¨

If this Form is a post-effective amendment filed pursuant to Rule 462(d) under the Securities Act, check the following box and list the Securities Act registration statement number of the earlier effective registration statement for the same offering. ¨

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. (Check one):

| | |
|---|---|
| Large accelerated filer ¨ | Accelerated filer ¨ |
| Non-accelerated filer x<br>(Do not check if a smaller reporting company) | Smaller reporting company ¨ |

**The registrant hereby amends this registration statement on such date or dates as may be necessary to delay its effective date until the registrant shall file a further amendment which specifically states that this registration statement shall thereafter become effective in accordance with Section 8(a) of the Securities Act of 1933, as amended, or until the registration statement shall become effective on such date as the Securities and Exchange Commission, acting pursuant to said Section 8(a), may determine.**

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**The information in this preliminary prospectus is not complete and may be changed. These securities may not be sold until the registration statement filed with the Securities and Exchange Commission is effective. This preliminary prospectus is not an offer to sell nor does it seek an offer to buy these securities in any jurisdiction where the offer or sale is not permitted.**

SUBJECT TO COMPLETION, DATED OCTOBER 6, 2011

**PRELIMINARY PROSPECTUS**

## Shares

# Sanchez Energy Corporation

## COMMON STOCK

Sanchez Energy Corporation is offering shares of its common stock. This is the initial public offering of our common stock and no public market currently exists for our common stock. We currently estimate that the initial public offering price of our common stock will be between $ and $ per share. We intend to apply to list our common stock on the New York Stock Exchange under the symbol SN.

**Investing in our common stock involves risks. See Risk Factors beginning on page 17.**

| | Per Share | Total |
|---|---|---|
| Initial Public Offering Price | $ | $ |
| Underwriting Discounts and Commissions | $ | $ |
| Proceeds, Before Expenses, to Us | $ | $ |

The underwriters may also purchase up to an additional shares of common stock from us at the public offering price, less the underwriting discounts and commissions, within 30 days of the date of this prospectus to cover any over-allotments. If the underwriters exercise this option in full, the total underwriting discounts and commissions will be $ , and our total proceeds, after underwriting discounts and commissions, will be $ .

**The Securities and Exchange Commission and state securities regulators have not approved or disapproved of these securities, or determined if this prospectus is truthful or complete. Any representation to the contrary is a criminal offense.**

The underwriters expect to deliver the shares of common stock to purchasers on , 2011.

# Johnson Rice & Company L.L.C.

## Macquarie Capital

**, 2011**

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**You should rely only on the information contained in this prospectus or in any free writing prospectus we may authorize to be delivered to you. Neither we nor the underwriters have authorized anyone to provide you with additional or different information. We and the underwriters are offering to sell, and seeking offers to buy, shares of common stock only in jurisdictions where offers and sales are permitted.**

This prospectus contains forward-looking statements that are subject to a number of risks and uncertainties, many of which are beyond our control. Please read Risk Factors and Forward-Looking Statements.

### Industry and Market Data

The market data and certain other statistical information used throughout this prospectus are based on independent industry publications, government publications or other published independent sources. Although we believe these third-party sources are reliable and that the information is accurate and complete, we have not independently verified the information nor have we ascertained the underlying economic or operational assumptions relied upon therein.

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## PROSPECTUS SUMMARY

*This summary highlights information contained elsewhere in this prospectus. Because this summary provides only a brief overview of the key aspects of the offering, it does not contain all of the information that you should consider before investing in our common stock. You should read the entire prospectus carefully, including Risk Factors beginning on page 17, Management s Discussion and Analysis of Financial Condition and Results of Operations beginning on page 48 and the financial statements and the related notes appearing elsewhere in this prospectus, before making an investment decision. The information presented in this prospectus assumes that the underwriters do not exercise their option to purchase additional shares of common stock from us, unless otherwise indicated.*

*As used in this prospectus, unless otherwise indicated: (i) the company, we, our, us or similar terms refer collectively to Sanchez Energy Corporation and its operating subsidiaries after giving effect to the formation transactions described under Formation Transactions ; (ii) SOG refers to Sanchez Oil & Gas Corporation, a Delaware corporation; (iii) SEP I refers to Sanchez Energy Partners I, LP, a Delaware limited partnership; (iv) Sanchez Group refers to SOG, SEP I and their affiliates (but excludes the company); and (v) SEP Holdings III refers to SEP Holdings III, LLC, a Delaware limited liability company and a wholly owned subsidiary of SEP I, which will be contributed to us as part of the formation transactions. See Organizational Structure of Sanchez Energy Corporation for additional information.*

*Our estimated proved reserve information as of December 31, 2010 and June 30, 2011 is based on reports prepared by Ryder Scott Company, L.P., or Ryder Scott, our independent reserve engineers. We have included a glossary of some of the oil and natural gas terms used in this prospectus in Appendix A.*

### Overview

We are an independent exploration and production company focused on the exploration, acquisition and development of unconventional oil and natural gas resources and recently formed for the purpose of acquiring SEP I s unconventional oil and natural gas assets, which are held in SEP Holdings III and will be contributed to us as part of the formation transactions. We have accumulated approximately 39,000 net leasehold acres in the oil and condensate, or black oil and volatile oil, windows of the Eagle Ford Shale in Gonzales, Zavala and Frio Counties of South Texas. We use the term black oil to describe a quality of oil with an API gravity of 40º or less and with a gas-to-oil ratio of 500 mcf per barrel or less. We use the term volatile oil to describe a quality of oil with an API gravity greater than 40º and with a gas-to-oil ratio of greater than 500 mcf per barrel. The majority of our capital expenditure budget for the period from July 2011 through December 2012 will be focused on the development and expansion of our oil focused Eagle Ford Shale acreage and operations. We plan to continue to aggressively pursue additional leasehold and strategic acquisitions in the Eagle Ford Shale.

Our management team and the Sanchez Group have a proven track record in identifying, acquiring, and executing large drilling programs and have operated a wide range of drilling projects over the last 40 years, primarily focused as an operator in the South Texas and onshore Gulf Coast areas. Various members of the Sanchez Group have been in the oil and natural gas business since 1972, have drilled or participated in over 900 wells, directly and through joint ventures, and have invested substantial amounts of capital in the oil and natural gas industry. During this period, they have carefully cultivated their relationships with mineral and surface rights owners in and around our South Texas and onshore Gulf Coast areas, which we believe gives us a competitive advantage in acquiring additional leasehold positions in these areas.

Our Eagle Ford Shale acreage is comprised of approximately 9,300 net acres in Gonzales County, Texas, which we refer to as our Palmetto area, and approximately 29,500 net acres in Zavala and Frio Counties, Texas, which we refer to as our Maverick area. Hilcorp Energy Company, together with its affiliates, or Hilcorp, recently entered into a definitive agreement for the sale of 141,000 net acres in the Eagle Ford Shale, including

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its 50% ownership interest in our Palmetto area, to Marathon Oil Corporation, or Marathon, for approximately $3.5 billion, or an average of $24,822 per acre, before adjusting for acquired production and reserves and subject to closing adjustments. Starting November 1, 2011, when the acquisition is expected to close, we expect Marathon to be our 50/50 working interest partner in our Palmetto area, as successor to Hilcorp.

We own all rights and depths on the majority of our Eagle Ford Shale acreage. We believe this acreage to be prospective for other zones, including the Buda Limestone, Austin Chalk and Pearsall Shale formations that lie above and below the Eagle Ford Shale. We are currently evaluating these other zones, which may present us with additional drilling locations. Several of our existing wells are either producing from or have logged pay in the Buda Limestone and the Austin Chalk formations.

In addition, we have approximately 1,500 net acres in the Haynesville Shale in Natchitoches Parish, Louisiana, which are operated by Chesapeake Energy Corporation and Encana Corporation. We do not currently anticipate spending any capital on our Haynesville acreage in the near future. The majority of our Haynesville leases extend through 2012 and 2013, giving us and our partners the option to accelerate drilling should natural gas prices increase. Finally, we have amassed approximately 82,000 net acres in northern Montana, which we believe may be prospective for the Heath, Three Forks and Bakken Shales.

Our capital expenditure budget for the period from July 2011 through December 2012 is approximately $95 million, and is anticipated to consist of the following:

Approximately $70 million for drilling and completing wells in the Eagle Ford Shale; and

Approximately $25 million for expansion of our Eagle Ford Shale acreage position.

The following table presents summary data for each of our primary project areas as of June 30, 2011, unless otherwise indicated:

| | | | | Capital Expenditure Budget from July 2011 through December 2012 | | | |
|---|---|---|---|---|---|---|---|
| | Net Acreage | Identified Drilling Locations(1) Gross | Net | Gross Wells | Net Wells | Drilling Capex (in millions) | Estimated Net Proved Reserves(2) (mmboe) |
| Palmetto Gonzales | 9,329 | 155 | 76 | 14 | 7 | $ 50 | 2.9 |
| Maverick Zavala, Frio | 29,425 | 309 | 244 | 7 | 4 | 20 | 0.1 |
| Total Eagle Ford Shale | 38,754 | 464 | 320 | 21 | 11 | 70 | 3.0 |
| Haynesville Shale | 1,499 | 72 | 18 | - | - | - | 0.2 |
| Heath, Three Forks and Bakken Shales | 82,274 | - | - | - | - | - | - |
| Total | 122,527 | 536 | 338 | 21 | 11 | $ 70 | 3.2 |

(1) Total identified drilling locations are calculated using 120 acre spacing in our Eagle Ford Shale areas and 80 acre spacing in our Haynesville Shale area on the undeveloped portion of our acreage. We are currently evaluating our acreage in the Heath, Three Forks and Bakken Shales and have not identified any drilling locations on that acreage.

(2) Based on Ryder Scott estimated proved reserve report as of June 30, 2011.

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## Our Properties

### Eagle Ford Shale

The Eagle Ford Shale is one of the fastest growing unconventional shale trends in North America. According to the Smith Weekly Rig Count, since January 2010, the rig count in the Eagle Ford Shale has grown 581% from 27 rigs to 184 rigs as of August 19, 2011. Based on a recent study by the Society of Petroleum Engineers, the aerial extent of the trend is thought to be approximately 11 million acres. Based on publicly available information, we believe that average drilling and completion costs in the trend have ranged between $5.5 million and $8.1 million per well with estimated ultimate recoveries, or EURs, ranging from 225,000 to 850,000 boe per well, and initial 30-day average production has ranged between 200 to 2,000 boe/d per well. There have been a number of recent publicly-reported transactions in the trend that have yielded per acre valuations ranging from approximately $5,000 per acre to $25,000 per acre. Based on our experience and that of other companies operating in this trend, we believe that the Eagle Ford Shale can be characterized as having low geologic risks and repeatable drilling opportunities.

In the Eagle Ford Shale, we have assembled approximately 39,000 net acres with an average working interest of approximately 69%. Using 120 acre well-spacing for horizontal well development, we believe that there could be up to 464 gross and up to 320 net locations for potential future drilling on our acreage. Consistent with other operators in this area, we plan to perform multi-stage hydraulic fracturing with 12 to 20 stages on each lateral well. For the period from July 2011 through December 2012, we plan on drilling 21 gross (11 net) wells on our Eagle Ford Shale acreage and plan on spending approximately $70 million on drilling and completion and approximately $25 million on additional leasehold acquisitions and other related expenditures in the Eagle Ford Shale.

In our Palmetto area, we have approximately 9,300 net acres in Gonzales County, Texas with an average working interest of approximately 49%. We believe that our Palmetto acreage lies in the volatile oil window where we anticipate drilling, completion and facilities costs on our acreage to be between $5.5 million and $7.5 million per well. We have participated in the drilling of four gross wells on our acreage that had an average initial 30-day per well choke restricted production rate of 788 boe/d. We have identified up to 155 gross and up to 76 net locations for potential future drilling in our Palmetto area. For the period from July 2011 through December 2012, we plan to spend approximately $50 million to drill 14 gross (7 net) wells in our Palmetto area.

In our Maverick area, we have approximately 29,500 net operated acres in Zavala and Frio Counties, Texas with an average working interest of approximately 79%. We believe that our Maverick acreage lies in the black oil window, where we anticipate drilling, completion and facilities costs on our acreage to be between $5.8 million and $6.5 million per well. We have identified up to 309 gross and up to 244 net locations for potential future drilling on our Maverick acreage. We have drilled one horizontal well that had an initial 30-day average production rate of 242 boe/d. We expect to drill one vertical well in 2011 to test the feasibility of a vertical development program and compare horizontal and vertical completion economic returns. For the period from July 2011 through December 2012, we plan to spend approximately $20 million to drill 7 gross (4 net) wells in our Maverick area, including the one vertical well to be drilled in 2011.

### Haynesville Shale

We have assembled approximately 1,500 net acres in Natchitoches Parish, Louisiana that are prospective for the Haynesville Shale. We have an average working interest of approximately 25% and the operators on our Haynesville Shale acreage are Chesapeake Energy Corporation and Encana Corporation. Four gross wells have been drilled to date, and we have participated in three of those wells. We believe that our acreage position is in the core of the Haynesville Shale fairway. We anticipate drilling, completion and facilities costs on our acreage to be between $8.0 and $10.0 million per well. We have identified 72 gross and 18 net locations for potential future drilling on our acreage. We do not currently anticipate spending any capital on our Haynesville Shale acreage in the near term. The majority of our Haynesville Shale leases extend through 2012 and 2013, giving us and our partners the option to accelerate drilling should natural gas prices increase.

**Heath, Three Forks and Bakken Shales**

We have acquired approximately 82,000 net acres in Lewis and Clark, Meagher, and Cascade Counties of Montana that we believe may be prospective for the Heath, Three Forks and Bakken Shales. We plan to monitor industry activity in our area as we develop our plans. Our lease terms are for five years with an option to renew for another five years at $10 per acre, giving us time to allow industry activity to develop the trend before we devote significant drilling capital to our acreage position. To the east of our acreage, EOG Resources, Inc., Cabot Oil & Gas Corporation, Endeavour International Corporation, Cirque Resources LP and Central Montana Resources LLC have indicated their intention to drill exploratory wells in this area.

**Our Business Strategies**

Our primary business objective is to increase stockholder value by building reserves, production and cash flows at an attractive return on invested capital. To achieve our objective, we intend to execute the following business strategies:

*Aggressively Develop Our Eagle Ford Shale Leasehold Positions.* We intend to aggressively drill and develop our acreage position to maximize the value of our resource potential. The up to 464 gross and up to 320 net locations for potential future drilling that we have identified in our Eagle Ford Shale area will be our primary targets in the near term as we believe the Eagle Ford Shale to be the highest rate of return project that we currently possess. We anticipate drilling 14 gross (7 net) wells in our Palmetto area and 7 gross (4 net) wells in our Maverick area through December 2012 with an aggregate drilling and completion capital expenditure budget of approximately $70 million.

*Pursue Strategic Acquisitions and Grow Our Leasehold Position in the Eagle Ford Shale and Seek Entry into New Basins*. We believe that we will be able to identify and acquire additional acreage and producing assets in the Eagle Ford Shale. For the period from July 2011 through December 2012, we have budgeted approximately $25 million for additional leasehold acquisitions in the Eagle Ford Shale. We also plan to selectively target additional domestic basins that would allow us to employ our strategies on large undeveloped acreage positions similar to our Eagle Ford Shale areas.

*Leverage our Relationship with Our Affiliates to Expand Unconventional Oil Assets.* Our largest stockholder is controlled by certain members of the Sanchez Group. Various members of the Sanchez Group have drilled or participated in over 900 wells, directly and through joint ventures, and have invested substantial amounts of capital in the oil and natural gas industry since 1972. During this period, they have carefully cultivated their relationships with mineral and surface rights owners in and around our South Texas and onshore Gulf Coast areas and compiled an extensive technological database, which we believe gives us a competitive advantage in acquiring additional leasehold positions in these areas. We will have access to the unrestricted, proprietary portions of the technological database related to our properties, and SOG will otherwise be required to interpret and use the database, to the extent relating to our properties for our benefit. The majority of the database covers the South Texas and onshore Gulf Coast areas and includes more than 6,400 square miles of 3D seismic data and 48,000 miles of 2D seismic data used for regional interpretation, 395,000 well logs, 13,000 LAS files and 30,000 scanned well documents, as well as a fully integrated suite of the latest interpretive

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geologic software. We plan on leveraging our affiliates expertise, industry relationships and size to opportunistically expand reserves and our leasehold positions in the Eagle Ford Shale and other onshore unconventional oil resources.

*Enhance Returns by Focusing on Operational and Cost Efficiencies.* We are focused on continuous improvement of our operating measures and have significant experience in successfully converting early-stage resource opportunities into cost-efficient development projects. We believe the magnitude and concentration of our acreage within our project areas provide us with the opportunity to capture economies of scale, including the ability to drill multiple wells from a single drilling pad, utilizing centralized production and fluid handling facilities and reducing the time and cost of rig mobilization.

*Adopt and Employ Leading Drilling and Completion Techniques.* We are focused on enhancing our drilling and completion techniques to maximize recovery. Industry techniques with respect to drilling and completion have significantly evolved over the last several years, resulting in increased initial production rates and recoverable hydrocarbons per well through the implementation of longer laterals and more tightly spaced fracturing stimulation stages. We continuously evaluate industry drilling results and monitor the results of other operators to improve our operating practices, and we expect our drilling and completion techniques will continue to evolve.

*Maintain Substantial Financial Liquidity to Capitalize on Opportunity and Limit Commodity Price Volatility.* Following the completion of this offering and the other transactions described under Formation Transactions, we will have approximately $ million in cash, assuming an initial public offering price of $ per share (the midpoint of the price range set forth on the cover page of this prospectus) and no outstanding indebtedness. We believe this strong liquidity position will allow us to grow production and proved reserves, to capitalize on acreage acquisition opportunities and to weather any potential volatility in commodity prices.

**Our Competitive Strengths**

We believe that the following competitive strengths will allow us to successfully execute our business strategies:

*Geographically Concentrated Leasehold Position in One of North America s Leading Unconventional Oil Resource Trends*. We have assembled a current leasehold position of approximately 39,000 net leasehold acres in the Eagle Ford Shale, which we believe to be one of the highest rates of return unconventional oil and natural gas areas in North America. Our geographically concentrated acreage position allows us to establish economies of scale with respect to drilling, production, operating and administrative costs in addition to further leveraging our base of technical expertise in our project areas. We believe that offset operator activity and well results around our project areas have significantly de-risked our acreage positions such that we believe that there are low geologic risks and repeatable drilling opportunities across our acreage position.

*Large, Multi-Year Inventory*. We have an inventory of up to 464 gross and up to 320 net locations for potential future drilling on our Eagle Ford Shale acreage position and 72 gross and 18 net locations for potential future drilling on our Haynesville acreage position. For the period from July 2011 through December 2012, we plan on drilling 21 gross (11 net) wells on our Eagle Ford Shale acreage. The drilling and completion of these wells would represent approximately

5% of the total gross identified locations and approximately 3% of the total net identified locations on our Eagle Ford Shale acreage. As the industry continues to refine drilling and completion technologies, we may be able to enhance total recovery and inventory through the drilling of in-fill locations on our acreage positions. In addition, we have amassed approximately 82,000 net acres in Lewis and Clark, Meagher, and Cascade Counties of Montana that we believe may be prospective for the Heath, Three Forks and Bakken Shales. If we are successful in developing this acreage, we could materially expand our multi-year inventory.

*Our Relationship with Members of the Sanchez Group and Our Services Agreement Provide Us with Extensive Technical Expertise and Access to Long Standing Relationships with Mineral Owners*. Certain members of the Sanchez Group have been in the oil and natural gas business since 1972 and have drilled or participated in over 900 wells, directly and through joint ventures, in and around our South Texas and onshore Gulf Coast areas. This long operating history in the basins in which we operate provides us with extensive knowledge of the basins and the ability to leverage longstanding relationships with mineral owners. We believe that this expertise and these relationships, together with our services agreement, should allow us to develop our assets more efficiently and grow our acreage positions faster than our competitors.

*Significant Financial Flexibility*. Following the completion of this offering and the other transactions described under Formation Transactions, we will have approximately $ million in cash, assuming an initial public offering price of $ per share (the midpoint of the price range set forth on the cover page of this prospectus) and no outstanding indebtedness. We will use this cash to fund our capital expenditures, and, in particular, our drilling, exploration and acquisition programs through December 2012, our other operating expenses, and for general corporate purposes.

**Eagle Ford Shale Well Results**

In July 2011, we completed our first Maverick area Eagle Ford horizontal well, the Alpha Ware #1H, in Zavala County, Texas. This well was a 6,513 foot lateral well and was completed using a 20 stage hydraulic fracture stimulation. The 30-day average initial production rate from this well was 242 boe/d. Through August 8, 2011, the Alpha Ware #1H has produced a total of approximately 7,866 boe. We are the operator of the well and have a 60% working interest in the well.

In February 2011, we completed our fourth Eagle Ford horizontal well in our Palmetto area, the Barnhart #4H, in Gonzales County, Texas. This well was a 5,507 foot lateral well and was completed using a 16 stage hydraulic fracture stimulation. The 30-day average initial production rate from this well was 893 boe/d using a 15/64 inch restricted choke. Through August 8, 2011, the Barnhart #4H has produced a total of approximately 123,562 boe. We have a 50% working interest in the well.

In November 2010, we completed our third Eagle Ford horizontal well in our Palmetto area, the Barnhart #3H, in Gonzales County, Texas. This well was a 5,320 foot lateral well and was completed using a 16 stage hydraulic fracture stimulation. The 30-day average initial production rate from this well was 663 boe/d using a 15/64 inch restricted choke. Through August 8, 2011, the Barnhart #3H has produced a total of approximately 91,960 boe. We have a 50% working interest in the well.

In October 2010, we completed our second Eagle Ford horizontal well in our Palmetto area, the Barnhart #2H, in Gonzales County, Texas. This well was a 5,100 foot lateral well and was completed using a 12 stage hydraulic fracture stimulation. The 30-day average initial production rate from this well was 1,102 boe/d using a 13/64 inch restricted choke. Through August 8, 2011, the Barnhart #2H has produced a total of approximately 139,821 boe. We have a 50% working interest in the well.

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In July 2010, we completed our first Eagle Ford horizontal well in our Palmetto area, the Barnhart #1H, in Gonzales County, Texas. This well was a 3,902 foot lateral well and was completed using a 12 stage hydraulic fracture stimulation. The 30-day average initial production rate from this well was 491 boe/d using a 17/64 inch restricted choke. Through August 8, 2011, the Barnhart #1H has produced a total of approximately 72,865 boe. We have a 50% working interest in the well.

**Our Principal Business Relationships**

SEP I will be our largest stockholder following consummation of this offering and the other transactions described under Formation Transactions, holding approximately % of our post-offering outstanding common stock, assuming that the underwriters do not exercise their over-allotment option. SEP I was formed in late 2007 in order to facilitate the expansion of exploration activities previously begun in the early 2000 s by SOG and several independent parties to joint exploration agreements. SOG and the other parties contributed their assets to the newly formed SEP I and a second phase of equity fundraising was completed in early 2008. As a result, SOG and its affiliates became the largest limited partner in SEP I as well as its general partner. Collectively, SOG and its affiliates own approximately 24% of the limited partnership interests in SEP I. The unconventional assets acquired by SEP I are being contributed to us in exchange for cash and common stock in the transactions described under Formation Transactions.

Except for the lock-up period described under Underwriting, SEP I is not subject to any contractual obligation to maintain its ownership in us. For more information on the potential effects of a disposition of our common stock by SEP I, please read Risk Factors Risks Relating to This Offering A substantial portion of our total outstanding shares may be sold into the market. This could cause the market price of our common stock to drop significantly, even if our business is doing well.

**Our Relationship with SOG and Other Members of the Sanchez Group**

SOG, headquartered in Houston, Texas, is a private full service oil and natural gas company engaged in the exploration and development of oil and natural gas primarily in the South Texas and onshore Gulf Coast areas on behalf of its affiliates. SOG provides all the employee support to SEP I and other members of the Sanchez Group under the terms of a management services agreement and will provide similar services for us. SOG, as it is known today, had its beginnings in 1972, when A. R. Sanchez, Sr., A. R. Sanchez, Jr. and a group of other partners from Houston and Laredo, Texas, drilled their first well on the Hereford Ranch in Webb County, Texas. A.R. Sanchez Jr. is also the founder, Chief Executive Officer and Chairman of the Board of Directors of SOG. He has over 38 years of experience in the oil and natural gas industry and was involved in the discovery of several major oil and natural gas fields in Texas, including Bob West, Hereford, George West, Escobas, Highlands, La Sal Vieja, and Palmetto Eagle Ford fields. SOG s major areas of activity have been in the onshore Gulf Coast, Mid-Continent and Rocky Mountain regions. Since 1972, various members of the Sanchez Group have participated in and managed the drilling of over 900 wells, investing a substantial amount of capital in, among other things, well costs, seismic and acreage.

SOG has approximately 70 permanent employees and numerous contract professionals. These individuals are experienced energy professionals with expertise in finance and operations and broad technical skills in the oil and natural gas business. In connection with the ongoing business of SOG, its employees review a large number of potential acquisitions and are involved in decisions relating to the acquisition and disposition of oil and natural gas assets by the various portfolio companies in which SOG owns interests, including SEP I.

Although there is no obligation to do so, to the extent consistent with their fiduciary duties and other obligations to the investors and other parties associated with SOG, SOG and its affiliates may refer to us or allow us to participate in new acquisitions by its portfolio companies and may cause its portfolio companies to contribute or sell oil and natural gas assets to us in transactions that would be beneficial to all parties. Given this potential alignment of interests and the overlapping ownership of the management of SOG, SEP I and other members of the Sanchez Group and us, we believe that we will benefit from the collective expertise of the employees of SOG, their extensive network of industry relationships, and the access to potential acquisition opportunities that would not otherwise be available to us. For a summary of the process by which such mutually agreeable prices will be determined, please read Certain Relationships and Related Party Transactions Review, Approval or Ratification of Transactions with Related Persons.

**Risk Factors**

An investment in our common stock involves a high degree of risk. You should consider and read carefully all of the risks and uncertainties described in Risk Factors beginning on page 17, together with all of the other information contained in this prospectus, including the financial statements and the related notes appearing at the end of this prospectus before deciding to invest in our common stock.

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**Formation Transactions**

Concurrently with the closing of this offering, the following transactions, which we refer to as the formation transactions, will occur:

- SEP I will contribute to us 100% of the limited liability company interests of SEP Holdings III, which owns interests in unconventional oil and natural gas assets consisting of undeveloped leasehold, proved oil and natural gas reserves and related equipment and other assets, referred to collectively herein as our properties.

- In exchange for the limited liability company interests described above and as further described in Use of Proceeds, we will pay SEP I approximately $ million from the proceeds of this offering and issue to SEP I approximately million shares of our common stock.

- We will enter into a services agreement with SOG, pursuant to which SOG (directly or through its subsidiaries) will agree to provide us with the services and data that we believe are necessary to manage, operate and grow our business and we will agree to reimburse SOG for all direct and indirect costs incurred on our behalf.

For additional information, see Certain Relationships and Related Party Transactions.

**Organizational Structure of Sanchez Energy Corporation**

The diagram below illustrates our organizational structure based on total shares outstanding after giving effect to this offering and the related formation transactions and assumes that the underwriters do not exercise their over-allotment option to purchase additional shares.

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**Principal Executive Offices and Internet Address**

Our principal executive offices are located at 1111 Bagby Street, Suite 1600, Houston, Texas 77002. Our telephone number is (713) 783-8000. Our website will be located at www.sanchezenergycorp.com following the completion of this offering. We expect to make available our periodic reports and other information filed with or furnished to the Securities and Exchange Commission, or the SEC, free of charge through our website, as soon as reasonably practicable after those reports and other information are electronically filed with or furnished to the SEC. Information on our website or any other website is not incorporated by reference into this prospectus and does not constitute a part of this prospectus.

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**The Offering**

| | |
|---|---|
| Common stock offered by us | shares.<br><br>shares, if the underwriters exercise their over-allotment option in full. |
| Common stock outstanding after this offering(1) | shares ( shares if the underwriters exercise their over-allotment option in full). |
| Use of proceeds | We will receive net proceeds of approximately $ million from the sale of the common stock offered by us, assuming an initial public offering price of $ per share (the midpoint of the price range set forth on the cover page of this prospectus) and after deducting estimated expenses and underwriting discounts and commissions of approximately $ million. We intend to use approximately $ million of the net proceeds as partial consideration (together with our issuance to SEP I of million shares of our common stock) for the contribution by SEP I of the limited liability company interests in SEP Holdings III. Each $1.00 increase (decrease) in the public offering price would increase (decrease) our net proceeds by approximately $ million.<br><br>We intend to use the remaining net proceeds of approximately $ million and any net proceeds from the exercise of the underwriters option to purchase additional common stock from us to fund our capital expenditures, and, in particular, our drilling, exploration and acquisition programs through December 2012, our other operating expenses, and for general corporate purposes. |
| Dividend policy | We do not anticipate paying any cash dividends on our common stock. See Dividend Policy. |
| Risk factors | You should carefully read and consider the information beginning on page 17 of this prospectus set forth under the heading Risk Factors and all other information set forth in this prospectus before deciding to invest in our common stock. |
| Exchange listing | We intend to apply to list our common stock on the New York Stock Exchange under the symbol SN. |

(1) The number of shares of common stock to be outstanding after this offering excludes shares of common stock expected to be reserved for issuance under our Long Term Incentive Plan. See Management Long Term Incentive Plan.

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## Summary Financial Data

The following table sets forth our summary financial data. The summary financial data as of December 31, 2009 and 2010 and for the years ended December 31, 2008, 2009 and 2010 are derived from our audited historical financial statements included elsewhere in this prospectus. The summary historical financial data as of June 30, 2011 and for the six months ended June 30, 2010 and 2011 are derived from our unaudited historical financial statements included elsewhere in this prospectus. The results of operations for the interim periods are not necessarily indicative of operating results for the entire year or any future period.

Our historical financial statements have been prepared on a carve-out basis from the accounts of SEP I. These carve-out financial statements include all assets, liabilities and results of operations of the unconventional oil and natural gas properties and related assets to be contributed to us by SEP I for the periods presented.

You should read the following table in conjunction with Formation Transactions, Use of Proceeds, Selected Financial Data, Management s Discussion and Analysis of Financial Condition and Results of Operations and our historical financial statements and the notes thereto included elsewhere in this prospectus. Among other things, those historical financial statements include more detailed information regarding the basis of presentation for the following information.

The following table presents a non-GAAP financial measure, Adjusted EBITDA, which we use in evaluating the financial performance and liquidity of our business. This measure is not calculated or presented in accordance with generally accepted accounting principles, or GAAP. We explain this measure below and reconcile it to the most directly comparable financial measures calculated and presented in accordance with GAAP.

| | Year Ended December 31, | | | Six Months Ended June 30, (Unaudited) | |
|---|---|---|---|---|---|
| | 2008 | 2009 | 2010 | 2010 | 2011 |
| | | | (in thousands) | | |
| **Statement of Operations Data:** | | | | | |
| Total revenues | $ - | $ 241 | $ 4,553 | $ 333 | $ 7,176 |
| Total operating costs and expenses | $ 1,247 | $ 196 | $ 7,311 | $ 2,902 | $ 5,650 |
| Operating income (loss) | $ (1,247) | $ 45 | $ (2,758) | $ (2,569) | $ 1,527 |
| Net income (loss) | $ (1,247) | $ 45 | $ (2,758) | $ (2,569) | $ 1,326 |
| **Other Financial Data:** | | | | | |
| Adjusted EBITDA | $ (1,247) | $ (1,612) | $ (1,328) | $ (2,495) | $ 3,490 |
| **Cash Flow Data:** | | | | | |
| Net cash provided by (used in) operating activities | $ (1,247) | $ (1,710) | $ (3,777) | $ (2,507) | $ 3,969 |
| Net cash provided by (used in) investing activities | $ (14,197) | $ 2,734 | $ (7,925) | $ (7,915) | $ (8,573) |
| Net cash provided by (used in) financing activities | $ 15,444 | $ (1,024) | $ 11,702 | $ 10,423 | $ 4,604 |

| | As of December 31, | | As of June 30, 2011 (Unaudited) | |
|---|---|---|---|---|
| | 2009 | 2010 | Historical | Pro Forma As Adjusted for This Offering |
| | | (in thousands) | | |
| **Balance Sheet Data:** | | | | |
| Cash and cash equivalents | $ - | $ - | $ - | $ |
| Working capital (deficit) | $ 59 | $ (1,818) | $ (3,611) | $ |
| Total assets | $ 13,275 | $ 26,764 | $ 35,849 | $ |
| Parent net investment/stockholders equity | $ 13,218 | $ 22,162 | $ 28,091 | $ |

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**Non-GAAP Financial Measures**

We include in this prospectus the non-GAAP financial measure Adjusted EBITDA and provide reconciliations of Adjusted EBITDA to net income (loss) and net cash provided by (used in) operating activities, our most directly comparable financial performance and liquidity measures calculated and presented in accordance with GAAP. We define Adjusted EBITDA as net income (loss):

Plus:

- Interest expense, including realized and unrealized losses on interest rate derivative contracts;
- Income tax expense (benefit);
- Depreciation, depletion, and amortization;
- Accretion of asset retirement obligations;
- Loss (gain) on settlement of asset retirement obligations;
- Loss (gain) on sale of oil and natural gas properties;
- Unrealized losses on derivatives;
- Impairment of oil and natural gas properties; and
- Other non-recurring items that we deem appropriate.

Less:

- Interest income;
- Unrealized gains on derivatives; and
- Other non-recurring items that we deem appropriate.

Adjusted EBITDA will be used as a supplemental financial measure by our management and by external users of our financial statements, such as investors, commercial banks and others, to assess:

- our operating performance as compared to that of other companies and partnerships in our industry, without regard to financing methods, capital structure or historical cost basis; and

- our ability to incur and service debt and fund capital expenditures.

Adjusted EBITDA should not be considered an alternative to net income, operating income, cash flow from operating activities or any other measure of financial performance or liquidity presented in accordance with GAAP. Our Adjusted EBITDA may not be comparable to similarly titled measures of another company because all companies may not calculate Adjusted EBITDA in the same manner. The following tables present our calculation of Adjusted EBITDA, a reconciliation of Adjusted EBITDA to net income (loss) and a reconciliation of Adjusted EBITDA to net cash provided by (used in) operating activities for each of the periods indicated.

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**Calculation of and Reconciliation of Net Income (Loss) to Adjusted EBITDA**

| | Year Ended December 31, | | | Six Months Ended June 30, | |
|---|---|---|---|---|---|
| | 2008 | 2009 | 2010 | 2010 | 2011 |
| | | | (in thousands) | | |
| Net income (loss) | $ (1,247) | $ 45 | $ (2,758) | $ (2,569) | $ 1,326 |
| Depreciation, depletion, and amortization | - | 415 | 1,428 | 73 | 1,961 |
| Accretion of asset retirement obligations | - | 0 | 2 | 1 | 2 |
| Unrealized loss on derivatives | - | - | - | - | 201 |
| Gain on sale of oil and natural gas properties | - | (2,686) | - | - | - |
| Impairment of properties | - | 614 | - | - | - |
| Adjusted EBITDA | $ (1,247) | $ (1,612) | $ (1,328) | $ (2,495) | $ 3,490 |

**Reconciliation of Net Cash Provided by (Used in) Operating Activities to Adjusted EBITDA**

| | Year Ended December 31, | | | Six Months Ended June 30, | |
|---|---|---|---|---|---|
| | 2008 | 2009 | 2010 | 2010 | 2011 |
| | | | (in thousands) | | |
| Net cash provided by (used in) operating activities | $ (1,247) | $ (1,710) | $ (3,777) | $ (2,507) | $ 3,969 |
| Net change in operating assets and liabilities | - | 98 | 2,449 | 12 | (479) |
| Adjusted EBITDA | $ (1,247) | $ (1,612) | $ (1,328) | $ (2,495) | $ 3,490 |

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**Summary Reserve and Operating Data**

The following tables present summary data with respect to our estimated net proved oil and natural gas reserves as of June 30, 2011, which is based on a report that has been prepared by Ryder Scott. These reserve estimates were prepared in accordance with the SEC s rules regarding oil and natural gas reserve reporting that are currently in effect. The following tables also contain certain summary information regarding production and operating data with respect to such properties for the periods presented.

Please read Management s Discussion and Analysis of Financial Condition and Results of Operations, Business and Properties Oil and Natural Gas Reserves and Production, and Risk Factors in evaluating the material presented below.

| | | As of June 30, 2011 (Unaudited) |
|---|---|---|
| **Estimated Proved Reserves** | | |
| Oil (mbbls) | | 2,596.1 |
| Natural gas (mmcf) | | 3,889.3 |
| Total (mboe)(1) | | 3,244.3 |
| Proved developed (mboe) | | 646.9 |
| Proved undeveloped (mboe) | | 2,597.5 |
| Proved developed reserves as a percentage of total proved reserves | | 19.9% |
| Standardized measure (in millions)(2) | $ | 69.5 |
| **Oil and Natural Gas Prices(3)** | | |
| Oil NYMEX WTI per bbl | $ | 90.09 |
| Natural gas NYMEX Henry Hub per mmbtu | $ | 4.21 |

(1) One boe is equal to six mcf of natural gas or one bbl of oil or natural gas liquids, or NGLs, based on an approximate energy equivalency. This is a physical correlation and does not reflect a value or price relationship between the commodities.

(2) Standardized measure is the present value of estimated future net revenues to be generated from the production of proved reserves, determined in accordance with the rules and regulations of the SEC without giving effect to non-property related expenses, such as general and administrative expenses, interest expense, or to depletion, depreciation and amortization. The future cash flows are discounted using an annual discount rate of 10%. Standardized measure does not give effect to derivative transactions. We expect to hedge a portion of our future estimated production from total proved reserves. Prior to the closing of this offering, we will not be treated as a taxable entity for federal income tax purposes. Future calculation of the standardized measure will include the effects of income taxes on future net revenues. For further discussion of income taxes, see Management s Discussion and Analysis of Financial Condition and Results of Operations.

(3) Our estimated net proved reserves and related standardized measure were determined using average index prices for oil and natural gas, without giving effect to derivative contracts, held constant throughout the life of our properties. The unweighted arithmetic average first-day-of-the-month prices for the prior twelve months were $90.09/bbl for oil and $4.21/mmbtu for natural gas at June 30, 2011. These prices were adjusted by lease for quality, transportation fees, geographical differentials, marketing bonuses or deductions and other factors affecting the price realized at the wellhead.

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| | Year Ended December 31, 2010 | Six Months Ended June 30, 2010 | Six Months Ended June 30, 2011 |
|---|---|---|---|
| | | (Unaudited) | |
| **Net Production:** | | | |
| Total production (mboe) | 61.1 | 4.8 | 85.2 |
| Average daily production (boe/d) | 167.4 | 26.4 | 470.8 |
| **Average Realized Sales Price:** | | | |
| Oil (mbbls) | $ 78.92 | $ 69.70 | $ 94.75 |
| Natural gas (mmcf) | $ 4.68 | $ - | $ 4.66 |
| **Average Realized Sales Price per boe(1):** | $ 74.50 | $ 69.70 | $ 84.22 |
| **Average Unit Costs per boe:** | | | |
| Lease operating expenses | $ 6.41 | $ 8.34 | $ 9.02 |
| Production and ad valorem taxes | $ 3.50 | $ 3.21 | $ 4.63 |
| General and administrative expenses | $ 86.32 | $ 580.47 | $ 29.61 |
| Depletion and depreciation | $ 23.36 | $ 15.26 | $ 23.01 |

(1) Amounts shown are based on oil and natural gas sales. We did not have any realized commodity derivative gains (losses) as of the dates presented.

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## RISK FACTORS

*An investment in our common stock involves a high degree of risk. You should consider and read carefully all of the risks and uncertainties described below, together with all of the other information contained in this prospectus, including the financial statements and the related notes appearing at the end of this prospectus before deciding to invest in our common stock. If any of the following risks actually occurs, our business, business prospects, financial condition, results of operations or cash flows could be materially adversely affected. In any such case, the trading price of our common stock could decline, and you could lose all or part of your investment. The risks below are not the only ones facing our company. Additional risks not currently known to us or that we currently deem immaterial may also adversely affect us. This prospectus also contains forward-looking statements, estimates and projections that involve risks and uncertainties. Our actual results could differ materially from those anticipated in the forward-looking statements as a result of specific factors, including the risks described below.*

### Risks Related to Our Business

***Drilling wells is speculative, often involving significant costs that may be more than our estimates, and may not result in any discoveries or additions to our future production or reserves. Any material inaccuracies in estimated reserves, estimated drilling costs or underlying assumptions will materially affect our business.***

Exploring for and developing oil and natural gas reserves involves a high degree of operational and financial risk, which precludes definitive statements as to the time required and costs involved in reaching certain objectives. The budgeted costs of drilling, completing and operating wells are often exceeded and can increase significantly when drilling costs rise due to a tightening in the supply of various types of oilfield equipment and related services. Drilling may be unsuccessful for many reasons, including geological conditions, weather, cost overruns, equipment shortages and mechanical difficulties. Exploratory wells bear a much greater risk of loss than development wells. Moreover, the successful drilling of an oil or natural gas well does not ensure a profit on investment. A variety of factors, both geological and market-related, can cause a well to become uneconomic or only marginally economic. Our initial drilling locations, and any potential additional locations that may be developed, require significant additional exploration and development, regulatory approval and commitments of resources prior to commercial development. If our actual drilling and development costs are significantly more than our estimated costs, we may not be able to continue our business operations as proposed and would be forced to modify our plan of operation.

***Our estimated oil and natural gas reserves will naturally decline over time, and we may be unable to develop, find or acquire additional reserves to replace our current and future production at acceptable costs, which would adversely affect our business, financial condition and results of operations.***

Our future oil and natural gas reserves, production volumes, and cash flow depend on our success in developing and exploiting our current reserves efficiently and finding or acquiring additional recoverable reserves economically. Our estimated oil and natural gas reserves will naturally decline over time as they are produced. Our success depends on our ability to economically develop, find or acquire additional reserves to replace our own current and future production. If we are unable to do so, or if expected development is delayed, reduced or cancelled, the average decline rates will likely increase.

***Developing and producing oil and natural gas are costly and high-risk activities with many uncertainties that could adversely affect our business, financial condition and results of operations.***

The cost of developing, completing and operating a well is often uncertain, and cost factors can adversely affect the economics of a well. Our efforts will be uneconomical if we drill dry holes or wells that are productive but do not produce as much oil and natural gas as we had estimated. Furthermore, our development and production operations may be curtailed, delayed or canceled as a result of other factors, including:

- high costs, shortages or delivery delays of rigs, equipment, labor or other services;

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- composition of sour gas, including sulfur and mercaptan content;
- unexpected operational events and conditions;
- reductions in oil and natural gas prices;
- increases in severance taxes;
- adverse weather conditions and natural disasters;
- facility or equipment malfunctions and equipment failures or accidents, including acceleration of deterioration of our facilities and equipment due to the highly corrosive nature of sour gas;
- title problems;
- pipe or cement failures, casing collapses or other downhole failures;
- compliance with ever-changing environmental and other governmental requirements;
- environmental hazards, such as natural gas leaks, oil spills, salt water spills, pipeline ruptures and discharges of toxic gases;
- lost or damaged oilfield development and service tools;
- unusual or unexpected geological formations and pressure or irregularities in formations;
- loss of drilling fluid circulation;
- fires, blowouts, surface craterings and explosions;
- uncontrollable flows of oil, natural gas or well fluids;
- loss of leases due to incorrect payment of royalties; and

other hazards, including those associated with sour gas such as an accidental discharge of hydrogen sulfide gas, that could also result in personal injury and loss of life, pollution and suspension of operations.

If any of these factors were to occur with respect to a particular field, we could lose all or a part of our investment in the field, or we could fail to realize the expected benefits from the field, either of which could materially and adversely affect our business, financial condition and results of operations.

We routinely apply hydraulic fracturing techniques in many of our drilling and completion operations. Hydraulic fracturing has recently become subject to increased public scrutiny and recent changes in federal and state law, as well as proposed legislative changes, could significantly restrict the use of hydraulic fracturing. Such laws could make it more difficult or costly for us to perform fracturing to stimulate production from dense subsurface rock formations and, in the event of local prohibitions against commercial production of natural gas, may preclude our ability to drill wells. In addition, such laws could make it easier for third parties opposing the hydraulic fracturing process to initiate legal proceedings based on allegations that specific chemicals used in the fracturing process could adversely affect groundwater. If hydraulic fracturing becomes regulated at the federal level as a result of federal legislation or regulatory initiatives by the U.S. Environmental Protection Agency, or the EPA, or other federal agencies, our fracturing activities could become subject to additional permitting requirements and result in permitting delays, financial assurance requirements, more stringent construction specifications, increased monitoring, reporting and recordkeeping obligations, plugging and abandonment requirements, as well as potential increases in costs. Additionally, on August 23, 2011, the EPA published a

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proposed rule in the Federal Register that would establish new air emission controls for oil and natural gas production and natural gas processing operations. The EPA is currently receiving public comment and recently conducted public hearings regarding the proposed rules and must take final action on them by February 28, 2012. Compliance with such rules could result in significant costs, including increased capital expenditures and operating costs, and could adversely impact our business. Please read Risks Related to our Business Federal and state legislative and regulatory initiatives relating to hydraulic fracturing could result in increased costs and additional operating restrictions or delays and Business and Properties Environmental Matters and Regulations Water and Other Water Discharges and Spills.

Additionally, hydraulic fracturing, drilling, transportation and processing of hydrocarbons bear an inherent risk of loss of containment. Potential consequences include loss of reserves, loss of production, loss of economic value associated with the affected wellbore, contamination of soil, ground water, and surface water, as well as potential fines, penalties or damages associated with any of the foregoing consequences.

***Our acquisition, development and production operations will require substantial capital expenditures, and we expect to fund these capital expenditures using cash generated from our operations or the issuance of debt and equity securities, or some combination thereof. Our failure to obtain the funds for necessary future growth capital expenditures could have a material adverse effect on our business, financial condition and results of operations.***

The oil and natural gas industry is capital intensive. We expect to make substantial growth capital expenditures in our business for the acquisition, development and production of oil and natural gas reserves. We intend to finance our future growth and capital expenditures with cash flows from operations and the issuance of debt and equity securities, or some combination thereof.

Our cash flows from operations and access to capital are subject to a number of variables, including:

- our estimated proved oil and natural gas reserves;
- the amount of oil, natural gas and NGLs we produce;
- the prices at which we sell our production;
- the costs of developing, producing, and transporting our oil and natural gas assets, including costs attributable to governmental regulation and taxation;
- our ability to acquire, locate and produce new reserves;
- fluctuations in our working capital needs;
- interest payments and debt service requirements;
- prevailing economic conditions;
- the ability and willingness of banks and other lenders to lend to us; and

- our ability to access the equity and debt capital markets.

If additional capital is needed to fund our growth capital expenditures, our ability to access the capital markets for future equity or debt offerings may be limited by our financial condition at the time of any such financing or offering, as well as by adverse market conditions resulting from, among other things, general economic conditions and contingencies and uncertainties that are beyond our control.

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***A decline in oil, natural gas or NGLs prices will cause a decline in our cash flow from operations, which could adversely affect our business, financial condition and results of operations.***

The oil and natural gas markets are very volatile, and we cannot predict future oil and natural gas prices. Prices for oil and natural gas may fluctuate widely in response to relatively minor changes in the supply of and demand for oil and natural gas, market uncertainty and a variety of additional factors that are beyond our control, such as:

- domestic and foreign supply of and demand for oil and natural gas;
- weather conditions and the occurrence of natural disasters;
- overall domestic and global economic conditions;
- political and economic conditions in oil and natural gas producing countries globally, including terrorist attacks and threats, escalation of military activity in response to such attacks or acts of war;
- actions of the Organization of Petroleum Exporting Countries, or OPEC, and other state-controlled oil companies relating to oil price and production controls;
- the effect of increasing liquefied natural gas deliveries to and exports from the United States;
- the impact of the U.S. dollar exchange rates on oil and natural gas prices;
- technological advances affecting energy supply and energy consumption;
- domestic and foreign governmental regulations and taxation;
- the impact of energy conservation efforts;
- the proximity, capacity, cost and availability of oil and natural gas pipelines and other transportation facilities;
- the availability of refining capacity; and
- the price and availability of alternative fuels.

In the past, oil and natural gas prices have been extremely volatile, and we expect this volatility to continue. For example, for the five years ended December 31, 2010, the NYMEX WTI oil price ranged from a high of $145.29 per bbl to a low of $31.41 per bbl, while the NYMEX

Henry Hub natural gas price ranged from a high of $13.31 per mmbtu to a low of $1.83 per mmbtu. Such volatility may affect the amount of our net estimated proved reserves and will affect the standardized measure of discounted future net cash flows of our net estimated proved reserves.

Natural gas prices are closely linked to the supply of natural gas and consumption patterns in the United States of the electric power generation industry and certain industrial and residential users where natural gas is the principal fuel. The domestic natural gas industry continues to face concerns of oversupply due to the success of new trends and continued drilling in these trends, despite lower natural gas prices.

Our revenue, profitability and cash flow depend upon the prices of and demand for oil and natural gas, and a drop in prices can significantly affect our financial results and impede our growth. In particular, declines in commodity prices will:

- limit our ability to enter into commodity derivative contracts at attractive prices;

- reduce the value and quantities of our reserves, because declines in oil and natural gas prices would reduce the amount of oil and natural gas that we can economically produce;

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- reduce the amount of cash flow available for capital expenditures; and

- limit our ability to borrow money or raise additional capital.

***An increase in the differential between the NYMEX or other benchmark prices of oil and natural gas and the wellhead price we receive for our production could adversely affect our business, financial condition and results of operations.***

The prices that we receive for our oil and natural gas production sometimes reflect a discount to the relevant benchmark prices, such as NYMEX, that are used for calculating hedge positions. The difference between the benchmark price and the price we receive is called a basis differential. Increases in the basis differential between the benchmark prices for oil and natural gas and the wellhead price we receive could adversely affect our business, financial condition and results of operations. We do not have or currently plan to have any commodity derivative contracts covering the amount of the basis differentials we experience in respect of our production. As such, we will be exposed to any increase in such differentials, which could adversely affect our business, financial condition and results of operations.

SEP I will contribute to us at the closing of this offering a commodity derivative contract with a deferred premium cost of approximately $1.9 million, and, in the future, we expect to enter into commodity derivative contracts for a portion of our estimated production from total estimated proved developed producing reserves that could result in both realized and unrealized hedging losses. We also expect to adopt a hedging policy designed to reduce the impact to our cash flows from commodity price volatility. Our hedging strategy and future hedging transactions will be determined by our management, which is not under any obligation to enter into commodity derivative contracts covering any specific portion of our production.

The prices at which we enter into commodity derivative contracts covering our production in the future will be dependent upon oil and natural gas prices at the time we enter into these transactions, which may be substantially higher or lower than past or current oil and natural gas prices. Accordingly, our price hedging strategy may not protect us from significant declines in oil and natural gas prices realized for our future production. Conversely, our hedging strategy may limit our ability to realize incremental cash flows from commodity price increases. As such, our hedging strategy may not protect us from changes in oil and natural gas prices that could have a significant adverse effect on our liquidity, business, financial condition and results of operation.

***Economic uncertainty could negatively impact the prices for oil and natural gas, limit our access to the debt and equity markets, increase our cost of capital, and may have other negative consequences that we cannot predict.***

Economic uncertainty in the United States could create financial challenges if conditions do not improve. Most recently, Standard & Poor s downgraded the U.S. credit rating to AA+ from its top rank of AAA, which has increased the possibility of other credit-rating agency downgrades which could have a material adverse effect on the financial markets and economic conditions in the United States and throughout the world. Our ability to access capital may be restricted at a time when we would like, or need, to raise capital. If our cash flow from operations is less than anticipated and our access to capital is restricted, we may be required to reduce our operating and capital budget, which could have a material adverse effect on our business, financial condition and results of operations. Ongoing uncertainty may also reduce the values we are able to realize in asset sales or other transactions we may engage in to raise capital, thus making these transactions more difficult and less economic to consummate. Additionally, demand for oil and natural gas may deteriorate and result in lower prices for oil and natural gas, which could have a negative impact on our business, financial condition and results of operations. Lower prices could also adversely affect the collectability of our trade receivables and cause our commodity hedging arrangements to be ineffective if our counterparties are unable to perform their obligations.

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***We are increasing production in areas of high industry activity, which may impact our ability to obtain the personnel, equipment, services, resources and facilities access needed to complete our development activities as planned or result in increased costs.***

Our strategy is to expand drilling activity in areas in which industry activity has increased rapidly, particularly in the Eagle Ford Shale trend in South Texas. As a result, demand for personnel, equipment, hydraulic fracturing, water and other services and resources, as well as access to transportation, processing and refining facilities in these areas has increased, as has the costs for those items. A delay or inability to secure the personnel, equipment, services, resources and facilities access necessary for us to complete our development activities as planned could result in a rate of oil and natural gas production below the rate forecasted, and significant increases in costs would impact our profitability.

***Shortages of equipment, services and qualified personnel could reduce our cash flow and adversely affect results of operations.***

The demand for qualified and experienced field personnel to drill wells and conduct field operations, geologists, geophysicists, engineers and other professionals in the oil and natural gas industry can fluctuate significantly, often in correlation with oil and natural gas prices and activity levels in new regions, causing periodic shortages. During periods of high oil and natural gas prices, SOG has experienced shortages of equipment, including drilling rigs and completion equipment, as demand for rigs and equipment has increased along with higher commodity prices and increased activity levels. In addition, there is currently a shortage of hydraulic fracturing capacity in many of the areas in which we operate. Higher oil and natural gas prices generally stimulate increased demand and result in increased prices for drilling rigs, crews and associated supplies, oilfield equipment and services and personnel in our exploration and production operations. These types of shortages or price increases could significantly decrease our profit margin, cash flow and operating results and/or restrict or delay our ability to drill those wells and conduct those operations that we currently have planned and budgeted, causing us to miss our forecasts and projections.

***If we do not purchase additional acreage or make acquisitions on economically acceptable terms, our future growth will be limited.***

Our ability to grow depends in part on our ability to make acquisitions on economically acceptable terms. We may be unable to make such acquisitions because we are:

- unable to identify attractive acquisition candidates or negotiate acceptable purchase contracts with their owners;
- unable to obtain financing for such acquisitions on economically acceptable terms; or
- outbid by competitors.

If we are unable to acquire properties containing estimated proved reserves, our total level of estimated proved reserves will decline as a result of our production.

***Certain of our undeveloped leasehold acreage is subject to leases that will expire over the next several years unless production is established on units containing the acreage or the leases are extended.***

Certain of our undeveloped leasehold acreage is subject to leases that will expire unless production in paying quantities is established during their primary terms or we obtain extensions of the leases. Our drilling plans for our undeveloped leasehold acreage are subject to change based upon various factors, including factors that are beyond our control, such as drilling results, oil and natural gas prices, the availability and cost of capital, drilling and production costs, availability of drilling services and equipment, gathering system and pipeline transportation constraints and regulatory approvals. Because of these uncertainties, we do not know if our undeveloped leasehold acreage will ever be drilled or if we will be able to produce crude oil or natural gas from these or any other potential drilling locations. If our leases expire, we will lose our right to develop the related

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properties on this acreage. As of June 30, 2011, we had leases representing 3,790 net acres (3,645 of which were in the Eagle Ford Shale) expiring in 2011, 4,797 net acres (4,646 of which were in the Eagle Ford Shale) expiring in 2012, and 21,150 net acres (21,126 of which were in the Eagle Ford Shale) expiring in 2013. As such, our actual drilling activities may materially differ from those presently identified, which could adversely affect our business, financial condition and results of operations.

***Availability of adequate gathering systems and transportation take-away capacity may hinder our access to suitable oil and natural gas markets or delay our production.***

Our ability to bring oil, natural gas and NGLs production to market depends on a number of factors including the availability and proximity of pipelines and processing facilities. The recent growth in production in the Eagle Ford Shale, especially of natural gas and NGLs production, has limited the availability of transportation take-away capacity for these products in certain parts of this trend. If we are unable to obtain adequate amounts of take-away capacity to meet our growing production levels, we may have to delay initial production or shut in our wells awaiting a pipeline connection or capacity or sell our production at significantly lower prices than those quoted on NYMEX or than we currently project, which could adversely affect our business, financial condition and results of operations.

***We have drilled only five wells in the Eagle Ford Shale, we are not the operator of our wells in the Haynesville Shale and we have not drilled wells in the Heath, Three Forks and Bakken Shales, and thus we have limited information regarding reserves and decline rates in the Eagle Ford Shale, Haynesville Shale, and the Heath, Three Forks and Bakken Shales. Wells drilled in these shale areas are more expensive and more susceptible to mechanical problems in drilling and completion techniques than wells in conventional areas.***

We have drilled only five wells in the Eagle Ford Shale, we are not the operator of our wells in the Haynesville Shale and we have not drilled wells in the Heath, Three Forks and Bakken Shales. Other operators in the Eagle Ford Shale, Haynesville Shale, and the Heath, Three Forks and Bakken Shales have significantly more experience in the drilling and completion of these wells, including the drilling and completion of horizontal wells. In addition, we have limited information with respect to the ultimate recoverable reserves and production decline rates in these areas. The wells drilled in the Eagle Ford Shale, Haynesville Shale, and the Heath, Three Forks and Bakken Shales are primarily horizontal and require more stimulation, which makes them more expensive to drill and complete. The wells will also be more susceptible to mechanical problems associated with the drilling and completion of the wells, such as casing collapse and lost equipment in the wellbore due to the length of the lateral portions of these unconventional wells. The fracturing of these shale formations will be more extensive and complicated than fracturing geological formations in conventional areas of operation.

***Our hedging transactions could result in cash losses, limit potential gains and materially impact our liquidity.***

Many of the derivative contracts to which we may be a party will require us to make cash payments to the extent the applicable index exceeds a predetermined price, thereby limiting our ability to realize the benefit of increases in oil and natural gas prices. If our actual production and sales for any period are less than our hedged production and sales for that period (including reductions in production due to operational delays) or if we are unable to perform our drilling activities as planned, we might be forced to satisfy all or a portion of our hedging obligations without the benefit of the cash flow from our sale of the underlying physical commodity, which may materially impact our liquidity, business, financial condition and results of operations.

***Federal and state legislative and regulatory initiatives relating to hydraulic fracturing could result in increased costs and additional operating restrictions or delays.***

Hydraulic fracturing is a process used by oil and natural gas exploration and production operators in the completion of certain oil and natural gas wells whereby water, sand and chemicals are injected under pressure into subsurface formations to stimulate natural gas and, to a lesser extent, oil production. This process is typically regulated by state agencies. The EPA, however, recently asserted federal regulatory authority over hydraulic fracturing involving diesel additives under the federal Safe Drinking Water Act s, or SDWA, Underground

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Injection Control, or UIC, Program by posting a new requirement on its website that requires facilities to obtain permits to use diesel fuel in hydraulic fracturing operations. The U.S. Energy Policy Act of 2005, which exempts hydraulic fracturing from regulation under the SDWA, prohibits the use of diesel fuel in the fracturing process without a UIC permit. Although the EPA has yet to take any action to enforce or implement this newly-asserted regulatory authority, industry groups have filed suit challenging the EPA s recent decisions as a final agency action and, thus, violative of the notice-and-comment rulemaking procedures of the Administrative Procedures Act. At the same time, the EPA has commenced a study of the potential adverse effects that hydraulic fracturing may have on water quality and public health, with results of the study anticipated to be available by late 2012, and a committee of the U.S. House of Representatives also has commenced its own investigation into hydraulic fracturing practices. Additionally, legislation has been introduced in the U.S. Congress to amend the SDWA to subject hydraulic fracturing processes to regulation under that Act and to require the disclosure of chemicals used by the oil and natural gas industry in the hydraulic fracturing process. Further, certain members of the Congress have called upon the U.S. Government Accountability Office to investigate how hydraulic fracturing might adversely affect water resources, the SEC to investigate the natural gas industry and any possible misleading of investors or the public regarding the economic feasibility of pursuing natural gas deposits in shales by means of hydraulic fracturing, and the U.S. Energy Information Administration to provide a better understanding of that agency s estimates regarding natural gas reserves, including reserves from shale formations, as well as uncertainties associated with those estimates. Finally, the Shale Gas Subcommittee of the Secretary of Energy Advisory Board released a report on August 11, 2011, proposing recommendations to reduce the potential environmental impacts from shale gas production. These ongoing or proposed studies, depending on their degree of pursuit and any meaningful results obtained, could spur initiatives to further regulate hydraulic fracturing under the SDWA or other regulatory mechanism. Also, some states have adopted, and other states are considering adopting, regulations that could restrict hydraulic fracturing in certain circumstances or otherwise require the public disclosure of chemicals used in the hydraulic fracturing process. For example, Texas adopted a law in June 2011 requiring disclosure to the Railroad Commission of Texas and the public of certain information regarding the components used in the hydraulic fracturing process. Furthermore, in July 2011, the EPA proposed several new emissions standards to reduce volatile organic compound, or VOC, emissions from several types of processes and equipment used in the oil and natural gas industry, including a 95 percent reduction in VOCs emitted during the construction or modification of hydraulically-fractured wells. Additionally, on August 23, 2011, the EPA published a proposed rule in the Federal Register that would establish new air emission controls for oil and natural gas production and natural gas processing operations. The EPA is currently receiving public comment and recently conducted public hearings regarding the proposed rules and must take final action on them by February 28, 2012. If these or any other new laws or regulations that significantly restrict hydraulic fracturing are adopted, such laws could make it more difficult or costly for us to drill and produce from conventional or tight formations, increase our costs of compliance and doing business and make it easier for third parties opposing the hydraulic fracturing process to initiate legal proceedings. In addition, if hydraulic fracturing is regulated at the federal level, fracturing activities could become subject to additional permitting and financial assurance requirements, more stringent construction specifications, increased monitoring, reporting and recordkeeping obligations, plugging and abandonment requirements and also to attendant permitting delays and potential increases in costs. Such legislative changes could cause us to incur substantial compliance costs, and compliance or the consequences of failure to comply by us could have a material adverse effect on our business, financial condition and results of operations. At this time, it is not possible to estimate the potential impact on our business that may arise if federal or state legislation governing hydraulic fracturing is enacted into law.

***Our hedging transactions expose us to counterparty credit risk.***

Our hedging transactions expose us to risk of financial loss if a counterparty fails to perform under a derivative contract. Disruptions in the financial markets could lead to sudden changes in a counterparty s liquidity, which could impair its ability to perform under the terms of the derivative contract. We are unable to predict sudden changes in a counterparty s creditworthiness or ability to perform under contracts with us. Even if we do accurately predict sudden changes, our ability to mitigate that risk may be limited depending upon market conditions.

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***Our estimated reserves and future production rates are based on many assumptions that may prove to be inaccurate. Any material inaccuracies in these reserve estimates or underlying assumptions will materially affect the quantities and present value of our estimated reserves.***

Numerous uncertainties are inherent in estimating quantities of oil and natural gas reserves and future production. It is not possible to measure underground accumulations of oil or natural gas in an exact way. Oil and natural gas reserve engineering is complex, requiring subjective estimates of underground accumulations of oil and natural gas and assumptions concerning future oil and natural gas prices, future production levels and operating and development costs. In estimating our level of oil and natural gas reserves, we and our independent reserve engineers make certain assumptions that may prove to be incorrect, including assumptions relating to:

- the level of oil, natural gas and NGL prices;
- future production levels;
- capital expenditures;
- operating and development costs;
- the effects of regulation;
- the accuracy and reliability of the underlying engineering and geologic data; and
- the availability of funds.

If these assumptions prove to be incorrect, our estimates of our reserves, the economically recoverable quantities of oil and natural gas attributable to any particular group of properties, the classifications of reserves based on risk of recovery and our estimates of the future net cash flows from our estimated reserves could change significantly. Moreover, the variability is likely to be higher for probable and possible reserve estimates. For example, if the prices used in our reserve report as of June 30, 2011 had been $10.00 less per barrel for oil and $1.00 less per mmbtu for natural gas, then the standardized measure of our estimated proved reserves as of that date would have decreased by approximately $17.6 million, from approximately $69.5 million to approximately $51.9 million.

Our standardized measure is calculated using unhedged oil, natural gas and NGL prices and is determined in accordance with the rules and regulations of the SEC. Over time, we may make material changes to reserve estimates to take into account changes in our assumptions and the results of actual development and production.

The reserve estimates we make for wells or fields that do not have a lengthy production history are less reliable than estimates for wells or fields with lengthy production histories. A lack of production history may contribute to inaccuracy in our estimates of proved reserves, future production rates and the timing of development expenditures.

***Prospects that we decide to drill may not yield oil or natural gas in commercially viable quantities.***

Our prospects are in various stages of evaluation. There is no way to predict with certainty in advance of drilling and testing whether any particular prospect will yield oil or natural gas in sufficient quantities to recover drilling or completion costs or to be economically viable. The use of seismic data and other technologies, and the study of producing fields in the same area, will not enable us to know conclusively before drilling whether oil or natural gas will be present or, if present, whether oil or natural gas will be present in commercially viable quantities.

Moreover, the analogies we draw from available data from other wells, more fully explored prospects or producing fields may not be applicable to our drilling prospects.

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***The present value of future net revenues from our estimated reserves is not necessarily the same as the current market value of our estimated oil and natural gas reserves.***

The present value of future net revenues from our estimated reserves is not necessarily the same as the current market value of our estimated oil and natural gas reserves. We base the estimated discounted future net cash flows from our estimated reserves on prices and costs in effect as of the date of the estimate. However, actual future net cash flows from our oil and natural gas properties also will be affected by factors such as:

- the actual prices we receive for oil, natural gas and NGLs;
- our actual operating costs in producing oil, natural gas and NGLs;
- the amount and timing of actual production;
- the amount and timing of our capital expenditures;
- the supply of and demand for oil, natural gas and NGLs; and
- changes in governmental regulations or taxation.

The timing of both our production and our incurrence of expenses in connection with the development and production of oil and natural gas properties will affect the timing of actual future net cash flows from our estimated reserves, and thus their actual present value. In addition, the 10% discount factor we use when calculating discounted future net cash flows in compliance with Accounting Standards Codification 932, Extractive Activities Oil and Natural Gas, may not be the most appropriate discount factor based on interest rates in effect from time to time and risks associated with us or the oil and natural gas industry in general.

***We may experience a financial loss if SOG is unable to sell a significant portion of our oil and natural gas production.***

Under our services agreement, SOG will sell our oil, natural gas and NGL production on our behalf. SOG s ability to sell our production depends upon market conditions and the demand for oil, natural gas and NGLs from SOG s customers.

In recent years, a number of energy marketing and trading companies have discontinued their marketing and trading operations, which has significantly reduced the number of potential purchasers for our production. This reduction in potential customers has reduced overall market liquidity. If any one or more of our significant customers reduces the volume of oil and natural gas production it purchases and SOG is unable to sell those volumes to other customers, then the volume of our production that SOG sells on our behalf could be reduced, which could have an adverse affect on our business, financial condition and results of operations.

In addition, a failure by any of these companies, or any purchasers of our production, to perform their payment obligations to us could have a material adverse effect on our business, financial condition and results of operations. To the extent that purchasers of our production rely on access to the debt or equity markets to fund their operations, there could be an increased risk that those purchasers could default in their contractual obligations to us. If for any reason we were to determine that it was probable that some or all of the accounts receivable from any one or more of the purchasers of our production were uncollectible, we would recognize a charge to our earnings in that period for the probable loss and could suffer a material reduction in our liquidity.

***Lower oil and natural gas prices may cause us to record ceiling limitation impairments, which would reduce our stockholders equity.***

We use the full-cost method of accounting and accordingly, we capitalize all costs associated with the acquisition, exploration and development of oil and natural gas properties, including unproved and unevaluated property costs. Under full cost accounting rules, the net capitalized cost of oil and natural gas properties may not exceed a ceiling limit that is based upon the present value of estimated future net revenues from net proved

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reserves, discounted at 10%, plus the lower of the cost or fair market value of unproved properties and other adjustments as required by Regulation S-X under the Securities Act. If net capitalized costs of oil and natural gas properties exceed the ceiling limit, we must charge the amount of the excess to earnings. This is called a ceiling limitation impairment. The risk that we will experience a ceiling limitation impairment increases when oil and natural gas prices are depressed, if we have substantial downward revisions in estimated net proved reserves or if estimates of future development costs increase significantly. No assurance can be given that we will not experience a ceiling limitation impairment in future periods.

***Our identified drilling location inventories are scheduled out over several years, making them susceptible to uncertainties that could materially alter the occurrence or timing of their drilling.***

Our management has specifically identified and scheduled drilling locations as an estimation of our future drilling activities on our existing acreage through December 2012. These identified drilling locations represent a significant part of our growth strategy. Our ability to drill and develop these locations depends on a number of uncertainties, including the availability of capital, seasonal conditions, regulatory approvals, oil and natural gas prices, costs and drilling results. Because of these uncertainties, we do not know if the numerous potential drilling locations we have identified will ever be drilled or if we will be able to produce oil or natural gas from these or any other potential drilling locations. As such, our actual drilling activities may materially differ from those presently identified, which could adversely affect our business, financial condition and results of operations.

***Any acquisitions we complete or geographic expansions we undertake will be subject to substantial risks that could have a negative impact on our business, financial condition and results of operations.***

Any acquisition involves potential risks, including, among other things:

- mistaken assumptions about estimated proved reserves, future production, revenues, capital expenditures, operating expenses and costs, including synergies;
- an inability to successfully integrate the assets or businesses we acquire;
- a decrease in our liquidity by using a significant portion of our cash and cash equivalents to finance acquisitions;
- a significant increase in our interest expense or financial leverage if we incur debt to finance acquisitions;
- the assumption of unknown liabilities, losses or costs for which we are not indemnified or for which any indemnity we receive is inadequate;
- the diversion of management s attention from other business concerns;
- mistaken assumptions about the overall cost of equity or debt;
- an inability to hire, train or retain qualified personnel to manage and operate our growing business and assets;

- facts and circumstances that could give rise to significant cash and certain non-cash charges; and

- customer or key employee losses at the acquired businesses.

Further, we may in the future expand our operations into new geographic areas with operating conditions and a regulatory environment that may not be as familiar to us as our existing project areas. As a result, we may encounter obstacles that may cause us not to achieve the expected results of any such acquisitions, and any adverse conditions, regulations or developments related to any assets acquired in new geographic areas may have a negative impact on our business, financial condition and results of operations.

Our decision to acquire a property will depend in part on the evaluation of data obtained from production reports and engineering studies, geophysical and geological analyses and seismic data and other information, the results of which are often inconclusive and subject to various interpretations. Our reviews of acquired properties are inherently incomplete because it generally is not feasible to perform an in-depth review of the individual properties involved in each acquisition, given time constraints imposed by sellers. Even a detailed review of records and properties may not necessarily reveal existing or potential problems, nor will it permit a buyer to become sufficiently familiar with the properties to assess fully their deficiencies and potential. Inspections may not always be performed on every well, and environmental problems, such as groundwater contamination, are not necessarily observable even when an inspection is undertaken.

***We may be unable to compete effectively with larger companies, which may adversely affect our ability to generate revenue.***

The oil and natural gas industry is intensely competitive with respect to acquiring prospects and properties, marketing oil and natural gas, and securing equipment and trained personnel. Many of our competitors are large independent oil and natural gas companies that possess and employ financial, technical and personnel resources substantially greater than those of the Sanchez Group. Those entities may be able to develop and acquire more properties than our financial or personnel resources permit. Our ability to acquire additional properties and to discover reserves in the future will depend on our ability to evaluate and select suitable properties and to consummate transactions in a highly competitive environment. Many of our larger competitors not only drill for and produce oil and natural gas but also carry on refining operations and market petroleum and other products on a regional, national or worldwide basis. These companies may be able to pay more for oil and natural gas properties and evaluate, bid for and purchase a greater number of properties than our financial, technical or personnel resources permit. In addition, there is substantial competition for investment capital in the oil and natural gas industry. These larger companies may have a greater ability to continue development activities during periods of low oil and natural gas prices and to absorb the burden of present and future federal, state, local and other laws and regulations. Furthermore, we may not be able to aggregate sufficient quantities of production to compete with larger companies that are able to sell greater volumes of production to intermediaries, thereby reducing the realized prices attributable to our production. Any inability to compete effectively with larger companies could have a material adverse impact on our business, financial condition and results of operations.

***Our operations are subject to operational hazards and unforeseen interruptions for which we may not be adequately insured.***

There are a variety of operating risks inherent in our wells and other operating properties and facilities, such as leaks, explosions, mechanical problems and natural disasters, all of which could cause substantial financial losses. Any of these or other similar occurrences could result in the disruption of our operations, substantial repair costs, personal injury or loss of human life, significant damage to property, environmental pollution, impairment of our operations and substantial revenue losses. The location of our wells and other operating properties and facilities near populated areas, including residential areas, commercial business centers and industrial sites, could significantly increase the level of damages resulting from these risks.

Insurance against all operational risks is not available to us. We are not fully insured against all risks, including development and completion risks that are generally not recoverable from third parties or insurance. In addition, pollution and environmental risks generally are not fully insurable. Additionally, we may elect not to obtain insurance if we believe that the cost of available insurance is excessive relative to the perceived risks presented. Losses could, therefore, occur for uninsurable or uninsured risks or in amounts in excess of existing insurance coverage. Moreover, insurance may not be available in the future at commercially reasonable costs or on commercially reasonable terms. Changes in the insurance markets due to weather, adverse economic conditions, and the aftermath of the Macondo well incident in the Gulf of Mexico have made it more difficult for us to obtain certain types of coverage. As a result, we may not be able to obtain the levels or types of insurance we would otherwise have obtained prior to these market changes, and we cannot be sure the insurance coverage

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we do obtain will not contain large deductibles or fail to cover certain hazards or cover all potential losses. Losses and liabilities from uninsured and underinsured events and delay in the payment of insurance proceeds could have a material adverse effect on our business, financial condition and results of operations.

***Our assets and operations can be adversely affected by weather and other natural phenomena.***

Our assets and operations can be adversely affected by hurricanes, floods, earthquakes, tornadoes and other natural phenomena and weather conditions, including extreme temperatures. Insurance may be inadequate, and in some instances, we may not be able to obtain insurance on commercially reasonable terms, or insurance might not be available at all. A significant disruption in operations or a significant liability for which we were not fully insured could have a material adverse effect on our business, financial condition and results of operations.

Our customers energy needs vary with weather conditions. To the extent weather conditions are affected by climate change or demand is impacted by regulations associated with climate change, customers energy use could increase or decrease depending on the duration and magnitude of the changes, leading either to increased investment or decreased revenues.

***Seasonal weather conditions and lease stipulations adversely affect our ability to conduct drilling activities in some of the areas where we operate.***

Oil and natural gas operations in some of the areas where we operate are adversely affected by seasonal weather conditions and lease stipulations designed to protect various wildlife. In certain areas on federal lands, drilling and other oil and natural gas activities can only be conducted during limited times of the year. This limits our ability to operate in those areas and can intensify competition during those times for drilling rigs, oil field equipment, services, supplies and qualified personnel, which may lead to periodic shortages. These constraints and the resulting shortages or high costs could delay our operations and materially increase our operating and capital costs.

***Our properties are located in regions which make us vulnerable to risks associated with operating in one major contiguous geographic area, including the risk and related costs of damage or business interruptions from hurricanes.***

Our properties are primarily located in the Eagle Ford Shale in South Texas, and as a result of this geographic concentration, we are disproportionately affected by any delays or interruptions in production or transportation in these areas caused by governmental regulation, transportation capacity constraints, natural disasters, regional price fluctuations and other factors. Such disturbances have in the past and will in the future have any or all of the following adverse effects on our business:

- interruptions to our operations as we suspend production in advance of an approaching storm;
- damage to our facilities and equipment, including damage that disrupts or delays our production;
- disruption to the transportation systems we rely upon to deliver our products to our customers; and
- damage to or disruption of our customers facilities that prevents us from taking delivery of our products.

Although we maintain property and casualty insurance, we cannot predict whether we will continue to be able to obtain insurance for hurricane-related damages or, if obtainable and carried, whether this insurance will be adequate to cover our losses. In addition, we expect any insurance of this nature to be subject to substantial deductibles and to provide for premium adjustments based on claims. Any future hurricane-related costs and work interruptions could adversely affect our business, financial condition and results of operations.

***Our lack of diversification will increase the risk of an investment in us.***

Our current business focus is on the oil and natural gas industry in a limited number of properties, primarily in the Eagle Ford Shale in South Texas. Larger companies have the ability to manage their risk by

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diversification. However, we currently lack diversification, in terms of both the nature and geographic scope of our business. As a result, we will likely be impacted more acutely by factors affecting our industry or the regions in which we operate than we would if our business were more diversified, increasing our risk profile.

***We cannot control activities on properties that we do not operate and are unable to control their proper operation and profitability.***

We do not operate all of the properties in which we own an ownership interest. As a result, we have limited ability to exercise influence over, and control the risks associated with, the operations of these non-operated properties. The failure of an operator of our wells to adequately perform operations, an operator s breach of the applicable agreements or an operator s failure to act in ways that are in our best interests could reduce our production, revenues and reserves. The success and timing of our drilling and development activities on properties operated by others therefore depend upon a number of factors outside of our control, including:

- the nature and timing of the operator s drilling and other activities;
- the timing and amount of required capital expenditures;
- the operator s geological and engineering expertise and financial resources;
- the approval of other participants in drilling wells; and
- the operator s selection of suitable technology.

***Our historical financial information may not be representative of the results we would have achieved as a stand-alone public company and may not be a reliable indicator of our future results.***

The historical financial information that we have included in this prospectus has been prepared on a carve-out basis from the accounts of SEP I and may not necessarily reflect what our financial position, results of operations or cash flows would have been had we been an independent, stand-alone entity during the periods presented or those that we will achieve in the future. SEP I did not account for us, and we were not operated, as a separate, stand-alone company for the historical periods presented. The costs and expenses reflected in our historical financial information include allocations of general and administrative expenses for employee, management, and administrative support provided by SOG to SEP I. These allocations were primarily based on the ratio of capital expenditures between the entities to which SOG provides services and us, and also on other factors, such as time spent on general management services and producing property activities. Although SOG will continue to provide these services to us pursuant to a services agreement and management believes such allocations are reasonable, such allocations may not be indicative of the actual expense that would have been incurred had we been an independent, stand-alone entity during the periods presented. In addition, we have not adjusted our historical financial information to reflect changes that will occur in our cost structure and operations as a result of our transition to becoming a stand-alone public company, including potential increased costs associated with reduced economies of scale and increased costs associated with the SEC reporting and the New York Stock Exchange, or the NYSE, requirements. Therefore, our historical financial information may not necessarily be indicative of what our financial position, results of operations or cash flows will be in the future. For additional information, see Selected Financial Data and Management s Discussion and Analysis of Financial Condition and Results of Operations, and our financial statements and related notes included elsewhere in this prospectus.

***We are subject to complex federal, state, local and other laws and regulations that could adversely affect the cost, manner or feasibility of conducting our operations.***

Our oil and natural gas development and production operations are subject to complex and stringent laws and regulations. To conduct our operations in compliance with these laws and regulations, we must obtain and maintain numerous permits, approvals and certificates from various federal, state and local governmental

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authorities. We may incur substantial costs in order to maintain compliance with these existing laws and regulations. In addition, our costs of compliance may increase if existing laws and regulations are revised or reinterpreted, or if new laws and regulations become applicable to our operations.

Our business is subject to federal, state and local laws and regulations as interpreted and enforced by governmental authorities possessing jurisdiction over various aspects of the exploration for, and production and processing of, oil and natural gas. Failure to comply with such laws and regulations, as interpreted and enforced, could have a material adverse effect on our business, financial condition and results of operations. Please read Business and Properties Environmental Matters and Regulation and Business and Properties Other Regulation of the Oil and Natural Gas Industry for a description of the laws and regulations that affect us.

***Climate change legislation or regulations restricting emissions of greenhouse gases could result in increased operating costs and reduced demand for the oil and natural gas that we produce.***

On April 2, 2007, the U.S. Supreme Court ruled, in Massachusetts, et al. v. EPA, that the federal Clean Air Act definition of pollutant includes carbon dioxide and other greenhouse gases, or GHGs, and, therefore, the EPA has the authority to regulate carbon dioxide emissions from automobiles. Thereafter, on December 15, 2009, the EPA published its findings that emissions of carbon dioxide, methane, and other GHGs present an endangerment to public health and the environment because emissions of such gases are, according to the EPA, contributing to the warming of the earth s atmosphere and other climate changes. These findings allow the EPA to adopt and implement regulations that restrict emissions of GHGs under existing provisions of the federal Clean Air Act. The EPA subsequently adopted two sets of regulations under the existing Clean Air Act, one that requires a reduction in emissions of GHGs from motor vehicles and another that requires certain stationary sources to obtain permits and employ technologies to reduce GHG emissions. The EPA published the motor vehicle final rule in May 2010 and it became effective January 2011 and applies to vehicles manufactured in model years 2012-2016. The EPA adopted the stationary source rule in May 2010, and it also became effective January 2011, applying first to the largest emitters of GHGs and providing the potential for application to smaller emitters in later years. Both rules remain the subject of several lawsuits filed by industry groups in the U.S. Court of Appeals for the District of Columbia Circuit. Additionally, the EPA requires reporting of GHG emissions from certain emission sources. In October 2009, the EPA published a final rule requiring the reporting of GHG emissions from specified large GHG emission sources in the U.S., including natural gas liquids fractionators and local natural gas/distribution companies, beginning in 2011 for emissions occurring in 2010. Furthermore, in November 2010, the EPA expanded its existing GHG reporting rule to include onshore oil and natural gas production, processing, transmission, storage, and distribution facilities. The final rule, which may be applicable to many of our facilities, will require reporting of GHG emissions from such facilities on an annual basis, with reporting beginning in 2012 for emissions occurring in 2011. The EPA also plans to implement GHG emissions standards for power plants in May 2012 and for refineries in November 2012.

In June 2009, the U.S. House of Representatives passed the American Clean Energy and Security, or ACES, Act that, among other things, would have established a cap-and-trade system to regulate GHG emissions and would have required an 80% reduction in GHG emissions from sources within the United States between 2012 and 2050. The ACES Act did not pass the Senate, however, and so was not enacted by the 111th Congress. The United States Congress is likely to consider again a climate change bill in the future. In addition, almost one-half of the states have already taken legal measures to reduce emissions of GHGs, primarily through the planned development of GHG emission inventories and/or regional GHG cap and trade programs. Most of these cap and trade programs work by requiring either major sources of emissions or major producers of fuels to acquire and surrender emission allowances, with the number of allowances available for purchase reduced each year until the overall GHG emission reduction goal is achieved. As the number of GHG emission allowances declines each year, the cost or value of allowances is expected to escalate significantly. Furthermore, some states have enacted renewable portfolio standards, which require utilities to purchase a certain percentage of their energy from renewable fuel sources. The adoption of any legislation or regulations that require reporting of GHGs or otherwise limit emissions of GHGs from our equipment and operations could require us to incur increased operating costs, such as costs to monitor and report GHG emissions, purchase and operate emissions

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control systems to reduce emissions of GHGs associated with our operations, acquire emissions allowances or comply with new regulatory requirements. Any GHG emissions legislation or regulatory programs applicable to power plants or refineries could also increase the cost of consuming, and thus could adversely affect demand for the oil and natural gas that we produce. Consequently, legislation and regulatory programs to reduce GHG emissions could have an adverse effect on our business, financial condition and results of operations. Please read Business and Properties Environmental Matters and Regulation.

***Our operations are subject to environmental and operational safety laws and regulations that may expose us to significant costs and liabilities.***

We may incur significant delays, costs and liabilities as a result of stringent and complex environmental, health and safety requirements applicable to our oil and natural gas development and production operations. These laws and regulations may impose numerous obligations applicable to our operations, including that they may (i) require the acquisition of permits to conduct exploration, drilling and production operations; (ii) restrict the types, quantities and concentration of various substances that can be released into the environment or injected into formations in connection with oil and natural gas drilling, production and transportation activities; (iii) govern the sourcing and disposal of water used in the drilling and completion process; (iv) limit or prohibit drilling activities on certain lands lying within wilderness, wetlands and other protected areas; (v) require remedial measures to mitigate pollution from former and ongoing operations, such as requirements to close pits and plug abandoned wells; (vi) result in the suspension or revocation of necessary permits, licenses and authorizations; (vii) impose substantial liabilities for pollution resulting from drilling and production operations; and (viii) require that additional pollution controls be installed. Numerous governmental authorities, such as the EPA and analogous state agencies, have the power to enforce compliance with these laws and regulations and the permits issued under them, often requiring difficult and costly compliance or corrective actions. Failure to comply with these laws and regulations may result in the assessment of sanctions, including administrative, civil or criminal penalties, the imposition of investigatory or remedial obligations, the suspension or revocation of necessary permits, licenses and authorizations, the requirement that additional pollution controls be installed and, in some instances, the issuance of orders limiting or prohibiting some or all of our operations. In addition, we may experience delays in obtaining or be unable to obtain required permits, which may delay or interrupt our operations and limit our growth and revenue. These laws and regulations are complex, change frequently and have tended to become increasingly stringent over time.

There is inherent risk of incurring significant environmental costs and liabilities in the performance of our operations due to our handling of petroleum hydrocarbons and wastes, because of air emissions and wastewater discharges related to our operations, and as a result of historical industry operations and waste disposal practices. Under certain environmental laws and regulations, we could be subject to joint and several strict liability for the removal or remediation of previously released materials or property contamination regardless of whether we were responsible for the release or contamination or the operations were in compliance with all applicable laws at the time those actions were taken. Private parties, including the owners of properties upon which our wells are drilled and facilities where our petroleum hydrocarbons or wastes are taken for reclamation or disposal, also may have the right to pursue legal actions to enforce compliance as well as to seek damages for non-compliance with environmental laws and regulations or for personal injury or property or natural resource damages. In addition, the risk of accidental spills or releases could expose us to significant liabilities that could have a material adverse effect on our business, financial condition and results of operations. Changes in environmental laws and regulations occur frequently, and any changes that result in more stringent or costly waste control, handling, storage, transport, disposal or cleanup requirements could require us to make significant expenditures to attain and maintain compliance and may otherwise have a material adverse effect on our competitive position, business, financial condition and results of operations. We may not be able to recover some or any of these costs from insurance. Please read Business and Properties Environmental Matters and Regulation for more information.

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***The third parties on whom we rely for gathering and transportation services are subject to complex federal, state and other laws that could adversely affect the cost, manner or feasibility of conducting our business.***

The operations of the third parties on whom we rely for gathering and transportation services are subject to complex and stringent laws and regulations that require obtaining and maintaining numerous permits, approvals and certifications from various federal, state and local government authorities. These third parties may incur substantial costs in order to comply with existing laws and regulations. If existing laws and regulations governing such third-party services are revised or reinterpreted, or if new laws and regulations become applicable to their operations, these changes may affect the costs that we pay for such services. Similarly, a failure to comply with such laws and regulations by the third parties on whom we rely could have a material adverse effect on our business, financial condition and results of operations. Please read Business and Properties Environmental Matters and Regulation and Business and Properties Other Regulation of the Oil and Natural Gas Industry for a description of the laws and regulations that affect the third parties on whom we rely.

***The recent adoption of derivatives legislation by the U.S. Congress could have an adverse effect on our ability to use derivative contracts to reduce the effect of commodity price, interest rate and other risks associated with our business.***

The U.S. Congress recently adopted comprehensive financial reform legislation that establishes federal oversight and regulation of the over-the-counter derivatives market and entities that participate in that market. The Commodity Futures Trading Commission, or the CFTC, has also proposed regulations to set position limits for certain futures and option contracts in the major energy markets, although it is not possible at this time to predict whether or when the CFTC will adopt those rules or include comparable provisions in its rulemaking under the new legislation. The financial reform legislation may require us to comply with margin requirements and with certain clearing and trade-execution requirements, although the application of those provisions to us is uncertain at this time. The financial reform legislation may also require the counterparties to our derivative contracts to spin off some of their derivatives contracts to a separate entity, which may not be as creditworthy as the current counterparty. The new legislation and any new regulations could significantly increase the cost of derivative contracts (including through requirements to post collateral), materially alter the terms of derivative contracts, reduce the availability of derivatives to protect against risks we encounter, reduce our ability to monetize or restructure our existing derivative contracts, and increase our exposure to less creditworthy counterparties. If we reduce our use of derivatives as a result of the legislation and regulations, our results of operations may become more volatile and our cash flows may be less predictable, which could adversely affect our ability to plan for and fund capital expenditures. Finally, the legislation was intended, in part, to reduce the volatility of oil and natural gas prices, which some legislators attributed to speculative trading in derivatives and commodity contracts related to oil and natural gas. Our revenues could therefore be adversely affected if a consequence of the legislation and regulations is to lower commodity prices. Any of these consequences could have a material adverse effect on our business, financial condition and results of operations.

***Our ability to produce oil and natural gas could be impaired if we are unable to acquire adequate supplies of water for our drilling and completion operations or are unable to dispose of the water we use at a reasonable cost and within applicable environmental rules.***

Our inability to locate sufficient amounts of water, or dispose of or recycle water used in our exploration and production operations, could adversely impact our operations. Moreover, the imposition of new environmental initiatives and regulations could include restrictions on our ability to conduct certain operations such as hydraulic fracturing or disposal of waste, including, but not limited to, produced water, drilling fluids and other wastes associated with the exploration, development or production of oil and natural gas. The Clean Water Act imposes restrictions and strict controls regarding the discharge of produced waters and other oil and natural gas waste into navigable waters. Permits must be obtained to discharge pollutants to waters and to conduct construction activities in waters and wetlands. The Clean Water Act and similar state laws provide for civil, criminal and administrative penalties for any unauthorized discharges of pollutants and unauthorized discharges of reportable quantities of oil and other hazardous substances. Many state discharge regulations, and the Federal National Pollutant Discharge Elimination System general permits issued by the EPA, prohibit the discharge of

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produced water and sand, drilling fluids, drill cuttings and certain other substances related to the oil and natural gas industry into coastal waters. The EPA has also adopted regulations requiring certain oil and natural gas exploration and production facilities to obtain permits for storm water discharges. Compliance with environmental regulations and permit requirements governing the withdrawal, storage and use of surface water or groundwater necessary for hydraulic fracturing of wells may increase our operating costs and cause delays, interruptions or termination of our operations, the extent of which cannot be predicted.

***Because we are a relatively small company, the requirements of being a public company, including compliance with the reporting requirements of the Securities Exchange Act of 1934, as amended, and the requirements of the Sarbanes-Oxley Act may strain our resources, increase our costs and distract management, and we may be unable to comply with these requirements in a timely or cost-effective manner.***

We have no history operating as a publicly-traded company. As a public company with listed equity securities, we will need to comply with new laws, regulations and requirements, including the reporting obligations of the Securities Exchange Act of 1934, as amended, or the Exchange Act, certain corporate governance provisions of the Sarbanes-Oxley Act of 2002, related regulations of the SEC and the requirements of the NYSE with which we are not required to comply as a private company. Complying with these statutes, regulations and requirements will occupy a significant amount of time from our board of directors and management and will significantly increase our legal and financial compliance costs and make such compliance more time-consuming and costly. We will need to:

- institute a more comprehensive compliance function;
- design, establish, evaluate and maintain a system of internal controls over financial reporting in compliance with the requirements of Section 404 of the Sarbanes-Oxley Act of 2002 and the related rules and regulations of the SEC and the Public Company Accounting Oversight Board;
- comply with rules promulgated by the NYSE;
- prepare and distribute periodic public reports in compliance with our obligations under the federal securities laws;
- establish new internal policies, such as those relating to disclosure controls and procedures and insider trading;
- involve and retain to a greater degree outside counsel and accountants in the above activities; and
- establish an investor relations function.

In addition, we also expect that being a public company subject to these rules and regulations will make it more difficult and expensive for us to obtain director and officer liability insurance and we may be required to accept greater coverage than we desire or to incur substantial costs to obtain coverage. These factors could also make it more difficult for us to attract and retain qualified executive officers and qualified members to serve on our board of directors, particularly the audit committee of the board of directors.

We are not currently required to comply with the SEC s rules implementing Section 404 of the Sarbanes-Oxley Act of 2002 and are therefore not required to make a formal assessment of the effectiveness of our internal control over financial reporting for that purpose. Upon becoming a public company, we will be required to comply with the SEC s rules implementing Section 302 of the Sarbanes-Oxley Act of 2002, which will require our management to certify financial and other information in our quarterly and annual reports and provide an annual management report on the effectiveness of our internal control over financial reporting. We will not be required to make our first assessment of our internal control over financial reporting until the year following our first annual report required to be filed with the SEC. To comply with the requirements of being a public company, we will need to upgrade our systems, including information technology, implement additional

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financial and management controls, reporting systems and procedures and hire additional accounting, finance and legal staff.

Our efforts to develop and maintain our internal controls may not be successful, and we may be unable to maintain effective controls over our financial processes and reporting in the future and comply with the certification and reporting obligations under Sections 302 and 404 of the Sarbanes-Oxley Act of 2002. Further, our remediation efforts may not enable us to remedy or avoid material weaknesses or significant deficiencies in the future. Any failure to remediate material weaknesses or significant deficiencies and to develop or maintain effective controls, or any difficulties encountered in our implementation or improvement of our internal controls over financial reporting could result in material misstatements that are not prevented or detected on a timely basis, which could potentially subject us to sanctions or investigations by the SEC, the NYSE or other regulatory authorities. Ineffective internal controls could also cause investors to lose confidence in our reported financial information.

***We may incur more taxes and certain of our projects may become uneconomic if certain federal income tax deductions currently available with respect to oil and natural gas exploration and production are eliminated as a result of future legislation.***

The President s proposed budget for fiscal year 2012 and his proposed American Jobs Act of 2011 contain proposals to eliminate certain key U.S. federal income tax preferences currently available to oil and natural gas exploration and production companies. These changes include, but are not limited to (i) the repeal of the percentage depletion allowance for oil and natural gas properties, (ii) the elimination of current deductions for intangible drilling and development costs, (iii) the elimination of the deduction for certain U.S. production activities and (iv) an extension of the amortization period for certain geological and geophysical expenditures. It is unclear whether any of the foregoing changes will actually be enacted or how soon any such changes could become effective. The passage of any legislation as a result of the budget proposal or any other similar change in U.S. federal income tax law could eliminate and/or defer certain tax deductions that are currently available with respect to oil and natural gas exploration and production. Any such change could materially adversely affect our business, financial condition and results of operations by increasing the after-tax costs we incur which would in turn make it uneconomic to drill some locations if commodity prices are not sufficiently high, resulting in lower revenues and decreases in production and reserves.

***Failure of our service providers or disruptions to our outsourcing relationships might negatively impact our ability to conduct our business.***

We rely on SOG for certain services necessary for us to be able to conduct our business. SOG may outsource some or all of these services to third parties, and a failure of all or part of SOG s relationships with its outsourcing providers could lead to delays in or interruptions of these services. Our reliance on SOG and others as service providers and on SOG s outsourcing relationships, and our limited ability to control certain costs, could have a material adverse effect on our business, financial condition and results of operations.

Some studies indicate a high failure rate of outsourcing relationships. A deterioration in the timeliness or quality of the services performed by the outsourcing providers or a failure of all or part of these relationships could lead to loss of institutional knowledge and interruption of services necessary for us to be able to conduct our business. The expiration of such agreements or the transition of services between providers could lead to similar losses of institutional knowledge or disruptions.

***Acts of terrorism could have a material adverse effect on our business, financial condition and results of operations.***

Our assets and the assets of our customers and others may be targets of terrorist activities that could disrupt our business or cause significant harm to our operations, such as full or partial disruption to the ability to produce, process, transport or distribute oil, natural gas or NGLs. Acts of terrorism as well as events occurring in response to or in connection with acts of terrorism could cause environmental repercussions that could result in a significant decrease in revenues or significant reconstruction or remediation costs.

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***Our use of 2D and 3D seismic data is subject to interpretation and may not accurately identify the presence of oil and natural gas, which could adversely affect the results of our drilling operations.***

Even when properly used and interpreted, 2D and 3D seismic data and visualization techniques are only tools used to assist geoscientists in identifying subsurface structures and hydrocarbon indicators and do not enable the interpreter to know whether hydrocarbons are, in fact, present in those structures. In addition, the use of 3D seismic and other advanced technologies requires greater pre-drilling expenditures than traditional drilling strategies, and we could incur losses as a result of such expenditures. As a result, our drilling activities may not be successful or economical and our overall drilling success rate or our drilling success rate for activities in a particular area could decline.

**Risks Related to Our Relationships with Members of the Sanchez Group**

***As long as we are controlled by SEP I, your ability to influence the outcome of matters requiring stockholder approval will be limited.***

After the completion of this offering, SEP I will own % of our outstanding common stock. As long as SEP I has voting control of our company, SEP I will have the ability to take many stockholder actions, including the election or removal of directors, irrespective of the vote of, and without prior notice to, any other stockholder. As a result, SEP I will have the ability to influence or control all matters affecting us, including:

- the composition of our board of directors and, through our board of directors, decision-making with respect to our business direction and policies, including the appointment and removal of our officers;
- any determinations with respect to acquisitions of businesses, mergers or other business combinations;
- our acquisition or disposition of assets; and
- our capital structure.

SEP I s interests may not be the same as, or may conflict with, the interests of our other stockholders. As a result, actions that SEP I takes with respect to us, as our controlling stockholder, may not be favorable to us. In addition, this voting control may discourage transactions involving a change of control of our company, including transactions in which you, as a holder of our common stock, might otherwise receive a premium for your shares over the then-current market price. Furthermore, SEP I is not prohibited from selling a controlling interest in our company to a third party without your approval or without providing for a purchase of your shares.

***We may have potential business conflicts of interest with the Sanchez Group regarding our past and ongoing relationships, and because of SEP I s controlling ownership in us, the resolution of these conflicts may not be favorable to us.***

Conflicts of interest may arise between members of the Sanchez Group and us in a number of areas relating to our past and ongoing relationships, including:

- labor, tax, employee benefit, indemnification and other matters arising under agreements with SOG;
- employee recruiting and retention;

- sales or distributions by SEP I of all or any portion of its ownership interest in us, which could be to one of our competitors; and

- business opportunities that may be attractive to both members of the Sanchez Group and us.

We may not be able to resolve any potential conflicts, and, even if we do so, the resolution may be less favorable to us than if we were dealing with an unaffiliated party.

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Finally, in connection with this offering, we will enter into several agreements with members of the Sanchez Group. These agreements will be made in the context of a parent-subsidiary relationship. The terms of these agreements may be more or less favorable to us than if they had been negotiated with unaffiliated third parties. While we are controlled by SEP I, SEP I may seek to cause us to amend these agreements on terms that may be less favorable to us than the original terms of the agreement.

***Pursuant to the terms of the amended and restated certificate of incorporation that we will adopt in connection with the closing of this offering, SEP I and its affiliates will not be required to offer corporate opportunities to us, and our directors and officers may be permitted to offer certain corporate opportunities to SEP I or its affiliates before us.***

At the completion of this offering, our board of directors will include persons who are also directors and/or officers of members of the Sanchez Group. Our amended and restated certificate of incorporation that we will adopt in connection with the closing of this offering will provide that:

- SEP I and its affiliates are free to compete with us in any activity or line of business;

- we do not have any interest or expectancy in any business opportunity, transaction, or other matter in which SEP I or its affiliates engage or seek to engage merely because we engage in the same or similar lines of business;

- to the fullest extent permitted by law, SEP I and its affiliates will have no duty to communicate their knowledge of, or offer, any potential business opportunity, transaction, or other matter to us, and SEP I and its affiliates are free to pursue or acquire such business opportunity, transaction, or other matter for themselves or direct the business opportunity, transaction, or other matter to its affiliates; and

- if any director or officer of any member of the Sanchez Group who is also one of our officers or directors becomes aware of a potential business opportunity, transaction, or other matter (other than one expressly offered to that director or officer in writing solely in his or her capacity as our director or officer), that director or officer will have no duty to communicate or offer that business opportunity to us, and will be permitted to communicate or offer that business opportunity to such member of the Sanchez Group (or its affiliates) and that director or officer will not, to the fullest extent permitted by law, be deemed to have (1) breached or acted in a manner inconsistent with or opposed to his or her fiduciary or other duties to us regarding the business opportunity or (2) acted in bad faith or in a manner inconsistent with our best interests or those of our stockholders.

***Following this offering, we will continue to depend on SOG to provide us with certain services for our business. The services that SOG will provide to us following the completion of this offering may not be sufficient to meet our needs, and we may have difficulty finding replacement services or be required to pay increased costs to replace these services after our agreements with SOG expire.***

Certain services required by us for the operation of our business are currently provided by SOG, including general and administrative services, geological, geophysical and reserve engineering, lease and land administration, marketing, accounting, operational services, information technology services, compliance, insurance maintenance and management of outside professionals. Prior to the completion of this offering, we will enter into a services agreement with SOG. The services provided under the services agreement will commence on the date this offering is completed and terminate five years thereafter. The term will automatically extend for additional 12-month periods and will be terminable by either party at any time upon 180 days written notice. As a result, we will depend on SOG for services following this offering. See Certain Relationships and Related Party Transactions Agreements Governing the Transaction Services and Licensing Agreements. While these services are being provided to us by SOG, our operational flexibility to modify or implement changes with respect to such services or the amounts we pay for them will be limited. After the expiration or termination of this agreement, we may not be able to replace these services or enter into appropriate third-party agreements on terms and conditions, including cost, comparable to those that we will receive from SOG under our agreements with SOG.

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***We may assume unknown liabilities in connection with this offering and in many instances may have no recourse against SEP I or other third parties for losses occurring after this offering.***

As part of our acquisition of 100% of the limited liability company interests of SEP Holdings III, the properties we acquire from SEP I will be subject to all existing liabilities, some of which may be unknown at the closing of this offering. Unknown liabilities might include liabilities for cleanup or remediation of undisclosed or unknown environmental conditions, claims that have not been asserted or threatened prior to completion of this offering and tax liabilities. In addition, we will acquire the properties from SEP I on an as is basis and we will have limited or no recourse after closing against the Sanchez Group for liabilities associated with the properties acquired from SEP I for breaches of representations or warranties by SEP I or for title defects, and we cannot assure you that we have identified all areas of existing or potential exposure. Further, to the extent we will have indemnification rights or a claim for damages for such liabilities, we cannot assure you that the indemnifying party will be able to fulfill its contractual obligations or otherwise satisfy any claims we may have at law or equity.

***We may lose our rights to the Sanchez Group s technological database, including its 3D and 2D seismic data, under certain circumstances.***

In connection with a services agreement that we will enter into with SOG at the closing of this offering, we will have access to the unrestricted, proprietary portions of the technological database owned and maintained by the Sanchez Group and related to our properties, and SOG will otherwise be required to interpret and use the database, to the extent relating to our properties, for our benefit under that agreement. See Certain Relationships and Related Party Transactions Agreements Governing the Transaction Services and Licensing Agreements. This database includes the 2D and 3D seismic data used for our exploration and development projects as well as the well logs, LAS files, scanned well documents and other well documents and software that are necessary for our daily operations. This information is critical for the operation and expansion of our business. Under certain circumstances, including if SOG provides at least 180 days advance written notice of its desire to terminate the services agreement, the agreement will terminate and we will lose our rights to this technological database unless members of the Sanchez Group permit us to retain some or all of these rights, which they may decline to do in their sole discretion. In such event, we are unlikely to be able to obtain rights to similar information under substantially similar commercial terms or to continue our business operations as proposed and our liquidity, business, financial condition and results of operations will be materially and adversely affected and it could delay or prevent an acquisition of us.

**Risks Relating to This Offering**

***An active and liquid trading market for our common stock may not develop.***

Prior to this offering, our common stock was not traded on any market. An active and liquid trading market for our common stock may not develop or be maintained after this offering. Liquid and active trading markets usually result in less price volatility and more efficiency in carrying out investors purchase and sale orders. The market price of our common stock could vary significantly as a result of a number of factors, some of which are beyond our control. In the event of a drop in the market price of our common stock, you could lose a substantial part or all of your investment in our common stock. The initial public offering price will be negotiated between us and the representative of the underwriters and may not be indicative of the market price of our common stock after this offering. Consequently, you may not be able to sell shares of our common stock at prices equal to or greater than the price paid by you in the offering.

***Our stock price may be volatile, and purchasers of our common stock could incur substantial losses.***

Our stock price may be volatile. The stock market in general has experienced extreme volatility that has often been unrelated to the operating performance of particular companies. As a result of this volatility, investors may not be able to sell their common stock at or above the initial public offering price. The market price for our common stock may be influenced by many factors, including, but not limited to:

- the price of oil and natural gas;

- the success of our exploration and development operations, and the marketing of any oil we produce;
- regulatory developments in the United States and foreign countries where we operate;
- the recruitment or departure of key personnel;
- quarterly or annual variations in our financial results or those of companies that are perceived to be similar to us;
- market conditions in the industries in which we compete and issuance of new or changed securities;
- analysts reports or recommendations;
- the failure of securities analysts to cover our common stock after this offering or changes in financial estimates by analysts;
- the inability to meet the financial estimates of analysts who follow our common stock;
- our issuance of any additional securities;
- investor perception of our company and of the industry in which we compete; and
- general economic, political and market conditions.

***A substantial portion of our total outstanding shares may be sold into the market. This could cause the market price of our common stock to drop significantly, even if our business is doing well.***

All of the shares being sold in this offering will be freely tradable without restrictions or further registration under the federal securities laws, unless purchased by our affiliates as that term is defined in Rule 144 under the Securities Act. The remaining shares of common stock outstanding upon the closing of this offering will be held initially by SEP I and will be restricted securities as defined in Rule 144 under the Securities Act. Restricted securities may be sold in the U.S. public market only if registered or if they qualify for an exemption from registration, including by reason of Rules 144 or 701 under the Securities Act. All of our restricted shares will be eligible for sale in the public market beginning in 2012, subject in certain circumstances to the volume, manner of sale and other limitations under Rule 144, and also the lock-up agreements described under Underwriting in this prospectus. In addition, SEP I and its transferees will have the right to require us to register the resale of their shares. See Certain Relationships and Related Party Transactions Agreements Governing the Transactions Registration Rights Agreement. Additionally, we intend to register all shares of our common stock that we may issue under our employee benefit plans. Once we register these shares, they can be freely sold in the public market. Sales of a substantial number of shares of our common stock, or the perception in the market that the holders of a large number of shares intend to sell shares, could reduce the market price of our common stock.

***If you purchase shares of our common stock in this offering, you will suffer immediate and substantial dilution of your investment.***

The initial public offering price of our common stock is substantially higher than the net tangible book value per share of our common stock. Therefore, if you purchase shares of our common stock in this offering, your interest will be diluted immediately to the extent of the difference between the initial public offering price per share of our common stock and the net tangible book value per share of our common stock after this offering. See Dilution.

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***We have broad discretion in the use of our net proceeds from this offering and may not use them effectively.***

Our management will have broad discretion in the application of the net proceeds from this offering and could spend the proceeds in ways that do not improve our operating results or enhance the value of our common stock. Our stockholders may not agree with the manner in which our management chooses to allocate and spend the net proceeds. The failure by our management to apply these funds effectively could result in financial losses that could have a material adverse effect on our business and cause the price of our common stock to decline. Pending their use, we may invest our net proceeds from this offering in a manner that does not produce income or that loses value. See Use of Proceeds in this prospectus.

***We are subject to anti-takeover provisions in our amended and restated certificate of incorporation and amended and restated bylaws and under Delaware law that could delay or prevent an acquisition of our company, even if the acquisition would be beneficial to our stockholders.***

Provisions in our amended and restated certificate of incorporation and amended and restated bylaws may delay or prevent an acquisition of us. These provisions may also frustrate or prevent any attempts by our stockholders to replace or remove our current management by making it more difficult for stockholders to replace members of our board of directors, who are responsible for appointing the members of our management team. Furthermore, because we are incorporated in Delaware, we are governed by the provisions of Section 203 of the Delaware General Corporation Law, which prohibits, with some exceptions, stockholders owning in excess of 15% of our outstanding voting stock from merging or combining with us. Finally, our amended and restated bylaws will establish advance notice requirements for nominations for election to our board of directors and for proposing matters that can be acted upon at stockholder meetings. Although we believe these provisions together provide an opportunity to receive higher bids by requiring potential acquirers to negotiate with our board of directors, they would apply even if an offer to acquire us may be considered beneficial by some stockholders. See Description of Capital Stock Anti-Takeover Effects of Provisions of Our Amended and Restated Certificate of Incorporation, our Amended and Restated Bylaws and Delaware Law.

***We will be a controlled company within the meaning of the NYSE rules and, as a result, will qualify for, and intend to rely on, exemptions from certain corporate governance requirements that provide protection to stockholders of other companies.***

After the completion of this offering, SEP I will own more than 50% of the voting power of all then outstanding shares of our capital stock entitled to vote generally in the election of directors, and we will be a controlled company under the NYSE corporate governance standards. As a controlled company, we intend to rely on certain exemptions from the NYSE standards that will enable us not to comply with certain NYSE corporate governance requirements, including the requirements that:

- a majority of our board of directors consists of independent directors;
- we have a nominating and governance committee that is composed entirely of independent directors, with a written charter addressing the committee s purpose and responsibilities;
- we have a compensation committee that is composed entirely of independent directors, with a written charter addressing the committee s purpose and responsibilities; and
- we conduct an annual performance evaluation of the nominating and governance committee and compensation committee.

We intend to rely on some or all of these exemptions, and, as a result, you will not have the same protection afforded to stockholders of companies that are subject to all of the NYSE corporate governance requirements.

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**FORWARD-LOOKING STATEMENTS**

This prospectus contains forward-looking statements that are subject to a number of risks and uncertainties, many of which are beyond our control, which may include statements about our:

- business strategies;
- ability to replace the reserves we produce through drilling and property acquisitions;
- drilling locations;
- oil and natural gas reserves;
- technology;
- realized oil and natural gas prices;
- production volumes;
- lease operating expenses;
- general and administrative expenses;
- future operating results;
- cash flows and liquidity;
- availability of drilling and production equipment;
- availability of oil field labor;
- capital expenditures;

availability and terms of capital;

marketing of oil and natural gas;

general economic conditions;

competition in the oil and natural gas industry;

effectiveness of risk management activities;

environmental liabilities;

counterparty credit risk;

governmental regulation and taxation;

developments in oil-producing and natural-gas producing countries; and

plans, objectives, expectations and intentions.

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These types of statements, other than statements of historical fact included in this prospectus, are forward-looking statements. These forward-looking statements may be found in Prospectus Summary, Risk Factors, Management s Discussion and Analysis of Financial Condition and Results of Operations, Business and Properties and other sections of this prospectus. In some cases, you can identify forward-looking statements by terminology such as may, will, could, should, expect, plan, project, intend, anticipate, believe, estimate, pr target, continue, the negative of such terms or other comparable terminology.

The forward-looking statements contained in this prospectus are largely based on our expectations, which reflect estimates and assumptions made by our management. These estimates and assumptions reflect our best judgment based on currently known market conditions and other factors. Although we believe such estimates and assumptions to be reasonable, they are inherently uncertain and involve a number of risks and uncertainties that are beyond our control. In addition, management s assumptions about future events may prove to be inaccurate. All readers are cautioned that the forward-looking statements contained in this prospectus are not guarantees of future performance, and we cannot assure any reader that such statements will be realized or that the forward-looking events and circumstances will occur. Actual results may differ materially from those anticipated or implied in the forward-looking statements due to factors described in Risk Factors and elsewhere in this prospectus. All forward-looking statements speak only as of the date of this prospectus. We do not intend to update or revise any forward-looking statements as a result of new information, future events or otherwise. These cautionary statements qualify all forward-looking statements attributable to us or persons acting on our behalf.

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## USE OF PROCEEDS

We will receive net proceeds of approximately $ million from the sale of the common stock offered by us, assuming an initial public offering price of $ per share (the midpoint of the price range set forth on the cover page of this prospectus) and after deducting estimated expenses and underwriting discounts and commissions of approximately $ million.

An increase or decrease in the initial public offering price of $1.00 per share of common stock would cause the net proceeds that we will receive from the offering, after deducting estimated expenses and underwriting discounts and commissions, to increase or decrease by approximately $ million.

The following table sets forth our proceeds from the offering of shares of our common stock and our uses of the proceeds that we expect to receive from this offering.

| Proceeds (in millions) | | Uses of Proceeds (in millions) | |
|---|---|---|---|
| Gross proceeds from this offering | $ | Cash consideration to SEP I for the contribution by SEP I to us of all the limited liability company interests in SEP Holdings III[2] | $ |
| | | Underwriting discounts and commissions[3] | $ |
| | | Fees and expenses associated with this offering and the formation transactions | $ |
| | | Drilling and exploration expenditures[4] | $ |
| | | Acquisition expenditures[4] | $ |
| | | Other operating expenses[4] | $ |
| | | General corporate purposes[4] | $ |
| Total[1] | $ | Total | $ |

(1) If the underwriters exercise their option to purchase additional shares of common stock in full, the gross proceeds would be $ million.
(2) In addition to the cash consideration, we will issue million shares of common stock to SEP I for the contribution by SEP I to us of all the limited liability company interests in SEP Holdings III.
(3) If the underwriters exercise their option to purchase shares of common stock in full, the underwriting discounts and commissions will be $ million.
(4) Pending use of the remaining net proceeds of this offering, and any proceeds from the exercise of the underwriters option to purchase additional shares of common stock from us, we intend to invest the net proceeds in interest bearing, investment-grade securities.

## DIVIDEND POLICY

We do not anticipate declaring or paying any cash dividends to holders of our common stock in the foreseeable future. We currently intend to retain future earnings, if any, to finance the expansion of our business. Our future dividend policy is within the discretion of our board of directors and will depend upon various factors, including our results of operations, financial condition, capital requirements and investment opportunities.

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## CAPITALIZATION

The following table shows our unaudited cash and cash equivalents and capitalization as of June 30, 2011:

- on a historical basis;
- on a pro forma basis to reflect our change in tax status from a partnership to a corporation and the recording of a distribution payable to SEP I in connection with the acquisition of our properties; and
- on a pro forma as adjusted basis to reflect (i) our change in tax status from a partnership to a corporation and the recording of a distribution payable to SEP I in connection with the acquisition of our properties and (ii) the issuance and sale of common stock to the public at an assumed initial offering price of $ per share (the midpoint of the price range set forth on the cover of this prospectus), and the application of the net proceeds from this offering as described under Use of Proceeds.

We derived this table from, and it should be read in conjunction with and is qualified in its entirety by reference to, the historical financial statements and the accompanying notes included elsewhere in this prospectus. You should also read this table in conjunction with Management s Discussion and Analysis of Financial Condition and Results of Operations.

| | As of June 30, 2011 | | |
|---|---|---|---|
| | Historical | Pro Forma<br>(in thousands) | Pro Forma As Adjusted |
| **Cash and cash equivalents** | $ - | | |
| **Distribution payable** | $ - | | |
| **Parent net investment/stockholders equity:** | | | |
| Parent net investment | 28,091 | | |
| Common stock, $0.01 par value; 1,000 shares authorized, none issued and outstanding (historical and pro forma); [150,000,000] shares authorized, shares issued and outstanding (pro forma as adjusted) | - | | |
| Paid-in capital | - | | |
| Retained earnings | - | | |
| **Total parent net investment/stockholders equity** | 28,091 | | |
| **Total capitalization** | $ 28,091 | | |

Each $1.00 increase (decrease) in the assumed initial public offering price of $ per share (the midpoint of the price range set forth on the cover page of this prospectus) would increase (decrease) our pro forma as adjusted cash and cash equivalents by approximately $ million.

The number of shares of common stock shown as issued and outstanding in the table set forth above excludes shares of common stock expected to be reserved for issuance under our Long Term Incentive Plan.

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## DILUTION

Dilution is the amount by which the offering price paid by the purchasers of common stock sold in this offering will exceed the net tangible book value per share after this offering. Net tangible book value is our total tangible assets less total liabilities. Assuming an initial offering price of $ per share (the midpoint of the price range set forth on the cover of this prospectus), as of June 30, 2011, after giving effect to the transactions described under Prospectus Summary Formation Transactions, including this offering of common stock and the application of the related net proceeds, our pro forma as adjusted net tangible book value was $ million, or $ per share. Purchasers of common stock in this offering will experience substantial and immediate dilution in net tangible book value per common share for accounting purposes, as illustrated in the following table:

| | | |
|---|---|---|
| Assumed initial offering price per share | | $ |
| Pro forma net tangible book value per share before this offering(1) | $ | |
| Increase in net tangible book value per share attributable to purchasers in this offering | | |
| Less: Pro forma as adjusted net tangible book value per share after this offering(2) | | |
| Immediate dilution in net tangible book value per share to purchasers in this offering(3) | | $ |

(1) Determined by dividing the pro forma net tangible book value of our net assets immediately prior to the offering by the number of shares to be issued to SEP I as partial consideration for its contribution of the limited liability company interests in SEP Holdings III.
(2) Determined by dividing our pro forma as adjusted net tangible book value, after giving effect to the application of the expected net proceeds of this offering, by the total number of shares outstanding after this offering.
(3) If the assumed initial offering price were to increase or decrease by $1.00 per share, then dilution in net tangible book value per share would equal $ or $ , respectively. The information discussed above is illustrative only and will be adjusted based on the actual public offering price and other terms of this offering determined at pricing.

The following table sets forth the number of shares that we will issue and the total consideration contributed to us by SEP I, in respect of its shares and by the purchasers of shares in this offering upon consummation of the transactions contemplated by this prospectus:

| | Shares Purchased | | Total Consideration | |
|---|---|---|---|---|
| | Number | Percent | $ (in millions) | Percent |
| Existing stockholders(1) | | .0% | $ | .0% |
| Purchasers in the offering(2) | | .0% | | .0% |
| Total | | 100.0% | $ | 100.0% |

(1) The assets contributed by SEP I were recorded at historical cost in accordance with GAAP.
(2) Total consideration is after deducting underwriting discounts and estimated offering expenses.

If the underwriters exercise their option to purchase additional shares in full, the following will occur:

- the percentage of shares of our common stock held by existing stockholders would decrease to % of the total number of shares of our common stock outstanding after this offering; and

- the percentage of shares of our common stock held by new investors would increase to approximately % of the total number of shares of our common stock outstanding after this offering.

In addition, we may choose to raise additional capital due to market conditions or strategic considerations even if we believe we have sufficient funds for our current or future operating plans. To the extent that we raise additional capital through the sale of equity or convertible debt securities, the issuance of these securities could result in further dilution to our stockholders.

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## SELECTED FINANCIAL DATA

The selected financial data as of December 31, 2009 and 2010 and for the years ended December 31, 2008, 2009 and 2010 are derived from our audited historical financial statements included elsewhere in this prospectus. The selected historical financial data as of June 30, 2011 and for the six months ended June 30, 2010 and 2011 are derived from our unaudited historical financial statements included elsewhere in this prospectus and from our financial records. The selected financial data as of December 31, 2008 is derived from SEP I s financial records. The results of operations for the interim periods are not necessarily indicative of operating results for the entire year or any future period.

Our historical financial statements have been prepared on a carve-out basis from the accounts of SEP I. These carve-out financial statements include all assets, liabilities and results of operations of the unconventional oil and natural gas properties and related assets to be contributed to us by SEP I for the periods presented.

Financial information for periods prior to 2008 is not presented. The properties did not have any production for periods prior to SEP I s acquisition of them and we believe that the omission of financial information for these periods is immaterial and unnecessary with respect to an understanding of our financial results and condition or any related trends and business prospects.

You should read the following table in conjunction with Use of Proceeds, Management s Discussion and Analysis of Financial Condition and Results of Operations and our financial statements included elsewhere in this prospectus. Among other things, those historical financial statements include more detailed information regarding the basis of presentation for the following information.

| | Year Ended December 31, | | | Six Months Ended June 30, | |
|---|---|---|---|---|---|
| | 2008 | 2009 | 2010 | 2010 | 2011 |
| | | | | (Unaudited) | |
| | | | (in thousands) | | |
| **Revenues:** | | | | | |
| Oil sales | $ - | $ 241 | $ 4,404 | $ 333 | $ 6,801 |
| Natural gas sales | - | - | 149 | | |