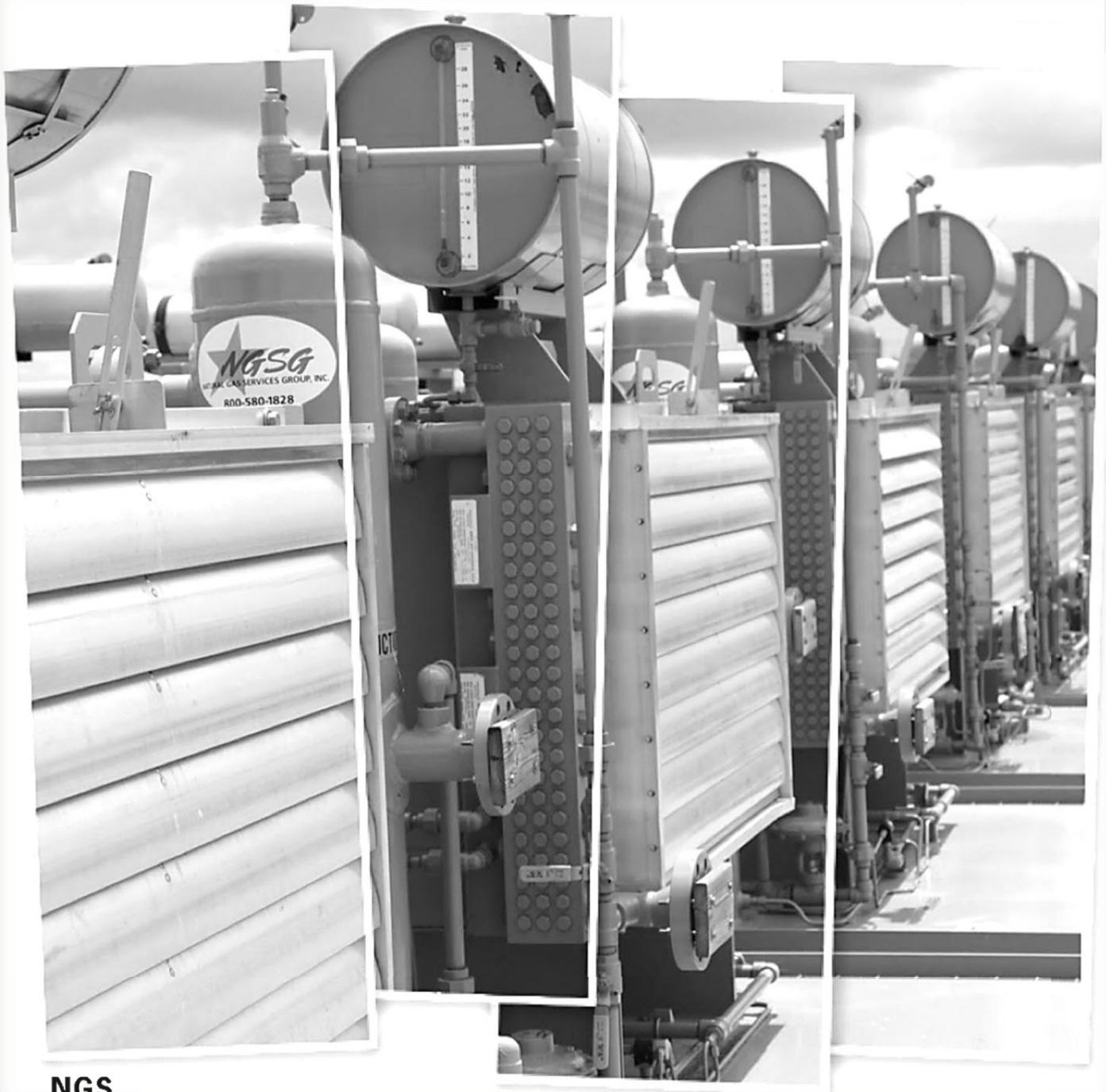




# 2014

# ANNUAL REPORT



**NGS**  
**LISTED**  
**NYSE**

# 2014 LETTER TO OUR SHAREHOLDERS

Fellow NGSG Shareholders,

2014 was a record year in many respects for NGSG. Our rental revenues, total revenues and total gross margins were at the highest levels in the history of the company.

Total revenue and rental revenue peaked at approximately \$97 million and \$79 million, respectively, and gross margin, operating income, net income and EBITDA increased each quarter throughout the year. We continued to grow our rental fleet to a total of 2,879 compressor units at year-end, a gain of 323 units. This enabled us to achieve a 14% increase in rental revenues while our gross margins strengthened to 60%, the highest level since 2010.

Comparing our progress since 2010, the bottom of the last cycle, NGSG has increased total revenues 80% and our rental revenues have almost doubled. Unit fleet size grew 51%; equating to over \$150 million in growth capital investment generated strictly through our operational cash flow. In spite of this growth, NGSG's total short and long-term debt was less than \$500 thousand and our cash balance was approximately \$6.2 million at the end of 2014.

While 2014 was an excellent year for the company, the last half of the year saw a dramatic deterioration in the price of crude oil and associated drilling activities. Although NGSG is not directly tied to drilling products and services, we are linked to production activities which will ultimately be affected, although typically on a delayed and less severe basis.

This is a commodity-driven business and there is little we can do about the supply and demand aspects of hydrocarbons, but we have positioned the company for the inevitable highs and lows in this industry. For example, rental revenues now approximate about 75% of our total revenues. Rentals tend to be impacted to a lesser degree than sales revenues and enable NGSG to continue to collect rental fleet payments through periods of lower activity. Our mix of gas and oil oriented compressors in the rental fleet is about 50/50 and provides the company with better diversification than we have historically had. I'm also proud to add that more than three-quarters of our executive and operational management have been together as a team since the last downturn in 2009-2010. With minimal debt and our strong cash generation capability, we anticipate growing our net cash balances through the coming year.

While we are well-positioned, we are prepared for an impact to our activity and anticipate pricing and utilization pressure. As is always the case, our large horsepower compressor fabrication and sales business will experience the greatest impact. To counter some of those effects, we have implemented both defensive and aggressive measures. Defensively, we are reducing all unnecessary costs, our fabrication activity has shrunk dramatically and we are enlisting our suppliers in an effort to reduce our cost base. From an aggressive perspective, we are concentrating on sales and product initiatives.



*Stephen C. Taylor*  
Chairman of the Board,  
President & Chief Executive Officer,  
Natural Gas Services Group, Inc.

Additional sales consultants have been placed into markets where we feel we can gain share and we have already announced two new products, our vapor recovery unit (VRU) and our first 400-500 horsepower rental units. Although we will not see any appreciable contribution from these products immediately, we think this is a good time to introduce our products and services.

I want to thank our shareholders, employees and board members for their interest, work and support on behalf of NGSG this past year. Although down turning markets are unpredictable in their breadth and depth, I am confident that NGSG will emerge in a preferred position.

As always, you are invited to NGSG's annual meeting in Midland, Texas on June 18, 2015, beginning at 8:30 am CDT. The meeting will be held at the Midland Petroleum Club at 501 West Wall Street

Sincerely,  
*Stephen Taylor*  
President and Chief Executive Officer

**NATURAL GAS SERVICES GROUP, INC.**  
**508 West Wall Street, Suite 550**  
**Midland, Texas 79701**

**Important Notice Regarding the Availability of Proxy Materials for the  
Shareholder Meeting to be Held on Thursday, June 18, 2015**

**The proxy statement and annual report to shareholders are available at  
[www.proxyvote.com](http://www.proxyvote.com).**

**NOTICE OF ANNUAL MEETING OF SHAREHOLDERS  
To be held on Thursday, June 18, 2015**

**NOTICE IS HEREBY GIVEN** that the Annual Meeting of Shareholders of Natural Gas Services Group, Inc., a Colorado corporation (the "Company"), will be held at the Petroleum Club of Midland, 501 West Wall Street, Midland, Texas 79701 on Thursday, June 18, 2015 at 8:30 a.m., Central Time, for the purpose of considering and voting upon proposals:

1. To elect two Directors to serve until the Annual Meeting of Shareholders to be held in 2018 or until their successors are elected and qualify;
2. To ratify the appointment of BDO USA, LLP as the Company's independent registered public accounting firm for 2015;
3. To consider an advisory vote on the compensation of our named executive officers; and
4. To transact such other business as may properly be presented at the meeting, or at any adjournment(s) of the meeting.

Only shareholders of record at the close of business on April 20, 2015 are entitled to notice of and to vote at the meeting and at any adjournment(s) of the meeting. On that day, 12,733,527 shares of our common stock were outstanding and entitled to vote. A complete list of our shareholders entitled to vote at the meeting will be available for examination at our offices in Midland, Texas during ordinary business hours for a period of ten (10) days prior to the annual meeting.

Our Board of Directors recommends that you vote **FOR** the (i) election of the two director nominees named in this proxy statement, (ii) the ratification of the appointment of BDO USA, LLP as our independent registered public accounting firm for 2015; and (iii) approval, on an advisory basis, of the compensation programs of our named executive officers.

We cordially invite you to attend the meeting. To ensure your representation at the meeting, please vote promptly even if you plan to attend the meeting. Voting now will not prevent you from voting in person at the meeting if you are a shareholder of record and wish to do so.

BY ORDER OF THE BOARD OF DIRECTORS

/s/ Stephen C. Taylor

April

\_\_\_\_\_  
Stephen C. Taylor

29, 2015

Chairman of the Board, President and Chief  
Executive Officer

**NATURAL GAS SERVICES GROUP, INC.**

**508 West Wall Street, Suite 550  
Midland, Texas 79701**

**PROXY STATEMENT  
FOR THE  
ANNUAL MEETING OF SHAREHOLDERS  
TO BE HELD ON THURSDAY, JUNE 18, 2015**

**GENERAL INFORMATION**

We are providing this proxy statement to you as part of a solicitation by the Board of Directors of Natural Gas Services Group, Inc. for use at our 2015 Annual Meeting of Shareholders and at any adjournment or postponement that may take place. We will hold the meeting at the Petroleum Club of Midland, 501 West Wall Street, Midland, Texas 79701 on Thursday, June 18, 2015 at 8:30 a.m., Central Time.

We are taking advantage of Securities and Exchange Commission, or SEC, rules that allow us to deliver our proxy materials to our shareholders on the Internet. Under these rules, we are sending most of our shareholders a two-page notice regarding the Internet availability of proxy materials instead of a full set of proxy materials. If you receive this two-page notice, you will not receive printed copies of the proxy materials unless you specifically request them. Instead, this notice tells you how to access and review on the Internet all of the important information contained in the proxy materials. This notice also tells you how to submit your proxy card on the Internet and how to request to receive a printed copy of our proxy materials.

We expect to mail, or provide notice and electronic delivery of, this proxy statement and accompanying proxy card to shareholders beginning on or about May 7, 2015.

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## QUESTIONS AND ANSWERS ABOUT THE PROXY MATERIALS AND THE MEETING

**Q: Why am I receiving these materials?**

A: Our Board is providing these proxy materials to you in connection with our 2015 Annual Meeting of Shareholders, which will take place on Thursday, June 18, 2015. As a shareholder on the record date for the meeting, you are invited to attend the meeting. We also encourage you to vote on the matters described in this proxy statement.

**Q: What information is contained in these materials?**

A: This proxy statement includes information about the nominees for director and the other matters to be voted on at the meeting. The proxy statement also includes information about the voting process and requirements, the compensation of directors and some of our executive officers, and certain other required information.

**Q: What can I vote on at the meeting?**

A: There are three matters to be voted on at the meeting:

1. To elect two Directors to serve until the Annual Meeting of Shareholders to be held in 2018, or until their successors are elected and qualified;
2. To ratify the appointment of BDO USA, LLP as the Company's independent registered public accounting firm for 2015;
3. To consider an advisory vote on the compensation of our named executive officers; and
4. To transact such other business as may properly be presented at the meeting, or at any adjournment(s) of the meeting.

**Q: How does the Board recommend that I vote on each of the matters?**

A: Our Board recommends that you vote **FOR** each of the director nominees and **FOR** the ratification of the appointment of BDO USA, LLP as our independent registered public accounting firm for 2015. With respect to Proposal #3, the Board of Directors recommends that you vote **FOR** approval, on an advisory basis, of the compensation programs of our named executive officers as disclosed in the Compensation Discussion and Analysis, the compensation tables, and the related disclosure contained in the proxy statement set forth under the caption "Executive Compensation" of this proxy statement.

**Q: Why did I receive a two-page notice in the mail regarding the Internet availability of proxy materials this year instead of a full set of proxy materials?**

A: We are taking advantage of SEC rules that allow us to deliver proxy materials to our shareholders on the Internet. Under these rules, we are sending most of our shareholders a two-page notice regarding the Internet availability of proxy materials instead of a full set of proxy materials. If you receive this two-page notice, you will not receive printed copies of the proxy materials unless you specifically request them. Instead, this notice tells you how to access and review on the Internet all of the important information contained in the proxy materials. This notice also tells you how to submit your proxy card on the Internet and how to request to receive a printed copy of our proxy materials. Shareholders may also request to receive proxy materials in printed form by mail or electronically by email on an ongoing basis.

**Q: Can I receive next year's proxy materials by email?**

A: Yes. All shareholders who have active email accounts and Internet access may sign up for email delivery of shareholder materials. To sign up, go to [www.proxyvote.com](http://www.proxyvote.com) and click on "Electronic Enrollment." If you have multiple registered or beneficial accounts, you need to enroll for each account. If you elect to receive proxy materials by email, we will not mail you any proxy-related materials next year. Your enrollment in the email program will remain in effect as long as your account remains active or until you cancel it.

**Q: Who is entitled to vote at our annual meeting of shareholders?**

A: Holders of our outstanding common stock on April 20, 2015, are entitled to one vote per share on each of the items being voted on at the meeting. We refer to this date as the Record Date. On the Record Date, we had 12,733,527 shares of common stock outstanding. We have no other classes of stock outstanding.

**Q: What shares can I vote?**

A: You can vote all shares you owned on the Record Date. These shares include (1) shares held directly in your name as the shareholder of record and (2) shares held for you as the beneficial owner through a stockbroker, bank or other nominee.

**Q: What is the difference between holding shares as a shareholder of record and as a beneficial owner?**

A: Most of our shareholders hold their shares through a stockbroker, bank or other nominee rather than directly in their own name. There are some important distinctions between shares held of record and those owned beneficially.

*Shareholder of Record*

If your shares are registered in your name with our transfer agent, Computershare, you are the shareholder of record for those shares and are receiving proxy-related materials directly from us. As the shareholder of record, you have the right to grant your voting proxy directly to us or to vote in person at the meeting.

*Beneficial Owner*

If your shares are held in a stock brokerage account, by a bank or other nominee (commonly referred to as being held in “street name”) you are the beneficial owner of those shares. Your broker, bank or nominee is the shareholder of record and therefore has forwarded proxy-related materials to you as beneficial owner. As the beneficial owner, you have the right to direct your broker, bank or other nominee how to vote your shares and are also invited to attend the meeting. However, since you are not the shareholder of record, you may not vote your shares in person at the meeting unless you obtain a signed proxy from your broker, bank or nominee giving you the right to vote the shares.

**Q: How do I vote if I am a shareholder of record (as described in the question and answer above)?**

A: You can vote on the Internet or by telephone by following the instructions you received in the mail or by email. If you received a full printed set of our proxy materials in the mail, you can also vote by mail by signing and returning the proxy card provided with those materials. Finally, you can vote in person at the meeting.

**Q: How do I vote if I am a beneficial owner (as described in the question and answer above)?**

A: You can vote on the Internet or by telephone by following the instructions you received in the mail or by email. If you received a full printed set of our proxy materials in the mail, you can also vote by mail. You can vote in person at the meeting *only if you obtain a signed proxy from your broker, bank or nominee giving you this right.*

**Q: Can I change my vote or revoke my proxy?**

A: Yes. You can change your vote or revoke your proxy at any time before the final vote at the meeting. You can do this by casting a later proxy through any of the available methods described in the questions and answers above. If you are a shareholder of record, you can also revoke your proxy by delivering a written notice of your revocation to our Corporate Secretary at our principal executive office at 508 West Wall Street, Suite 550, Midland, Texas 79701. If you are a beneficial owner, you can revoke your proxy by following the instructions sent to you by your broker, bank or other nominee.

**Q: What does it mean if I get more than one set of proxy-related materials?**

A: It means you hold shares registered in more than one account. Follow the instructions in each set of proxy-related materials to ensure that all of your shares are voted.



**Q: What is the quorum requirement for the meeting?**

A: For a “quorum” to exist at the meeting, shareholders holding a majority of the votes entitled to be cast by the shareholders entitled to vote must be present in person or represented by proxy at the meeting. There must be a quorum for any action to be taken at the meeting (other than adjournment or postponement of the meeting). If you submit a properly completed proxy, even if you abstain from voting, then your shares will be counted for purposes of determining the presence of a quorum.

If a broker indicates on a proxy that it lacks discretionary authority as to certain shares to vote on a particular matter, commonly referred to as “broker non-votes,” those shares will still be counted for purposes of determining the presence of a quorum at the meeting. Please see the next question and answer for further information about “broker non-votes.”

**Q: What are broker non-votes and how are broker non-votes and abstentions counted?**

A: If you are a beneficial owner and hold your shares in street name and do not provide your broker or other nominee with voting instructions, the broker, bank, or other nominee will determine if it has the discretionary authority to vote on the particular matter. The New York Stock Exchange permits brokers to vote their customers' shares on routine matters when the brokers have not received voting instructions from the customers. The ratification of independent public accountants is an example of a routine matter on which brokers may vote. Brokers may not vote their customers' shares on non-routine matters unless they have received instructions from the customers. Non-voted shares on non-routine matters are referred to as broker non-votes. The ratification of the appointment of BDO USA, LLP as our independent public accountants for 2015 (Proposal 2) is a matter considered “routine” under application rules. The election of directors (Proposal 1) and the advisory vote to approve named executive officer compensation (Proposal 3) are matters considered “non-routine” under applicable rules. A broker or other nominee cannot vote without instructions on non-routine matters. Abstentions and broker non-votes will have no effect on Proposal 1, as the election of Directors is determined by counting the votes actually cast where abstentions and broker non-votes are not treated as votes cast. With respect to the advisory vote to approve the named executive officers compensation programs (Proposal 3) where the vote required is a majority of votes present and entitled to vote, abstentions will be equivalent to a vote cast against the proposals and broker non-votes will have no effect.

**Q: What is the voting requirement to approve each of the matters?**

A: Directors are elected by a plurality of the votes cast at the Annual Meeting. This means that the nominee for election as Director who receives the greatest number of votes cast in favor of his or her election will be elected to the Board of Directors. The ratification of the appointment of BDO USA, LLP as the Company’s independent registered public accounting firm and the advisory vote on the compensation programs of our named executive officers are approved if the votes cast in favor of the matter exceed the votes cast against the matter. If you are a beneficial owner and do not provide the shareholder of record with voting instructions, your shares may constitute broker non-votes for certain matters (as described in the question and answer immediately above). In tabulating the voting result for a proposal, shares that constitute broker non-votes are not considered as being entitled to vote on that proposal.

**Q: How can I vote on each of the matters and how will the votes be counted?**

A: In the election of directors, you may vote “FOR,” “AGAINST,” or “ABSTAIN” with respect to each of the two nominees. If you elect to abstain from the election of directors, the abstention will not have any effect on the election of directors. In tabulating the voting results for the election of directors, only “FOR” and “AGAINST” votes are counted.

For the (i) ratification of the appointment of BDO USA, LLP as our independent auditors, and (ii) advisory vote on compensation of our named executive officers advisory vote on compensation of our named executive officers, you may vote “FOR,” “AGAINST,” or “ABSTAIN” with respect to these two proposals. If you elect to abstain from voting on any of these proposals, the abstention will have the same effect as an “AGAINST” vote with respect to such proposal.

If you sign and return your proxy card or voting instruction form without giving specific voting instructions, your shares will be voted as recommended by our Board. If you are a beneficial holder and do not return a voting instruction form, your broker may only vote on the ratification of the appointment of BDO USA, LLP (Proposal 2).

**Q: Who will count the votes?**

A: Broadridge, an international investor relations company, is assisting us with the voting of proxies for our meeting. Prior to the meeting, Broadridge will provide us with a tabulation of the votes cast prior to the meeting. We believe that Broadridge will use procedures that are consistent with Colorado law concerning the voting of shares, the determination of the presence of a quorum and the determination of the outcome of each matter submitted for a vote. In addition, we will appoint a voting inspector at the meeting to count and tabulate any votes cast at the meeting.

**Q: Who may attend the meeting?**

A: All shareholders as of the Record Date may attend. Please bring to the meeting:

- proof of ownership such as: a copy of your proxy or voting instruction card; the two-page notice regarding the internet availability of proxy materials you received in the mail; or a copy of a brokerage or bank statement showing your share ownership as of the Record Date; and
- proof of *identification* such as a valid driver's license or passport.

**Q: How will voting on any other business be conducted?**

A: We do not expect any matters to be presented for a vote at the meeting other than the three matters described in this proxy statement. If you grant a proxy, either of the officers named as proxy holders, Stephen C. Taylor and G. Larry Lawrence, or their nominees or substitutes, will have the discretion to vote your shares on any additional matters that are properly presented for a vote at the meeting and at any adjournment or postponement that may take place. If, for any unforeseen reason, any of our nominees is not available as a candidate for director, the persons named as the proxy holder will vote your proxy for another candidate or other candidates nominated by our Board.

**Q: May I propose actions for consideration at next year's meeting of shareholders?**

A: Yes. For your proposal to be considered for inclusion in our proxy statement for next year's meeting, we must receive your written proposal no later than December 21, 2015. If we change the date of next year's meeting by more than 30 days from the date of this year's meeting, then the deadline is a reasonable time before we begin to print and send our proxy materials. You should also be aware that your proposal must comply with SEC regulations regarding shareholder proposals.

Similarly, for you to raise a proposal (including a director nomination) from the floor at next year's meeting, we must receive a written notice of the proposal no later than March 9, 2016. If we change the date of next year's meeting by more than 30 days from the date of this year's meeting, then we must receive your written proposal at least 150 days before the date of next year's meeting for the proposal to be timely.

**Q: Who is paying for this proxy solicitation?**

A: We will pay the cost of soliciting the proxies. In addition, our officers, directors and employees may solicit proxies or votes in person, by telephone or by email. These people will not be paid any additional compensation for these activities. We will send copies of proxy-related materials or additional solicitation materials to brokers, fiduciaries and custodians who will forward these materials to the beneficial owners of our shares. On request, we will reimburse brokers and other persons representing beneficial owners of shares for their reasonable expenses in forwarding these materials to beneficial owners.

## **HOUSEHOLDING OF PROXY MATERIALS**

In an effort to reduce printing costs and postage fees, we have adopted a practice called “householding.” Under this practice, shareholders who have the same address and last name and do not participate in email delivery of proxy-related materials will receive only one set of our proxy statement, annual report or notice of internet availability of proxy-related materials unless one or more of these people notifies us that he or she wishes to continue to receive individual copies.

If you share an address with another shareholder and receive only one set of proxy-related materials and would like to request a separate copy for this year’s annual meeting or for any future meetings, please: (1) call our Investor Relations contact at (432) 262-2700; (2) send an email message to [alicia.dada@ngsgi.com](mailto:alicia.dada@ngsgi.com); or (3) mail your request to Natural Gas Services Group, Inc., 508 West Wall Street, Suite 550, Midland, Texas 79701, Attn: Investor Relations. Similarly, you may also contact us through any of these methods if you receive multiple copies of the materials and would prefer to receive a single copy in the future.

## PROPOSAL 1 - ELECTION OF DIRECTORS

Our Board of Directors is divided into three classes (commonly known as a “staggered” Board), each class to be as nearly equal in number as possible. At each annual meeting of shareholders, members of one of the classes, on a rotating basis, are elected for a three-year term. The authorized number of Directors is currently set at nine. We currently have five directors serving on our Board. Our Board of Directors may fill the vacancies if a qualified candidate is vetted. The following table sets forth, by class, the members of our Board of Directors as of the date of this proxy statement:

Terms Expiring at the 2015 Annual Meeting	Terms Expiring at the 2016 Annual Meeting	Terms Expiring at the 2017 Annual Meeting
David L. Bradshaw	John W. Chisholm	Charles G. Curtis
William F. Hughes		Stephen C. Taylor

Shareholders will be electing two Directors at the meeting. The Board is recommending Mr. Bradshaw and Mr. Hughes for re-election to the Board of Directors to serve three year terms expiring at the annual meeting of shareholders in 2018.

The persons named in the enclosed form of proxy will vote the shares represented by such proxy for the election of the nominees for Director named above unless other instructions are shown on the proxy card. If, at the time of the meeting, either or both of these nominees becomes unavailable for any reason, which is not expected, the persons entitled to vote the proxy will vote for such substitute nominee or nominees, if any, as they determine in their sole discretion, or we may reduce the size of the Board.

Biographical information and qualifications for each person nominated as a Director, and for each person whose term of office as a Director will continue after the 2015 Annual Meeting, is set forth below.

### **Nominees for Directors for Terms to Expire in 2018**

#### ***David L. Bradshaw***

David L. Bradshaw, 60, joined our board in December of 2011. Since 2005, Mr. Bradshaw has acted as a consultant in the oil and gas exploration and production sector and has overseen his investments in this area. From August 2007 through November 2009, Mr. Bradshaw served as a Director and Audit Committee Chairman for Triangle Petroleum, a publicly traded company listed on the American Stock Exchange. From November 2007 through November 2008, Mr. Bradshaw served as a Director for Comet Ridge Limited, an Australian company listed on the Australian Securities Exchange. From 1986 to 2005, Mr. Bradshaw worked for Tipperary Corporation, a U.S. public company listed on the American Stock Exchange. During his tenure at Tipperary, the company was involved in oil and gas exploration and production, and natural gas processing and transportation. He held the positions of Chief Executive Officer from 1996 to 2005, Chairman of the Board from 1997 to 2005, Chief Financial Officer from 1990 to 1996 and Chief Operating Officer from 1993 to 1996. Mr. Bradshaw also served as Chief Executive Officer and Chairman of Tipperary Oil & Gas (Australia) Pty Ltd from 1999 to 2005, a subsidiary of Tipperary, which explored for and produced natural gas in Queensland, Australia. From 1983 to 1986, Mr. Bradshaw was an owner and officer of Bradcorp, Inc. a private exploration and production company. Prior to this, Mr. Bradshaw spent six years in public accounting serving predominantly oil and gas clients. Mr. Bradshaw graduated from Texas A&M University with a BBA in Accounting in 1976 and a MBA in 1977, and is also a Certified Public Accountant.

Mr. Bradshaw's educational and professional training and achievements as a Certified Public Accountant and MBA, along with his past experience as both a Chief Financial Officer and Chief Executive Officer of a public company involved in the natural resources industry, provides us with considerable accounting and corporate finance skills. In addition, Mr. Bradshaw's career spanning over thirty years in the oil and gas industry and as a public accountant. His executive management positions in both private and public companies bring us significant leadership, planning and management skills and background.

#### ***William F. Hughes, Jr.***

William F. Hughes Jr., 62, has served as a Director since December 2003. Mr. Hughes has over 30 years experience in the engineering and construction industry as a Registered Civil Engineer and licensed building contractor. From 1974 to 1979, he served as an officer in the United States Air Force. From 1979 to 1986, he was a project design engineer for Cushman & Associates. From 1986 to 1996, he served as a Project Manager on a variety of public works and industrial construction projects. Since 1983, Mr. Hughes has been co-owner of The Whole Wheatery, LLC, a natural foods store located in Lancaster,

California. Mr. Hughes holds a Bachelor of Science degree in Civil Engineering from the United States Air Force Academy and a Master of Science in Engineering from the University of California at Los Angeles.

Mr. Hughes' career experience in the engineering and construction industry brings us invaluable skills which are applicable to our manufacturing processes. In addition, Mr. Hughes provides leadership skills arising from his service as an officer with the U.S. Air Force and U.S. Air Force Academy graduate.

### **Continuing Directors Whose Terms Expire in 2016**

#### ***John W. Chisholm***

John W. Chisholm, 60, was appointed as a Director of Natural Gas Services Group in December 2006 to fill a vacancy created by expanding the size of the Board from seven to eight Directors and was first elected as a Director of Natural Gas Services Group at the annual meeting of shareholders held in June 2007. Mr. Chisholm is the founder of Wellogix, an oil and gas software company that develops software aimed at expediting the exchange of enterprise data and communication of complex engineered services. Prior to founding Wellogix, Mr. Chisholm co-founded and served as President of ProTechnics Company from 1985 until its sale to Core Laboratories in December of 1996. Mr. Chisholm served as Senior Vice President of Global Sales and Marketing of Core Laboratories until 1998, when he started Chisholm Energy Partners, an investment fund focused on mid-size energy service companies. From 2002 to 2009 Mr. Chisholm served on the Board of Directors of Flotek Industries, Inc., and became interim President in August 2009. In August 2010 Mr. Chisholm became President of the company and was appointed Chief Executive officer in March 2012. Flotek Industries, Inc. is a public company which files reports under the Securities Exchange Act of 1934. Mr. Chisholm holds a Business Administration degree from Fort Lewis College in Colorado. He currently serves on the Editorial Advisory Board on Middle East Technology of the Oil & Gas Journal.

Mr. Chisholm brings significant natural resources experience to our Board, in connection with his background in supplying drilling and production related products and services to the oil, gas and mining industries, and his investment fund experience with mid-size energy service companies is an invaluable resource as the Company assesses its capital and liquidity needs.

In addition Mr. Chisholm's experience as a board member and executive officer of a public company provides us with a wealth of leadership and management skills.

### **Continuing Directors Whose Terms Expire in 2017**

#### ***Charles G. Curtis***

Charles G. Curtis, 82, has served as a Director of Natural Gas Services Group since April 2001. Since 2002, substantially all of Mr. Curtis' business activities have been devoted to managing personal investments. From 1992 until 2002, Mr. Curtis was the President and Chief Executive Officer of Curtis One, Inc., a manufacturer of aluminum and steel mobile stools and mobile ladders. From 1988 to 1992, Mr. Curtis was the President and Chief Executive Officer of Cramer, Inc., a manufacturer of office furniture. Mr. Curtis has a Bachelor of Science degree from the United States Naval Academy and a Master of Science degree in Aeronautical Engineering from the University of Southern California.

Mr. Curtis has been a long-standing member of the Board since prior to the Company's initial public offering in 2002 and as such he brings a wealth of knowledge regarding the Company's history, growth and industry. Through his manufacturing career and engineering educational background, Mr. Curtis assists the Board and the Company in connection with its compressor manufacturing business. As a past U.S. Naval Officer and U.S. Naval Academy graduate, Mr. Curtis also brings leadership skills to the Board and Company.

#### ***Stephen C. Taylor***

Stephen C. Taylor, 61, has been President and Chief Executive Officer of Natural Gas Services Group since January 2005. He was elected as a Director of Natural Gas Services Group at the annual meeting of shareholders in June 2005. Effective January 1, 2006, Mr. Taylor was appointed Chairman of the Board of Directors. Immediately prior to joining Natural Gas Services Group, Mr. Taylor held the position of General Manager - US Operations for Trican Production Services, Inc. from 2002 through 2004. Mr. Taylor joined Halliburton Resource Management in 1976, becoming its Vice President - Operations in 1989. Beginning in 1993, he held multiple senior level management positions with Halliburton Energy Services until 2000 when he was elected Senior Vice President/Chief Operating Officer of Enventure Global Technology, LLC, a joint-venture deep water drilling technology company owned by Halliburton Company and Shell Oil Company. Mr. Taylor elected early retirement from Halliburton Company

in 2002 to join Trican Production Services, Inc. Mr. Taylor holds a Bachelor of Science degree in Mechanical Engineering from Texas Tech University and a Master of Business Administration degree from the University of Texas at Austin.

Mr. Taylor's senior management experience in the natural resources industry provides the Board and our company with significant insight into our business. Mr. Taylor's engineering and advanced business training (MBA) uniquely suits him to provide leadership, technical expertise and financial acumen to our Board and to the operations of our company in connection with his position as our chief executive officer.

## THE BOARD OF DIRECTORS AND ITS COMMITTEES

Natural Gas Services Group's Board of Directors held four meetings in 2014. Each Director attended at least 75% of the total number of Board meetings held while such person was a Director. Each Director also attended at least 75% of all of the meetings held by all committees of the Board of Directors for which he served (during the periods that he served). The Board of Directors acts from time to time by unanimous written consent in lieu of holding a meeting.

Our non-management directors hold regularly scheduled executive sessions in which those directors meet without management participation. Generally, the Chairman of the Governance and Personnel Development Committee presides over these sessions. Charles G. Curtis is currently that Chairman.

We typically schedule a Board meeting in conjunction with our annual meeting of shareholders. Although we do not have a formal policy on the matter, we expect our Directors to attend each annual meeting, absent a valid reason, such as illness or an unavoidable schedule conflict. Last year, all of the individuals then serving as Directors attended our 2014 Annual Meeting of Shareholders.

To assist it in carrying out its duties, the Board has delegated certain authority to four separately designated standing committees. These committees are described below.

### **Audit Committee**

The primary functions of our Audit Committee include:

- assisting the Board in fulfilling its oversight responsibilities as they relate to our accounting policies, internal controls, financial reporting practices and legal and regulatory compliance;
- hiring our independent registered public accounting firm;
- monitoring the independence and performance of our independent registered public accounting firm;
- maintaining, through regularly scheduled meetings, a line of communication between the Board, our financial management and independent registered public accounting firm; and
- overseeing compliance with our policies for conducting business, including ethical business standards.

The members of the Audit Committee are David L. Bradshaw (Chairman), Charles G. Curtis, and William F. Hughes, Jr. Our common stock is listed for trading on the New York Stock Exchange, or "NYSE". Under rules of the NYSE, the Audit Committee is to be comprised of three or more Directors, each of whom must be independent. Our Board has determined that all of the members of the Audit Committee are independent, as defined under the applicable NYSE rules and listing standards. In addition, our Board of Directors has determined that David L. Bradshaw is qualified as an "audit committee financial expert" as that term is defined in the rules of the Securities and Exchange Commission. The Audit Committee met nine times during the last fiscal year. The audit committee has also received from, and discussed with, BDO the matters required to be discussed by Public Accounting oversight Board Auditing standard No. 16. (Communications with Audit Committees).

Any shareholder may obtain free of charge a printed copy of our Audit Committee Charter by sending a written request to Investor Relations, Natural Gas Services Group, Inc., 508 West Wall Street, Suite 550, Midland, Texas 79701. You can also view and print a copy of our Audit Committee Charter by clicking on the "Governance" tab at the Investor Relations page of our website at [www.ngsgi.com](http://www.ngsgi.com).

## **Compensation Committee**

The functions of our Compensation Committee include:

- assisting the Board in overseeing the management of our human resources;
- evaluating our Chief Executive Officer's performance and compensation;
- formulating and administering our overall compensation principles and plans; and
- evaluating management.

The Compensation Committee's policy is to offer the executive officers competitive compensation packages that will permit us to attract and retain individuals with superior abilities and to motivate and reward such individuals in an appropriate fashion in the long-term interests of Natural Gas Services Group and its shareholders. Currently, executive compensation is comprised of salary and cash bonuses and awards of long-term incentive opportunities in the form of restricted stock awards under the 2009 Restricted Stock/Unit Plan.

The members of the Compensation Committee are William F. Hughes, Jr. (Chairman), John W. Chisholm and David L. Bradshaw. Our Board has determined that all of the members of the Compensation Committee are independent, as defined under the applicable NYSE rules and listing standards. During the last fiscal year there were seven meetings of the Compensation Committee.

### *Compensation Committee Interlocks and Insider Participation*

The Compensation Committee members are not officers or employees of our company, and there is not, nor was there during fiscal 2014, any compensation committee interlock (in other words, no executive of our company serves as a Director or on the compensation committee of a company that has one or more executives serving on our Board of Directors or our Compensation Committee).

Any shareholder may obtain free of charge a printed copy of our Compensation Committee Charter by sending a written request to Investor Relations, Natural Gas Services Group, Inc., 508 West Wall Street, Suite 550, Midland, Texas 79701. You can also view and print a copy of our Compensation Committee Charter by clicking on the "Governance" tab at the Investor Relations page of our website at [www.ngsgi.com](http://www.ngsgi.com).

## **Governance and Personnel Development Committee**

Our Governance and Personnel Development Committee primarily focuses on:

- generally overseeing the governance of the Board and its committees;
- interpreting the Governance Guidelines, the Code of Business Conduct and Ethics and other similar governance documents adopted by the Board; and
- overseeing the evaluation of the Board and its committees.

The members of the Governance and Personnel Development Committee are Charles G. Curtis (Chairman), John W. Chisholm and William F. Hughes, Jr. Our Board has determined that each of the Governance and Personnel Development Committee members is independent, as defined under the applicable NYSE rules and listing standards. During the last fiscal year there were four meetings of the Governance and Personnel Development Committee.

Any shareholder may obtain free of charge a printed copy of our Governance Committee Charter by sending a written request to Investor Relations, Natural Gas Services Group, Inc., 508 West Wall Street, Suite 550, Midland, Texas 79701. You can also view and print a copy of our Governance Committee Charter by clicking on the "Governance" tab at the Investor Relations page of our website at [www.ngsgi.com](http://www.ngsgi.com).



## **Nominating Committee**

The functions of our Nominating Committee include:

- identifying individuals qualified to become board members, consistent with the criteria approved by the Board;
- recommending Director nominees and individuals to fill vacant positions; and
- overseeing executive development and succession and diversity efforts.

The members of the Nominating Committee are John W. Chisholm (Chairman), David L. Bradshaw, and Charles G. Curtis. Our Board of Directors has determined that each of the Nominating Committee members is independent as defined under the applicable NYSE rules and listing standards. During the last fiscal year there were four meetings of the Nominating Committee.

Any shareholder may obtain free of charge a printed copy of our Nominating Committee Charter by sending a written request to Investor Relations, Natural Gas Services Group, Inc., 508 West Wall Street, Suite 550, Midland, Texas 79701. You can also view and print a copy of our Nominating Committee Charter by clicking on the “Governance” tab at the Investor Relations page of our website at [www.ngsgi.com](http://www.ngsgi.com). Our Nominating Committee does not have a diversity policy; however, as discussed below, the Committee’s goal is to nominate candidates who possess a range of experiences and backgrounds which will contribute to the board’s overall effectiveness in meeting its duties and forwarding the goals of our company.

Our Nominating Committee will consider a Director candidate recommended by a shareholder. A candidate must be highly qualified in terms of business experience and be both willing and expressly interested in serving on the Board. A shareholder wishing to recommend a candidate for the Committee’s consideration should forward the candidate’s name and information about the candidate’s qualifications to Natural Gas Services Group, Inc., Nominating Committee, 508 West Wall Street, Suite 550, Midland, Texas 79701, Attn.: John W. Chisholm. Submissions must include sufficient biographical information concerning the recommended individual, including age, employment history for at least the past five years indicating employers' names and description of the employer’s business, educational background and any other biographical information that would assist the Committee in determining the qualifications of the individual. The Committee will consider recommendations received by a date not later than 120 calendar days before the date our proxy statement was released to shareholders in connection with the prior year’s annual meeting for nomination at that annual meeting. The Committee will consider nominations received after that date at the annual meeting subsequent to the next annual meeting.

The Committee evaluates nominees for Directors recommended by shareholders in the same manner in which it evaluates other nominees for Directors. Minimum qualifications include the factors discussed above.

## **Director Independence**

The Board has determined that each of the following four members of the Board is “independent” within the meaning of applicable listing standards of the NYSE and under the standards, set forth in Exhibit A to our Governance and Personnel Development Charter, (“Governance Charter”) which are consistent with the NYSE listing standards: David L. Bradshaw, John W. Chisholm, Charles G. Curtis, and William F. Hughes, Jr. A copy of Exhibit A to our Governance Charter is available at our website, [www.ngsgi.com](http://www.ngsgi.com), under the heading “Investor Relations—Governance.” The Board has made an affirmative determination that each of the four directors named above satisfies these categorical standards. In making its determination, the Board examined relationships between directors or their affiliates with us and our affiliates and determined that each such relationship, if any, did not impair the director’s independence.

## **The Board's Leadership Structure**

Under our Corporate Governance Guidelines, our Chief Executive Officer also serves as our Chairman of the Board, and that person is responsible to the Board for the overall management and functioning of the company. Stephen C. Taylor serves as both Chairman of the Board and our President and Chief Executive Officer ("CEO"). The Board believes this is the most effective Board leadership structure at the present time and believes that Mr. Taylor, in his role as Chairman/CEO, has the ability to execute on both our short-term and long-term strategies necessary for the challenging marketplace in which we compete. The independent directors believe that Mr. Taylor's detailed and in-depth knowledge of the issues, opportunities and challenges facing us and our business make him the best qualified director to develop agendas that ensure that the Board's time and attention are focused on the most critical matters. Further, as the individual with primary responsibility for managing day-to-day operations, Mr. Taylor is best positioned to chair regular Board meetings and ensure that key business issues and risks are brought to the attention of our Board and/or Audit Committee. We believe that the creation of a lead independent director position is not necessary at this time.

Each of our directors, other than Mr. Taylor, is independent, and the Board believes that the independent directors provide effective oversight of management. The Board may subsequently decide, however, to change that leadership structure which would require a revision to our Corporate Governance Guidelines. The Board believes that it has in place safeguards to ensure that we maintain the highest standards of corporate governance and continued accountability of the CEO to the Board. These safeguards include:

- All members of the Board are independent directors except for Mr. Taylor.
- Each of the Board's standing committees, including the Audit, Compensation, Governance and Nominating Committees, are comprised of and chaired solely by non-employee directors who meet the independence requirements under the NYSE listing standards and other governing laws and regulations. As noted above, these committees meet frequently.
- Review and determination of Mr. Taylor's compensation and performance remains within the purview of the Compensation Committee.
- The independent directors continue to meet in executive sessions without management present to discuss the effectiveness of the company's management, the quality of the Board meetings and any other issues and concerns.

## **Role in Risk Oversight**

Our Board of Directors oversees the management of risks inherent in the operation of our business and the implementation of our strategic plan. Our executive management is responsible for the day-to-day management of risks we face. The Board is periodically advised by management on the status of various factors that could impact our business and operating results, including oil and gas industry issues, operational issues (such as compressor manufacturing issues, backlog for compressor equipment,) legal and regulatory risks. The full Board is also responsible for reviewing our strategy, business plan, and capital expenditure budget.

Our Board committees assist the Board in fulfilling its oversight responsibilities in certain areas of risk. Our Audit Committee serves an important role in providing risk oversight, as further detailed in its charter. One of the Audit Committee's primary duties and responsibilities is to monitor the integrity of our financial statements, financial reporting processes, systems of internal controls regarding finance, and disclosure controls and procedures. The Compensation Committee assists the Board with risk management relating to our compensation policies and programs, and the Governance and Nominating Committee assists with risk management relating to Board organization, membership and structure, succession planning for our directors and executive officers, and corporate governance.

## CODE OF ETHICS

Our Board of Directors has adopted a Code of Business Conduct and Ethics, or “Code”, which is posted on our website at [www.ngsgi.com](http://www.ngsgi.com). You may also obtain a copy of our Code by requesting a copy in writing at 508 West Wall Street, Suite 550, Midland, Texas 79701 or by calling us at (432) 262-2700.

Our Code provides general statements of our expectations regarding ethical standards that we expect our Directors, officers and employees, including our Chief Executive Officer and principal financial officer, to adhere to while acting on our behalf. Among other things, the Code provides that:

- we will comply with all laws, rules and regulations;
- our Directors, officers and employees are to avoid conflicts of interest and are prohibited from competing with us or personally exploiting our corporate opportunities;
- our Directors, officers and employees are to protect our assets and maintain our confidentiality;
- we are committed to promoting values of integrity and fair dealing; and that
- we are committed to accurately maintaining our accounting records under generally accepted accounting principles and timely filing our periodic reports.

Our Code also contains procedures for our employees to report, anonymously or otherwise, violations of the Code.

## EXECUTIVE OFFICERS

Biographical information for the executive officers of Natural Gas Services Group who are not Directors is set forth below. There are no family relationships between any Director or executive officer and any other Director or executive officer. Executive officers serve at the discretion of the Board of Directors and until their successors have been duly elected and qualified, unless sooner removed by the Board of Directors. Officers are elected by the Board of Directors annually at its first meeting following the annual meeting of shareholders.

G. Larry Lawrence, 63, became our Chief Financial Officer, Principal Accounting Officer and Corporate Secretary on July 1, 2011. Previously, Mr. Lawrence was our Controller since September 2010. From June 2006 to August 2010, Mr. Lawrence was self employed as a management consultant doing business as Crescent Consulting. Overlapping this time, from September 2006 to August 2009, he also served as the CFO of Lynx Operating Company. Lynx is a private company engaged in oil and gas production and gas processing activities. From May 2004 through April 2006 Mr. Lawrence served as Controller of Pure Resources, an exploration and production company and wholly owned subsidiary of Unocal Corporation which was acquired by Chevron Corporation. From June 2000 through May 2004, Mr. Lawrence was a practice manager of the Parson Group, LLC, a financial management consulting firm whose services included Sarbanes Oxley engagements with oil and natural gas industry clients. From 1973 through May 2000, Mr. Lawrence was employed by Atlantic Richfield Company where he most recently (from 1993 through 2000) served as Controller of ARCO Permian. Since May 2006, Mr. Lawrence serves as a director of Legacy Reserves, LP. Mr. Lawrence has a Bachelor of Arts in Accounting, with honors, from Dillard University.

James R. Hazlett, 59, has served as Vice President Technical Services since June 2005. He also served as Vice President of Sales of Screw Compression Systems, Inc. from 1997 until June 2007 when Screw Compression Systems, Inc. was merged into Natural Gas Services Group. After the merger in June 2007, Mr. Hazlett continues to remain employed by Natural Gas Services Group as Vice President-Technical Services. From 1982 to 1996 Mr. Hazlett served in management roles for Ingersoll Rand/Dresser Rand working with compression of all types in several different departments from sales and service to engineering. From 1978 to 1982 Mr. Hazlett was employed by the down-hole tool division of Hughes Tool designing and installing gas lift and plunger systems. Mr. Hazlett holds a Bachelor of Science degree from the College of Engineering at Texas A&M University and has over 37 years of industry experience.

## EXECUTIVE COMPENSATION

### Compensation Discussion and Analysis

#### *Compensation Discussion and Analysis*

The compensation discussion and analysis provides information regarding our executive compensation program in 2014 for the following executive officers of the Company (collectively, the "named executive officers").

Stephen C. Taylor, our Chairman, President, and Chief Executive Officer;  
G. Larry Lawrence, our Chief Financial Officer; and  
James R. Hazlett, our Vice President Technical Services.

#### *Introduction and Overview*

The Compensation Committee or, the "Committee," of the Board of Directors is responsible for determining the types and amounts of compensation we pay to our executives. The Committee operates under a written charter that you can view on our website at [www.ngsgi.com](http://www.ngsgi.com). The Board of Directors has determined that each member of the Committee meets the independence and financial literacy requirements of the NYSE. The Board determines, in its business judgment, whether a particular Director satisfies the requirements for membership on the Committee set forth in the Committee's charter. None of the members of the Committee are current or former employees of Natural Gas Services Group or any of its subsidiaries.

The Committee is responsible for formulating and administering our overall compensation principles and plans. This includes establishing the compensation paid to our CEO, meeting and consulting with our CEO to establish the compensation paid to our other executive officers, counseling our CEO as to different compensation approaches, administering our stock option plan, monitoring adherence to our compensation philosophy and conducting an annual, and sometimes more frequent, review of our compensation programs and philosophy regarding executive compensation.

The Committee periodically meets in executive session without members of management or management Directors present and reports to the Board of Directors on its actions and recommendations.

#### *Compensation Philosophy and Objectives*

Our compensation philosophy is to provide an executive compensation program that:

- rewards performance and skills necessary to advance our objectives and further the interests of our shareholders;
- is fair and reasonable and appropriately applied to each executive officer;
- is competitive with compensation programs offered by our competitors ; and
- serves as an adequate retention tool in a competitive market.

The overall objectives of our compensation philosophy are to:

- provide a competitive level of current annual income that attracts and retains qualified executives at a reasonable cost to us;
- retain and motivate executives to accomplish our company goals;
- provide long-term incentive compensation opportunities at levels appropriate for the respective responsibilities and performance of each executive;
- align compensation and benefits with our business strategies and goals;
- encourage the application of a decision making process that takes into account both short-term and long-term risks and the sometimes volatile nature of our industry; and
- align the financial interests of our executives with those of our shareholders through the potential grant of equity based rewards.

Our Committee supports these objectives by emphasizing compensation arrangements that we believe are reasonable and will attract and retain qualified executives and reward them for their efforts to further our long-term growth and success. At the same time, we remain cognizant of and aim to balance our executive compensation arrangements with the interests and concerns of our shareholders.

We have chosen to implement a relatively streamlined compensation framework for our executives. We feel that our compensation philosophies and practices are appropriate given our relatively small size as a public company. By continuing a relatively streamlined compensation framework for our executives, we believe that we are able to establish a higher degree of transparency, understanding and certainty for our executives as well as the investing public, while at the same time avoiding complex benefit packages and agreements that can be, in some ways, difficult to understand and require significant time and cost to properly administer. In the end, we believe our compensation arrangements provide the desired results: fair and reasonable pay for achievements beneficial to Natural Gas Services Group and its shareholders.

#### *Fiscal Year 2014 Performance*

In 2014, our financial performance continued to demonstrate strong growth that provided excellent shareholder value. Some of our financial and operational highlights include:

- increasing gross operating margins by 11.4% to \$53.8 million for 2014 from \$48.3 million for 2013;
- achieving in 2014 record high revenue of \$97 million, a 9.0% increase in revenue from 2013;
- a 7% increase in EBITDA;
- generating \$34.6 million from operations, while investing \$53.1 million in capital for equipment;
- controlling S,G&A expense to 10.6% of revenues;
- increasing rental revenue by 14.4%;
- internally funding over \$175 million in growth capital since 2010 while maintaining a very low debt level when compared to competitors;
- maintaining high margins and maintaining high ratios of operating income, net income, and EBITDA when compared to gross revenues relative to competitors;
- aggressive expansion into new geographic areas;
- positioning our business to emphasize servicing oil and gas production rather than drilling projects in order offset drilling slowdowns as witnessed in the latter half of 2014: and
- maintaining safety performance.

#### **Elements of Our Compensation Program**

In order to achieve the objectives set forth above in our compensation philosophy and objectives, we have structured an executive compensation program that provides our named executive officers with the following:

Element	Characteristics	Primary Objective
Base Salary	Cash	Attract and retain highly talented individuals
Short-Term Incentives	Cash-based performance awards	Reward for corporate and individual performance
Long-Term Incentives	Restricted stock with vesting period	Align the interests of our employees and shareholders by providing employees with incentive to perform technically and financially in a manner that promotes share price appreciation
Other Benefits	401(k) matching plans and employee health benefit plans	Provide benefits that promote employee health and support employees in attaining financial security

We do not presently and have not in the past used any of the following types of executive compensation:

- defined benefit pension plans;
- employee stock purchase/ownership plans;
- supplemental executive retirement plans/benefits; or
- deferred compensation plans.

#### *Assistance Provided to the Committee*

The Committee makes all compensation decisions regarding our executive officers. Stephen C. Taylor, our Chief Executive Officer, annually reviews the performance of each of our executive officers (other than the Chief Executive Officer whose performance is reviewed by the Committee) and presents recommendations to the Committee with respect to salary and cash bonus percentage adjustments and restricted stock grants for our executives (other than the Chief Executive Officer whose salary, cash bonus percentage adjustments and restricted stock grants are determined solely by the Committee). The Committee may exercise its discretion in modifying any recommendations made by our Chief Executive Officer.

The Committee also seeks the input and insight of Mr. Taylor concerning specific factors that Mr. Taylor believes to be appropriate for the Committee's consideration and which the Committee may not be aware of, such as extraordinary efforts or accomplishments of our executive officers. Mr. Taylor also advises the Committee on general topics such as the morale of our executives.

Natural Gas Services Group's accounting department assists the Committee in the compensation process by gathering and organizing data, which is then presented to the Committee by Mr. Taylor for the Committee's review.

In the past, our Committee had not used any outside compensation consultants due to our relative small size; however, in late 2012 our Committee hired an independent compensation consultant, Longnecker & Associates ("Longnecker"), to obtain objective, expert advice and assist with compensation matters for 2013 and 2014 concerning our Chief Executive Officer. Longnecker advised the Compensation Committee on a variety of compensation related issues in 2013 and 2014 with respect to our Chief Executive Officer, including:

- competitive pay analysis on executive compensation;
- pay levels of Chief Executive Officers; and
- our executive compensation program design, including short-term incentive plan design, long-term incentive plan design, and pay mix.

In the course of conducting its activities, Longnecker communicated with the Compensation Committee and presented its findings and recommendations for discussion. During 2014, Longnecker also met with our Chief Executive Officer to review its compensation report.

In 2014, Longnecker did not provide any services to the Company, or receive any payments from the Company, other than in its capacity as a consultant to the Compensation Committee. The Compensation Committee has assessed whether the services provided by Longnecker raised any conflicts of interest pursuant to the SEC rules, and has concluded that no such conflicts of interest existed during 2014.

## Competitive Pay Analysis

To evaluate the competitiveness of our Chief Executive Officer's base salary, target total cash compensation (i.e., base salary plus target short-term cash incentive award), long-term incentive awards, and total direct compensation (i.e. base salary, target short-term cash incentive award, and long-term incentive awards), Longnecker provided the Committee competitive pay information derived from a custom peer group (the "Custom Peer Group") and referred to a variety of published compensation surveys. The companies comprising the Custom Peer Group in Longnecker's January 2014 compensation report included:

### NGS Custom Peer Group

#### Company Name

#### Company Description

Gulfmark Offshore, Inc.	GulfMark Offshore, Inc. provides offshore marine support and transportation services primarily to companies involved in the offshore exploration and production of oil and natural gas.
Exterran Partners, LP	Exterran Partners, L.P. provides natural gas contract operations services to customers in the United States.
Dawson Geophysical Co.	Dawson Geophysical Company provides onshore seismic data acquisition and processing services in the United States.
Bolt Technology Corp.	Bolt Technology develops, manufactures and sells worldwide marine seismic data acquisition equipment and underwater remotely operated robotic vehicles used in offshore seismic exploration for oil and gas.
Pioneer Energy Services corp.	Pioneer Energy Services, through its subsidiaries, provides contract land drilling services and production services in the United States and Colombia.
Vaalco Energy, Inc.	VAALCO Energy, Inc., an independent energy company, together with its subsidiaries, engages in the acquisition, exploration, development, and production of crude oil and natural gas.
Team, Inc.	Team Inc. provides specialty industrial services in the United States, Canada, Europe, and internationally related to the construction, maintenance and monitoring of pressurized piping and associated systems in the refining, petrochemical, power, pipeline and other heavy industrial industries.
Tesco Corp.	Tesco Corporation, together with its subsidiaries, is engaged in the design, manufacture and service delivery of technology-based solutions for the upstream energy industry worldwide.
RigNet, Inc.	RigNet, Inc. provides remote communications services for the oil and gas industry.
Mitcham Industries, Inc.	Mitcham Industries, Inc., through its subsidiaries, engages in the leasing, sale, and service of geophysical and other equipment to the seismic industry worldwide.
USA Compression Partners, LP	USA Compression Partners provides natural gas compression services under term contracts with customers in the oil and gas industry in the U.S.
Warren Resources, Inc.	Warren Resources, Inc., an independent energy company, engages in the exploration, development, and production of onshore oil and natural gas reserves in the United States.
Flotek Industries Inc.	Flotek Industries develops and supplies drilling, completion and production technologies and related services to the energy and mining industries in the U.S. and internationally.

The Compensation Committee, with the assistance of the compensation consultant, reviewed the companies comprising the Custom Peer Group in order to maintain its appropriateness for the competitive pay analysis. These companies were generally selected since they are all companies in the energy and energy services industry and, the majority relatively similar annual revenues and market capitalization. The Compensation Committee believes the Custom Peer Group reflects our current competitors for employee talent and that it provides an appropriate peer set for the purposes of evaluating our pay practices and the Chief Executive Officer's pay levels.



The published compensation surveys consisted of the following:

- Economic Research Institute, 2013 ERI Executive Compensation Assessor
- Tower Watson, 2013/2014 Top Management Compensation
- Mercer, Inc., 2013 US General Benchmark
- Kenexa, 2013 CompAnalyst Benchmark Survey
- Longnecker & Associates, 2013 Long-term Incentive Survey
- WorldatWork, 2013/2014 Total Salary Increase Budget Survey

The Compensation Committee used the competitive pay information as a “market check” to ensure, in its subjective judgment, that the Chief Executive Officer’s base salary, target total cash compensation, long-term incentive awards and total direct compensation remain competitive. The Compensation Committee does not target any individual pay component to fall within a specific range or percentile of the competitive pay information. While the competitive pay information is important to the Compensation Committee’s approval process, it is just one of several factors considered by the Compensation Committee in approving executive compensation and the Compensation Committee has discretion in determining the nature and extent of its use.

#### *Individual and Company Performance - Base Salary and Equity Awards*

The Compensation Committee also evaluates compensation, particularly base salary levels and equity awards (restricted stock awards), through an analysis of each executive officer’s individual performance and the overall performance of Natural Gas Services Group, our goal being to strengthen the link between what we pay our executives and the performance of Natural Gas Services Group. Factors the Committee considers in our analysis include:

- the individual performance, leadership, business knowledge and level of responsibility of our officers;
- the particular skill-set and longevity of service of the officer;
- the effectiveness of the officer in implementing our overall strategy; and
- the general financial performance and health of the Company.

#### *Specific Company Financial Metrics - Cash Bonuses*

With respect to compensation we pay in the form of cash bonuses, the Committee sets target performance levels for three specific company financial metrics. The Committee relies on whether these targets are achieved and the individual performance of our executive officers to determine whether cash bonuses are awarded and the amounts of such bonuses. The three financial metrics the Committee considers are:

- total revenues;
- EBITDA; and
- net income before taxes.

EBITDA is calculated from our audited financial statements by adding to net income, or loss, (1) amortization and depreciation expense, (2) interest expense and (3) provision for income tax expense.

We believe that our core executive compensation mix of base salary, cash bonuses and equity awards, while fairly limited, presently provides enough diversity for us to link executive compensation to our short-term and long-term objectives. For instance, annual income is linked to short-term objectives and providing competitive salary levels to attract and retain top talent, while equity awards are more closely linked to the long-term objectives of earnings per share and increased market value of our common stock.

## *Base Salary*

We provide our executive officers and other employees with base salary to compensate them for services rendered during the fiscal year. Each year the Committee receives base salary recommendations from our Chief Executive Officer for all of our executive officers (other than our Chief Executive Officer whose base salary is evaluated by the Committee on an annual basis).

In January 2014, the Compensation Committee reviewed the 2013 performance of our Chief Executive Officer, Stephen C. Taylor, along with the competitive pay information provided in Longnecker's report in setting Mr. Taylor's base salary for 2014. Before the increase in salary for 2014, Mr. Taylor's base salary fell to slightly less than the 50<sup>th</sup> percentile bracket.

In connection with that review, the Committee increased the base salary of Mr. Taylor from \$459,250 in 2013 to \$505,175 in 2014, which moved Mr. Taylor's base salary to approximately the 56<sup>th</sup> percentile bracket. The increase was made in recognition of Mr. Taylor's leadership and contributions to the Company's strong 2013 financial and operational results, which included: (i) increasing gross operating margins by 10% from \$43.8 million to \$48.3 million; (ii) achieving in 2013 a 7.9% increase in revenue when 2012 is adjusted for a large non-reoccurring sale from the fleet, 9% increase in operating income; 13% increase in net income and a 13% increase in EBITDA; (iii) generating \$39.2 million from operations while investing \$43.3 million in capital for equipment, (iv) increasing earnings per share by 12%; (v) controlling S,G&A expense within the target of 9% of revenues; (vi) increasing rental revenue by 22%; increasing the Company's common stock price from approximately \$17 at the beginning of 2013 to approximately \$27.50 at the end of 2013, an increase of nearly 62%; and (vii) maintaining safety performance.

While the Compensation Committee reviewed the competitive pay information in connection with setting Mr. Taylor's base salary adjustments, together with his contributions toward our goals, the Compensation Committee did not target his base salary to fall within a specific range or percentile of the competitive pay information.

With respect to our other two named executive officers other than our CEO, James Hazlett, our Vice President of Technical Services, base salary for 2014 was \$190,000 compared to \$177,500 for 2013. The base salary of G. Larry Lawrence, our Vice President and Chief Financial Officer, for 2014, was \$170,000 compared to \$150,000 for most of 2013. We continue, as we have in the past, to rely on the following factors in evaluating and determining the amount of compensation we pay these executives:

- our general knowledge of executive compensation levels in the natural gas compression industry and similarly sized energy service companies;
- each executive's individual performance and the overall performance of Natural Gas Services Group; and
- specific company financial metrics and the application of specific weights to such metrics.

The applicability of these factors varies depending on the type of compensation being evaluated and determined. For instance, we do not rely on weighted company financial metrics to evaluate and determine base salary levels, but such factor is the primary means through which we evaluate and determine the amount of the cash bonuses we award to our executives. Below is a more detailed discussion of how these factors apply to the different types of compensation we utilize.

### *Short-Term Incentives - Annual Incentive Bonus Plan*

In 2006, the Committee adopted an Annual Incentive Bonus Plan or, the "IBP," that provides guidelines for the calculation of annual non-equity incentive based compensation in the form of cash bonuses to our executives, subject to Committee oversight and modification. The bonuses awarded under the IBP are short-term awards in recognition of the overall performance and efforts made by our executives during a particular year. Each year, the Committee approves the group of executives eligible to participate in the IBP and establishes target award opportunities for such executives. For 2014, the Committee modified Mr. Taylor's target award opportunity to up to 100% of his base salary. Target award opportunity was 45% of average base salary for Messrs. Lawrence and Hazlett.

In 2014, 90% of an executive officer's IBP award was based on achievement of company financial objectives relating to:

- total revenues;
- EBITDA; and
- net income before taxes.

Each of these three components accounts for 30% of the total company financial objective portion of the IBP. The remaining 10% of an executive officer's IBP award is based upon individual performance as evaluated by our CEO (except with respect to our CEO whose individual performance is evaluated by the Committee).

Each year, the Committee sets a target level for each component of the company financial objective portion of the IBP. The payment of awards under the IBP is based upon whether these target levels are achieved for the year. Payout on each of the three financial objectives is as follows:

- 75% of the bonus amount attributable to a financial component will be paid if we achieve at least 90% of the target amount;
- 100% of the bonus amount attributable to a financial component will be paid if we achieve at least 100% of the target amount; and
- 125% of the bonus amount attributable to a financial component will be paid if we achieve at least 110% of the target amount.

Thus, if we achieve 100% on each of the target levels for each of the three components of the company financial objective portion of the IBP, an executive with a base salary of \$100,000 and a target award opportunity of 40% will receive a cash bonus of \$40,000, assuming the executive receives the full amount (10%) of the individual performance portion of the IBP. If we do not achieve at least 90% of the target levels for all of the components, the Committee will decrease the target award opportunity for each executive officer by a percentage of up to 30% for each component in which there is a shortfall.

For instance, if we meet all target levels except that we achieve less than 90% of the target level for EBITDA, the Committee will decrease the executive's award opportunity by up to 30%. With respect to the executive described above, the award opportunity for such executive would be reduced from 40% to as low as 28% (the target bonus of 40% multiplied by 70%), in which case the executive would receive a cash bonus of \$28,000, assuming the executive receives the full amount of the individual performance portion of the IBP. Had we achieved at least 90% of the target level for EBITDA, but less than 100%, then the executive would receive 75% of the bonus amount attributable to EBITDA component, which would equate to an additional \$9,000 for a total bonus of \$37,000.

Similarly, if we achieve at least 110% of each of the three financial component targets, then the executive described above would receive a bonus of \$49,000 (\$4,000 for the individual performance portion plus \$45,000 for achieving at least 110% on each of the three financial components calculated by multiplying \$40,000 times 90% times 125%).

The following table sets forth the bonus financial criteria and target thresholds set by the Committee and compares such thresholds to actual performance achieved and the resulting bonus payout percentages earned in 2014:

#### 2014 Annual Incentive Bonus Plan

Bonus Criteria	Base Target	Actual Performance	% of Base Achieved	Base Target Payout
Revenue	\$ 100,000,000	\$ 96,974,300	97.0%	22.5%
Net Income before Taxes	23,627,000	22,158,000	93.8%	22.5%
EBITDA*	44,740,000	43,675,000	97.6%	22.5%
Personal Performance				10.0%
Total				77.5%

\* EBITDA is defined as the Company's earnings before interest, income taxes, depreciation, and amortization, and is an indicator of operating performance.

The following table sets forth the maximum bonus eligibility set by the Committee for 2014 for each of our named executive officers, and based upon the payout percentages noted in the table above, the bonus payout amount earned by each named executive for 2014 under our Annual Incentive Bonus Plan:

Name	Title	Base Salary	Max Bonus Eligibility	Max Bonus \$	Bonus Payout %	Bonus Payouts
Stephen C. Taylor	President & CEO	\$ 505,175	100%	\$ 505,175	77.5%	\$ 391,511
G. Larry Lawrence	Chief Financial Officer	\$ 170,000	45%	\$ 76,500	77.5%	\$ 59,288
James R. Hazlett	VP- Technical Services	\$ 190,000	45%	\$ 85,500	77.5%	\$ 66,263

As noted in the tables above, actual financial performance for 2014 fell short of each of the three financial metrics set for 2014, but actual results exceeded 90% of the financial metric, thereby entitling each of the named executive officers to 75% of 90% of the maximum bonus payout for each of the three financial metrics.

With respect to the personal performance criteria, the Committee awarded Messrs. Taylor, Lawrence and Hazlett the maximum amount payable under this component, or 10% of the maximum bonus amount that could have been earned in 2014. In addition to the Committee's non-quantitative evaluation of each executive's performance, with respect to all of the named executives, the Committee made this award in recognition of the Company's 2014 financial and operational performance.

With respect to Mr. Taylor's personal performance criteria, the Committee based its full award on (i) his successful strategic expansion into marketing our products to customers in oil shale plays and for his geographic expansion of our business; (ii) successful foresight and positioning of the Company to adjust capital outlays and production to mitigate the sudden downturn in business attributed to the plunging price of oil in the latter part of 2014; and (iii) his continuing to maintain superior cost control, industry leading margins in gross margin, operating income and EBITDA while doing so with a lean corporate staff designed to keep overhead costs down.

With respect to Mr. Lawrence's personal performance criteria, the Committee also based its full award on his success in converting to new COSO 2013 internal control framework ahead of schedule, managing cash flow required to fund \$53.1 million in capital expenditures and continuing to strengthen the Company's accounting and finance department as necessary to meet the demands of a public company.

With respect to Mr. Hazlett's personal performance criteria, the Committee also based its full award on his on-time and on-budget management of our compressor fabrication expansion in Midland, Texas, the successful ramp-up of rental equipment fabrication and his leadership of our product engineering and development activities.

Based on the foregoing, each of our named executive officers received bonus payouts of 77.5% of the maximum potential bonus amount (75% multiplied by 90% plus 10%).

#### *Long-Term Incentives - Restricted Stock Awards*

We consider restricted stock to be a type of long-term incentive compensation that motivates our executive officers to work toward our long-term growth and allows them to participate in the growth and profitability of Natural Gas Services Group. We believe that restricted stock aligns the interests of our executive officers with our shareholders in that our executive officers will benefit from the options only to the extent that the value of our common stock increases. With the exception of Mr. Taylor, our Chief Executive Officer, the number of shares of restricted stock granted to an executive officer is based on a subjective determination of an officer's individual performance and his current contributions and potential for future contributions to the overall performance of Natural Gas Services Group. In Mr. Taylor's employment agreement we have agreed to award Mr. Taylor a restricted stock award or equivalent equity awards in January of each year with an aggregate minimum value equal to at least 175% of his Base Salary, subject to one-year vesting terms and other standard terms which shall be established by the Compensation Committee taking into account the performance of the Company, Mr. Taylor and industry norms. Our compensation consultant concurred with our approach relating to long-term incentives and recommended that we continue the practice.

In 2009, we adopted the 2009 Restricted Stock/Unit Plan (the "Plan") and it went into effect upon its approval by our shareholders at our 2009 annual meeting. The Compensation Committee does not have any specific program or plan with regard to the timing or dating of restricted stock or unit grants. However, the Committee's practice will likely be to grant awards after

Natural Gas Services Group's annual earnings releases. We have not and do not plan to purposefully time the release of material non-public information for the purpose of affecting the value of executive compensation.

During the first quarter of 2015, the Company granted the following restricted stock awards in connection with our 2014 financial results and personal accomplishments of our named executive officers:

Name	Dollar Value of the Award	Number of Restricted Shares Awarded
Stephen C. Taylor, CEO and President	\$ 1,629,169	83,590
James R. Hazlett, Vice President - Technical Services	\$ 375,000	20,000
G. Larry Lawrence, Chief Financial Officer	\$ 375,000	20,000

Pursuant to Mr. Taylor's employment agreement, we are required to grant a restricted stock award or equivalent equity awards in January of each year with an aggregate minimum value equal to at least 175% of his Base Salary, subject to one-year vesting terms. See "*Compensation Agreements with Management*" beginning on page 35 of this Proxy Statement for information concerning Mr. Taylor's new employment agreement.

The Committee also reviewed Mr. Taylor's total compensation level along with Company's performance and Mr. Taylor's personal performance in connection with determining the value of the 2014 restricted stock award. As a result of the Committee's review, the Committee awarded Mr. Taylor (i) 48,760 shares of restricted common stock pursuant to the terms of his employment agreement and (ii) an additional \$34,830 shares of restricted common stock in recognition of our strong 2014 financial and operational results and performance, for a total award of 83,590 shares of restricted common stock. The restricted shares are subject to a one year vesting period, although such vesting is subject to acceleration and will immediately vest in the case of (i) death, disability or retirement of the recipient employee, or (ii) a change of control in the Company, as set forth in the Plan.

On March 19, 2015, the Compensation Committee awarded 20,000 shares of restricted common stock to each of G. Larry Lawrence, our Chief Financial Officer and James R. Hazlett, our Vice President - Technical Services. The restricted shares are subject to a one year vesting requirement from the date of grant. All of the restricted shares are subject to acceleration and will immediately vest in the case of (i) death, disability or retirement of the recipient employee, or (ii) a change of control in the Company, as set forth in the Plan.

The additional restricted shares which were issued to Mr. Taylor in excess of the 175% of his Base Salary obligation under the terms of his employment agreement, and the restricted stock awards to our other two named executive officers were made in recognition of the Company's financial and operation performance as set forth under "Fiscal Year 2014 Performance" on page 16 of this Proxy Statement.

Further information concerning these awards is set forth in column (i) of the "Summary Compensation Table" on page 26 and column (i) of the "Grants of Plan-Based Awards for Fiscal 2014" on page 28.

#### *Other Compensation*

We maintain a 401(k) retirement plan in which all of our executives and employees are eligible to participate. We match executive and employee contributions to our 401(k) plan, on an equal percentage basis, with cash contributions. The Company matching portion is equal to one-half of the employee's annual contribution up to a maximum of 3% of the employee's salary. Our matching amounts for our executive officers are included in column (i) of the "Summary Compensation Table" on page 26.

Other than the reductions that can occur with respect to the target award opportunities of our executives under our Annual Incentive Bonus Plan, we do not have a written policy or formula regarding the adjustment, reduction or recovery of awards or payments if company performance measures are restated or adjusted in a manner that would reduce the award or payment. However, the Committee does consider compensation realized or potentially realizable from prior compensation awards in setting new types and amounts of compensation, the result of such consideration being varying increases in annual salaries and cash bonuses, with percentage increases in some cases being smaller than previous years.

### *Total Direct Compensation*

In determining the extent to which our chief executive officer compensation program meets the Committee's compensation philosophy and objectives, the Committee emphasizes the competitiveness of total compensation (the aggregate of base salary, annual cash bonus incentive payment, and the grant value of long-term incentive plan award). In reviewing the Custom Peer Group data from Longnecker's study and discussing with Longnecker the pay practices of our peers, the Committee targeted its total compensation for Mr. Taylor, our Chief Executive Officer, at approximately the 75<sup>th</sup> percentile bracket considering our 2014 financial and operational which have been noted above.

### *Employment Agreements*

We employed Mr. Taylor in January 2005. On October 23, 2013, we entered into a new written employment agreement with Stephen C. Taylor, our President and Chief Executive Officer. We do not have written employment agreements with any of our other executive officers. On April 24, 2015, we entered into an amendment with Mr. Taylor to his Employment Agreement pursuant to which the "modified single trigger" change of control provision was changed to a "double trigger" change of control. Under the "modified single trigger provision", Mr. Taylor could voluntarily terminate the Employment Agreement for any reason immediately upon a change in control and collect severance benefits. Under the new "double trigger" change of control provision, a change of control must occur followed by the Company or its successor terminating Mr. Taylor's employment other than for cause, death, or disability, or by Mr. Taylor terminating his employment for Good Reason. See "*Compensation Agreements with Management*" beginning on page 35 of this Proxy Statement for detailed information concerning Mr. Taylor's employment agreement, as amended.

### *Allocation of Amounts and Types of Compensation*

Other than the restricted stock awards we grant to our executives from time to time and the determinations made by the Committee as to specific target award opportunities under our IBP, the allocation of different amounts and types of compensation has not been a consideration for us, except with respect to our Chief Executive Officer whose employment agreement requires an annual restricted stock award or similar equity award with a value of at least 175% of his base salary. The Committee has not adopted a specific policy or target for the allocation between amounts or types of compensation. We believe that the use of stock awards in our compensation package will align the interests of our management and employees with our stockholders. Notwithstanding moderately increasing the use of stock-based compensation, we intend to maintain and continue our practice of having a simplified, but effective and competitive, compensation package.

### *Change of Control and Severance Arrangements*

Our 1998 Stock Option Plan, as amended, and our 2009 Restricted Stock/Unit Plan contains change of control provisions. In addition, Mr. Taylor's employment agreement contains change of control and severance provisions. Information regarding these provisions is provided under the caption "Potential Payments Upon Termination or Change of Control" on page 32.

### *Stock Ownership/Retention Guidelines*

We have not in the past had written guidelines or policy statements that required our executives to maintain specified levels of stock ownership or adhere to specified "holding" practices with regard to our common stock.

### *Perquisites*

We provide limited perquisites to our executives. The primary perquisites include allowing our executives a choice of receiving an automobile allowance or personal use of a company-provided automobile and matching contributions made by Natural Gas Services Group under our 401(k) plan. Although we provide Mr. Taylor with one club membership, since his use of the club is limited solely for business entertainment, we have not considered it to be a perquisite and have not valued it as such for inclusion in column (i) of the "Summary Compensation Table" on page 26.

Our executives also participate in the same medical, dental and life insurance plans as other employees. However, we pay a greater percentage of the premiums for health insurance for our executives than we do for our other employees.

### *Limit on Deductibility of Certain Compensation*

Provisions of the Internal Revenue Code that restrict the deductibility of certain compensation over \$1 million dollars per year have not been a factor in our considerations or recommendations. Section 162(m) of the Code currently imposes a \$1 million limitation on the deductibility of certain compensation paid to specified executives. Excluded from the limitation is compensation that is “performance based.” For compensation to be performance based, it must meet certain criteria, including being based on predetermined objective standards approved by shareholders. The Committee has not taken the requirements of Section 162(m) into account in designing executive compensation.

### *Say-on-Pay*

At our 2014 Annual Meeting of Stockholders held in June 2014, we submitted a proposal to our stockholders regarding our executive compensation practices. The proposal was an advisory vote on the 2013 compensation awarded to our named executive officers (commonly known as a “say-on-pay” vote). Excluding broker non-votes, our stockholders approved our 2013 compensation with 67.6% of the shares that voted on the proposal voted in favor.

We believe that the outcome of our say-on-pay vote indicates our stockholders' support of our compensation approach, specifically our efforts to retain and motivate our named executive officers. In light of this stockholder support, the Committee determined not to change its approach to 2014 compensation as described in this proxy statement. The Compensation Committee will continue to consider the outcome of say-on-pay votes when making future compensation decisions for our named executive officers.

### **Compensation Committee Report**

The Committee has reviewed and discussed the Compensation Discussion and Analysis with management. Based on its review and discussions, the Committee recommended to the Board of Directors that the Compensation Discussion and Analysis be included in our proxy statement for the 2015 Annual Meeting of Shareholders.

#### Members of the Compensation Committee

William F. Hughes, Jr. (Chairman)  
John W. Chisholm  
David L. Bradshaw

## Executive Compensation

The table below sets forth the compensation earned by, and paid to our CEO, Stephen C. Taylor, and our other named executive officers for services rendered to us for the fiscal years ended December 31, 2014, 2013 and 2012.

**Summary Compensation Table**

Name and Principal Position (a)	Year (b)	Salary (c)	Bonus <sup>(1)</sup> (d)	Stock Awards <sup>(2)</sup> (e)	Option Awards <sup>(3)</sup> (f)	Non-Equity Incentive Plan Compensation <sup>(4)</sup> (g)	Change in Pension Value and Nonqualified Deferred Compensation Earnings (h)	All Other Compensation <sup>(5)</sup> (i)	Total (j)
Stephen C. Taylor, Chairman, President & CEO	2014	\$ 540,949	\$ 7,267	\$ 1,629,169	\$ —	\$ 391,511	\$ —	\$ 14,444	\$ 2,583,340
	2013	444,798	8,405	1,389,196	86,860 <sup>(6)</sup>	444,324	—	15,752	2,389,335
	2012	411,211	3,786	1,148,821	139,518 <sup>(7)</sup>	409,150	—	14,277	2,126,763
G. Larry Lawrence, Chief Financial Officer	2014	180,708	2,445	375,000	16,910 <sup>(8)</sup>	59,288	—	12,645	646,996
	2013	152,308	3,020	456,150	16,899 <sup>(9)</sup>	66,854	—	13,573	708,804
	2012	129,687	1,356	187,500	16,910 <sup>(10)</sup>	60,256	—	12,517	408,226
James R. Hazlett, Vice President, Technical Services	2014	200,228	3,574	375,000	33,809 <sup>(11)</sup>	66,263	—	29,259	708,133
	2013	180,989	3,574	456,150	33,819 <sup>(12)</sup>	76,325	—	30,119	780,976
	2012	163,350	1,549	187,500	72,758 <sup>(13)</sup>	70,036	—	30,033	525,226

- (1) The amounts reflected in column (d) reflect payments under the company's profit sharing program administered to all employees.
- (2) The amounts in column (e) reflect the grant date fair value of stock granted under our 2009 Restricted Stock/Unit Plan.
- (3) The amounts in column (f) reflect the dollar amounts recognized for financial statement reporting purposes for the fiscal years ended December 31, 2012, 2013 and 2014, in accordance with FASB ASC Topic 718, associated with stock option grants under our 1998 Stock Option Plan. Assumptions used to calculate these amounts are included in footnote 8 for our audited financial statements for the fiscal year ended December 31, 2012; footnote 8 for our audited financial statement for fiscal year ended December 31, 2013; and footnote 8 for our audited financial statement for fiscal year ended December 31, 2014.
- (4) The amounts in column (g) reflect the cash bonus awards to the named executive officers under our Annual Incentive Bonus Plan, which is discussed in further detail on page 20 under the caption "Short-Term Incentives - Annual Incentive Bonus Plan."
- (5) The amounts shown in column (i) include matching contributions made by Natural Gas Services Group to each named executive officer under our 401(k) plan and the aggregate incremental cost to Natural Gas Services Group of perquisites provided to our named executive officers as follows:



Name	Year	Automobile Allowance	Personal Use of Company Provided Automobiles	Additional Incremental Portion of Health Insurance Premiums Paid for Officers Only	401(k) Plan	Total <sup>(a)</sup>
Stephen C. Taylor	2014	\$ —	\$ 1,800	\$ 7,285	\$ 5,359	\$ 14,444
	2013	—	1,800	6,715	7,237	15,752
	2012	—	1,237	6,716	6,324	14,277
G. Larry Lawrence	2014	10,200	—	—	2,445	12,645
	2013	10,200	—	—	3,373	13,573
	2012	9,808	—	—	2,709	12,517
James R. Hazlett	2014	10,200	—	16,463	2,596	29,259
	2013	10,200	—	15,828	4,091	30,119
	2012	10,200	—	15,828	4,005	30,033
Total	2014	20,400	1,800	23,748	10,400	56,348
	2013	20,400	1,800	22,543	14,701	59,444
	2012	20,008	1,237	22,544	13,038	56,827

- (6) This amount reflects the dollar amount recognized for financial statement reporting purposes for the fiscal year ended December 31, 2013, in accordance with FASB ASC Topic 718, for 10,000 shares of common stock that vested on January 18, 2013 under the stock option granted to Mr. Taylor on January 18, 2010.
- (7) This amount reflects the dollar amount recognized for financial statement reporting purposes for the fiscal year ended December 31, 2012, in accordance with FASB ASC Topic 718, for (a) 10,000 shares of common stock that vested on January 28, 2012 under the stock option granted to Mr. Taylor on January 28, 2009, (b) 10,000 shares of common stock that vested on January 18, 2012 under the stock option granted to Mr. Taylor on January 18, 2010.
- (8) This amount reflects the dollar amount recognized for financial statement reporting purposes for the fiscal year ended December 31, 2014, in accordance with FASB ASC Topic 718, for 1,667 shares of common stock that vested on January 24, 2014 under the stock option granted to Mr. Lawrence on January 24, 2011.
- (9) This amount reflects the dollar amount recognized for financial statement reporting purposes for the fiscal year ended December 31, 2013, in accordance with FASB ASC Topic 718, for 1,666 shares of common stock that vested on January 24, 2013 under the stock option granted to Mr. Lawrence on January 24, 2011.
- (10) This amount reflects the dollar amount recognized for financial statement reporting purposes for the fiscal year ended December 31, 2012 in accordance with FASB ASC Topic 718, for 1,667 shares of common stock that vested on January 24, 2012 under the stock option granted to Mr. Lawrence on January 24, 2011.
- (11) This amount reflects the dollar amount recognized for financial statement reporting purposes for the fiscal year ended December 31, 2014, in accordance with FASB ASC Topic 718, for 3,333 shares of common stock that vested on January 24, 2014 under the stock option granted to Mr. Hazlett on January 24, 2011.
- (12) This amount reflects the dollar amount recognized for financial statement reporting purposes for the fiscal year ended December 31, 2013, in accordance with FASB ASC Topic 718, for 3,334 shares of common stock that vested on January 24, 2013 under the stock option granted to Mr. Hazlett on January 24, 2011.
- (13) This amount reflects the dollar amount recognized for financial statement reporting purposes for the fiscal year ended December 31, 2012 in accordance with FASB ASC Topic 718, for (a) 3,333 shares of common stock that vested on December 9, 2012 under the stock option granted to Mr. Hazlett on December 9, 2009, and (b) 3,333 shares of common stock that vested on January 24, 2012 under the stock option granted to Mr. Hazlett on January 24, 2011.

## Grants of Plan Based Awards

The table below sets forth the estimated future payouts under non-equity incentive plan awards and restricted stock awards granted and the grant date fair value of such awards.

### Grants of Plan-Based Awards for Fiscal 2014

Name	Grant Date	Estimated Future Payouts Under Non-Equity Incentive Plan Awards <sup>(1)</sup>			Estimated Future Payouts Under Equity Incentive Plan Awards			All Other Stock Awards: Number of Shares of Stock or Units (#) <sup>(2)</sup>	All Other Option Awards: Number of Securities Underlying Option (#)	Exercise or Base Price of Option Awards (\$/Sh)	Grant Date Fair Value of Stock and Option Awards (\$)
		Threshold (\$)	Target (\$)	Maximum (\$)	Threshold (#)	Target	Maximum (\$)				
(a)	(b)	(c)	(d)	(e)	(f)	(g)	(h)	(i)	(j)	(k)	(l)
Stephen C. Taylor	1/15/2015	—	—	—	—	—	—	83,590	—	\$ 19.49	\$ 1,629,169
G. Larry Lawrence	3/19/2015	—	—	—	—	—	—	20,000	—	18.75	375,000
James R. Hazlett	3/19/2015	—	—	—	—	—	—	20,000	—	18.75	375,000

- (1) No awards were made under the non-equity Incentive Plan for 2014 except as described of the performance goals under our Annual Incentive Bonus Plan, or the "IBP." More information regarding the IBP and the calculation of awards is provided below and under the caption "Short-Term Incentives - Annual Incentive Bonus Plan" on page 21.
- (2) The information shown in this column reflects awards of restricted stock earned in 2014 (but issued in early 2015) our named executive officers pursuant to our 2009 Restricted Stock/Unit Plan.

The table below sets forth the estimated future payouts under non-equity incentive plan awards and restricted stock awards granted and the grant date fair value of such awards.

## Annual Incentive Bonus Plan

Our Annual Incentive Bonus Plan or, the "IBP," provides for annual non-equity incentive based compensation in the form of cash bonuses to our executive officers. Our Compensation Committee administers and determines from year to year the executives that are eligible to participate in the IBP. The Committee establishes target award opportunities for the executives eligible to participate in the plan. These target award opportunities are expressed as a percentage of an executive's base salary. An executive's target award opportunity is the maximum cash bonus an executive is eligible to receive in any one year under the IBP.

The Committee establishes annual target levels for Natural Gas Services Group's total revenues, EBITDA and net income before taxes and assigns a weight of 30% to each of these components. The executive's individual performance is assigned a weight of 10%. If during the year Natural Gas Services Group achieves all of the target levels established by the Committee for total revenues, EBITDA and net income before taxes, and it is determined by the Committee that an executive is entitled to the full 10% weight assigned to individual performance, the executive is entitled to receive the maximum cash bonus amount for the executive for that year. If any one of the target levels is not met or it is determined that an executive is not entitled to the full 10% weight assigned to individual performance, the cash bonus award for the executive is reduced accordingly. More information regarding the IBP and the calculation of awards is provided under the caption "Short-Term Incentives – Annual Incentive Bonus Plan" on page 21.

## 1998 Stock Option Plan

Our 1998 Stock Option Plan provides for the issuance of stock options to purchase up to 750,000 shares of our common stock. The purpose of this plan is to attract and retain the best available personnel for positions of substantial responsibility and to provide long-term incentives to employees and consultants and to promote the long-term growth and success of our business. The plan is administered by the Compensation Committee of the Board of Directors. At its discretion, the Compensation Committee determines the persons to whom stock options may be granted and the terms upon which options will be granted. In addition, the Compensation Committee may interpret the plan and may adopt, amend and rescind rules and regulations for its administration. Option awards are generally granted with an exercise price equal to the closing price of our common stock at the date of grant and generally vest based on three years of continuous service and have ten-year contractual terms.

As of December 31, 2014, stock options to purchase a total of 432,269 shares of our common stock were outstanding under the 1998 Stock Option Plan. There were no shares included that relate to our non-employee directors under the compensation arrangements described under the caption “Compensation of Directors” on page 34.

A total of 186,419 shares of common stock were available at December 31, 2014 for future grants of stock options under the 1998 Stock Option Plan. Since the beginning of 2015, we have issued options for 50,000 shares of common stock which has left 136,419 shares available under the 1998 Stock Option Plan as of the date of this proxy statement.

## 2009 Restricted Stock/Unit Plan

The purpose of our 2009 Restricted Stock/Unit Plan (the “2009 Plan”) is to retain our employees and directors having experience and ability, to attract new employees and directors whose services are considered valuable, to encourage the sense of proprietorship, and to stimulate the active interest of such persons in our development and financial success. We believe that grants of restricted stock and restricted stock units are an increasingly important means to retain and compensate employees and directors.

### *General Description*

*Shares Reserved for Issuance under the 2009 Plan.* A total of 800,000 shares of our common stock are reserved for issuance under the 2009 Plan. The number of shares of our common stock available under the 2009 Plan will be subject to adjustment in the event of a stock split, stock or other extraordinary dividend, or other similar change in our common stock or capital structure.

*Administration.* The Plan is administered by the plan administrator, defined as one or more committees the Company designates consisting of independent directors. The draft of the Plan appoints our Compensation Committee as the administrator (the “Committee”).

Generally, the Committee has the authority, in its discretion, (a) to select officers, directors and employees to whom awards may be granted from time to time, (b) to determine whether and to what extent, awards are granted, (c) to determine the number of shares of our common stock, or the amount of other consideration to be covered by each award, (d) to approve award agreements for use under the Plan, (e) to determine the terms and conditions of any award (including the vesting schedule applicable to the award), (f) to amend the terms of any outstanding award granted under the Plan, (g) to construe and interpret the terms of the Plan and awards granted, and (h) to take such other action not inconsistent with the terms of the Plan, as the Committee deems appropriate.

*Types of Awards; Eligibility.* Awards of restricted stock and restricted stock units (RSUs) may be granted under the Plan. Awards of restricted stock are shares of our common stock that are awarded subject to such restrictions on transfer as the Committee may establish. Awards of RSUs are units valued by reference to shares of common stock that entitle a participant to receive, upon the settlement of the unit, one share of our common stock for each unit. Awards may be granted to our officers, directors and employees and our related entities, if any. Each award granted under the Plan shall be designated in an award agreement.

*Terms and Vesting of Awards.* As noted above, the Committee determines the terms and conditions of each award granted to a participant, including the restrictions applicable to shares underlying awards of restricted stock and the dates these restrictions lapse and the award vests, as well as the vesting and settlement terms applicable to RSUs. When an award vests, we deliver to the participant a certificate for the number of shares without any legend or restrictions (except as necessary to comply with applicable state and federal securities laws).

In addition to time-based vesting requirements, the Committee is also authorized to establish quantitative and qualitative performance goals in order for awards to vest. For instance, quantitative performance standards, including, but not limited to, financial measurements such as (a) increase in share price, (b) earnings per share, (c) total shareholder return, (d) operating margin, (e) gross margin, (f) return on equity, (g) return on assets, (h) net operating income, (i) pre-tax profit, (j) cash flow, (k) revenue, (l) expenses, and (m) EBITDA, or other performance goal requirements may be adopted by the Committee and set forth in the particular restricted stock or RSU agreement which must be met in order for shares to vest.

*Termination of Service.* Unless otherwise set forth in an individual award agreement, the Plan and forms of award agreements provide that in the event a participant's continuous service with us terminates as a result of death, disability or retirement (an "Acceleration Event"), unvested shares or RSUs at the time of termination due to an Acceleration Event will immediately become vested, but only to the extent that such unvested shares or RSUs would have vested within the 12 months following the Acceleration Event. However, the Committee may revise this default provision on an individual basis as it deems advisable. For example, the Committee could elect to accelerate vesting for all unvested shares and/or RSUs upon the occurrence of an Acceleration Event, or conversely provide that all unvested shares and/or RSUs are forfeited upon the occurrence of an Acceleration Event. In the case of a termination of service other than by an Acceleration Event, any unvested shares or RSUs will immediately become null and void, except that with respect to Restricted Stock awards, the Board of Directors may vest any or all unvested shares in its discretion in the case of any termination of service.

In addition, subject to revision by the Committee, the default provisions of the Plan and form of award agreements provide that a Change of Control triggers accelerated vesting of all shares or units. Under the 2009 Plan, a Change in Control Event is generally defined as:

- a complete liquidation or dissolution;
- acquisition of 50% or more of our stock by any individual or entity including by tender offer or a reverse merger;
- a merger or consolidation in which we are not the surviving entity; or
- during any period not longer than 12 consecutive months, members of the Board who at the beginning of such period cease to constitute at least a majority of the Board, unless the election, or the nomination for election of each new Board member, was approved by a vote of at least 3/4 of the Board members then still in office who were Board members at the beginning of such period.

*Restricted Stock.* Under an award of restricted stock, we issue shares of our common stock in the participant's name; however, the participant's rights in the stock are restricted until the shares vest. If the vesting requirements are not met prior to the end of the vesting period, the shares are forfeited. In connection with an award of restricted stock, since actual shares are issued and outstanding, the participant is legally entitled to vote the shares and receive any dividends declared and paid on our common stock prior to the satisfaction of the vesting requirements. However, as discussed above, Participants who hold unvested restricted stock may not sell, assign or transfer such shares until they have vested.

*Restricted Stock Units.* Like a restricted stock award, a restricted stock unit is a grant valued in terms of our common stock. Unlike a restricted stock award, none of our common stock is issued at the time the RSU award is granted. Instead, the award is a mere promise to deliver shares of our common stock upon satisfaction of the vesting requirements. Upon satisfaction of the vesting requirements of the award, we then issue and deliver the number of shares subject to the award. If the vesting requirements are not satisfied prior to the end of the vesting period, the units expire and no shares are issued. Since shares of our common stock are not issued in connection with RSUs until such time as the vesting conditions have been satisfied, participants in the Plan who receive awards of RSUs will not have any voting rights and will not be entitled to dividends until such time as the units vest and shares of our common stock are issued.

*Amendment, Suspension or Termination of the Plan.* We may at any time amend, suspend or terminate the Plan. The Plan will be for a term of ten (10) years unless sooner terminated. Awards may be granted under the Plan upon it becoming effective, but awards granted prior to obtaining shareholder approval will be rescinded if the shareholders do not approve the Plan. We may amend the Plan subject to compliance with applicable provisions of federal securities laws, state corporate and securities laws, the Internal Revenue Code, and the rules of the NYSE (or such other stock exchange as our common stock may be traded upon at the time).

*Change in Capitalization.* Subject to any required action by our shareholders, the number of shares of common stock covered by outstanding awards, the number of shares of common stock that have been authorized for issuance under the 2009 Plan, the exercise or purchase price of each outstanding award, the maximum number of shares of common stock that may be granted subject to awards to any participant in a calendar year, and the like, shall be proportionally adjusted by the Committee in

the event of: (i) any increase or decrease in the number of issued shares of common stock resulting from a stock split, stock dividend, combination or reclassification or similar event affecting our common stock; (ii) any other increase or decrease in the number of issued shares of common stock effected without receipt of consideration by us; or (iii) any other transaction with respect to common stock including a corporate merger, consolidation, acquisition of property or stock, separation (including a spin-off or other distribution of stock or property), reorganization, liquidation (whether partial or complete), distribution of cash or other assets to shareholders other than a normal cash dividend, or any similar transaction; provided, however, that conversion of any of our convertible securities shall not be deemed to have been “effected without receipt of consideration.” Except as the Committee determines, no issuance by us of shares of any class, or securities convertible into shares of any class, shall affect, and no adjustment by reason hereof shall be made with respect to, the number of shares of common stock subject to an award.

As of April 14, 2015, we had issued 471,841 shares of restricted stock under the 2009 Plan, of which 313,131 have vested and become unrestricted.

### Outstanding Equity Awards at Fiscal Year-End

The following table shows certain information about stock options outstanding as of December 31, 2014 and held by our Chief Executive Officer, Stephen C. Taylor, and each other named executive officer.

#### Outstanding Equity Awards at 2014 Fiscal Year-End

Name (a)	Option Awards					Stock Awards			
	Number of Securities Underlying Unexercised Options (#) Exercisable (b)	Number of Securities Underlying Unexercised Options (#) Unexercisable (c)	Equity Incentive Plan Awards: Number of Securities Underlying Unexercised Options (#) (d)	Option Exercise Price (\$) (e)	Option Expiration Date (f)	Number of Shares of Stock That Have Not Vested (#) (g)	Market Value of Shares of Stock that Have Not Vested (\$) (h)	Equity Incentive Plan Awards: Number of Unearned Shares or Other Rights that Have Not Vested (#) (i)	Equity Incentive Plan Awards: Market or Payout Value of Unearned Shares or Other Rights that Have Not Vested (\$) (j)
Stephen C. Taylor	45,000	—	—	\$ 9.22	8/26/2015	—	—	—	—
	15,000	—	—	\$ 14.22	11/21/2016	—	—	—	—
	40,000	—	—	\$ 20.06	1/15/2018	—	—	—	—
	25,000	—	—	\$ 17.51	9/10/2018	—	—	—	—
	30,000	—	—	\$ 9.95	1/28/2019	—	—	—	—
	23,852	—	—	\$ 7.84	3/17/2019	—	—	—	—
	30,000	—	—	\$ 19.90	1/18/2020	—	—	—	—
	—	—	—			49,420	\$ 1,389,196	—	—
G. Larry Lawrence	5,000	—	—	\$ 17.81	1/24/2021	—	—	—	—
	—	—	—			3,333	\$ 49,628	—	—
	—	—	—			15,000	\$ 456,150	—	—
James R. Hazlett	5,000	—	—	\$ 17.51	9/10/2018	—	—	—	—
	10,000	—	—	\$ 17.74	12/9/2019	—	—	—	—
	10,000	—	—	\$ 17.81	1/24/2021	—	—	—	—
	—	—	—			3,333	\$ 49,628	—	—
	—	—	—			15,000	\$ 456,150	—	—

## Option Exercises and Stock Vested in 2014

In the table below, we show certain information about (i) the number of shares of common stock acquired upon exercise of stock options by each of the named executive officers in 2014 and the value realized on exercise of the stock options and (ii) stock awards.

Name (a)	Option Awards		Stock Awards	
	Number of Shares Acquired on Exercise (#) (b)	Value Realized on Exercise (\$) (c)	Number of Shares Acquired on Vesting (d)	Value Realized on Vesting (e)
Stephen C. Taylor	—	—	56,950	\$ 1,747,796
G. Larry Lawrence	—	—	15,001	455,680
James R. Hazlett	—	—	15,001	455,680

## Potential Payments Upon Termination or Change of Control

Our 1998 Stock Option Plan and 2009 Restricted Stock/Unit Plan contains “change of control” provisions. These provisions are designed to provide some assurance that we will be able to rely upon each executive’s services and advice as to the best interests of Natural Gas Services Group and our shareholders without concern that the executive might be distracted by the personal uncertainties and risks created by any proposed or threatened change of control and to promote continuity of our executive team.

Under our stock option plan, the Committee may adjust the stock options held by our executives upon the occurrence of a change of control. With this authority, the Committee may in its discretion elect to accelerate the vesting of any stock options that were not fully vested and allow for the exercise of such options as to all shares of stock subject thereto.

Likewise, under our 2009 Restricted Stock/Unit Plan, a change in control will accelerate the vesting of all awards under the plan unless the Committee has provided otherwise in a particular award under the plan. In addition, upon death, disability or retirement, any vesting or other restrictions on the restricted stock awards will accelerate or lapse such that all shares underlying a restricted stock award will become unencumbered.

As noted in the tables above and summarized below, our named executive officers have stock options and restricted stock awards which are subject to certain vesting requirements.

At December 31, 2014, our named executive officers had the following number of unvested restricted stock awards which were subject to forfeiture as of that date:

- Stephen C. Taylor -- 49,420 shares
- G. Larry Lawrence -- 18,333 shares
- James R. Hazlett -- 18,333 shares

Each of these restricted stock awards could have become vested and issued without restrictions on December 31, 2014 assuming a change of control were to have occurred on that date. In addition, the restricted stock awards would have been issued without restrictions on December 31, 2014, assuming the named executive officer had died, became disabled or retired. The closing price of our common stock on December 31, 2014, was \$23.04 per share. Accordingly, on December 31, 2014, had there been a change in control event or had the named executive officer died, became disabled or retired, the vesting terms of the restricted stock awards would have lapsed and the shares would have become unrestricted. As a result, there was a potential for Messrs. Taylor, Hazlett and Lawrence to realize immediate value upon the lapse of restrictions on restricted stock awards as follows: Mr. Taylor --\$1,138,637; Mr. Hazlett --\$422,392; and Mr. Lawrence --\$422,392.

As described under “Compensation Agreements with Management” on page 35, we entered into a written employment agreement with Stephen C. Taylor, President, Chief Executive Officer and Chairman of the Board in October 2013. Under the employment agreement, Mr. Taylor is eligible for certain benefits in connection with a change in control. These provisions were included in Mr. Taylor’s initial employment agreement with us and were continued in his current agreement as part of our

negotiations with Mr. Taylor as to the terms of his employment and as an inducement for him to continue his employ with our company. The change of control and severance provisions were designed to promote stability and continuity with respect to Mr. Taylor's employment as our Chief Executive Officer and President.

The following table summarizes the benefits in effect as of December 31, 2014 that Mr. Taylor would receive assuming that a qualifying termination (i.e., a termination described in footnote 2 below) in connection with a change in control, death or disability or a termination by the Company without cause, or a voluntary termination by Mr. Taylor with and without good reason, occurred on December 31, 2014. Those payments that are available generally to salaried employees that do not discriminate in scope, terms or operation in favor of executive officers are also not included in this table.

**Chief Executive Officer Potential Payments Table**

Named Executive Officer	Qualifying Termination in Connection with a change in Control, Voluntary Resignation with Good Reason, or Termination by Company without Cause (1) (\$)	Death or Disability (2) (\$)	Termination by Company with Cause, Voluntary Termination without Good Reason (\$)	Retirement (2) (\$)
Stephen C. Taylor				
Acceleration of Unvested Restricted Stock Units (3)	\$ 1,138,637	\$ 1,138,637	\$ —	\$ 1,138,637
Severance	3,409,931	—	—	—
Medical, Dental, and Vision Benefits	34,362	—	—	—
Life Insurance Premiums	907	—	—	—
<b>TOTAL</b>	<b>4,583,837</b>	<b>1,138,637</b>	<b>—</b>	<b>1,138,637</b>

- (1) See "Compensation Agreements with Management" beginning on page 35 for definitions and discussion of Mr. Taylor's severance package in connection with termination due to change of control, voluntary resignation with good reason or termination by the Company without cause.
- (2) In the event of Mr. Taylor's employment terminates on account of death, disability, or qualified retirement, 100% of unvested Restricted Stock awards will immediately vest.
- (3) The value attributable to the acceleration of unvested Restricted Stock awards is based upon the number of awards multiplied by the closing price of our common stock (\$23.04) on December 31, 2014.

## Compensation of Directors

We use a combination of cash and equity-based incentive compensation to attract and retain qualified candidates to serve on our Board of Directors. In setting compensation for our Directors, we consider the substantial amount of time that Directors expend in fulfilling their duties to us and our shareholders, as well as the skill-sets required to fulfill these duties.

The following table discloses the cash, equity awards and other compensation earned, paid or awarded, as the case may be, to each of our non-employee Directors during the fiscal years ended December 31, 2014, 2013 and 2012.

Name	Year	Fees Earned Or Paid (\$) <sup>(1)</sup>	Stock Awards (\$) <sup>(2)</sup>	Option Awards (\$)	Non-Equity Incentive Plan Compensation (\$)	Change in Pension Value and Nonqualified Deferred Compensation Earnings	All Other Compensation (\$)	Total (\$)
(a)		(b)	(c)	(d)	(e)	(f)	(g)	(h)
Charles G. Curtis	2014	\$ 50,000	\$ 68,944	\$ —	\$ —	\$ —	\$ —	\$ 118,944
	2013	30,000	46,875	—	—	—	—	76,875
	2012	25,000	33,575	—	—	—	—	58,575
David L. Bradshaw	2014	60,000	68,944	—	—	—	—	128,944
	2013	40,000	46,875	—	—	—	—	86,875
	2012	33,333	37,003	—	—	—	—	70,336
John Chisholm	2014	50,000	68,944	—	—	—	—	118,944
	2013	30,000	46,875	—	—	—	—	76,875
	2012	25,000	33,575	—	—	—	—	58,575
William F. Hughes	2014	60,000	68,944	—	—	—	—	128,944
	2013	40,000	46,875	—	—	—	—	86,875
	2012	33,333	33,575	—	—	—	—	66,908

- (1) Our non-employee Directors are paid a quarterly cash fee for their attendance at each meeting of our Board of Directors. The cash fee payable to our non-employee Directors for 2014 was \$11,250 per quarter. Each of our non-employee Directors received a cash fee payment of \$11,250 for the four quarters in 2014, totaling \$45,000. In addition, (i) the Chairman of the Audit Committee, David L. Bradshaw and the Chairman of the Compensation Committee, William F. Hughes Jr., were entitled to an additional quarterly cash fee in the amount of \$3,750 and (ii) the Chairman of the Nominating Committee John W. Chisholm, and the Chairman of the Governance and Personnel Development Committee, Charles G. Curtis, were entitled to an additional quarterly cash fee in the amount of \$1,250. In 2013, our non-employee Directors were paid a quarterly cash fee for their attendance at each meeting of our Board of Directors. The cash fee payable to our non-employee Directors was \$7,500 per quarter. Each of our non-employee Directors received a cash fee payment of \$7,500 for the four quarters in 2013, totaling \$30,000. In addition, the Chairman of the Audit Committee, David L. Bradshaw was entitled to an additional quarterly cash fee in the amount of \$2,500; and the Chairman of the Compensation Committee, William F. Hughes Jr., was entitled the same additional quarterly cash fee of \$2,500. In 2012, the quarterly cash fee for attendance at each meeting of our Board of Directors was \$6,250. In addition, the Chairman of the Audit and Compensation Committee was entitled to an additional quarterly cash fee in the amount 33% of their base cash fee.
- (2) On March 20, 2014, each of our non-employee Directors were granted 3,288 restricted shares of common stock at an issue price of \$30.41 per share; on March 21, 2013, each of our non-employee Directors were granted 2,500 restricted shares of common stock at an issue price of \$18.75 per share; on March 28, 2012, each of our non-employee Directors were granted 2,500 restricted shares of common stock at an issue price of \$13.43 per share.

### *Cash Compensation Paid to Independent Directors*

We pay our non-employee Directors a quarterly cash fee for their attendance at each meeting of our Board of Directors. The cash fee payable to our non-employee Directors for 2014 was \$11,250 per quarter. In addition, the Chairmen of the Audit and Compensation Committees were entitled to an additional quarterly cash fee in the amount of \$3,750; while the Chairmen of the Nominating and Governance and Personnel Development committees were entitled to an additional quarterly cash fee of \$1,250.



### *Equity Based Compensation Paid to Independent Directors*

In 2012 and 2013, each independent Director received a static grant of 2,500 shares of restricted shares of Company common stock for each year. For 2014, our Board of Directors revised the Company's compensation policy for independent directors so that in lieu of issuing a static 2,500 restricted shares of Company common stock as in past years, the independent directors now receive an annual award of restricted shares based upon a review of equity award values paid by other public companies in the Company's peer group and the Company's market and financial performance in comparison to such peer group companies. For 2014, based upon the Company's performance compared to its peer group, the Compensation Committee recommended and the Board approved an equity award value of \$100,000 in restricted stock. In connection therewith, each of our four independent directors was granted for 2014 the amount of 3,288 shares of restricted stock pursuant to the Plan, based upon the closing price of \$30.41 per share as of March 20, 2014, the date of the grant. The restricted shares are subject to vesting whereby no shares will vest during the first year, and then upon the first anniversary date of the award, one-fourth of the shares will vest every three months so that all restricted shares will have vested on the second anniversary date of the grant of the award. Notwithstanding the vesting schedule, all of the restricted shares are subject to acceleration and will immediately vest in the case of (i) death, disability, or retirement of the recipient or (ii) a change of control in the Company, as set forth in the Restricted Stock Plan.

Directors who are our employees do not receive any compensation for their services as Directors.

#### *Other*

All Directors are reimbursed for their expenses incurred in connection with attending meetings.

We provide liability insurance for our Directors and officers. The cost of this coverage for 2014 was \$108,350.

We do not offer non-employee Directors travel accident insurance, life insurance or a pension or retirement plan.

### **Compensation Agreements with Management**

On October 23, 2013, we and Stephen C. Taylor entered into a new employment agreement (the "Employment Agreement"), pursuant to which Mr. Taylor continues his employment as our President and Chief Executive Officer. The new Employment Agreement became effective on the same date and Mr. Taylor's previous employment agreement with us, which was set to expire on October 25, 2013, was terminated in connection therewith.

On April 24, 2015, we entered into an amendment with Mr. Taylor to his Employment Agreement pursuant to which the "modified single trigger" change of control provision was changed to a "double trigger" change of control. Under the "modified single trigger provision", Mr. Taylor could voluntarily terminate the Employment Agreement and for any reason and collect severance benefits. Under the new "double trigger" change of control provision, a change of control must occur followed by the Company or its successor terminating Mr. Taylor's employment other than for cause, death, or disability, or by Mr. Taylor terminating his employment for Good Reason. We discuss the definitions of "Change of Control" and "Good Reason" below, along with Mr. Taylor's severance benefits in connection with these events.

The term of the Employment Agreement is for three years but the agreement contains an "evergreen" feature whereby the agreement is automatically extended on a monthly basis on the last day of each month so that the term of the agreement will always be three years unless written notice of nonrenewal is given by the Company. If a notice of nonrenewal is given, the term of employment then ends three years from the date of that written notice of nonrenewal unless terminated earlier as described below. The Employment Agreement provides for Mr. Taylor to receive a base salary, potential cash bonus, equity compensation, and certain other benefits, which are summarized below.

**Base Salary.** Mr. Taylor's annual 2013 base salary of \$459,250 ("Base Salary") remained the same for the remainder of 2013. However, the Base Salary will be reviewed annually at the beginning of the year by, and may be increased at the discretion of, the Compensation Committee of the Board of Directors of the Company (the "Compensation Committee").

**Bonus.** Mr. Taylor will continue to be eligible for an annual cash bonus under the Company's current Annual Incentive Bonus Plan. Mr. Taylor's annual bonus opportunity payable upon achievement of "target" levels shall be at least ninety percent (90%) of Base Salary for 2013 and at least one hundred percent (100%) thereafter. The performance metrics, weighting and thresholds for each annual bonus opportunity will be determined by the Company's Board of Directors or Compensation Committee in good faith following consultation with Mr. Taylor.

**Annual Equity Compensation.** Mr. Taylor will be eligible for annual grants of equity-based incentive awards under the Company's equity compensation plans. The Company has agreed to award Mr. Taylor a restricted stock award or equivalent equity awards in January of each year with an aggregate minimum value equal to at least 175% of the Executive's Base Salary, subject to one-year vesting terms and other standard terms which shall be established by the Compensation Committee taking into account the performance of the Company, Mr. Taylor and industry norms.

**Benefits.** The Company will provide Mr. Taylor such retirement, and other benefits as are customarily provided to similarly situated executives of the Company, including paid vacation, coverage under the Company's medical, life, disability and other insurance plans, and reimbursement for all reasonable business expenses in accordance with the Company's expense reimbursement policy.

**Termination.** The Company or Mr. Taylor may terminate the agreement prior to the expiration of its Term at any time upon written notice.

*Severance upon Early Termination.* Mr. Taylor will be entitled to the following severance benefits during the first ten years of his employment:

(A) If (i) the Company terminates Mr. Taylor's agreement without Cause (ii) Mr. Taylor terminates the agreement for Good Reason or due to a Change of Control event (as defined below) followed by the Company or its successor terminating Mr. Taylor's agreement without cause or Mr. Taylor terminating the agreement for Good Reason or (iii) Mr. Taylor's employment is terminated due to death or disability, then he will receive (a) a lump sum payment equal to 300% of Base Salary and Annual Bonus; (b) vesting of all unvested equity awards or other long-term incentive compensation; (c) continuation of health insurance benefits and payment of any life insurance premiums for a period of 36 months after termination; and (d) receipt of any other vested benefits which had not yet been paid prior to the date of termination.

(B) If Mr. Taylor's employment is terminated for Cause or he voluntarily resigns, then he will be entitled to any unpaid compensation earned through the date of termination and receipt of any other vested benefits which had not yet been paid prior to the date of termination.

(C) If Mr. Taylor retires in compliance with the Company's retirement policy, then he will be entitled to (i) any unpaid compensation earned through the date of retirement; (ii) vesting of all unvested equity awards or other long-term incentive compensation; and (iii) receipt of any other vested benefits which had not yet been paid prior to the date of termination.

After the tenth anniversary date of Mr. Taylor's employment agreement, in the event the Company delivers to Mr. Taylor a Notice of Nonrenewal and:

(A) his employment is automatically terminated upon the expiration of the remaining three year term, Mr. Taylor shall be entitled to (i) any unpaid compensation earned through the date of retirement; (ii) vesting of all unvested equity awards or other long-term incentive compensation; and (iii) receipt of any other vested benefits which had not yet been paid prior to the date of; or

(B) his employment is terminated prior to the expiration of the remaining three year term, unless said termination is due to Cause, voluntary resignation or retirement, then Mr. Taylor shall be entitled to (i) lump sum payment of his Base Salary at the time of termination for the remainder of the three year term of the agreement; (ii) a lump sum cash payment equal to 100% of the Annual Bonus for each full year (if any) remaining in the three year term, plus a pro-rata portion of such Annual Bonus for any partial remaining year in the three year term; (iii) vesting of all unvested equity awards or other long-term incentive compensation; (iv) continuation of health insurance benefits and payment of any life insurance premiums for the remainder of the three year term of the agreement; and (v) receipt of any other vested benefits which had not yet been paid prior to the date of termination.

Under the Employment Agreement, a "Change of Control" event includes (i) the acquisition by a person, entity or group of related persons or entities of more than 30% of the total voting power in the Company (excluding sales to underwriters in a public offering); (ii) consummation of the sale of 50% or more of the Company's assets; (iii) consummation of a merger or consolidation of the Company with or into an entity unless the voting securities of the Company immediately prior to the merger or consolidation continue to represent more than 70% of the voting power of the surviving entity after the merger or consolidation; and (iv) replacement of at least a majority of the incumbent members of the Company's Board of Directors, excluding directors whose election to the Board was approved by at least a majority of the then incumbent directors, subject to further limited exceptions as set forth in the "Change of Control" definition in Employment Agreement.

Under the Employment Agreement, a "Good Reason" event includes (i) a material diminution of Mr. Taylor's duties, control, authority or status or position or a requirement that the Executive report to a corporate officer or employee instead of reporting directly to the board of directors; (ii) a material reduction in Mr. Taylor's compensation; (iii) a material breach by the Company of the Employment Agreement; or (iv) a relocation of more than 50 miles of Mr. Taylor's principal office with the Company or its successor. And in connection with a termination due to Change of Control, the following provisions also constitute "Good Reason" events: (i) a material diminution of Mr. Taylor's duties, control, authority or status or position or a requirement that Mr. Taylor report to a corporate officer or employee instead of reporting directly to the Company's or successor's board of directors depending on its composition after the change in control; (ii) the failure of the Company or successor to continue in effect any plan in which Mr. Taylor participates immediately prior to the Change in Control which is material to total compensation, unless an equitable arrangement has been made with respect to any such plan on a basis not less favorable, both in terms of the amount or timing of payment of benefits provided; and (iii) a material breach by the Company or its successor of the Employment Agreement or any other material agreement between Mr. Taylor and the Company or its successor.

**Non-Competition and Non-Solicitation.** In connection with the payment of the severance benefits described above, for a period of two years following Mr. Taylor's separation from the Company, he may not compete with the Company in any geographic area within a 100 mile radius of a Company owned or leased facility which is Company staffed and actively engaging in business on behalf of the Company.

**Clawbacks.** Mr. Taylor's incentive compensation will be subject to clawback regulations in effect under applicable law.

We do not have any written employment agreements with our other named executive officers.

#### **Limitation on Directors' and Officers' Liability**

Our Articles of Incorporation provide our Directors and Officers with certain limitations on liability to us or any of our shareholders for damages for breach of fiduciary duty as a Director or officer involving certain acts or omissions of any such Director or Officer.

This limitation on liability may have the effect of reducing the likelihood of derivative litigation against Directors and Officers and may discourage or deter shareholders or management from bringing a lawsuit against Directors and Officers for breach of their duty of care even though such an action, if successful, might otherwise have benefited our shareholders and us.

Our Articles of Incorporation and bylaws provide certain indemnification privileges to our Directors, employees, agents and officers against liabilities incurred in legal proceedings. Also, our Directors, employees, agents or officers who are successful, on the merits or otherwise, in defense of any proceeding to which he or she was a party, are entitled to receive indemnification against expenses, including attorneys' fees, incurred in connection with the proceeding.

We are not aware of any pending litigation or proceeding involving any of our Directors, Officers, employees or agents as to which indemnification is being or may be sought, and we are not aware of any other pending or threatened litigation that may result in claims for indemnification by any of our Directors, officers, employees or agents.

Even though we maintain Directors' and Officers' liability insurance, the indemnification provisions contained in our Articles of Incorporation and bylaws remain in place.

#### **Procedures for Reviewing Certain Transactions**

On March 7, 2007, we adopted a written policy for the review, approval or ratification of related party transactions. All of our officers, Directors and employees are subject to the policy. Under this policy, the Audit Committee will review all related party transactions for potential conflict of interest situations. Generally, our policy defines a "related party transaction" as a transaction in which we are a participant and in which a related party has an interest. A "related party" is:

- any of our Directors, Officers or employees or a nominee to become a Director;
- an owner of more than 5% of our outstanding common stock;
- certain family members of any of the above persons; and
- any entity in which any of the above persons is employed or is a partner or principal or in which such person has a 5% or greater ownership interest.

### *Approval Procedures*

Before entering into a related party transaction, the related party or our department responsible for the potential transaction must notify the CEO or the Audit Committee of the facts and circumstances of the proposed transaction. If the amount involved is equal to or less than \$100,000, the proposed transaction will be submitted to the CEO. If the amount involved exceeds \$100,000, the proposed transaction will be submitted to the Audit Committee. Matters to be submitted will include:

- the related party's relationship to us and interest in the transaction;
- the material terms of the proposed transaction;
- the benefits to us of the proposed transaction;
- the availability of other sources of comparable properties or services; and
- whether the proposed transaction is on terms comparable to terms available to an unrelated third party or to employees generally.

The CEO or the Audit Committee, as applicable, will then consider all of the relevant facts and circumstances available, including the matters described above and, if applicable, the impact on a director's independence. Neither the CEO nor any member of the Audit Committee is permitted to participate in any review, consideration or approval of any related party transaction if such person or any of his or her immediate family members is the related party. After review, the CEO or the Audit Committee, as applicable, may approve, modify or disapprove the proposed transaction. Only those related party transactions that are in, or are not inconsistent with, our best interests and that of our shareholders will be approved.

### *Ratification Procedures*

If one of our officers or Directors becomes aware of a related party transaction that has not been previously approved or ratified by the CEO or the Audit Committee then, if the transaction is pending or ongoing, the transaction must be submitted, based on the amount involved, to either the CEO or the Audit Committee and the CEO or the Audit Committee will consider the matters described above. Based on the conclusions reached, the CEO or the Audit Committee, as applicable, will evaluate all options, including ratification, amendment or termination of the related party transaction. If the transaction is completed, the CEO or the Audit Committee will evaluate the transaction, taking into account the same factors as described above, to determine if rescission of the transaction or any disciplinary action is appropriate, and will request that we evaluate our controls and procedures to determine the reason the transaction was not submitted to the CEO or the Audit Committee for prior approval and whether any changes to the procedures are recommended.

We did not have any related party transactions in 2014 with our Officers or Directors.

## PRINCIPAL SHAREHOLDERS AND SECURITY OWNERSHIP OF MANAGEMENT

For purposes of the following tables, "beneficial ownership" is determined in accordance with Rule 13d-3 under the Securities Exchange Act of 1934, pursuant to which a person or group of persons is deemed to have "beneficial ownership" of any shares of Common Stock that such person has the right to acquire within 60 days.

The following table indicates the beneficial ownership of our Common Stock as of April 15, 2015 by: (1) each of our current directors and nominees for election; (2) our chief executive officer, principal accounting officer and our other named executive officers (as defined in Item 402(a) (3) of Regulation S-K) (together as a group, the " *Named Executive Officers* "); and (3) all of our current directors, nominees and executive officers as a group, based on our records and data supplied by each of the current directors, nominees and executive officers.

Name of Beneficial Owner and Position	Amount and Nature of Beneficial Ownership <sup>(1)</sup>	Percent of Class
<b>Directors &amp; Nominees Who Are Not Named Executive Officers</b>		
John W. Chisholm Current Director	31,280 <sup>(2)</sup>	*
Charles G. Curtis Current Director	79,137 <sup>(3)</sup>	*
William F. Hughes, Jr. Current Director & Director Nominee	143,220 <sup>(4)</sup>	1.12%
David L. Bradshaw Current Director & Director Nominee	13,988	*
<b>Named Executive Officers</b>		
Stephen C. Taylor Chief Executive Officer, Current Director	429,283 <sup>(5)</sup>	3.33%
James R. Hazlett Vice President – Technical Services	105,010 <sup>(6)</sup>	*
G. Larry Lawrence Chief Financial Officer	55,000 <sup>(7)</sup>	*
All Directors (and nominees) and executive officers as a group (7 persons)	856,918 <sup>(8)</sup>	6.61%

\* Less than one percent.

(1) The number of shares listed includes all shares of common stock owned by, or which may be acquired within 60 days of April 15, 2015 upon exercise of warrants and options held by the shareholder (or group). Beneficial ownership is calculated in accordance with the rules of the Securities and Exchange Commission. Unless otherwise indicated, all shares of common stock are held directly with sole voting and investment powers. As of April 15, 2015, none of the shares of common stock owned by our officers and Directors had been pledged as collateral to secure repayment of loans.

(2) Includes 15,000 shares of common stock that may be acquired upon exercise of stock options granted under our 1998 Stock Option Plan.

(3) Includes 15,000 shares of common stock that may be acquired upon exercise of stock options granted under our 1998 Stock Option Plan.

(4) Includes 110,500 shares of common stock indirectly owned by Mr. Hughes through the William and Cheryl Hughes Family Trust and 10,000 shares that may be acquired upon exercise of stock options granted under our 1998 Stock Option Plan. Mr. and Mrs. Hughes are co-trustees of the William and Cheryl Hughes Family Trust and have shared voting and investment powers with respect to the shares held by the trust. Mr. and Mrs. Hughes are beneficiaries of the trust along with their two children.

(5) Includes 163,852 shares of common stock that may be acquired upon exercise of stock options granted to Mr. Taylor as an inducement for his employment and under our 1998 Stock Option Plan.

(6) Includes 25,000 shares of common stock that may be acquired upon exercise of stock options granted under our 1998 Stock Option Plan.

(7) Includes 5,000 shares of common stock that may be acquired upon exercise of stock options granted under our 1998 Stock Option Plan.

(8) Includes 238,852 shares of common stock that may be acquired upon exercise of stock options.

The following table sets forth information as of April 15, 2015 regarding the beneficial owners of more than five percent of the outstanding shares of our Common Stock. To our knowledge, there are no beneficial owners of more than five percent of the outstanding shares of our Common Stock as of April 15, 2015 other than those set forth below.

Name and Address of Beneficial Owner	Amount and Nature of Beneficial Ownership	Percent of Class
Blackrock, Inc. 40 East 52 <sup>nd</sup> Street New York, New York 10022	799,353 <sup>(1)</sup>	6.28%
Neuberger Berman Group LLC 605 Third Avenue New York, New York 10158	1,255,535 <sup>(2)</sup>	9.86%
Dimensional Fund Advisors Palisades West, Building One, 6300 Bee Cave Road Austin, Texas 78746	915,246 <sup>(3)</sup>	7.19%

(1) According to the filing, Blackrock, Inc. has the sole voting and dispositive power over the shares reported in the table above.

(2) As reported in Amendment No. 6 to Schedule 13G filed with the Securities and Exchange Commission on February 12, 2015. According to the filing, Neuberger Berman Group LLC and Neuberger Berman LLC beneficially own the shares.

(3) As reported in Amendment No. 3 to schedule 13G filed with the Securities and Exchange Commission in February 5, 2015. According to the filing, Dimensional Fund Advisors holds voting and/or investment power over the shares, but economic ownership is beneficially by four investment companies.

#### **Section 16(a) Beneficial Ownership Reporting Compliance**

Section 16(a) of the Securities Exchange Act of 1934, as amended, requires our Directors, officers and persons who beneficially own more than 10% of our Common Stock to file certain reports of beneficial ownership with the Securities and Exchange Commission. These reports show the Directors', officers' and greater than 10% stockholders' ownership and the changes in ownership of our common stock and other equity securities. The SEC regulations also require that a copy of all such Section 16(a) forms filed must be furnished to us by the person or entity filing the report.

Based on a review of Section 16(a) filings furnished to us, all transactions in our equity securities required to be reported by Section 16(a) of the Securities Exchange Act of 1934, as amended, were reported on a timely basis.

## REPORT OF THE AUDIT COMMITTEE

Our Audit Committee is responsible for overseeing the integrity of our financial statements; financial reporting processes; compliance with legal and regulatory requirements; the independent registered public accounting firm qualifications and independence; and the performance of our internal accounting functions and independent registered public accounting firm.

Our independent registered public accounting firm is responsible for performing an independent audit of our financial statements in accordance with the Standards of the Public Company Accounting Oversight Board (United States) and to issue a report thereon. The Audit Committee reviews with management our financial statements and management's assessment of internal controls over financial reporting; reviews with the independent registered accounting firm their independent report on the condition of the company's financial statements; and reviews the activities of the independent registered public accounting firm. The Audit Committee selects our independent registered public accounting firm each year. The Audit Committee also considers the adequacy of our internal controls and accounting policies. The chairman and members of the Audit Committee are all independent Directors of our Board of Directors within the meaning of Section 303A of the New York Stock Exchange Listed Company Manual.

The Audit Committee has reviewed and discussed our audited financial statements with our management. The Audit Committee has also received from, and discussed with, BDO the matters required to be discussed by Public Company Accounting Oversight Board Auditing Standard No. 16 (Communications with Audit Committees)." In addition, the Audit Committee has received the written disclosures and the letter from our independent registered public accounting firm required by the Public Company Accounting Oversight Board in Rule 3200T. In addition, the Audit Committee has received the written disclosures and the letter from our independent registered public accounting firm matters pertaining to their independence. Based upon the reviews and discussions referred to above, the Audit Committee recommended to the Board of Directors that the audited financial statements be included in our Annual Report on Form 10-K for 2014 for filing with the Securities and Exchange Commission. See "*Proposal 2 – Ratification of Appointment of Independent Registered Accounting Firm*" on the following page for further information.

Respectfully submitted by the Audit Committee,

David L. Bradshaw, Chairman

Charles G. Curtis

William F. Hughes, Jr.



## **PROPOSAL 2 – RATIFICATION OF APPOINTMENT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM**

We are asking the stockholders to ratify the Audit Committee’s appointment of BDO USA, LLP as our independent registered public accounting firm for the fiscal year ending December 31, 2015. BDO USA, LLP is a registered public accounting firm with the Public Company Accounting Oversight Board (“PCAOB”), as required by the Sarbanes-Oxley Act of 2002 and the rules of the PCAOB. Shareholder ratification of the appointment is not required under the laws of the State of Colorado, but the Board believes it is important to allow the shareholder to vote on the proposal. In the event the shareholders fail to ratify the appointment, the Audit Committee will reconsider this appointment. Even if the appointment is ratified, the Audit Committee, in its discretion, may direct the appointment of different independent registered public accounting firm at any time during the year if the Audit Committee determines that such a change would be in our best interests and that of our shareholders.

BDO USA, LLP representatives are expected to attend the 2015 Annual Meeting in person. They will have an opportunity to make a statement if they desire to do so and will be available to respond to appropriate shareholder questions.

**The Board of Directors recommends that the shareholders vote “FOR” the ratification of the appointment of BDO USA, LLP as our independent registered public accounting firm for the fiscal year ending December 31, 2015.**

### **Principal Accountant Fees**

Our principal accountant for the fiscal years ended December 31, 2012, 2013 and 2014 was BDO USA, LLP.

#### *Audit Fees*

The aggregate fees billed for professional services rendered by BDO USA, LLP for the audit of our financial statements for our fiscal years ended December 31, 2013 and 2014 and the review of the financial statements on Forms 10-Q for the fiscal quarters in such fiscal years were approximately \$231,000 and \$236,000 respectively.

#### *Audit Related Fees*

During the years ended December 31, 2013 and 2014, there were no audit related fees.

#### *Tax Fees*

We were not billed by BDO USA, LLP during the years ended December 31, 2013 or 2014.

#### *All Other Fees*

No other fees were billed by BDO USA, LLP, during our fiscal years ended December 31, 2013 and 2014, other than as described above.

### **Audit Committee Pre-Approval Policies and Procedures**

As of the date of this proxy statement, our Audit Committee has not established general pre-approval policies and as of December 31, 2014, our Audit Committee had not established pre-approval policies and procedures for the engagement of our principal accountant to render audit or non-audit services. However, in accordance with Section 10A(i) of the Exchange Act, our Audit Committee, as a whole, approves the engagement of our principal accountant prior to the accountant rendering audit or non-audit services.

Certain rules of the Securities and Exchange Commission provide that an auditor is not independent of an audit client if the services it provides to the client are not appropriately approved, subject, however, to a *de minimus* exception contained in the rules. The Audit Committee pre-approved all services provided by BDO USA, LLP in 2014 and the *de minimus* exception was not used.

### **PROPOSAL 3 – CONSIDERATION OF AN ADVISORY VOTE ON EXECUTIVE COMPENSATION OF OUR NAMED EXECUTIVE OFFICERS**

The Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010 (the “Dodd-Frank Act”), gives the stockholders the right to endorse or not endorse the compensation of our named executive officers as disclosed in this Proxy Statement in accordance with the SEC’s rules. The proposal, commonly known as a “Say On Pay” proposal, gives our stockholders the opportunity to express their views on the Company’s executive compensation.

At the Company’s annual meeting of stockholders held in June 2011, our shareholders recommended that the advisory vote on the Say-on-Pay of our named executives in our proxy materials be submitted annually, notwithstanding that our Board of Directors recommended that the advisory vote be submitted every third year. In light of the recommendation of the shareholders, we intend to include the Say-on-Pay advisory vote in our proxy materials on an annual basis until the next shareholder vote on the frequency of Say-on-Pay or our Board of Directors otherwise determines that a different frequency of Say-on-Pay vote is in the best interests of the shareholders.

We are asking our stockholders to indicate whether or not they support the compensation program as described in this proxy statement. This proposal is not intended to address any specific item of compensation, but rather the overall compensation of the named executive officers and the compensation policies, methodologies and practices described in this proxy statement. Accordingly, we ask our stockholder to vote “FOR” the following resolution at our annual meeting:

“RESOLVED, that the stockholders approve the compensation of the Company’s named executive officers, as disclosed in the Compensation Discussion and Analysis, the compensation tables, and the related disclosure contained in the proxy statement set forth under the caption “Executive Compensation” of this proxy statement.”

The Company believes its compensation philosophy and programs are strongly linked to performance and results and appropriately aligned with the interests of stockholders. Our compensation philosophy is to provide an executive compensation program that:

- rewards performance and skills necessary to advance our objectives and further the interests of our shareholders;
- is fair and reasonable and appropriately applied to each executive officer;
- is competitive with compensation programs offered by our competitors; and
- is appropriately focused on achieving annual financial and operational goals through the Company’s cash bonus plan and on maximizing stockholder value over the long term, through grants of restricted shares and stock options.

**The Board of Directors recommends that you vote FOR approval, on an advisory basis, of the compensation programs of our named executive officers as disclosed in the Compensation Discussion and Analysis, the compensation tables, and the related disclosure contained in the proxy statement set forth under the caption “Executive Compensation” of this proxy statement.**

## SHAREHOLDER PROPOSALS

Under SEC Rule 14a-8, if a shareholder wants us to include a proposal in our proxy statement and form of proxy for presentation at our 2016 Annual Meeting of Shareholders, the proposal must be received by us at our principal executive offices at 508 West Wall Street, Suite 550, Midland, Texas 79701 by December 21, 2015, unless the date of our 2016 Annual Meeting of Shareholders is more than 30 days from the anniversary date of our 2015 Annual Meeting of Shareholders, in which case the deadline is a reasonable time before we print and mail our proxy materials for the 2016 Annual Meeting of Shareholders. The proposal should be sent to the attention of the Secretary of Natural Gas Services Group.

Rule 14a-4 of the SEC's proxy rules allows a company to use discretionary voting authority to vote on matters coming before an annual meeting of shareholders for the prior year's annual meeting of shareholders or the date specified by an overriding advance notice provision in the company's bylaws. Our bylaws do not contain such an advance notice provision. Accordingly, for our 2016 annual meeting, shareholders' written notices must be received by us before March 9, 2016 for any proposal a shareholder wishes to bring before the meeting but for which such shareholder does not seek to have a written proposal considered for inclusion in the proxy statement and form of proxy. Your notice should be addressed to President, Natural Gas Services Group, Inc., 508 West Wall Street, Suite 550, Midland, Texas 79701.

In order to curtail controversy as to the date on which a proposal was received by us, it is suggested that proponents submit their proposals by certified mail-return receipt requested. Such proposals must also meet the other requirements established by the SEC for shareholder proposals.

## **COMMUNICATIONS WITH THE BOARD OF DIRECTORS**

Because of our relatively small size, to date we have not developed formal processes by which shareholders or other interested parties may communicate directly with Directors. Until formal procedures are developed and posted on our website ([www.ngsgi.com](http://www.ngsgi.com)), any communication to one or more members of our Board of Directors may be made by sending them in care of Investor Relations, Natural Gas Services Group, Inc., 508 West Wall Street, Suite 550, Midland, Texas 79701. Shareholders should clearly note on the mailing envelope that the letter is a “Shareholder-Board Communication.” All such communications will be forwarded to the intended recipients.

## OTHER MATTERS

Our Board of Directors does not know of any matters to be presented at the meeting other than the matters set forth herein. If any other business should come before the meeting, the person's named in the enclosed proxy card will vote such proxy according to their judgment on such matters.

**New York Stock Exchange Certification.** We listed our common stock on the New York Stock Exchange in October 2008. The certification of our Chief Executive Officer required by the NYSE Listing Standards, Section 303A.12(a), relating to our compliance with the NYSE Corporate Governance Listing Standards, was submitted to the NYSE on May 6, 2014 in connection with our listing on the exchange. The certifications of our Chief Executive Officer and Principal Accounting Officer required by the SEC in connection with our Annual Report on Form 10-K for the year ended December 31, 2014 were submitted to the SEC on March 13, 2015 with our Annual Report on Form 10-K.

You may obtain our Annual Report on Form 10-K for the fiscal year ended December 31, 2014 without charge upon written request to Stephen C. Taylor, President, at Natural Gas Services Group, Inc., 508 West Wall Street, Suite 550, Midland, Texas 79701. In addition, the exhibits to the Annual Report on Form 10-K for the fiscal year ended December 31, 2014 may be obtained by any shareholder upon written request to Mr. Taylor.

In addition, we use our website as a channel of distribution for company information. We make available free of charge on the Investor Relations section of our website ([www.ngsgi.com](http://www.ngsgi.com)) our Annual Report on Form 10-K, Quarterly Reports on Form 10-Q, and Current Reports on Form 8-K. We also make available through our website other reports filed with or furnished to the SEC under the Securities Exchange Act of 1934, as amended, including our proxy statements and reports filed by officers and directors under Section 16(a) of the Exchange Act, as well as our Code of Business Ethics and the charters to our various Committees of our Board of Directors. We do not intend for information contained in our website to be part of this proxy statement.

BY ORDER OF THE BOARD OF DIRECTORS

Midland, Texas  
April 29, 2015

/s/ Stephen C. Taylor  

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Stephen C. Taylor  
Chairman of the Board, President and Chief  
Executive Officer

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



FORM 10-K

[ x ] ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the fiscal year ended **December 31, 2014**

or

[ ] TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the transition period from \_\_\_\_\_ to \_\_\_\_\_

Commission file number: 1-31398

NATURAL GAS SERVICES GROUP, INC.

(Exact Name of Registrant as Specified in its Charter)

<u>Colorado</u>	<u>75-2811855</u>
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)
<u>508 W. Wall St. Suite 550, Midland, Texas</u>	<u>79701</u>
(Address of principal executive offices)	(Zip Code)
<u>Registrant's telephone number, including area code:</u>	<u>(432) 262-2700</u>

Securities registered pursuant to Section 12(b) of the Act:

<u>Title of each class</u>	<u>Name of each exchange on which registered</u>
<u>Common Stock, \$.01 par value</u>	<u>New York Stock Exchange</u>

Securities registered pursuant to section 12(g) of the Act: None.

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act.

Yes  No

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Act.

Yes  No

Indicate by check mark whether the registrant: (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days.

Yes  No

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files).

Yes  No

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K.[]

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

(Check one):

Large Accelerated Filer  Accelerated Filer  Non-Accelerated Filer  Smaller Reporting Company

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).

Yes  No

The aggregate market value of voting and non-voting common equity held by non-affiliates of the Registrant as of June 30, 2014 was approximately \$404,885,655 based on the closing price of the common stock on that date on the New York Stock Exchange.

At February 13, 2015, there were 12,581,360 shares of common stock outstanding.

## Documents Incorporated by Reference

Certain information called for in Items 10, 11, 12, 13 and 14 of Part III are incorporated by reference to the registrant's definitive proxy statement for the annual meeting of shareholders to be held on June 18, 2015.



FORM 10-K  
NATURAL GAS SERVICES GROUP, INC.  
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## SPECIAL NOTE REGARDING FORWARD-LOOKING STATEMENTS

This Annual Report on Form 10-K contains certain forward-looking statements, within the meaning of Section 27A of the Securities Act of 1933, as amended, and information pertaining to us, our industry and the oil and natural gas industry that is based on the beliefs of our management, as well as assumptions made by and information currently available to our management. All statements, other than statements of historical facts contained in this Annual Report on Form 10-K, including statements regarding our future financial position, growth strategy, budgets, projected costs, plans and objectives of management for future operations, are forward-looking statements. We use the words “may,” “will,” “expect,” “anticipate,” “estimate,” “believe,” “continue,” “intend,” “plan,” “budget” and other similar words to identify forward-looking statements. You should read statements that contain these words carefully and should not place undue reliance on these statements because they discuss future expectations, contain projections of results of operations or of our financial condition and/or state other “forward-looking” information. We do not undertake any obligation to update or revise publicly any forward-looking statements. Although we believe our expectations reflected in these forward-looking statements are based on reasonable assumptions, no assurance can be given that these expectations or assumptions will prove to have been correct. Important factors that could cause actual results to differ materially from the expectations reflected in the forward-looking statements include, but are not limited to, the following factors and the other factors described in this Annual Report on Form 10-K under the caption “Risk Factors”:

- conditions in the oil and natural gas industry, including the supply and demand for natural gas and wide fluctuations in the prices of oil and natural gas;
- regulation or prohibition of new well completion techniques;
- competition among the various providers of compression services and products;
- changes in safety, health and environmental regulations;
- changes in economic or political conditions in the markets in which we operate;
- failure of our customers to continue to rent equipment after expiration of the primary rental term;
- the inherent risks associated with our operations, such as equipment defects, malfunctions and natural disasters;
- our inability to comply with covenants in our debt agreements and the decreased financial flexibility associated with our debt;
- future capital requirements and availability of financing;
- fabrication and manufacturing costs;
- general economic conditions;
- acts of terrorism; and
- fluctuations in interest rates.

We believe that it is important to communicate our expectations of future performance to our investors. However, events may occur in the future that we are unable to accurately predict or that we are unable to control. When considering our forward-looking statements, you should keep in mind the risk factors and other cautionary statements in this Annual Report on Form 10-K.

## PART I

### ITEM 1. BUSINESS

Unless the context otherwise requires, references in this Annual Report on Form 10-K to “Natural Gas Services Group,” the “Company,” “we,” “us,” “our” or “ours” refer to Natural Gas Services Group, Inc. Certain specialized terms used in describing our natural gas compressor business are defined in "Glossary of Industry Terms" on page 8.

#### The Company

We are a leading provider of small to medium horsepower compression equipment to the natural gas industry. We focus primarily on the non-conventional natural gas and oil production business in the United States (such as coal bed methane, gas shale, tight gas and oil shales), which, according to data from the Energy Information Administration ("EIA"), is the single largest and fastest growing segment of U.S. energy production. We manufacture, fabricate and rent natural gas compressors that enhance the production of natural gas wells and provide maintenance services for those compressors. In addition, we sell custom fabricated natural gas compressors to meet customer specifications dictated by well pressures, production characteristics and particular applications. We also manufacture and sell flare systems for oil and gas plant and production facilities.

The vast majority of our rental operations are in non-conventional natural gas and oil regions, which typically have lower initial reservoir pressures, lower production pressures and/or faster well decline rates. These areas usually require compression to be installed sooner and with greater frequency.

Natural gas compressors are used in a number of applications for the production and enhancement of gas wells and in gas transportation lines and processing plants. Compression equipment is often required to boost a well's production to economically viable levels and enable gas to continue to flow in the pipeline to its destination.

We increased our revenue to \$97.0 million in 2014 from \$53.9 million in 2010. During the same period, income from operations increased to \$22.0 million from \$11.4 million. Our compressor rental fleet has grown to 2,879 compressors at December 31, 2014 from 1,909 compressors at the end of 2010.

Our revenue increased to \$97.0 million from \$89.2 million for the year ended December 31, 2014 compared to the year ended December 31, 2013.

Net income for the year ended December 31, 2014 decreased to \$14.1 million (\$1.11 per diluted share), as compared to \$14.4 million (\$1.15 per diluted share) for the year ended December 31, 2013.

At December 31, 2014, current assets were \$55.9 million, which included \$6.2 million of cash and cash equivalents. Current liabilities were \$14.1 million, and our line of credit due in 2017 was \$417,000. Our stockholders' equity as of December 31, 2014 was \$210.6 million.

We were incorporated in Colorado on December 17, 1998 and maintain our principal offices at 508 W. Wall St., Suite 550, Midland, Texas 79701 and our telephone number is (432) 262-2700.

#### Overview and Outlook

The market for compression equipment and services is substantially dependent on the condition of the natural gas and oil industry. In particular, the willingness of natural gas and oil companies to make capital expenditures on exploration, drilling and production of natural gas and oil in the U.S. The level of activity and capital expenditures has generally been dependent upon the prevailing view of future gas and oil prices, which are influenced by numerous factors, including the level of supply or demand for natural gas and oil and the impact on price of natural gas and oil, worldwide economic activity, interest rates and the cost of capital, environmental regulation, seasonal fluctuations and weather patterns. Natural gas and oil prices and the level of production activity have historically been characterized by significant volatility. Increasing oil and natural gas prices from 2005 through mid-2008 resulted in natural gas and oil operators increasing capital spending for exploration, development and production programs. However, in mid-2008, natural gas and oil prices began to decline. This decline resulted in reduced production and capital spending by some natural gas and oil companies, and had an impact on demand for compression equipment.

The reduction in capital expenditures and production in the natural gas and oil industry, combined with problems in the global economy, led to a downturn in the demand for our products and services in 2009 and 2010. In 2011 a slow recovery began which produced an improvement in the utilization rate on our rental fleet and stability in our sales backlog. In 2012 we saw growth in demand for our products and that growth continued in 2013 and 2014. Towards the end of 2014 oil prices began a steep decline which has resulted in capital budget cuts for many energy companies for 2015. These budget reductions will translate to fewer well completions and a softening of near-term demand for compression. See “Item 1 -- Business – Our Operating Units” and “Business – Backlog” for more information.

According to the U.S. Energy Information Administration (“EIA”), total consumption of natural gas in the United States increased 2.8% for the twelve months ended November 2014 compared to the same period 2013. This follows a 2.1% and a 5.1% increase in the periods from 2012 to 2013 and 2011 to 2012, respectively. EIA expects total natural gas consumption in the U.S. to increase slightly in 2015. While we anticipate long-term increased demand for natural gas, we expect our business to remain virtually flat or moderately decrease for 2015 due to the overall uncertainty in the combined oil and gas market.

### **Long-Term Industry Trends**

Natural gas prices historically have been volatile, and this volatility is expected to continue. Oil and natural gas are linked commodities with many drilling projects producing both products. The recent oil price collapse may make some of those drilling projects uneconomic. Uncertainty continues to exist as to the direction of future natural gas and near-term crude oil price and oil trends are down in the United States and worldwide. Over the last several years gas prices have not shown the resiliency that crude oil prices have and now crude prices are also down sharply. We believe that natural gas is a more environmentally friendly source of energy which is likely to result in increases in demand over time. Being primarily a provider of services and equipment to natural gas producers, we are impacted by changes in natural gas, crude oil and condensate prices. Longer term natural gas prices will be determined by the supply and demand for natural gas as well as the prices of competing fuels, such as oil and coal.

We believe part of the growth of the rental compression capacity in the U.S. market has been driven by the trend toward outsourcing by energy producers and processors. Renting does not require the purchaser to make large capital expenditures for new equipment or to obtain financing through a lending institution. This allows the customer’s capital to be used for additional exploration and production of natural gas and oil.

Notwithstanding the slow rise in natural gas prices, we believe that there will continue to be a growing demand for natural gas. We expect long-term demand for our products and services will increase as a result of:

- the increasing demand for and limited supply of energy, both domestically and abroad;
- continued non-conventional gas exploration and production;
- environmental considerations which provide strong incentives to use natural gas in place of other carbon fuels;
- the cost savings of using natural gas rather than electricity for heat generation;
- implementation of international environmental and conservation laws;
- the aging of producing natural gas reserves worldwide;
- the extensive supply of undeveloped non-conventional natural gas reserves
- the increased drilling for shale oil and its associated gas production; and
- the use of our equipment for gas lift on oil wells.

### **Our Operating Units**

We identify our operating units based upon major revenue sources as Gas Compressor Rental, Engineered Equipment Sales, Service and Maintenance and Corporate.

**Gas Compressor Rental.** Our rental business is primarily focused on non-conventional gas and oil production. We provide rental of small to medium horsepower compression equipment to customers under contracts typically having minimum initial terms of six to twenty four months. Historically, in our experience, most customers retain the equipment beyond the expiration of the initial term. By outsourcing their compression needs, we believe our customers are able to increase their revenues by producing a higher volume of natural gas due to greater equipment run-time. Outsourcing also allows our customers to reduce

their compressor downtime, operating and maintenance costs and capital investments and more efficiently meet their changing compression needs. We maintain and service compressor equipment rented to our customers.

The size, type and geographic diversity of our rental fleet enables us to provide our customers with a range of compression units that can serve a wide variety of applications, and to select the correct equipment for the job, rather than the customer trying to fit the job to its own equipment. We base our gas compressor rental rates on several factors, including the cost and size of the equipment, the type and complexity of service desired by the customer, the length of contract and the inclusion of any other services desired, such as installation, transportation and daily operation.

As of December 31, 2014, we had 2,879 natural gas compressors in our rental fleet totaling 401,361 horsepower, as compared to 2,556 natural gas compressors totaling 351,187 horsepower at December 31, 2013. As of December 31, 2014, we had 2,189 natural gas compressors totaling 301,392 horsepower rented to 102 customers, compared to 2,038 natural gas compressors totaling 283,165 horsepower rented to 95 customers at December 31, 2013. As of December 31, 2014, the utilization rate of our rental fleet was 76.0% compared to 79.7% as of December 31, 2013.

**Engineered Equipment Sales.** This operating unit includes the following components:

- **Compressor fabrication.** Fabrication involves the assembly of compressor components manufactured by us or other vendors into compressor units that are ready for rental or sale. In addition to fabricating compressors for our rental fleet, we engineer and fabricate natural gas compressors for sale to customers to meet their specifications based on well pressure, production characteristics and the particular applications for which compression is sought.
- **Compressor manufacturing.** We design and manufacture our own proprietary line of reciprocating compressor frames, cylinders and parts known as our “CiP”, or Cylinder-in-Plane, product line. We use the finished components to fabricate compressor units for our rental fleet or for sale to customers. We also sell finished components to other fabricators.
- **Flare fabrication.** We design, fabricate, sell, install and service flare stacks and related ignition and control devices for the onshore and offshore incineration of gas compounds such as hydrogen sulfide, carbon dioxide, natural gas and liquefied petroleum gases. Applications for this equipment are often environmentally and regulatory driven, and we believe we are a leading supplier to this market.
- **Parts sales and compressor rebuilds.** To provide customer support for our compressor and flare sales businesses, we stock varying levels of replacement parts at our Midland, Texas facility and at field service locations. We also provide an exchange and rebuild program for screw compressors and maintain an inventory of new and used compressors to facilitate this part of our business.

**Service and Maintenance.** We service and maintain compressors owned by our customers on an “as needed” basis. Natural gas compressors require routine maintenance and periodic refurbishing to prolong their useful life. Routine maintenance includes physical and visual inspections and other parametric checks that indicate a change in the condition of the compressors. We perform wear-particle analysis on all packages and perform overhauls on a condition-based interval or a time-based schedule. Based on our past experience, these maintenance procedures maximize component life and unit availability and minimize downtime.

## **Business Strategy**

During the downturn in the economy beginning in mid 2008, our strategy was to reduce expenses in line with the lower anticipated business activity, and fabricate compressor equipment only in direct response to market requirements. As the economy recovered, we adjusted this strategy to ensure that we kept pace with growth while balancing appropriate business risk. As we again enter an industry downturn, our proven strategy of reducing expenses and fabricating on an as needed basis will be in place for 2015. See “Item 7 – Management’s Discussion and Analysis of Financial Condition and Results of Operations – Our Performance Trends and Outlook” for more information. Our long-term intentions to grow our revenue and profitability are based on the following business strategies:

- **Expand rental fleet.** We intend to increase the size of our rental fleet by fabricating compressor units in numbers that correspond to the growth of the market and in relation to market share gains we may experience. We believe our growth will continue to be primarily driven through our placement of small to medium horsepower wellhead natural gas compressors for non-conventional natural gas and oil production.

- **Geographic expansion.** We will continue to consolidate our operations in existing areas, as well as pursue focused expansion into new geographic regions as opportunities are identified. We presently provide our products and services to a customer base of oil and natural gas exploration and production companies operating in Colorado, Kansas, Michigan, New Mexico, North Dakota, Ohio, Oklahoma, Pennsylvania, Texas, Utah, West Virginia and Wyoming.
- **Expand our 'secondary' product lines.** In addition to our primary rental and engineered product business lines, we will emphasize the growth of our other products, e.g., flares, CiP compressor products and general compressor maintenance and repair services.
- **Selectively pursue acquisitions.** We will continue to evaluate potential acquisitions that would provide us with access to new markets or enhance our current market position.

## Competitive Strengths

We believe our competitive strengths include:

- **Superior customer service.** Our emphasis on the small to medium horsepower markets has enabled us to effectively meet the evolving needs of our customers. We believe these markets have been under-served by our larger competitors which, coupled with our personalized services and in-depth knowledge of our customers' operating needs and growth plans, have allowed us to enhance our relationships with existing customers as well as attract new customers. The size, type and geographic diversity of our rental fleet enable us to provide customers with a range of compression units that can serve a wide variety of applications. We are able to select the correct equipment for the job, rather than the customer trying to fit its application to our equipment.
- **Diversified product line.** Our compressors are available as high and low pressure rotary screw and reciprocating packages. They are designed to meet a number of applications, including wellhead production, natural gas gathering, natural gas transmission, vapor recovery and gas and plunger lift. In addition, our compressors can be built to handle a variety of gas mixtures, including air, nitrogen, carbon dioxide, hydrogen sulfide and hydrocarbon gases. A diversified compression product line helps us compete by being able to satisfy widely varying pressure, volume and production conditions that customers encounter. Our "Flare King" product line provides flares and gas incineration devices to the industry for production maintenance and environmental compliance.
- **Purpose-built rental compressors.** Our rental compressor packages have been designed and built to address the primary requirements of our customers in the producing regions in which we operate. Our units are compact in design and are easy, quick and inexpensive to move, install and start-up. Our control systems are technically advanced and allow the operator to start and stop our units remotely and/or in accordance with well conditions. We believe our rental fleet is also one of the newest.
- **Experienced management team.** On average, each of our executive and operating team members have over 30 years of oilfield services industry experience. We believe our management team has successfully demonstrated its ability to grow our business during times of expansion and to manage through downturns.
- **Broad geographic presence.** We presently provide our products and services to a customer base of oil and natural gas exploration and production companies operating in Colorado, Kansas, Michigan, New Mexico, North Dakota, Ohio, Oklahoma, Pennsylvania, Texas, Utah, West Virginia and Wyoming. Our footprint allows us to service many of the natural gas producing regions in the United States. We believe that operating in diverse geographic regions allows us better utilization of our compressors, minimal incremental expenses, operating synergies, volume-based purchasing, leveraged inventories and cross-trained personnel. We also sell engineered compression products to international customers.
- **Long-standing customer relationships.** We have developed long-standing relationships providing compression equipment to many major and independent oil and natural gas companies. Our customers generally continue to rent our compressors after the expiration of the initial terms of our rental agreements, which we believe reflects their satisfaction with the reliability and performance of our services and products.

## Major Customers

Sales and rental income to Devon Energy Production, Inc. ("Devon") and EOG Resources, Inc. ("EOG") for the year ended December 31, 2014 amounted to 18% and 15% of our revenue, respectively. Sales and rental income to EOG and Devon in the year ended December 31, 2013 amounted to 18% and 15% of our revenue, respectively. Sales and rental income to EOG and Devon in the year ended December 31, 2012 amounted to 32% and 12% of our revenue. No other single customer accounted for more than 10% of our revenues in 2014, 2013 or 2012.

EOG, Promatcon Tepatguna ("Promatcon") and Occidental Permian, LTD. ("Oxy") amounted to 20%, 18% and 14% of our accounts receivable as of December 31, 2014. EOG and Devon amounted to 18% and 14% of our accounts receivable as of December 31, 2013. No other customers amounted to more than 10% of our accounts receivable as of December 31, 2014 and 2013. The loss of any of the above customers could have a material adverse effect on our business, financial condition, results of operations and cash flows, depending upon the demand for our compressors at the time of such loss and our ability to attract new customers.

## **Sales and Marketing**

Our sales force pursues the rental and sales market for compressors and flare equipment and other services in their respective territories. Additionally, our personnel coordinate with each other to develop relationships with customers who operate in multiple regions. Our sales and marketing strategy is focused on communication with current customers and potential customers through frequent direct contact, technical assistance, print literature, direct mail and referrals. Our sales and marketing personnel coordinate with our operations personnel in order to promptly respond to and address customer needs. Our overall sales and marketing efforts concentrate on demonstrating our commitment to enhancing the customer's cash flow through enhanced product design, fabrication, manufacturing, installation, customer service and support.

## **Competition**

We have a number of competitors in the natural gas compression segment, some of which have greater financial resources. We believe that we compete effectively on the basis of price, customer service, including the ability to place personnel in remote locations, flexibility in meeting customer needs, and quality and reliability of our compressors and related services.

Compressor industry participants can achieve significant advantages through increased size and geographic breadth. As the number of rental compressors in our rental fleet increases, the number of sales, support, and maintenance personnel required and the minimum level of inventory do not increase proportionately.

## **Backlog**

As of December 31, 2014, we had a sales backlog of approximately \$5.8 million compared to \$2.9 million as of December 31, 2013. We expect to fulfill the backlog in the first half of 2015. Sales backlog consists of firm customer orders for which a purchase or work order has been received, satisfactory credit or a financing arrangement exists, and delivery is scheduled. In addition, the major components of our compressors are acquired from suppliers through periodic purchase orders that in many instances require three or four months of lead time prior to delivery of the order.

## **Employees**

As of December 31, 2014, we had 353 total employees, none of which are represented by a labor union. We believe we have good relations with our employees.

## **Liability and Other Insurance Coverage**

Our equipment and services are provided to customers who are subject to hazards inherent in the oil and gas industry, such as blowouts, explosions, craterings, fires, and oil spills. We maintain liability insurance that we believe is customary in the industry and which includes environmental cleanup, but excludes product warranty insurance because the majority of components on our compressor unit are covered by the manufacturers. We also maintain insurance with respect to our facilities. Based on our historical experience, we believe that our insurance coverage is adequate. However, there is a risk that our insurance may not be sufficient to cover any particular loss or that insurance may not cover all losses. In addition, insurance rates have in the past been subject to wide fluctuation, and changes in coverage could result in less coverage, increases in cost or higher deductibles and retentions.

## **Government Regulation**

All of our operations and facilities are subject to numerous federal, state, foreign and local laws, rules and regulations related to various aspects of our business, including containment and disposal of hazardous materials, oilfield waste, other waste materials and acids.

To date, we have not been required to expend significant resources in order to satisfy applicable environmental laws and regulations. We do not anticipate any material capital expenditures for environmental control facilities or extraordinary

expenditures to comply with environmental rules and regulations in the foreseeable future. However, compliance costs under existing laws or under any new requirements could become material and we could incur liabilities for noncompliance.

Our business is generally affected by political developments and by federal, state, foreign and local laws and regulations, which relate to the oil and natural gas industry. The adoption of laws and regulations affecting the oil and natural gas industry for economic, environmental and other policy reasons could increase our costs and could have an adverse effect on our operations. The state and federal environmental laws and regulations that currently apply to our operations could become more stringent in the future.

We have utilized operating and disposal practices that were or are currently standard in the industry. However, materials such as solvents, thinner, waste paint, waste oil, wash down waters and sandblast material may have been disposed of or released in or under properties currently or formerly owned or operated by us or our predecessors. In addition, some of these properties have been operated by third parties over whom we have no control either as to such entities' treatment of materials or the manner in which such materials may have been disposed of or released.

The federal Comprehensive Environmental Response Compensation and Liability Act of 1980, commonly known as CERCLA, and comparable state statutes impose strict liability on:

- owners and operators of sites, and
- persons who disposed of or arranged for the disposal of "hazardous substances" found at sites.

### **Waste Management and Disposal**

The federal Resource Conservation and Recovery Act ("RCRA") and analogous state laws and their implementing regulations govern the generation, transportation, treatment, storage and disposal of hazardous and non-hazardous solid wastes. During the course of our operations, we generate wastes (including, but not limited to, used oil, antifreeze, filters, paints, solvents and abrasive blasting materials) in quantities regulated under RCRA. The EPA and various state agencies have limited the approved methods of disposal for these types of wastes. CERCLA and analogous state laws and their implementing regulations impose strict, and under certain conditions, joint and several liability without regard to fault or the legality of the original conduct on classes of persons who are considered to be responsible for the release of a hazardous substance into the environment. These persons include current and past owners and operators of the facility or disposal site where the release occurred and any company that transported, disposed of, or arranged for the transport or disposal of the hazardous substances released at the site. Under CERCLA, such persons may be subject to joint and several liability for the costs of cleaning up the hazardous substances that have been released into the environment, for damages to natural resources and for the costs of certain health studies. In addition, where contamination may be present, it is not uncommon for neighboring landowners and other third parties to file claims for personal injury, property damage and recovery of response costs allegedly caused by hazardous substances or other pollutants released into the environment.

We currently own or lease, and in the past have owned or leased, a number of properties that have been used in support of our operations for a number of years. Although we have utilized operating and disposal practices that were standard in the industry at the time, hydrocarbons, hazardous substances, or other regulated wastes may have been disposed of or released on or under the properties owned or leased by us or on or under other locations where such materials have been taken for disposal by companies sub-contracted by us. In addition, some of these properties may have been previously owned or operated by third parties whose treatment and disposal or release of hydrocarbons, hazardous substances or other regulated wastes was not under our control. These properties and the materials released or disposed thereon may be subject to CERCLA, RCRA and analogous state laws. Under such laws, we could be required to remove or remediate historical property contamination, or to perform certain operations to prevent future contamination. We are not currently under any order requiring that we undertake or pay for any cleanup activities. However, we cannot provide any assurance that we will not receive any such order in the future.

The federal Water Pollution Control Act and the Oil Pollution Act of 1990 and implementing regulations govern:

- the prevention of discharges, including oil and produced water spills, and
- liability for drainage into waters.



## **Air Emissions**

Our operations are also subject to federal, state, and local regulations. The Clean Air Act and implementing regulations and comparable state laws and regulations regulate emissions of air pollutants from various industrial sources and also impose various monitoring and reporting requirements, including requirements related to emissions from certain stationary engines, such as those on our compressor units. These laws and regulations impose limits on the levels of various substances that may be emitted into the atmosphere from our compressor units and require us to meet more stringent air emission standards and install new emission control equipment on all of our engines built after July 1, 2008. In addition, the EPA issued regulations in 2012 that require the reduction of emissions of volatile organic compounds, air toxics and methane, a greenhouse gas, at certain oil and gas operations. We are not currently aware of material impacts to our operations associated with these rules.

We believe that our existing environmental control procedures are adequate and that we are in substantial compliance with environmental laws and regulations, and the phasing in of emission controls and other known regulatory requirements should not have a material adverse affect on our financial condition or operational results. However, it is possible that future developments, such as new or increasingly strict requirements and environmental laws and enforcement policies there under, could lead to material costs of environmental compliance by us. While we may be able to pass on the additional cost of complying with such laws to our customers, there can be no assurance that attempts to do so will be successful. Some risk of environmental liability and other costs are inherent in the nature of our business, however, and there can be no assurance that environmental costs will not rise.

In recent years, increased concern has been raised over the protection of the environment. Legislation to regulate emissions of greenhouse gases has been introduced in Congress, and there has been a wide-ranging policy debate, both nationally and internationally, regarding the impact of these gases and possible means for their regulation. In addition, efforts have been made and continue to be made in the international community toward the adoption of international treaties or protocols that would address global climate change issues, such as the United Nations Climate Change Conference in Copenhagen in 2009. Also, the EPA has undertaken new efforts to collect information regarding greenhouse gas emissions and their effects. Recently, the EPA declared that certain greenhouse gases represent a danger to human health and proposed to expand its regulations relating to those emissions. To the extent that new laws or other governmental actions restrict the energy industry or impose additional environmental protection requirements that result in increased costs to the oil and gas industry, we could be adversely affected. We cannot determine to what extent our future operations and earnings may be affected by new legislation, new regulations or changes in existing regulations.

## **Occupational Safety and Health**

We are subject to the requirements of Occupational Safety and Health Administration ("OSHA") and comparable state statutes. These laws and the implementing regulations strictly govern the protection of the health and safety of employees. The OSHA hazard communication standard, the EPA community right-to-know regulations under Title III of CERCLA, and similar state statutes require that we maintain and/or disclose information about hazardous materials used or produced in our operations. We believe that we are in compliance with these applicable requirements and with other comparable laws.

## **Patents, Trademarks and Other Intellectual Property**

We believe that the success of our business depends more on the technical competence, creativity and marketing abilities of our employees than on any individual patent, trademark, or copyright. Nevertheless, as part of our ongoing research, development and manufacturing activities, we may seek patents when appropriate on inventions concerning new products and product improvements. We do not own any unexpired patents. Although we continue to use the patented technology and consider it useful in certain applications, we do not consider the expired patent to be material to our business as a whole.

## **Suppliers and Raw Materials**

Fabrication of our rental compressors involves the purchase by us of engines, compressors, coolers and other components, and the assembly of these components on skids for delivery to customer locations. These major components of our compressors are acquired through periodic purchase orders placed with third-party suppliers on an "as needed" basis, which typically requires a three to four month lead time with delivery dates scheduled to coincide with our estimated production schedules. Although we do not have formal continuing supply contracts with any major supplier, we believe we have adequate alternative sources available. In the past, we have not experienced any sudden and dramatic increases in the prices of the major components for our compressors. However, the occurrence of such an event could have a material adverse effect on the results of our operations and financial condition, particularly if we are unable to increase our rental rates and sale prices proportionate to any such component price increases.

## Available Information

We use our website as a channel of distribution for company information. We make available free of charge on the Investor Relations section of our website ( [www.ngsgi.com](http://www.ngsgi.com) ) our Annual Report on Form 10-K, Quarterly Reports on Form 10-Q, and Current Reports on Form 8-K. We also make available through our website other reports filed with or furnished to the SEC under the Securities Exchange Act of 1934, as amended, including our proxy statements and reports filed by officers and directors under Section 16(a) of the Exchange Act, as well as our Code of Business Ethics and the charters to our various Committees of our Board of Directors. Paper copies of our filings are also available, without charge upon written request, at Natural Gas Services Group, Inc., 508 West Wall Street, Suite 550, Midland, Texas 79701. The information contained in our website is not part of this Report.

## Glossary of Industry Terms

"CiP" - A branded, proprietary gas compressor product line designed, manufactured and packaged by the Company. The 'Cylinder in Plane' design results in a compact and vibration-free compressor unit that particularly lends itself to unconventional wellhead applications, air compression and compressed natural gas requirements.

"coal bed methane" – A natural gas generated during coal formation and provided from coal seams or adjacent sandstones.

"flare" – A tall stack equipped with burners used as a safety device at wellheads, refining facilities, gas processing plants, and chemical plants. Flares are used for the combustion and disposal of combustible gases. The gases are piped to a remote, usually elevated, location and burned in an open flame in the open air using a specially designed burner tip, auxiliary fuel, and steam or air. Combustible gases are flared most often due to emergency relief, overpressure, process upsets, startups, shutdowns, and other operational safety reasons. Natural gas that is uneconomical for sale is also flared. Often natural gas is flared as a result of the unavailability of a method for transporting such gas to markets.

"gas lift" – A production enhancement technique whereby natural gas is injected into an oil well to increase/improve the oil production.

"gas shale" – Fine grained rocks where the predominant gas storage mechanism is absorption and gas is stored in volumes that are potentially economic.

"oil shale" – Also referred to as tight oil, is petroleum that consists of light crude oil contained in petroleum-bearing formations of low-permeability, often shale or tight sandstone.

"reciprocating compressors" – A reciprocating compressor is a type of compressor which compresses vapor by using a piston in a cylinder and a back-and-forth motion.

"screw compressors" – A type of compressor used in low-pressure and vapor compression applications where two intermesh rotors create pockets of continuously decreasing volume, in which the gas is compressed and its pressure is increased.

"tight gas" – A gas bearing sandstone or carbonate matrix (which may or may not contain natural fractures) which exhibits a low-permeability (tight) reservoir.

## ITEM 1A. RISK FACTORS

You should carefully consider the following risks associated with owning our common stock. Although the risks described below are the risks that we believe are material, they are not the only risks relating to our industry, our business and our common stock. Additional risks and uncertainties, including those that we have not yet identified or that we currently believe are immaterial, may also adversely affect our business, financial condition or results of operations.

### Risks Associated With Our Industry

*Adverse macroeconomic and business conditions may significantly and negatively affect our results of operations.*

Economic conditions in the United States and abroad have, and will likely continue to, affect our revenue and profitability. The condition of domestic and global financial markets, continued low natural gas prices, and the potential for disruption and illiquidity in the credit markets could have an adverse effect on our operating results and financial condition, and if sustained for an extended period, such adverse effects could become significant. Uncertainty and turmoil in the credit markets may negatively impact the ability of our customers to finance purchases of our products and services and could result in a decrease in, or cancellation of, orders included in our backlog or adversely affect the collectability of our receivables. If the availability of credit to our customers is reduced, they may reduce their drilling and production expenditures, thereby decreasing demand for our products and services, which could have a negative impact on our financial condition. A prolonged period of depressed prices for gas and oil would likely result in delays or cancellation of projects by our customers, reducing the demand for our products and services.

*Decreased oil and natural gas prices and oil and gas industry expenditure levels could adversely affect our revenue.*

Our revenue is derived primarily from expenditures in the oil and natural gas industry, which, in turn, are based on budgets to explore for, develop and produce oil and natural gas. When these expenditures decline, our revenue will suffer. The industry's willingness to explore for, develop and produce oil and natural gas depends largely upon the prevailing view of future oil and natural gas prices. Prices for oil and natural gas historically have been, and are likely to continue to be, highly volatile. Many factors affect the supply and demand for oil and natural gas and, therefore, influence oil and natural gas prices, including:

- the level of oil and natural gas production;
- the level of oil and natural gas inventories;
- domestic and worldwide demand for oil and natural gas;
- the expected cost of developing new reserves;
- the cost of producing oil and natural gas;
- the level of drilling and completions activity;
- inclement weather;
- domestic and worldwide economic activity;
- regulatory and other federal and state requirements in the United States;
- the ability of the Organization of Petroleum Exporting Countries and other large producers to set and maintain production levels and prices for oil;
- political conditions in or affecting oil and natural gas producing countries;
- terrorist activities in the United States and elsewhere;
- the cost of developing alternate energy sources;
- environmental regulation; and
- tax policies.

Depending on the market prices of oil and natural gas, companies exploring for oil and natural gas may cancel or curtail their drilling programs, thereby reducing demand for our equipment and services. Our rental contracts are generally short-term, and oil and natural gas companies tend to respond quickly to upward or downward changes in prices. Any reduction in drilling and production activities may materially erode both pricing and utilization rates for our equipment and services and adversely affects our financial results. As a result, we may suffer losses, be unable to make necessary capital expenditures and be unable to meet our financial obligations.

***The intense competition in our industry could result in reduced profitability and loss of market share for us.***

We compete with the oil and natural gas industry's largest equipment and service providers who have greater name recognition than we do. These companies also have substantially greater financial resources, larger operations and greater budgets for marketing, research and development than we do. They may be better able to compete because of their broader geographic dispersion and ability to take advantage of international opportunities, the greater number of compressors in their fleet or their product and service diversity. As a result, we could lose customers and market share to those competitors. These companies may also be better positioned than us to successfully endure downturns in the oil and natural gas industry.

Our operations may be adversely affected if our current competitors or new market entrants introduce new products or services with better prices, features, performance or other competitive characteristics than our products and services. Competitive pressures or other factors also may result in significant price competition that could harm our revenue and our business. Additionally, we may face competition in our efforts to acquire other businesses.

***Our industry is highly cyclical, and our results of operations may be volatile.***

Our industry is highly cyclical, with periods of high demand and high pricing followed by periods of low demand and low pricing. Periods of low demand intensify the competition in the industry and often result in rental equipment being idle for long periods of time. We may be required to enter into lower rate rental contracts in response to market conditions, and our rentals and sales may decrease as a result of such conditions. Due to the short-term nature of most of our rental contracts, changes in market conditions can quickly affect our business. As a result of the cyclical nature of our industry, our results of operations may be volatile in the future.

***Increased regulation or ban of current fracturing techniques could reduce demand for our compressors***

Fracturing (frac) is a process that results in the creation of fractures in geological formations in order to stimulate production from oil and gas wells. Fracturing is also done to increase the rate and ultimate recovery of oil and natural gas. Hydraulic frac is the technique that has allowed domestic oil and natural gas exploration and production companies to produce massive shale deposits often referred to as unconventional plays. Concerns have been raised over possible environmental damages related to fluids used in the frac process. While the FRAC (Fracturing Responsibility and Awareness of Chemicals) Act has been introduced on multiple occasions in Congress, as of February 1, 2015 the Act has yet to be adopted. The FRAC Act seeks to amend the Safe Drinking Water Act so that hydraulic fracturing would be regulated on a federal level.

A ban of hydraulic fracturing would likely halt some projects, including unconventional projects, at least temporarily. Expanded regulations are likely to introduce a period of uncertainty as companies determine ways to proceed. Any curtailment could result in a reduction of demand for our compressors, potentially affecting both sales and rentals of our units.

***We are subject to extensive environmental laws and regulations that could require us to take costly compliance actions that could harm our financial condition.***

Our fabrication and maintenance operations are significantly affected by stringent and complex federal, state and local laws and regulations governing the discharge of substances into the environment or otherwise relating to environmental protection. In these operations, we generate and manage hazardous wastes such as solvents, thinner, waste paint, waste oil, wash down wastes, and sandblast material. We attempt to use generally accepted operating and disposal practices and, with respect to acquisitions, will attempt to identify and assess whether there is any environmental risk before completing an acquisition. Based on the nature of the industry, however, hydrocarbons or other wastes may have been disposed of or released on or under properties owned or leased by us or on or under other locations where such wastes have been taken for disposal. The waste on these properties may be subject to federal or state environmental laws that could require us to remove the wastes or remediate sites where they have been released. We could be exposed to liability for cleanup costs, natural resource and other damages as a result of our conduct or the conduct of, or conditions caused by, prior owners, lessees or other third parties. Environmental laws and regulations

have changed in the past, and they are likely to change in the future. If current existing regulatory requirements or enforcement policies change, we may be required to make significant unanticipated capital and operating expenditures.

Any failure by us to comply with applicable environmental laws and regulations may result in governmental authorities taking actions against our business that could harm our operations and financial condition, including the:

- issuance of administrative, civil and criminal penalties;
- denial or revocation of permits or other authorizations;
- reduction or cessation in operations; and
- performance of site investigatory, remedial or other corrective actions.

### **Risks Associated With Our Company**

***As of December 31, 2014, a significant majority of our compressor rentals were for terms of six months or less which, if terminated or not renewed, would adversely impact our revenue and our ability to recover our initial equipment costs.***

The length of our compressor rental agreements with our customers varies based on customer needs, equipment configurations and geographic area. In most cases, under currently prevailing rental rates, the initial rental periods are not long enough to enable us to fully recoup the average cost of acquiring or fabricating the equipment. We cannot be sure that a substantial number of our customers will continue to renew their rental agreements or that we will be able to re-rent the equipment to new customers or that any renewals or re-rentals will be at comparable rental rates. The inability to timely renew or re-rent a substantial portion of our compressor rental fleet would have a material adverse effect upon our business, financial condition, results of operations and cash flows.

***We could be subject to substantial liability claims that could harm our financial condition.***

Our products are used in production applications where an accident or a failure of a product can cause personal injury, loss of life, damage to property, equipment or the environment, or suspension of operations. While we maintain insurance coverage, we face the following risks under our insurance coverage:

- we may not be able to continue to obtain insurance on commercially reasonable terms;
- we may be faced with types of liabilities that will not be covered by our insurance, such as damages from significant product liabilities and from environmental contamination;
- the dollar amount of any liabilities may exceed our policy limits; and
- we do not maintain coverage against the risk of interruption of our business.

Any claims made under our policies will likely cause our premiums to increase. Any future damages caused by our products or services that are not covered by insurance, are in excess of policy limits or are subject to substantial deductibles, would reduce our earnings and our cash available for operations.

***We might be unable to employ qualified technical personnel, which could hamper our present operations or increase our costs.***

Many of the compressors that we sell or rent are mechanically complex and often must perform in harsh conditions. We believe that our success depends upon our ability to employ and retain a sufficient number of technical personnel who have the ability to design, utilize, enhance and maintain these compressors. Our ability to expand our operations depends in part on our ability to increase our skilled labor force. The demand for skilled workers is high, and supply is limited. A significant increase in the wages paid by competing employers could result in a reduction of our skilled labor force or cause an increase in the wage rates that we must pay or both. If either of these events were to occur, our cost structure could increase and our operations and growth potential could be impaired.

***We will require a substantial amount of capital to expand our compressor rental fleet and grow our business.***

During 2015, the amount we will spend on capital expenditures related to rental compression equipment will be determined primarily by the activity of our customers. We do not anticipate demand for our products exceeding what we can fund with internally generated funds and additional bank borrowing with our current bank line. The amount and timing of any of these capital expenditures may vary depending on a variety of factors, including the level of activity in the oil and natural gas exploration and production industry and the presence of alternative uses for our capital, including any acquisitions that we may pursue.

Historically, we have funded our capital expenditures through internally generated funds, borrowings under bank credit facilities. Although we believe that cash flows from our operations will provide us with sufficient cash to fund our planned capital expenditures for 2015, we cannot assure you that these sources will be sufficient. We may require additional capital to fund any unanticipated capital expenditures, including any acquisitions, and to fund our growth beyond 2015, and necessary capital may not be available to us when we need it or on acceptable terms. Our ability to raise additional capital will depend on the results of our operations and the status of various capital and industry markets at the time we seek such capital. Failure to generate sufficient cash flow, together with the absence of alternative sources of capital, could have a material adverse effect on our business, financial condition, results of operations or cash flow.

Of our \$30 million line of credit, we owe \$417,000 as of December 31, 2014. All outstanding principal and unpaid interest is due on December 31, 2017. Although we believe that we will be able to renew our existing line of credit, or obtain a new line of credit with another lender, we can provide no assurance that we will be successful in renewing our line of credit or obtaining a new line. In addition, any renewal of our existing line of credit or creation of a new line of credit may be on terms less favorable than our existing line. For instance, changes in the terms of a new line of credit may include, but not be limited to: a reduction in the borrowing amount, an increase in interest rate to be paid on borrowings under the line, or restrictive covenants that are more onerous than those on our existing line of credit.

We believe that the lender participating in our current credit agreement has adequate capital and resources. If our current lender were to encounter difficulties, it is possible that the borrowing capacity under our credit agreement would be reduced or eliminated. In the event that the availability under our credit agreement was reduced significantly, we could be required to obtain capital from alternate sources in order to finance our capital needs. Our options for addressing such capital constraints would include, but not be limited to (1) obtaining commitments from other banks to fund increased amounts under the terms of our credit agreement, (2) accessing the public capital markets, or (3) delaying certain projects. If it became necessary to access additional capital, any alternatives at the time may be on terms less favorable than under our existing credit agreement terms, which could have a material effect on our consolidated financial position, results of operations and cash flows. If future financing is not available to us when required, as a result of limited access to the credit markets or otherwise, or is not available to us on acceptable terms, we may be unable to take advantage of business opportunities or respond to competitive pressures, either of which could have a material adverse effect on our consolidated financial position, results of operations and cash flows.

***Our debt levels may negatively impact our current and future financial stability.***

Should we utilize our full debt capacity, growth beyond that point could be impacted. As of December 31, 2014, we had an aggregate of approximately \$417,000 of outstanding indebtedness, and accounts payable, accrued expenses and current income tax liability of approximately \$12.5 million. As a result of our indebtedness at any given point in time, we might not have the ability to incur any substantial additional indebtedness. The level of our indebtedness could have several important effects on our future operations, including:

- our ability to obtain additional financing for working capital, acquisitions, capital expenditures and other purposes may be limited;
- a significant portion of our cash flow from operations may be dedicated to the payment of principal and interest on our debt, thereby reducing funds available for other purposes; and
- our leverage if increased to an unacceptable level, could make us more vulnerable to economic downturns.

***If we are unable to service our debt, we will likely be forced to take remedial steps that are contrary to our business plan.***

As of December 31, 2014, we had \$417,000 due under our Line of Credit agreement which allows us to borrow up to \$30.0 million provided we maintain certain collateral and borrowing base requirements. We believe that our current cash position and the amount available under the current revolver are sufficient to meet our capital needs through 2015. However, if we were to materially increase our borrowings, it is possible that our business will not generate sufficient cash flow from operations to

meet our debt service requirements and the payment of principal when due depending on the amount of borrowings on the agreement at any given time. If this were to occur, we may be forced to:

- sell assets at disadvantageous prices;
- obtain additional financing; or
- refinance all or a portion of our indebtedness on terms that may be less favorable to us.

***Our current credit agreement contains covenants that limit our operating and financial flexibility and, if breached, could expose us to severe remedial provisions.***

Under the terms of our credit agreement, we must:

- comply with a minimum leverage ratio;
- comply with a commitment coverage ratio;
- not exceed specified levels of debt; and
- comply with limits on asset sales.

Our ability to meet the financial ratios and tests under our credit agreement can be affected by events beyond our control, and we may not be able to satisfy those ratios and tests. A breach of any one of these covenants could permit the bank to accelerate the debt so that it is immediately due and payable. If a breach occurred, no further borrowings would be available under our credit agreement. If we were unable to repay the debt, the bank could proceed against and foreclose on our assets, substantially all of which have been pledged as collateral to secure payment of our indebtedness.

***If we fail to acquire or successfully integrate additional businesses, our growth may be limited and our results of operations may suffer.***

As part of our business strategy, we intend to evaluate potential acquisitions of other businesses or assets. However, there can be no assurance that we will be successful in consummating any such acquisitions. Successful acquisition of businesses or assets will depend on various factors, including, but not limited to, our ability to obtain financing and the competitive environment for acquisitions. In addition, we may not be able to successfully integrate any businesses or assets that we acquire in the future. The integration of acquired businesses is likely to be complex and time consuming and place a significant strain on management and may disrupt our business. We also may be adversely impacted by any unknown liabilities of acquired businesses, including environmental liabilities. We may encounter substantial difficulties, costs and delays involved in integrating common accounting, information and communication systems, operating procedures, internal controls and human resources practices, including incompatibility of business cultures and the loss of key employees and customers. These difficulties may reduce our ability to gain customers or retain existing customers, and may increase operating expenses, resulting in reduced revenues and income and a failure to realize the anticipated benefits of acquisitions.

***The loss of one or more of our current customers could adversely affect our results of operations.***

Our business is dependent not only on securing new customers but also on maintaining current customers. We had two customers that accounted for approximately 33% of our revenue for the year ended December 31, 2014, and two customers that accounted for approximately 33% of our revenue for the year ended December 31, 2013. At December 31, 2014, three customers accounted for 52% of our accounts receivable. Unless we are able to retain our existing customers, or secure new customers if we lose one or more of our significant customers, our revenue and results of operations would be adversely affected. In addition, the default on payments by one or more of these significant customers may negatively impact our cash flow and current assets.

***Loss of key members of our management could adversely affect our business.***

In keeping with our streamlined approach to our business, our executive management team is limited to three officers: our (i) Chief Executive Officer, (ii) Chief Financial Officer and (iii) Vice President of Technical Services. We depend on the continued employment and performance of these three key members of our executive management team. In particular, we are significantly reliant upon the leadership and guidance of Stephen C. Taylor, who has been our President, Chief Executive Officer and Board member since 2004. In addition to his management duties, Mr. Taylor has been instrumental in our communications and standing with the investment community. If any of our key executives resign or become unable to continue in his present role and is not adequately replaced, our business operations could be materially adversely affected. We do not carry any key-man insurance on any of our officers or directors.

***Failure to effectively manage our growth and expansion could adversely affect our business and operating results and our internal controls.***

We have significantly expanded our operations since our formation in 1998 and anticipate that our growth will continue if we are able to execute our strategy, subject to the supply and demand for oil and natural gas. Future growth may place significant strain on our management and other resources. To manage our future growth, we must be able to, among other things:

- accurately assess the number of additional officers and employees we will require and the areas in which they will be required;
- attract, hire and retain additional highly skilled and motivated officers and employees;
- train and manage our work force in a timely and effective manner;
- upgrade and expand our office infrastructure so that it is appropriate for our level of activity; and
- improve our financial and management controls, reporting systems and procedures.

***Liability to customers under warranties and indemnification provisions may materially and adversely affect our earnings.***

We provide warranties as to the proper operation and conformance to specifications of the equipment we manufacture. Our equipment is complex and often deployed in harsh environments. Failure of this equipment to operate properly or to meet specifications may increase our costs by requiring additional engineering resources and services, replacement of parts and equipment or monetary reimbursement to a customer. We have in the past received warranty claims and we expect to continue to receive them in the future. To the extent that we incur substantial warranty claims in any period, our reputation, our ability to obtain future business and our earnings could be materially and adversely affected.

Our rental and sales contracts provide for varying forms of indemnification from our customers and in most cases may require us to indemnify our customers. Under some of our rental and sales contracts, liability with respect to personnel and property is customarily assigned on a “knock-for-knock” basis, which means that we and our customers assume liability for our respective personnel and property. However, in certain rental and sales contracts we assume liability for damage to our customer’s property and other third-party on the site resulting from our negligence. Since our products are used in production applications in the energy industry, expenses and liabilities in connection with accidents involving our products and services could be extensive and may exceed our insurance coverages.

***Failure to maintain effective internal controls could have a material adverse effect on our operations.***

Section 404 of the Sarbanes-Oxley Act requires annual management assessments of the effectiveness of our internal control over financial reporting. If we fail to maintain effective internal controls, we may not be able to ensure that we can conclude on an ongoing basis that we have effective internal controls over financial reporting in accordance with Section 404 of the Sarbanes-Oxley Act. Moreover, effective internal controls are necessary for us to produce reliable financial reports and to help prevent financial fraud. If, as a result of deficiencies in our internal controls, we cannot provide reliable financial reports or prevent fraud, our business decision process may be adversely affected, our business and operating results could be harmed, investors could lose confidence in our reported financial information, and the price of our stock could decrease as a result.



***A reduction in demand primarily for natural gas or prices for this commodity and credit markets could adversely affect our business.***

Our results of operations depend upon the level of activity in the energy market, including natural gas development, production, processing and transportation. Oil and natural gas prices and the level of drilling and exploration activity can be volatile. For example, oil and natural gas exploration and development activity and the number of well completions typically decline when there is a significant reduction in oil and natural gas prices or significant instability in energy markets. As a result, the demand for our natural gas compression services could be adversely affected. A reduction in demand could also force us to reduce our pricing substantially. Additionally, our customers' production from unconventional natural gas sources such as tight sands, shale and coal beds constitute the majority percentage of our business. Such unconventional sources are generally less economically feasible to produce in lower natural gas price environments. These factors could in turn negatively impact the demand for our products and services. A decline in demand for oil and natural gas or prices for those commodities and credit markets generally have a material adverse effect on our business, financial condition, results of operations.

***The erosion of the financial condition of our customers could adversely affect our business.***

Many of our customers finance their exploration and development activities through cash flow from operations, the incurrence of debt or the issuance of equity. During times when the oil or natural gas markets weaken, our customers are more likely to experience a downturn in their financial condition. Many of our customers' equity values substantially declined during the most recent recession, and in some cases access to capital markets may be an unreliable source of financing for some customers. The combination of a reduction in cash flow resulting from declines in commodity prices, a reduction in borrowing bases under reserve-based credit facilities and the lack of availability of debt or equity financing may result in flat or moderate growth in our customers' spending for our products and services in 2015. For example, our customers could seek to preserve capital by canceling month-to-month contracts, canceling or delaying scheduled maintenance of their existing natural gas compression equipment or determining not to enter into any new natural gas compression service contracts or purchase new compression equipment.

#### **Risks Associated With Our Common Stock**

***The price of our common stock may fluctuate.***

The trading price of our common stock and the price at which we may sell securities in the future is subject to substantial fluctuations in response to various factors, including our ability to successfully accomplish our business strategy, the trading volume of our stock, changes in governmental regulations, actual or anticipated variations in our quarterly or annual financial results, our involvement in litigation, general market conditions, the prices of oil and natural gas, announcements by us and our competitors, our liquidity, our ability to raise additional funds, and other events.

***Future sales of our common stock could adversely affect our stock price.***

Substantial sales of our common stock in the public market, or the perception by the market that those sales could occur, may lower our stock price or make it difficult for us to raise additional equity capital in the future. An aggregate of 23.6% of the outstanding shares of our common stock are owned by three institutional investors, each of which own more than 5% of our outstanding shares as of March 2, 2015. Potential sales of large amounts of these shares in a short period of time by one or more of these significant investors could have a negative impact on our stock price. In addition, potential sales of our common stock by our directors and officers, who beneficially own approximately 6.7% of the outstanding shares of our common stock as of March 2, 2015, could also have a negative impact on our stock price.

We currently have on file with the SEC an effective "universal" shelf registration statement on Form S-3, which enables us to sell, from time to time, our common stock and other securities covered by the registration statement in one or more public offerings. The shelf registration statement allows us to enter the public markets and consummate sales of the registered securities in rapid fashion and with little or no notice. Issuances of securities under our shelf registration statement may dilute our existing shareholders. See "Management's Discussion and Analysis of Financial Condition and Results of Operations — Liquidity and Capital Resources."

***We have a comparatively low number of shares of common stock outstanding and, therefore, our common stock may suffer from limited liquidity and its prices will likely be volatile and its value may be adversely affected.***

Because of our relatively low number of outstanding shares of common stock, the trading price of our common stock will likely be subject to significant price fluctuations and limited liquidity. This may adversely affect the value of your investment. In addition, our common stock price could be subject to fluctuations in response to variations in quarterly operating results, changes in management, future announcements concerning us, general trends in the industry and other events or factors as well as those described above.

***If we issue debt or equity securities, you may lose certain rights and be diluted.***

If we raise funds in the future through the issuance of debt or equity securities, the securities issued may have rights and preferences and privileges senior to those of holders of our common stock, and the terms of the securities may impose restrictions on our operations or dilute your ownership in our Company.

***If securities analysts downgrade our stock or cease coverage of us, the price of our stock could decline.***

The trading market for our common stock relies in part on the research and reports that industry or financial analysts publish about us or our business. We do not control these analysts. Furthermore, there are many large, well-established, publicly traded companies active in our industry and market, which may mean that it is less likely that we will receive widespread analyst coverage. If one or more of the analysts who do cover us downgrade our stock, our stock price would likely decline rapidly. If one or more of these analysts cease coverage of our company, we could lose visibility in the market, which in turn could cause our stock price to decline.

***We do not intend to pay, and have restrictions upon our ability to pay, dividends on our common stock.***

We have not paid cash dividends in the past and do not intend to pay dividends on our common stock in the foreseeable future. Net income from our operations, if any, will be used for the development of our business, including capital expenditures, and to retire debt. In addition, our credit agreement contains restrictions on our ability to pay cash dividends on our common stock.

***Provisions contained in our governing documents could hinder a change in control of us.***

Our articles of incorporation and bylaws contain provisions that may discourage acquisition bids and may limit the price investors are willing to pay for our common stock. Our articles of incorporation and bylaws provide that:

- directors are elected for three-year terms, with approximately one-third of the board of directors standing for election each year;
- cumulative voting is not allowed, which limits the ability of minority shareholders to elect any directors;
- the unanimous vote of the board of directors or the affirmative vote of the holders of not less than 80% of the votes entitled to be cast by the holders of all shares entitled to vote in the election of directors is required to change the size of the board of directors; and
- directors may be removed only for cause and only by the holders of not less than 80% of the votes entitled to be cast on the matter.

Our Board of Directors has the authority to issue up to five million shares of preferred stock. The Board of Directors can fix the terms of the preferred stock without any action on the part of our stockholders. The issuance of shares of preferred stock may delay or prevent a change in control transaction. In addition, preferred stock could be used in connection with the Board of Directors' adoption of a shareholders' rights plan (also known as a poison pill), which would make it much more difficult to effect a change in control of our company through acquiring or controlling blocks of stock. Also, our directors and officers as a group will continue to beneficially own stock and although this is not a majority of our stock, it confers substantial voting power in the election of directors and management of our company. This would make it difficult for other minority stockholders to effect a change in control or otherwise extend any significant control over our management. This may adversely affect the market price and interfere with the voting and other rights of our common stock.

**ITEM 1B. UNRESOLVED STAFF COMMENTS**

None.

**ITEM 2. PROPERTIES**

The table below describes the material facilities owned or leased by Natural Gas Services Group as of December 31, 2014:

Location	Status	Square Feet	Uses
Tulsa, Oklahoma	Owned and Leased	91,780	Compressor fabrication, rental and services
Midland, Texas	Owned	70,000	Compressor fabrication, rental and services
Lewiston, Michigan	Owned	15,360	Compressor fabrication, rental and services
Midland, Texas	Leased	13,135	Corporate offices
Bloomfield, New Mexico	Owned	7,000	Office and parts and services
Bridgeport, Texas	Leased	4,500	Office and parts and services
Midland, Texas	Owned	4,100	Parts and services
Godley, Texas	Leased	5,000	Parts and services
Vernal, Utah	Leased	3,200	Parts and services
Carrollton, Ohio	Leased	2,600	Parts and services
Loveland, Colorado	Leased	2,400	Parts and services
Wheeler, Texas	Leased	2,160	Parts and services
Grapevine, Texas	Leased	800	Sales
Total		<u>222,035</u>	

We believe that our properties are generally well maintained and in good condition and adequate for our purposes.

**ITEM 3. LEGAL PROCEEDINGS**

From time to time, we are a party to various legal proceedings in the ordinary course of our business. While management is unable to predict the ultimate outcome of these actions, it believes that any ultimate liability arising from these actions will not have a material effect on our financial position, results of operations or cash flow. We are not currently a party to any bankruptcy, receivership, reorganization, adjustment or similar proceeding, and we are not aware of any threatened litigation.

**ITEM 4. MINE SAFETY DISCLOSURES**

Not applicable.

## PART II

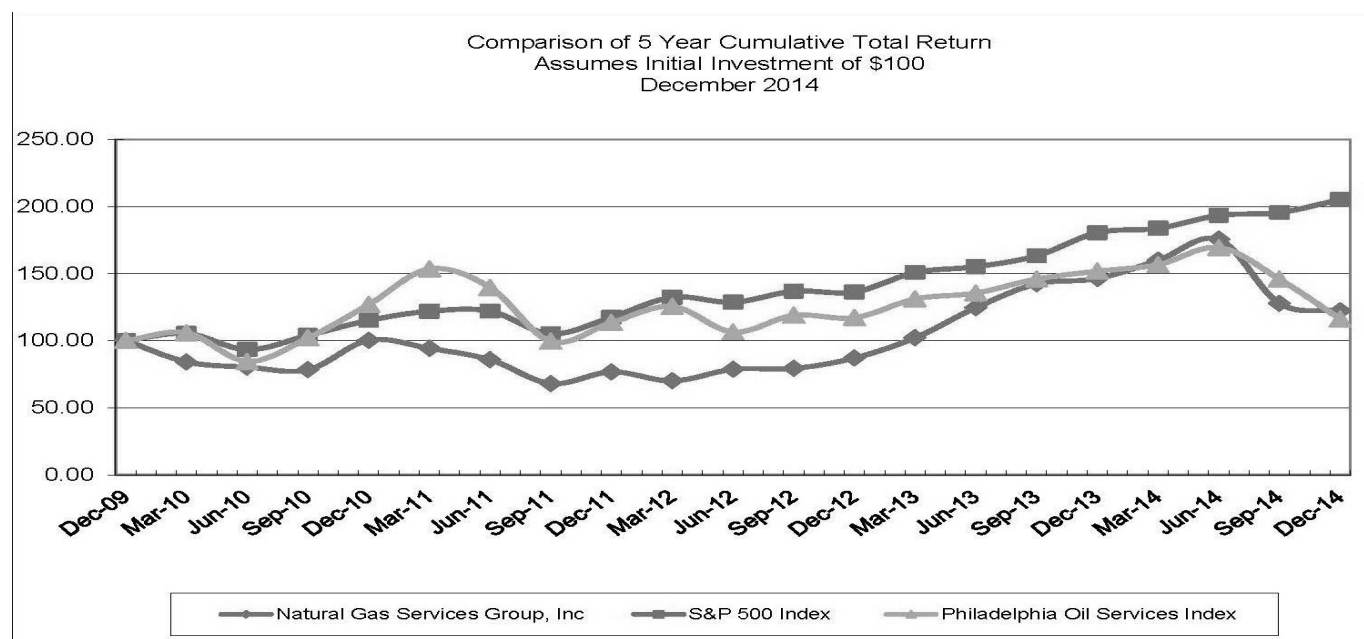
### ITEM 5. MARKET FOR REGISTRANT’S COMMON EQUITY, RELATED STOCKHOLDER MATTERS AND ISSUER PURCHASES OF EQUITY SECURITIES

Our common stock currently trades on the New York Stock Exchange under the symbol “NGS”. The following table sets forth for the periods indicated the high and low sales prices for our common stock as reported for 2014 and 2013.

2014	Low	High
First Quarter	\$26.19	\$34.81
Second Quarter	28.90	34.69
Third Quarter	23.80	33.36
Fourth Quarter	21.23	26.75
2013	Low	High
First Quarter	\$16.76	\$19.26
Second Quarter	18.82	23.86
Third Quarter	24.06	27.99
Fourth Quarter	25.26	30.52

As of December 31, 2014 as reflected by our transfer agent records, we had 16 record holders of our common stock. This number does not include any beneficial owners for whom shares of common stock may be held in “nominee” or “street” name. On March 6, 2015, the last reported sale price of our common stock as reported by the New York Stock Exchange was \$18.35 per share.

The following graph shows a five year comparison of the cumulative total stockholder return on Natural Gas Services Group common stock as compared to the cumulative total return of two other indexes: a custom composite index of the Philadelphia Oil Service Index and the Standard & Poor’s 500 Composite Stock Price Index. These comparisons assume an initial investment of \$100 and the reinvestment of dividends.



The performance graph shall not be deemed incorporated by reference by any general statement incorporating by reference the Annual Report on Form 10-K into any filing under the Securities Act of 1933 or the Securities Exchange Act of 1934, except to the extent that we specifically incorporate this information by reference, and shall not otherwise be deemed filed under those Acts.

## Dividends

To date, we have not declared or paid any dividends on our common stock. We currently do not anticipate paying any cash dividends in the foreseeable future on our common stock. Although we intend to retain our earnings, if any, to finance the growth of our business, our Board of Directors will have the discretion to declare and pay dividends in the future. Payment of dividends in the future will depend upon our earnings, capital requirements, and other factors, which our Board of Directors may deem relevant. Our credit agreement also contains restrictions on our paying dividends.

## Equity Compensation Plans

The following table summarizes certain information regarding our equity compensation plans as of December 31, 2014:

Plan Category	(a) Number of Securities to be Issued Upon Exercise of Outstanding Options, Warrants and Rights	(b) Weighted- average Exercise Price of Outstanding Options, Warrants and Rights	(c) Number of Securities Remaining Available for Future Issuance Under Equity Compensation Plans (Excluding Securities Reflected in Column (a))
Equity compensation plans approved by security holders:			
Stock Option Plan	432,269 <sup>(1)</sup>	\$ 17.55	186,419
Restricted Stock / Unit Plan	99,238	\$ 28.22	473,717
Equity compensation plans not approved by security holders	20,000 <sup>(2)</sup>	\$ 18.15	—
Total	<u>551,507</u>		<u>660,136</u>

(1) Total number of shares to be issued upon exercise of options granted to employees, officers, and directors under our 1998 stock option plan.

(2) Total number of shares to be issued upon exercise of options granted outside of our 1998 stock option plan to Stephen C. Taylor, our Chief Executive Officer, under the terms of his initial employment.

## Repurchase of Equity Securities

No repurchases of our securities were made by us or on our behalf by any “affiliated purchaser” during the year ended December 31, 2014.

## Sale of Unregistered Securities

We made no sales of unregistered securities during the year ended December 31, 2014.

## ITEM 6. SELECTED FINANCIAL DATA

In the table below, we provide you with selected historical financial data. We have derived this information from our audited financial statements for each of the years in the five-year period ended December 31, 2014. This information is only a summary and it is important that you read this information along with our audited financial statements and related notes and “Management’s Discussion and Analysis of Financial Condition and Results of Operations” under Item 7 below, which discusses factors affecting the comparability of the information presented. The selected financial information provided is not necessarily indicative of our future results of operations or financial performance.

	Year Ended December 31,				
	2014	2013	2012	2011	2010
	<i>(in thousands, except per share amounts)</i>				
<b>STATEMENTS OF INCOME AND OTHER INFORMATION:</b>					
Revenues	\$ 96,974	\$ 89,248	\$ 93,722	\$ 65,158	\$ 53,908
Costs of revenues, exclusive of depreciation and amortization shown separately below	43,147	40,943	49,907	30,394	24,750
Gross margin(1)	53,827	48,305	43,815	34,764	29,158
Depreciation and amortization	21,507	18,144	15,707	13,994	11,927
Other operating expenses	10,334	8,141	7,893	5,910	5,867
Operating income	21,986	22,020	20,215	14,860	11,364
Total other income (expense)	172	492	(4)	769	(64)
Income before income taxes	22,158	22,512	20,211	15,629	11,300
Income tax expense	8,030	8,122	7,526	5,869	4,272
Net income	\$ 14,128	\$ 14,390	\$ 12,685	\$ 9,760	\$ 7,028
Net income per common share:					
Basic	\$ 1.14	\$ 1.17	\$ 1.04	\$ 0.80	\$ 0.58
Diluted	\$ 1.11	\$ 1.15	\$ 1.03	\$ 0.80	\$ 0.58
Weighted average shares of common stock outstanding:					
Basic	12,434	12,324	12,220	12,148	12,108
Diluted	12,721	12,550	12,320	12,250	12,210
EBITDA(2)	\$ 43,675	\$ 40,712	\$ 35,936	\$ 29,678	\$ 23,421
Cash flows from:					
Operating Activities	\$ 34,564	\$ 39,244	\$ 35,418	\$ 33,623	\$ 28,798
Investing Activities	(53,102)	(43,324)	(23,761)	(35,506)	(21,861)
Financing Activities	276	437	39	(864)	(10,817)
Net change in cash and cash equivalents	\$ (18,262)	\$ (3,643)	\$ 11,696	\$ (2,747)	\$ (3,880)

	As of December 31,				
	2014	2013	2012	2011	2010
	<i>(in thousands)</i>				
<b>BALANCE SHEET INFORMATION:</b>					
Current assets	\$ 55,927	\$ 60,645	\$ 62,036	\$ 49,503	\$ 48,338
Total assets	283,563	256,589	232,751	212,164	188,769
Long-term debt (including current portion)	417	577	897	1,017	2,000
Stockholders’ equity	210,587	192,737	175,825	161,542	150,591

(1) Gross margin is defined, reconciled to net income and discussed immediately below under “-- Non-GAAP Financial Measures”.

(2) EBITDA is defined, reconciled to net income and discussed immediately below under “-- Non-GAAP Financial Measures”.

## Non-GAAP Financial Measures

### *Our definition and use of EBITDA*

“EBITDA” is a non-GAAP financial measure that we define as earnings (net income) from operations before interest, taxes, depreciation, and amortization. This term, as used and defined by us, may not be comparable to similarly titled measures employed by other companies and is not a measure of performance calculated in accordance with GAAP. EBITDA should not be considered in isolation or as a substitute for operating income, net income or loss, cash flows provided by operating, investing and financing activities, or other income or cash flow statement data prepared in accordance with GAAP. However, management believes EBITDA is useful to an investor in evaluating our operating performance because:

- it is widely used by investors in the energy industry to measure a company’s operating performance without regard to items excluded from the calculation of EBITDA, which can vary substantially from company to company depending upon accounting methods and book value of assets, capital structure and the method by which assets were acquired, among other factors;
- it helps investors to more meaningfully evaluate and compare the results of our operations from period to period by removing the impact of our capital structure and asset base from our operating structure; and
- it is used by our management for various purposes, including as a measure of operating performance, in presentations to our Board of Directors, as a basis for strategic planning and forecasting, and as a component for setting incentive compensation.

EBITDA has limitations as an analytical tool, and you should not consider it in isolation, or as a substitute for analysis of our results as reported under generally accepted accounting principles. Some of these limitations are:

- EBITDA does not reflect our cash expenditures, or future requirements for capital expenditures or contractual commitments;
- EBITDA does not reflect changes in, or cash requirements for, our working capital needs;
- EBITDA does not reflect the cash requirements necessary to service interest or principal payments on our debts; and
- although depreciation and amortization are non-cash charges, the assets being depreciated and amortized will often have to be replaced in the future, and EBITDA does not reflect any cash requirements for such replacements.

There are other material limitations to using EBITDA as a measure of performance, including the inability to analyze the impact of certain recurring items that materially affect our net income or loss, and the lack of comparability of results of operations of different companies. Please read the table below under “Reconciliation” to see how EBITDA reconciles to our net income, the most directly comparable GAAP financial measure.

### *Definition and use of gross margin*

We define gross margin as total revenue less costs (excluding depreciation and amortization expense). Gross margin is included as a supplemental disclosure because it is a primary measure used by our management as it represents the results of revenue and costs (excluding depreciation and amortization expense), which are key components of our operations. Gross margin differs from gross profit, in that gross profit includes depreciation expense. We believe gross margin is important because it focuses on the current operating performance of our operations and excludes the impact of the prior historical costs of the assets acquired or constructed that are utilized in those operations, the indirect costs associated with our selling, general and administrative activities, the impact of our financing methods and income taxes. Depreciation expense may not accurately reflect the costs required to maintain and replenish the operational usage of our assets and therefore may not portray the costs from current operating activity. Rather, depreciation expense reflects the systematic allocation of historical property and equipment values over the estimated useful lives.

Gross margin has certain material limitations associated with its use as compared to net income. These limitations are primarily due to the exclusion of certain expenses. Each of these excluded expenses is material to our results of operations. Because we use capital assets, depreciation expense is a necessary element of our costs and our ability to generate revenue and selling, general and administrative expense is a necessary cost to support our operations and required corporate activities. In order to compensate for these limitations, management uses this non-GAAP measure as a supplemental measure to other GAAP results to provide a more complete understanding of our performance.

As an indicator of our operating performance, gross margin should not be considered an alternative to, or more meaningful than, net income as determined in accordance with GAAP. Our gross margin may not be comparable to a similarly titled measure of another company because other entities may not calculate gross margin in the same manner.

### *Reconciliation*

The following table reconciles EBITDA and gross margin to our net income, the most directly comparable GAAP financial measure:

	Year Ended December 31,				
	2014	2013	2012	2011	2010
	<i>(in thousands)</i>				
Net Income	\$ 14,128	\$ 14,390	\$ 12,685	\$ 9,760	\$ 7,028
Interest expense, net	10	56	18	55	194
Income taxes	8,030	8,122	7,526	5,869	4,272
Depreciation and amortization	21,507	18,144	15,707	13,994	11,927
EBITDA	43,675	40,712	35,936	29,678	23,421
Other operating expenses	10,334	8,141	7,893	5,910	5,867
Other expenses (income)	(182)	(548)	(14)	(824)	(130)
Gross Margin	\$ 53,827	\$ 48,305	\$ 43,815	\$ 34,764	\$ 29,158

## **ITEM 7. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS**

The following discussion is intended to assist you in understanding our financial position and results of operations for each of the years ended December 31, 2014, 2013, and 2012. You should read the following discussion and analysis in conjunction with our audited financial statements and the related notes.

The following discussion contains forward-looking statements. For a description of limitations inherent in forward-looking statements, see "Special Note Regarding Forward-Looking Statements" on page (ii).

### **Overview**

We fabricate, manufacture, rent and sell natural gas compressors and related equipment. Our primary focus is on the rental of natural gas compressors. Our rental contracts generally provide for initial terms of six to 24 months. After the initial term of our rental contracts, most of our customers have continued to rent our compressors on a month-to-month basis. Rental amounts are paid monthly in advance and include maintenance of the rented compressors. As of December 31, 2014, we had 2,189 natural gas compressors totaling 301,392 horsepower rented to 102 customers, compared to 2,038 natural gas compressors totaling 283,165 horsepower rented to 95 customers at December 31, 2013. Of the 2,189 compressors rented at December 31, 2014, 1,784 were rented on a month-to-month basis.

We also fabricate natural gas compressors for sale to our customers, designing compressors to meet unique specifications dictated by well pressures, production characteristics and particular applications for which compression is sought. Fabrication of compressors involves the purchase by us of engines, compressors, coolers and other components, and then assembling these components on skids for delivery to customer locations. These major components of our compressors are acquired through periodic purchase orders placed with third-party suppliers on an "as needed" basis, which presently requires a three to four month lead time with delivery dates scheduled to coincide with our estimated production schedules. Although we do not have formal continuing supply contracts with any major supplier, we believe we have adequate alternative sources available. In the past, we have not experienced any sudden and dramatic increases in the prices of the major components for our compressors. However, the occurrence of such an event could have a material adverse effect on the results of our operations and financial condition, particularly if we were unable to increase our rental rates and sales prices proportionate to any such component price increases.

We also manufacture a proprietary line of compressor frames, cylinders and parts, known as our CiP (Cylinder-in-Plane) product line. We use finished CiP component products in the fabrication of compressor units for sale or rental by us or sell the finished component products to other compressor fabricators. We also design, fabricate, sell, install and service flare stacks



and related ignition and control devices for onshore and offshore incineration of gas compounds such as hydrogen sulfide, carbon dioxide, natural gas and liquefied petroleum gases. To provide customer support for our compressor and flare sales businesses, we stock varying levels of replacement parts at our Midland, Texas facility and at field service locations. We also provide an exchange and rebuild program for screw compressors and maintain an inventory of new and used compressors to facilitate this business.

We provide service and maintenance to our customers under written maintenance contracts or on an as required basis in the absence of a service contract. Maintenance agreements typically have terms of six months to one year and require payment of a monthly fee.

The following table sets forth our revenues from each of our three operating categories for the periods presented:

	Year Ended December 31,		
	2014	2013	2012
	(in thousands)		
Rental	\$ 78,983	\$ 69,062	\$ 56,477
Sales	17,200	19,479	36,375
Service and maintenance	791	707	870
Total	<u>\$ 96,974</u>	<u>\$ 89,248</u>	<u>\$ 93,722</u>

Our strategy for growth is focused on our compressor rental business. Margins, exclusive of depreciation and amortization, for our rental business historically run in the high 50% to low 60% range, while margins for the compressor sales business tend to be in the mid 20% range. If our rental business grows and contributes a larger percentage of our total revenues, we expect our overall company-wide margins to improve over time.

The oil and natural gas equipment rental and services industry is cyclical in nature. The most critical factor in assessing the outlook for the industry is the worldwide supply and demand for natural gas and oil and the corresponding changes in commodity prices. As demand and prices increase, oil and natural gas producers increase their capital expenditures for drilling, development and production activities. Generally, the increased capital expenditures ultimately result in greater revenues and profits for service and equipment companies.

In general, we expect our overall business activity and revenues to track the level of activity in the natural gas industry, with changes in domestic natural gas production and consumption levels and prices more significantly affecting our business than changes in crude oil and condensate production and consumption levels and prices. We also believe that demand for compression services and products is driven by declining reservoir pressure in maturing natural gas producing fields and, more recently, by increased focus by producers on non-conventional natural gas production, such as coal bed methane, gas shale and tight gas, which typically requires more compression than production from conventional natural gas reservoirs.

Demand for our products and services was strong throughout most of 2008, but in 2009 the demand declined due to lower natural gas prices, decreased demand for natural gas and the economic recession. During 2010, the economy began to recover and demand for our products began to strengthen. This recovery has continued through 2014 due to increasing oil prices, in spite of continued low natural gas prices. Towards the end of 2014 crude oil prices collapsed, placing uncertainty on the growth in demand for our products and services.

For fiscal year 2015, our forecasted capital expenditures will be directly dependent upon our customers' compression requirements and are not anticipated to exceed our internally generated cash flows. Any required capital will be for additions to our compressor rental fleet and/or addition or replacement of service vehicles. We believe that cash flows from operations will be sufficient to satisfy our capital and liquidity requirements through 2015. We may require additional capital to fund any unanticipated expenditures, including any acquisitions of other businesses, although that capital may not be available to us when we need it or on acceptable terms.

Notwithstanding the continued uncertain economy and low energy price environment, we believe the long-term trend in our market is favorable.

## Critical Accounting Policies and Practices

We have identified the policies below as critical to our business operations and the understanding of our results of operations. In the ordinary course of business, we have made a number of estimates and assumptions relating to the reporting of results of operations and financial condition in the preparation of our financial statements in conformity with accounting principles generally accepted in the United States. Actual results could differ significantly from those estimates under different assumptions and conditions. We believe that the following discussion addresses our most critical accounting policies, which are those that are most important to the portrayal of our financial condition and results of operations and require our most difficult, subjective, and complex judgments, often as a result of the need to make estimates about the effect of matters that are inherently uncertain.

Our critical accounting policies are as follows:

- revenue recognition;
- estimating the allowance for doubtful accounts receivable;
- accounting for income taxes;
- valuation of long-lived and intangible assets and goodwill; and
- valuation of inventory.

### *Revenue Recognition*

Revenue from the sales of custom and fabricated compressors and flare systems is recognized when title passes to the customer, the customer assumes risks and rewards of ownership, collectability is reasonably assured and delivery occurs as directed by our customer. However, in certain circumstances customers request a bill and hold arrangement, in which case sales revenue is recognized before delivery occurs. Under these bill and hold arrangements, the compressor or flare is available for shipment, the Company has fulfilled all of its pre-delivery performance obligations and the customer has completed and signed a bill and hold agreement. Revenue from sale of rental units is included in sales revenue when equipment is shipped or title is transferred to the customer. Exchange and rebuild compressor revenue is recognized when both the replacement compressor has been delivered and the rebuild assessment has been completed. Revenue from compressor services is recognized upon providing services to the customer. Maintenance agreement revenue is recognized as services are rendered. Rental revenue is recognized over the terms of the respective rental agreements. Deferred income represents payments received before a product is shipped.

### *Allowance for Doubtful Accounts Receivable*

We perform ongoing credit evaluations of our customers and adjust credit limits based upon payment history and the customer's current credit worthiness, as determined by our review of their current credit information. We continuously monitor collections and payments from our customers and maintain a provision for estimated credit losses based upon our historical experience and any specific customer collection issues that we have identified. While such credit losses have historically been within our expectations and the provisions established, we cannot guarantee that we will continue to experience the same credit loss rates that we have in the past. At December 31, 2014, three customers accounted for approximately 20%, 18% and 14% of our accounts receivable, and at December 31, 2013, two customers accounted for approximately 18% and 14% of our accounts receivable. A significant change in the liquidity or financial position of these customers could have a material adverse impact on the collectability of our accounts receivables and our future operating results. At December 31, 2014, our allowance for doubtful accounts balance was \$507,000 and \$436,000 at December 31, 2013.

### *Accounting for Income Taxes*

As part of the process of preparing our financial statements, we are required to estimate our federal income taxes as well as income taxes in each of the states in which we operate. This process involves us estimating our actual current tax exposure together with assessing temporary differences resulting from differing treatment of items for tax and accounting purposes. These differences result in deferred tax assets and liabilities, which are included in our balance sheet. We must then assess the likelihood that our deferred tax assets will be recovered from future taxable income and, to the extent we believe that recovery is not probable, we must establish a valuation allowance. To the extent we establish a valuation allowance or increase this allowance in a period, we must include an expense in the tax provision in the statement of operations.

Significant management judgment is required in determining our provision for income taxes, our deferred tax assets and liabilities and any valuation allowance recorded against our net deferred tax assets. We currently have no valuation allowance and fully expect to utilize all of our deferred tax assets.

### *Valuation of Long-Lived and Intangible Assets and Goodwill*

We assess the impairment of identifiable intangibles, long-lived assets and related goodwill annually or whenever events or changes in circumstances indicate that the carrying value may not be recoverable. Factors we consider important which could trigger an impairment review include the following:

- significant underperformance relative to expected historical or projected future operating results;
- significant changes in the manner of our use of the acquired assets or the strategy for our overall business;
- significant negative industry or economic trends; and
- significant decline in the market value of our stock.

When we determine that the carrying value of intangibles, long-lived assets and related goodwill may not be recoverable based upon the existence of one or more of the above indicators of impairment, we measure any impairment based on a projected discounted cash flow method using a discount rate determined by our management to be commensurate with the risk inherent in our current business model.

We completed a review of goodwill for impairment during the fourth quarter of 2014 under the guidance of Accounting Standards Update 2012-02. Our analysis considered multiple qualitative factors to determine whether events and circumstances indicate a low likelihood that we have experienced impairment to the stated value of goodwill. Our assessment included a review of changes in key company financial metrics, stock performance and other measures that are important to the company's success. The other measure included demand for our products and services, maintenance of customers and cost of producing our product. Based on the analysis we concluded that it is more likely than not that we have not incurred impairment and are not required to take further action. As a result, no impairment of goodwill was recorded in the year ending at December 31, 2014. Future impairment tests could result in impairments of our intangible assets or goodwill.

### *Inventories*

We value our inventory at the lower of the actual cost to purchase and/or manufacture the inventory or the current estimated market value of the inventory. We regularly review inventory quantities on hand and record a provision for excess and obsolete inventory based primarily on our estimated forecast of product demand and production requirements. At December 31, 2014, an adjustment to the allowance of \$298,000 was made to remove obsolete inventory which represents 1.1% of inventory. This adjustment was the result of our obsolescence review which is conducted each year. We ended 2014 with a balance of \$225,000.

### **Our Performance Trends and Outlook**

Given the current economic environment in North America and anticipated impact of continued low natural gas and oil prices and potentially cautious capital spending by customers, we expect the overall activity levels to remain flat or drop in 2015. Currently, we believe that weak commodity prices will continue throughout 2015. In addition, credit and capital markets could show signs of stress resulting from the weakness of commodity prices and will impact the level of capital spending by our customers in the near term. We believe that the recovery from the recent market uncertainty will continue to be slow. The result will likely be lagging capital spending by our customers and therefore slow growth in demand for our products and services and price pressure from competitors. We anticipate industry capital spending will be greatly decreased in 2015 compared to 2014 levels, and we believe our fabrication business will likely reflect this in our production level through 2015. We believe our rental operations business will be virtually flat or moderately down.

## Results of Operations

### Year Ended December 31, 2014 Compared to the Year Ended December 31, 2013

The table below shows our revenues, percentage of total revenues, gross margin, exclusive of depreciation and amortization, and gross margin percentage of each of our operating units for the years ended December 31, 2014 and December 31, 2013. Gross margin is the difference between revenue and cost of revenues, exclusive of depreciation and amortization expense.

	Revenue				Gross Margin, Exclusive of Depreciation and Amortization (1)			
	Year Ended December 31,		Year Ended December 31,		Year Ended December 31,		Year Ended December 31,	
	2014	2013	2014	2013	2014	2013	2014	2013
	<i>(dollars in thousands)</i>							
Rental	\$ 78,983	81.5%	\$ 69,062	77.4%	\$ 47,461	60.1%	\$ 40,045	58.0%
Sales	17,200	17.7%	19,479	21.8%	5,903	34.3%	7,897	40.5%
Service & Maintenance	791	0.8%	707	0.8%	463	58.5%	363	51.3%
Total	<u>\$ 96,974</u>		<u>\$ 89,248</u>		<u>\$ 53,827</u>	55.5%	<u>\$ 48,305</u>	54.1%

- (1) For a reconciliation of gross margin to its most directly comparable financial measure calculated and presented in accordance with GAAP, please read “Item 6. Selected Financial Data – Non-GAAP Financial Measures” in this Report.

Total revenue increased to \$97.0 million from \$89.2 million, or 8.7%, for the year ended December 31, 2014, compared to 2013. This was the result of a 11.7% decrease in sales revenue offset by a 14.4% increase in rental revenue and a 11.9% increase in service and maintenance revenue.

Rental revenue increased to \$79.0 million from \$69.1 million, or 14.4%, for the year ended December 31, 2014, compared to 2013. This increase was the result of improved rental pricing of our units and our ability to place additional units in service. As of December 31, 2014, we had 2,879 natural gas compressors in our rental fleet totaling 401,361 horsepower, as compared to 2,556 natural gas compressors totaling 351,187 horsepower at December 31, 2013. As of December 31, 2014, we had 2,189 natural gas compressors totaling 301,392 horsepower rented to 102 customers, compared to 2,038 natural gas compressors totaling 283,165 horsepower rented to 95 customers at December 31, 2013. The rental fleet had a utilization of 76.0% as of December 31, 2014 as compared to 79.7% at year end 2013.

Sales revenue decreased to \$17.2 million from \$19.5 million, or 11.7%, for the year ended December 31, 2014, compared to 2013. Our normal sales activity continues to reflect demand from our customers' continued investment in non-conventional shale plays which require compression for produced natural gas. The price of natural gas on December 31, 2014 was \$3.14/MMBtu, down from \$4.31/MMBtu one year ago. The price of natural gas remains at levels that are considered depressed. Because of lagging natural gas prices, along with economic uncertainty and continued tight credit markets, the energy industry continues to encounter reduced capital spending, particularly for goods and services with respect to natural gas activities. This has caused capital project funding to shift from gas projects to oil projects as the price of oil was not as volatile as gas, and oil prices have rebounded from its lows compared to natural gas prices. Since our compressors are increasingly used in the production of natural gas from shale plays which are driven by oil economics, we have been able to increase our sales. Our strategy over time has been to increase our rental revenues so that they are a larger component of total revenue, but we intend to maintain our ability to build and sell custom fabricated equipment. In support of this, we have continued to cultivate new sales-oriented customers and are entertaining requests for bids on larger reciprocating compressors instead of being solely focused on screw-type equipment. Sales included: (1) compressor unit sales, (2) flare sales, (3) parts sales and (4) compressor rebuilds.

The overall gross margin percentage increased to 55.5% for the twelve months ended December 31, 2014, from 54.1% for the same period ended December 31, 2013, exclusive of depreciation and amortization. This increase is the result of the relatively higher margin rentals comprising a larger share of total revenue. Rental revenue increased by 14.4% while sales revenue declined. Rental margins increased for the year ended December 31, 2014 compared to 2013 from 58.0% to 60.1%. Sales margin decreased to 34.3% from 40.5% for the year ended 2014 compared to 2013. Third party service and maintenance margins increased to 58.5% from 51.3% for the year ended December 31, 2014 compared to 2013. Service and maintenance represents less than 1% of our revenue providing minimal impact on our overall gross margin.

Selling, general, and administrative expense increased to \$10.3 million for the year ended December 31, 2014, as compared to \$8.1 million for 2013. This 26.9% increase is primarily due to our need to maintain consistent staffing levels, salary increases for existing staff (\$243,000) and non-cash expenses related to stock compensation (\$1.5 million).

Depreciation and amortization expense increased to \$21.5 million from \$18.1 million, or 18.5%, for the year ended December 31, 2014, compared to 2013. This increase was the net result of 323 new gas compressor rental units being added to the rental fleet in 2014, thus increasing the depreciable base.

Provision for income tax decreased to \$8.0 million from \$8.1 million, or 1.1%, and is the result of the decrease in taxable income. Our effective tax rate was 36.2% for 2014 and 36.1% for 2013.

**Year Ended December 31, 2013 Compared to the Year Ended December 31, 2012**

The table below shows our revenues, percentage of total revenues, gross margin, exclusive of depreciation and amortization, and gross margin percentage of each of our operating units for the years ended December 31, 2013 and December 31, 2012. Gross margin is the difference between revenue and cost of sales, exclusive of depreciation and amortization expense.

	Revenue				Gross Margin, Exclusive of Depreciation and Amortization (1)			
	Year Ended December 31,		Year Ended December 31,		Year Ended December 31,		Year Ended December 31,	
	2013	2012	2013	2012	2013	2012	2013	2012
	<i>(dollars in thousands)</i>							
Rental	\$ 69,062	77.4%	\$ 56,477	60.3%	\$ 40,045	58.0%	\$ 32,740	58.0%
Sales	19,479	21.8%	36,375	38.8%	7,897	40.5%	10,559	29.0%
Service & Maintenance	707	0.8%	870	0.9%	363	51.3%	516	59.3%
Total	<u>\$ 89,248</u>		<u>\$ 93,722</u>		<u>\$ 48,305</u>	54.1%	<u>\$ 43,815</u>	46.7%

(1) For a reconciliation of gross margin to its most directly comparable financial measure calculated and presented in accordance with GAAP, please read “Item 6. Selected Financial Data – Non-GAAP Financial Measures” in this Report.

Total revenue decreased to \$89.2 million from \$93.7 million, or 4.8%, for the year ended December 31, 2013, compared to 2012. This was the result of a 46.4% decrease in sales revenue, a 22.3% increase in rental revenue and a 18.7% decrease in service and maintenance revenue. The sales decrease was primarily due to a large non-recurring sale of rental units from our fleet to a single customer in 2012.

Rental revenue increased from \$56.5 million to \$69.1 million, or 22.3%, for the year ended December 31, 2013, compared to 2012. This increase was the result of improved rental pricing of our units and the achievement of higher fleet utilization. As of December 31, 2013, we had 2,556 natural gas compressors in our rental fleet totaling 351,187 horsepower, as compared to 2,279 natural gas compressors totaling 311,401 horsepower at December 31, 2012. As of December 31, 2013, we had 2,038 natural gas compressors totaling 283,165 horsepower rented to 95 customers, compared to 1,756 natural gas compressors totaling 245,340 horsepower rented to 100 customers at December 31, 2012. The rental fleet had a utilization of 79.7% as of December 31, 2013 as compared to 77.1% at year end 2012.

Sales revenue decreased to \$19.5 million from \$36.4 million, or 46.4%, for the year ended December 31, 2013, compared to 2012. This decrease was the result of the large one time sale from our fleet in 2012. Our normal sales activity continues to reflect demand from our customers' continued investment in non-conventional shale plays which require compression for produced natural gas. The price of natural gas on December 31, 2013 was \$4.31/MMBtu, up from \$3.43/MMBtu one year earlier. Despite this increase in natural gas prices, the price of natural gas remained at levels that are considered depressed. Because of lagging natural gas prices, along with economic uncertainty and continued tight credit markets, the energy industry continues to encounter reduced capital spending, particularly for goods and services with respect to natural gas activities. This has caused capital project funding to shift from gas projects to oil projects as the price of oil was not as volatile as gas, and oil prices have rebounded from its lows compared to natural gas prices. Since our compressors are increasingly used in the production of natural gas from shale plays which are driven by oil economics, we have been able to increase our sales. Our strategy over time has been to increase our rental

revenues so that they are a larger component of total revenue, but we intend to maintain our ability to build and sell custom fabricated equipment. In support of this, we have continued to cultivate new sales-oriented customers and are entertaining requests for bids on larger reciprocating compressors instead of being solely focused on screw-type equipment. Sales included: (1) compressor unit sales, (2) flare sales, (3) parts sales and (4) compressor rebuilds.

The overall gross margin percentage increased to 54.1% for the twelve months ended December 31, 2013, from 46.7% for the same period ended December 31, 2012, exclusive of depreciation and amortization. This increase is the result of the relatively higher margin rentals comprising a larger share of total revenue. Rental revenue increased by 22.3% while sales revenue declined. Rental margins were relatively flat for the year ended December 31, 2013 compared to 2012 at 58.0%. Sales margin increased to 40.5% from 29.0% for the year ended 2013 compared to 2012. Third party service and maintenance margins decreased to 51.3% from 59.3% for the year ended December 31, 2013 compared to 2012. Service and maintenance represents less than 1% of our revenue providing minimal impact on our overall gross margin.

Selling, general, and administrative expense increased to \$8.1 million for the year ended December 31, 2013, as compared to \$7.9 million for 2012. This 3.1% increase was primarily due to increases in staffing levels, salary increases for existing staff and expenses related to vesting of restricted shares.

Depreciation and amortization expense increased to \$18.1 million from \$15.7 million, or 15.5%, for the year ended December 31, 2013, compared to 2012. This increase was the net result of 277 new gas compressor rental units being added to the rental fleet in 2013, thus increasing the depreciable base.

Provision for income tax increased to \$8.1 million from \$7.5 million, or 7.9%, and was the result of the increase in taxable income. Our effective tax rate was 36.1% for 2013 and 37.2% for 2012.

## Liquidity and Capital Resources

Our working capital positions as of December 31, 2014 and 2013 are set forth below.

	2014	2013
	<i>(in thousands)</i>	
Current Assets:		
Cash and cash equivalents	\$ 6,181	\$ 24,443
Trade accounts receivable, net	10,408	6,750
Inventory, net	32,624	26,832
Prepaid income taxes	6,242	2,281
Prepaid expenses and other	472	339
Total current assets	<u>55,927</u>	<u>60,645</u>
Current Liabilities:		
Line of credit	—	577
Accounts payable	4,990	3,904
Accrued liabilities	6,624	6,487
Current income tax liability	851	350
Deferred income	1,635	873
Total current liabilities	<u>14,100</u>	<u>12,191</u>
Net working capital	<u>\$ 41,827</u>	<u>\$ 48,454</u>

Historically, we have funded our operations through public and private offerings of our equity securities, subordinated debt, bank borrowings and cash flow from operations. Proceeds of financings have been primarily used to repay debt, to fund the manufacture and fabrication of additional units for our rental fleet of natural gas compressors and for acquisitions. In recent years, we have primarily funded our operations through cash flow from operations and, to a lesser extent, borrowings under our bank line of credit, which is described below. For the year ended December 31, 2014, we invested approximately \$53.3 million in equipment for our rental fleet and service vehicles. We financed this activity with funds from operations.

## Cash flows

At December 31, 2014, we had cash and cash equivalents of \$6.2 million and working capital of \$41.8 million, and total debt of \$417,000 under our credit agreement, all which is due in 2017. Our cash and cash equivalent decreased from 2013 due to an increase in demand from our customers for additional rental compression. We had positive net cash flow from operating activities of approximately \$34.6 million during 2014. This was primarily from net income of \$14.1 million plus depreciation and amortization of \$21.5 million.

At December 31, 2013, we had cash and cash equivalents of \$24.4 million, working capital of \$48.5 million and total debt of \$577,000, under our line of credit. We had positive net cash flow from operating activities of approximately \$39.2 million during 2013. This was primarily from net income of \$14.4 million plus depreciation and amortization of \$18.1 million, and an increase in deferred taxes of \$7.7 million.

Raw materials and work in progress inventory increased to \$32.6 million as of the end of 2014, as compared to \$26.8 million as of the end of 2013. This increase is mainly a reflection of inventory management activity and the timing of jobs closing from work in progress to finished goods.

## Contractual Obligations and Commitments

We have contractual obligations and commitments that affect our results of operations, financial condition and liquidity. The following table is a summary of our significant cash contractual obligations (in thousands):

Cash Contractual Obligations	2015	2016	2017	2018	Thereafter	Total
Line of credit	\$ —	\$ —	\$ 417	\$ —	\$ —	\$ 417
Interest on line of credit	17	17	17	—	—	51
Purchase obligations	620	620	620	612	—	2,472
Other long term liabilities	—	—	—	155	—	155
Facilities and office leases	288	261	241	113	15	918
Equipment leases	13	7	2	—	—	22
Total	<u>\$ 938</u>	<u>\$ 905</u>	<u>\$ 1,297</u>	<u>\$ 880</u>	<u>\$ 15</u>	<u>\$ 4,035</u>

## Senior Bank Borrowings

On November 19, 2014, we amended and renewed our \$30 million Credit Agreement with JP Morgan Chase Bank, N.A. ("the Amended Credit Agreement"). The Amended Credit Agreement was extended to December 31, 2017, and the interest rate terms were amended. We also have a right to request from the lender, on an uncommitted basis, an increase of up to \$20 million on the aggregate commitment (which could potentially increase the commitment amount to \$50 million). As of December 31, 2014, we owed \$417,000 on the line of credit under the Credit Agreement.

**Borrowing Base.** At any time before the maturity of the Amended Credit Agreement, we may draw, repay and re-borrow amounts available under the borrowing base up to the maximum aggregate availability discussed above. Generally, the borrowing base equals the sum of (a) 80% of our eligible accounts receivable plus (b) 50% of the book value of our eligible general inventory (not to exceed 50% of the commitment amount at the time) plus (c) 75% of the book value of our eligible equipment inventory. JPMorgan Chase Bank (the "Lender") may adjust the borrowing base components if material deviations in the collateral are discovered in future audits of the collateral.

**Interest and Fees.** Under the terms of the Amended Credit Agreement, we have the option of selecting the applicable variable rate for each revolving loan, or portion thereof, of either (a) LIBOR multiplied by the Statutory Reserve Rate (as defined in the Amended Credit Agreement), with respect to this rate, for Eurocurrency funding, plus the Applicable Margin ("LIBOR-based"), or (b) CB Floating Rate, which is the Lender's Prime Rate less the Applicable Margin; provided, however, that no more than three LIBOR-based borrowings under the agreement may be outstanding at any one time. For purposes of the LIBOR-based interest rate, the Applicable Margin is 1.50%. For purposes of the CB Floating Rate, the Applicable Margin is 1.25%. Accrued interest is payable monthly on outstanding principal amounts, provided that accrued interest on LIBOR-based loans is payable at the end of each interest period, but in no event less frequently than quarterly. In addition, fees and expenses are payable in connection with

our requests for letters of credit (generally equal to the Applicable Margin for LIBOR-related borrowings multiplied by the face amount of the requested letter of credit) and administrative and legal costs.

*Maturity.* The maturity date of the Amended Credit Agreement is December 31, 2017, at which time all amounts borrowed under the agreement will be due and outstanding letters of credit must be cash collateralized. The agreement may be terminated early upon our request or the occurrence of an event of default.

*Security.* The obligations under the Amended Credit Agreement are secured by a first priority lien on all of our inventory and accounts and leases receivables, along with a first priority lien on a variable number of our leased compressor equipment the book value of must be maintained at a minimum of 2.00 to 1.00 commitment coverage ratio (such ratio being equal to (i) the amount of the borrowing base as of such date to (ii) the amount of the commitment as of such date.)

*Covenants.* The Amended Credit Agreement contains customary representations and warranties, as well as covenants which, among other things, limit our ability to incur additional indebtedness and liens; enter into transactions with affiliates; make acquisitions in excess of certain amounts; pay dividends; redeem or repurchase capital stock or senior notes; make investments or loans; make negative pledges; consolidate, merge or effect asset sales; or change the nature of our business.

*Events of Default and Acceleration.* The Amended Credit Agreement contains customary events of default for credit facilities of this size and type, and includes, without limitation, payment defaults; defaults in performance of covenants or other agreements contained in the transaction documents; inaccuracies in representations and warranties; certain defaults, termination events or similar events; certain defaults with respect to any other Company indebtedness in excess of \$50,000; certain bankruptcy or insolvency events; the rendering of certain judgments in excess of \$150,000; certain ERISA events; certain change in control events and the defectiveness of any liens under the secured revolving credit agreement. Obligations under the Amended Credit Agreement may be accelerated upon the occurrence of an event of default.

As of December 31, 2014, we were in compliance with all covenants in our Amended Credit Agreement. A default under our Amended Credit Agreement could trigger the acceleration of our bank debt so that it is immediately due and payable. Such default would have a material adverse effect on our liquidity, financial position and operations.

### ***Shelf Registration Statement***

We have an effective \$150 million “universal” shelf registration statement on Form S-3 on file with the Securities and Exchange Commission, which we filed in late 2012 and became effective in February 2013. This shelf registration statement enables us to sell, from time to time, the securities covered by the registration statement in one or more public offerings. The securities covered by the registration statement include common stock, preferred stock, depository shares, debt securities, rights to purchase common stock, units consisting of two or more of any of the registered securities and warrants to purchase any of the registered securities. We may offer any of these securities independently or together in any combination with other securities. The shelf registration statement allows us to enter the public markets and consummate sales of the registered securities in rapid fashion and with little or no notice. We have no immediate plans to issue securities under the shelf registration statement, but our management believes that it may facilitate access to additional liquidity in the future. However, there is no assurance that equity or debt capital would be available to us in the public markets should we determine to issue securities under the shelf registration statement.



## Components of Our Principal Capital Expenditures

Capital expenditures for the three years ended December 31, 2014:

Expenditure Category	2014	2013	2012
	<i>(in thousands)</i>		
Rental equipment, vehicles and shop equipment	\$ 53,342	\$ 43,419	\$ 23,766

The level of our expenditures will vary in future periods depending on energy market conditions and other related economic factors. Based upon existing economic and market conditions, we believe that our operating cash flow and additional bank borrowings are adequate to fully fund our net capital expenditures requirements for 2015. We also believe we have significant flexibility with respect to our financing alternatives and adjustment of our expenditure plans if circumstances warrant. When considered in relation to our total financial capacity, we do not have any material continuing commitments associated with expenditure plans related to our current operations can be met.

### Off-Balance Sheet Arrangements

From time-to-time, we enter into off-balance sheet arrangements and transactions that can give rise to off-balance sheet obligations. As of December 31, 2014, the off-balance sheet arrangements and transactions that we have entered into include operating lease agreements and purchase agreements. We do not believe that these arrangements are reasonably likely to materially affect our liquidity or availability of, or requirements for, capital resources.

We entered into a purchase agreement with a vendor in July 2008 pursuant to which we agreed to purchase up to \$4.8 million of our paint and coating requirements exclusively from the vendor. In connection with the execution of the agreement, the vendor paid us a \$300,000 fee which is considered to be a discount toward future purchases from the vendor. As of December 31, 2014 we had met \$2.3 million of this obligation. The \$300,000 payment we received is recorded as a long-term liability and will decrease as the purchase commitment is fulfilled. The long-term liability remaining as of December 31, 2014 was \$155,000.

### Recently Issued Accounting Pronouncements

On May 28, 2014, the FASB issued Accounting Standards Update (ASU) No. 2014-09, Revenue from Contracts with Customers (Topic 606), as part of a joint project with the International Accounting Standards Board (IASB) to clarify revenue-recognizing principles and develop a common revenue standard for U.S. GAAP and International Financial Reporting Standards (IFRS). ASU No. 2014-09 finalizes Proposed ASU Nos. 1820-100, 2011-230 and 2011-250 and is expected, among other things, to remove inconsistencies and weaknesses in revenue requirements and improve comparability of revenue recognition practices across entities, industries, jurisdictions and capital markets. In particular, the amendments in this ASU will be added to the FASB Accounting Standards Codification (FASB ASC) as Topic 606, Revenue from Contracts with Customers, and will supersede the revenue recognition requirements in FASB ASC 605, Revenue Recognition, as well as some cost guidance in FASB ASC Subtopic 605-35, Revenue Recognition-Construction-Type and Production-Type Contracts. The core principle of this ASU is that an entity should recognize revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. To achieve this core principle, the guidance provides that an entity should apply the following steps: (1) identify the contract(s) with a customer; (2) identify the performance obligation in the contract; (3) determine the transaction price; (4) allocate the transaction price to the performance obligations in the contract; and (5) recognize revenue when, or as, the entity satisfies a performance obligation. For public entities, the amendments in ASU No. 2014-09 are effective for annual reporting periods beginning after December 15, 2016, including interim periods within that reporting period, and early application is prohibited. Additionally, an entity should apply the amendments either retrospectively to each prior reporting period presented or retrospectively with the cumulative effect of initially applying this ASU recognized at the date of initial application. If an entity elects the latter, transition method, then it must also provide the additional disclosures in reporting periods that include the date of initial application of (1) the amount by which each financial statement line item is affected in the current reporting period, as compared to the guidance that was in effect before the change, and (2) an explanation of the reasons for significant changes. The new standard will be effective during our first quarter ending March 31, 2017. We are currently evaluating the new standard to determine which reporting option allows us to report the most meaningful information and are still evaluating the potential impact this new standard may have on our financial statements.

## **Environmental Regulations**

Various federal, state and local laws and regulations covering the discharge of materials into the environment, or otherwise relating to protection of human safety and health and the environment, affect our operations and costs. Compliance with these laws and regulations could cause us to incur remediation or other corrective action costs or result in the assessment of administrative, civil and criminal penalties and the issuance of injunctions delaying or prohibiting operations. In addition, we have acquired certain properties and plant facilities from third parties whose actions with respect to the management and disposal or release of hydrocarbons or other wastes were not under our control. Under environmental laws and regulations, we could be required to remove or remediate wastes disposed of or released by prior owners. In addition, we could be responsible under environmental laws and regulations for properties and plant facilities we lease, but do not own. Compliance with such laws and regulations increases our overall cost of business, but has not had a material adverse effect on our operations or financial condition. It is not anticipated, based on current laws and regulations, that we will be required in the near future to expend amounts that are material in relation to our total expenditure budget in order to comply with environmental laws and regulations but such laws and regulations are frequently changed and we are unable to predict the ultimate cost of compliance. We also could incur costs related to the cleanup of sites to which we send equipment and for damages to natural resources or other claims related to releases of regulated substances at such sites.

## **ITEM 7A. QUANTITATIVE AND QUALITATIVE DISCLOSURE ABOUT MARKET RISK**

### **Commodity Risk**

Our commodity risk exposure is the pricing applicable primarily to natural gas production and to lesser extent oil production. Realized commodity prices received for such production are primarily driven by the prevailing worldwide price for crude oil and spot prices applicable to natural gas. Depending on the market prices of oil and natural gas, companies exploring for such resources may cancel or curtail their drilling programs, thereby reducing demand for our equipment and services.

### **Financial Instruments and Debt Maturities**

Our financial instruments consist of cash and cash equivalents, trade receivables, accounts payable and our line of credit. The carrying amounts of cash and cash equivalents, trade receivables, and accounts payable approximate fair value because of the short-term nature of the instruments. The fair value of our bank borrowings approximate the carrying amounts as of December 31, 2014 and 2013, and were determined based upon interest rates currently available to us.

### **Customer Credit Risk**

We are exposed to the risk of financial non-performance by our customers. Our ability to collect on rentals and sales to our customers is dependent on the liquidity of our customer base. To manage customer credit risk, we monitor credit ratings of our customers. Unless we are able to retain our existing customers, or secure new customers if we lose one or more of our significant customers, our revenue and results of operations would be adversely affected. At December 31, 2014, three customers accounted for 52% of our accounts receivable.

## **ITEM 8. FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA**

Our audited financial statements and supplementary financial data are included in this Annual Report on Form 10-K beginning on page F-1.

## **ITEM 9. CHANGES IN AND DISAGREEMENTS WITH ACCOUNTANTS ON ACCOUNTING AND FINANCIAL DISCLOSURE**

None.

## **ITEM 9A. CONTROLS AND PROCEDURES**

### **Evaluation of Disclosure Controls and Procedures**

An evaluation was carried out under the supervision and with the participation of our management, including our President and Chief Executive Officer and our Vice President and Chief Financial Officer, of the effectiveness of the design of our “disclosure controls and procedures” (as such term is defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934, as amended or, the “Exchange Act”) as of December 31, 2014, pursuant to Exchange Act Rule 13a-15. Based upon

that evaluation, the President and Chief Executive Officer and our Principal Accounting Officer have concluded that our disclosure controls and procedures as of December 31, 2014, are effective to ensure that information required to be disclosed by us in the reports filed or submitted by us under the Exchange Act is recorded, processed, summarized, and reported within the time periods specified in the SEC's rules and forms and include controls and procedures designed to ensure that information required to be disclosed by us in such reports is accumulated and communicated to our management, including our principal executive and financial officers as appropriate to allow timely decisions regarding required disclosures. Due to the inherent limitations of control systems, not all misstatements may be detected. Those inherent limitations include the realities that judgments in decision-making can be faulty and that breakdowns can occur because of simple errors or mistakes. Additionally, controls could be circumvented by the individual acts of some persons or by collusion of two or more people. Our controls and procedures can only provide reasonable, not absolute, assurance that the above objectives have been met.

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

There were no changes in our internal control over financial reporting identified in connection with the evaluation required by paragraph (d) of Exchange Act Rules 13a-15 or 15d-15 that occurred during our last quarter that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

## **Management's Report on Internal Control Over Financial Reporting**

Our management, including the President and Chief Executive Officer and our Principal Accounting Officer, is responsible for establishing and maintaining adequate internal control over financial reporting, as defined in Rule 13a-15(f) and 15d-15(f) under the Exchange Act. Our internal control system is designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles. Our internal control over financial reporting includes those policies and procedures that:

- pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of our assets;
- provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with accounting principles generally accepted in the United States of America, and that our receipt and expenditures are being made only in accordance with authorizations of management and our Board of Directors; and
- provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use or disposition of our assets that could have a material effect on the financial statements.

All internal control systems, no matter how well designed, have inherent limitations. A system of internal control may become inadequate over time because of changes in conditions or deterioration in the degree of compliance with the policies or procedures. Therefore, even those systems determined to be effective can provide only reasonable assurance with respect to financial statement preparation and presentation.

Our management assessed the effectiveness of our internal control over financial reporting as December 31, 2014 using the criteria set forth by the Commission of Sponsoring Organizations of the Treadway Commission (COSO) in their 2013 Internal Control-Integrated Framework. Based on this assessment, our management concluded that, as of December 31, 2014, our internal control over financial reporting was effective.

Pursuant to the Section 404 of the Sarbanes-Oxley Act of 2002, we have included a report of management's assessment of the effectiveness of our internal controls as part of this annual report on Form 10-K for the fiscal year December 31, 2014. BDO USA, LLP, our independent registered public accounting firm, has issued an attestation report dated March 13, 2015 on the effectiveness of internal control over financial reporting. That report is included herein.

### **ITEM 9B. OTHER INFORMATION**

None.

## Report of Independent Registered Public Accounting Firm

To the Board of Directors and Stockholders  
Natural Gas Services Group, Inc.  
Midland, Texas

We have audited Natural Gas Services Group, Inc.'s (the "Company") internal control over financial reporting as of December 31, 2014, based on criteria established in *Internal Control-Integrated Framework (2013)* issued by the Committee of Sponsoring Organizations of the Treadway Commission (the COSO criteria). The Company's management is responsible for maintaining effective internal control over financial reporting and for its assessment of the effectiveness of internal control over financial reporting included in the accompanying "Item 9A. Management's Report on Internal Control Over Financial Reporting." Our responsibility is to express an opinion on the Company's internal control over financial reporting based on our audit.

We conducted our audit in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether effective internal control over financial reporting was maintained in all material respects. Our audit included obtaining an understanding of internal control over financial reporting, assessing the risk that a material weakness exists, and testing and evaluating the design and operating effectiveness of internal control based on the assessed risk. Our audit also included performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion.

A company's internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles. A company's internal control over financial reporting includes those policies and procedures that (1) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the company; (2) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the company are being made only in accordance with authorizations of management and directors of the company; and (3) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of the company's assets that could have a material effect on the financial statements.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

In our opinion, Natural Gas Services Group, Inc. maintained, in all material respects, effective internal control over financial reporting as of December 31, 2014, based on the COSO criteria.

We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the balance sheets of Natural Gas Services Group, Inc. as of December 31, 2014 and 2013 and the related statements of income, stockholders' equity and cash flows for each of the three years in the period ended December 31, 2014 and our report dated March 13, 2015 expressed an unqualified opinion thereon.

/s/ BDO USA, LLP

Houston, Texas  
March 13, 2015

### **PART III**

#### **ITEM 10. DIRECTORS, EXECUTIVE OFFICERS AND CORPORATE GOVERNANCE**

The information required by this item is incorporated herein by reference to the sections “Election of Directors,” “Executive Officers,” “Corporate Governance” and “The Board of Directors and its Committees” in our definitive proxy statement which will be filed with the Securities and Exchange Commission within 120 days after December 31, 2014.

We have adopted a Code of Business Conduct and Ethics that applies to our directors, officers and employees. The Code of Business Conduct and Ethics is posted in the "Investor Relations" section of our website at [www.ngsg.com](http://www.ngsg.com). The Code of Business Conduct and Ethics maybe obtained free of charge by writing to Natural Gas Services Group, Inc., Attn: Investor Relations, 508 W. Wall Street, Suite 550 Midland, Texas 79701.

#### **ITEM 11. EXECUTIVE COMPENSATION**

The information required by this item is incorporated herein by reference to the section “Executive Compensation” in our definitive proxy statement which will be filed with the Securities and Exchange Commission within 120 days after December 31, 2014.

#### **ITEM 12. SECURITY OWNERSHIP OF CERTAIN BENEFICIAL OWNERS AND MANAGEMENT AND RELATED STOCKHOLDER MATTERS**

The information required by this item is incorporated herein by reference to the section “Principal Shareholders and Security Ownership of Management” in our definitive proxy statement which will be filed with the Securities and Exchange Commission within 120 days after December 31, 2014.

#### **ITEM 13. CERTAIN RELATIONSHIPS AND RELATED TRANSACTIONS, AND DIRECTOR INDEPENDENCE**

The information required by this item is incorporated herein by reference to the sections “Related Person Transactions” and “Corporate Governance” in our definitive proxy statement which will be filed with the Securities and Exchange Commission within 120 days after December 31, 2014.

#### **ITEM 14. PRINCIPAL ACCOUNTANT FEES AND SERVICES**

The information required by this item is incorporated herein by reference to the section “Principal Accountant Fees and Services” in our definitive proxy statement which will be filed with the Securities and Exchange Commission within 120 days after December 31, 2014.

## PART IV

### ITEM 15. EXHIBITS AND FINANCIAL STATEMENTS

The following documents are filed as part of this Annual Report on Form 10-K:

(a)(1) and (a)(2) Financial Statements

For a list of Financial Statements, see “Index to Financial Statements” and incorporated herein by reference.

(a)(3) Exhibits

A list of exhibits to this Annual Report on Form 10-K is set forth below:

<u>Exhibit No.</u>	<u>Description</u>
3.1	Articles of Incorporation, as amended (Incorporated by reference to Exhibit 3.1 of the 10-QSB filed and dated November 10, 2004)
3.2	Bylaws (Incorporated by reference to Exhibit 3.4 of the Registrant's Registration Statement on Form SB-2, No. 333-88314)
4.1	Non-Statutory Stock Option Agreement (Incorporated by reference to Exhibit 10.2 to Form 8-K filed with the SEC on August 30, 2005)
4.2	Form of Senior Indenture (Incorporated by reference to Exhibit 4.1 of the Registrant's Registration Statement on Form S-3 (No. 333-161346) and filed on August 14, 2009)

- 10.1 Lease Agreement, dated March 26, 2008, between WNB Tower, LTD and Natural Gas Services Group, Inc. (Incorporated by reference to Exhibit 10.15 of the Registrant's Form 10-K for the fiscal year ended December 31, 2008 and filed with the Securities and Exchange Commission on March 9, 2009)
- 10.2 2009 Restricted Stock/Unit Plan (Incorporated by reference to Exhibit 10.1 of the Registrant's Current Report on Form 8-K dated September 18, 2009 and filed with the Securities and Exchange Commission on September 18, 2009.)
- 10.3 1998 Stock Option Plan, as amended (Incorporated by reference to Exhibit 10.2 of the Registrant's Current Report on Form 8-K dated September 18, 2009 and filed with the Securities and Exchange Commission on September 18, 2009.)
- 10.4 Lease Agreement, dated December 11, 2008, between Klement-Wes Partnership, LTD and Natural Gas Services Group, Inc. and commencing on January 1, 2009
- 10.5 Credit Agreement between Natural Gas Services Group, Inc. and JPMorgan Chase Bank, N.A., dated December 10, 2010 (Incorporated by reference to Exhibit 10.1 of the Registrant's Current Report on Form 8-K filed with the Securities and Exchange Commission on November 24, 2014.)
- 10.6 Third Amendment of Credit Agreement between Natural Gas Services Group, Inc. and JPMorgan Chase Bank, N.A., dated November 19, 2014 (Incorporated by reference to Exhibit 10.1 of the Registrant's Current report on Form 8-K filed with the Securities and Exchange Commission on January 9, 2012.)
- 10.7 Security Agreement between Natural Gas Services Group, Inc. and JPMorgan Chase Bank, N.A., dated December 10, 2010 (Incorporated by reference to Exhibit 10.2 of the Registrant's Current Report on Form 8-K filed with the Securities and Exchange Commission on December 16, 2011.)
- 10.8 First Amendment of Security Agreement between Natural Gas Services Group, Inc. and JPMorgan Chase Bank, N.A., dated December 31, 2011 (Incorporated by reference to Exhibit 10.2 of the Registrant's Current report on Form 8-K filed with the Securities and Exchange Commission on January 9, 2012.)
- 10.9 Promissory Note in the aggregate amount of \$30,000,000 issued to JPMorgan Chase Bank, N.A., dated December 31, 2014, in connection with the revolving credit line under the Credit Agreement with JPMorgan Chase Bank, N.A. (Incorporated by reference to Exhibit 10.2 of the Registrant's Current Report on Form 8-K filed with the Securities and Exchange Commission on November 24, 2014.)
- 10.10 Employment Agreement between Natural Gas Services Group, Inc. and Stephen C. Taylor dated October 23, 2013 (Incorporated by reference to Exhibit 10.1 of the Registrant's Current Report on Form 8-K filed with the Securities and Exchange Commission on October 25, 2013)
- \*23.1 Consent of BDO USA, LLP
- \*31.1 Certification of Chief Executive Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002
- \*31.2 Certification of Principal Accounting Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002
- \*32.1 Certification of Chief Executive Officer pursuant to Section 906 of the Sarbanes-Oxley Act of 2002
- \*32.2 Certification of Principal Accounting Officer pursuant to Section 906 of the Sarbanes-Oxley Act of 2002
- 101.INS XBRL Instance Document
- 101.SCH XBRL Taxonomy Extension Schema Document
- 101.CAL XBRL Taxonomy Extension Calculation Linkbase Document
- 101.DEF XBRL Taxonomy Extension Definition Linkbase Document
- 101.LAB XBRL Taxonomy Extension Label Linkbase Document
- 101.PRE XBRL Taxonomy Extension Presentation Linkbase Document

\* Filed herewith.



## SIGNATURES

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

### NATURAL GAS SERVICES GROUP, INC.

Date: March 13, 2015

By: /s/ Stephen C. Taylor

Stephen C. Taylor  
Chairman of the Board, President and Chief  
Executive Officer  
(Principal Executive Officer)

Pursuant to the requirements of the Securities Exchange Act of 1934, this report has been signed below by the following persons on behalf of the registrant and in the capacities and on the dates indicated:

<b>Signature</b>	<b>Title</b>	<b>Date</b>
<u>/s/ Stephen C. Taylor</u> Stephen C. Taylor	Chairman of the Board of Directors, Chief Executive Officer and President (Principal Executive Officer)	March 13, 2015
<u>/s/ G. Larry Lawrence</u> G. Larry Lawrence	Vice President and Chief Financial Officer (Principal Accounting Officer)	March 13, 2015
<u>/s/ Charles G. Curtis</u> Charles G. Curtis	Director	March 13, 2015
<u>/s/ William F. Hughes, Jr.</u> William F. Hughes, Jr.	Director	March 13, 2015
<u>/s/ David L. Bradshaw</u> David L. Bradshaw	Director	March 13, 2015
<u>/s/ John W. Chisholm</u> John W. Chisholm	Director	March 13, 2015

## INDEX TO FINANCIAL STATEMENTS

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## REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

To the Board of Directors and Stockholders  
Natural Gas Services Group, Inc.  
Midland, Texas

We have audited the accompanying balance sheets of Natural Gas Services Group, Inc. (the "Company") as of December 31, 2014 and 2013 and the related statements of income, stockholders' equity and cash flows for each of the three years in the period ended December 31, 2014. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audits to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Natural Gas Services Group, Inc. as of December 31, 2014 and 2013 and the results of its operations and its cash flows for each of the three years in the period ended December 31, 2014, in conformity with accounting principles generally accepted in the United States of America.

We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), Natural Gas Services Group, Inc.'s, internal control over financial reporting as of December 31, 2014, based on criteria established in *Internal Control—Integrated Framework (2013)* issued by the Committee of Sponsoring Organizations of the Treadway Commission, and our report dated March 13, 2015 expressed an unqualified opinion thereon.

/s/ BDO USA, LLP

Houston, Texas  
March 13, 2015

**NATURAL GAS SERVICES GROUP, INC.**  
**BALANCE SHEETS**  
*(in thousands, except per share amounts)*

**December 31,**

**2014**                      **2013**

**ASSETS**

**Current Assets:**

Cash and cash equivalents	\$	6,181	\$	24,443
Trade accounts receivable, net of allowance for doubtful accounts of \$507 and \$436, respectively		10,408		6,750
Inventory, net of allowance for obsolescence of \$225 and \$128, respectively		32,624		26,832
Prepaid income taxes		6,242		2,281
Prepaid expenses and other		472		339
Total current assets		55,927		60,645
Rental equipment, net of accumulated depreciation of \$106,179 and \$86,533, respectively		208,292		176,420
Property and equipment, net of accumulated depreciation of \$10,830 and \$9,692 respectively		7,362		7,429
Goodwill		10,039		10,039
Intangibles, net of accumulated amortization of \$1,257 and \$1,132, respectively		1,902		2,027
Other assets		41		29
Total assets	\$	283,563	\$	256,589

**LIABILITIES AND STOCKHOLDERS' EQUITY**

**Current Liabilities:**

Line of credit	\$	—	\$	577
Accounts payable		4,990		3,904
Accrued liabilities		6,624		6,487
Current income tax liability		851		350
Deferred income		1,635		873
Total current liabilities		14,100		12,191
Line of credit, non-current		417		—
Deferred income tax liability		58,304		51,464
Other long-term liabilities		155		197
Total liabilities		72,976		63,852

Commitments and contingencies (Note 9)

**Stockholders' Equity:**

Preferred stock, 5,000 shares authorized, no shares issued or outstanding	—	—	—	—
Common stock, 30,000 shares authorized, par value \$0.01; 12,466 and 12,366 shares issued and outstanding, respectively		124		123
Additional paid-in capital		95,065		91,344
Retained earnings		115,398		101,270
Total stockholders' equity		210,587		192,737
Total liabilities and stockholders' equity	\$	283,563	\$	256,589

See accompanying notes to these financial statements.

**NATURAL GAS SERVICES GROUP, INC.**  
**STATEMENTS OF INCOME**  
*(in thousands, except earnings per share)*

	<b>For the Years Ended December 31,</b>		
	<b>2014</b>	<b>2013</b>	<b>2012</b>
<b>Revenue:</b>			
Rental income	\$ 78,983	\$ 69,062	\$ 56,477
Sales	17,200	19,479	36,375
Service and maintenance income	791	707	870
Total revenue	<u>96,974</u>	<u>89,248</u>	<u>93,722</u>
<b>Operating costs and expenses:</b>			
Cost of rentals, exclusive of depreciation stated separately below	31,522	29,017	23,737
Cost of sales, exclusive of depreciation stated separately below	11,297	11,582	25,816
Cost of service and maintenance, exclusive of depreciation stated separately below	328	344	354
Selling, general, and administrative expenses	10,334	8,141	7,893
Depreciation and amortization	21,507	18,144	15,707
Total operating costs and expenses	<u>74,988</u>	<u>67,228</u>	<u>73,507</u>
<b>Operating income</b>	<u>21,986</u>	<u>22,020</u>	<u>20,215</u>
<b>Other income (expense):</b>			
Interest expense	(10)	(56)	(18)
Other income	182	548	14
Total other income (expense)	<u>172</u>	<u>492</u>	<u>(4)</u>
<b>Income before provision for income taxes</b>	<u>22,158</u>	<u>22,512</u>	<u>20,211</u>
Provision for income taxes:			
Current	1,190	399	554
Deferred	6,840	7,723	6,972
Total income tax expense	<u>8,030</u>	<u>8,122</u>	<u>7,526</u>
<b>Net income</b>	<u>\$ 14,128</u>	<u>\$ 14,390</u>	<u>\$ 12,685</u>
<b>Earnings per share:</b>			
Basic	\$ 1.14	\$ 1.17	\$ 1.04
Diluted	\$ 1.11	\$ 1.15	\$ 1.03
<b>Weighted average shares outstanding:</b>			
Basic	12,434	12,324	12,220
Diluted	12,721	12,550	12,320

See accompanying notes to these financial statements.

**NATURAL GAS SERVICES GROUP, INC.**  
**STATEMENTS OF STOCKHOLDERS' EQUITY**  
*(in thousands)*

	Preferred Stock		Common Stock		Additional Paid-In Capital	Retained Earnings	Total Stockholders' Equity
	Shares	Amount	Shares	Amount			
BALANCES, December 31, 2011	—	\$ —	12,179	\$ 122	\$ 87,225	\$ 74,195	\$ 161,542
Exercise of common stock options and warrants	—	—	23	—	180	—	180
Compensation expense on common stock options	—	—	—	—	440	—	440
Issuance of restricted stock	—	—	39	—	—	—	—
Compensation expense on restricted common stock	—	—	—	—	978	—	978
Net income	—	—	—	—	—	12,685	12,685
BALANCES, December 31, 2012	—	\$ —	12,241	\$ 122	\$ 88,823	\$ 86,880	\$ 175,825
Exercise of common stock options	—	—	53	—	829	—	829
Compensation expense on common stock options	—	—	—	—	198	—	198
Issuance of restricted stock	—	—	72	—	—	—	—
Tax benefit of equity compensation	—	—	—	—	10	—	10
Compensation expense on restricted common stock	—	—	—	1	1,484	—	1,485
Net income	—	—	—	—	—	14,390	14,390
BALANCES, December 31, 2013	—	\$ —	12,366	\$ 123	\$ 91,344	\$ 101,270	\$ 192,737
Exercise of common stock options	—	—	3	—	59	—	59
Compensation expense on common stock options	—	—	—	—	426	—	426
Issuance of restricted stock	—	—	97	—	—	—	—
Tax benefit of equity compensation	—	—	—	—	419	—	419
Compensation expense on restricted common stock	—	—	—	1	2,817	—	2,818
Net income	—	—	—	—	—	14,128	14,128
BALANCES, December 31, 2014	—	\$ —	12,466	\$ 124	\$ 95,065	\$ 115,398	\$ 210,587

See accompanying notes to these financial statements.

**NATURAL GAS SERVICES GROUP, INC.**  
**STATEMENTS OF CASH FLOWS**  
*(in thousands)*

	<b>For the Years Ended December 31,</b>		
	<b>2014</b>	<b>2013</b>	<b>2012</b>
<b>CASH FLOWS FROM OPERATING ACTIVITIES:</b>			
Net income	\$ 14,128	\$ 14,390	\$ 12,685
<b>Adjustments to reconcile net income to net cash provided by operating activities:</b>			
Depreciation and amortization	21,507	18,144	15,707
Deferred taxes	6,840	7,723	6,972
Gain on extinguishment of liability	—	(223)	—
Gain on disposal of assets	(160)	(48)	—
Inventory allowance	395	—	—
Stock based compensation	3,244	1,682	1,418
<b>Changes in current assets (increase) decrease in:</b>			
Trade accounts receivables	(3,658)	(59)	(1,012)
Inventory	(6,112)	(323)	456
Prepaid income taxes and prepaid expenses	(3,997)	(1,870)	(281)
<b>Changes in current liabilities increase (decrease) in:</b>			
Accounts payable and accrued liabilities	1,126	1,154	1,863
Current income tax liability	920	(162)	447
Deferred income	762	(1,154)	(2,836)
Other	(12)	—	(1)
Tax benefit from equity compensation	(419)	(10)	—
<b>NET CASH PROVIDED BY OPERATING ACTIVITIES</b>	<b>34,564</b>	<b>39,244</b>	<b>35,418</b>
<b>CASH FLOWS FROM INVESTING ACTIVITIES:</b>			
Purchases of rental, property and equipment	(53,342)	(43,419)	(23,766)
Proceeds from sale of property and equipment	240	95	5
<b>NET CASH USED IN INVESTING ACTIVITIES</b>	<b>(53,102)</b>	<b>(43,324)</b>	<b>(23,761)</b>
<b>CASH FLOWS FROM FINANCING ACTIVITIES:</b>			
Payments of other long-term liabilities, net	(42)	(82)	(21)
Repayments of line of credit, net	(160)	(320)	(120)
Tax benefit from equity compensation	419	10	—
Proceeds from exercise of stock options	59	829	180
<b>NET CASH PROVIDED BY FINANCING ACTIVITIES</b>	<b>276</b>	<b>437</b>	<b>39</b>
<b>NET CHANGE IN CASH AND CASH EQUIVALENTS</b>	<b>(18,262)</b>	<b>(3,643)</b>	<b>11,696</b>
<b>CASH AND CASH EQUIVALENTS AT BEGINNING OF PERIOD</b>	<b>24,443</b>	<b>28,086</b>	<b>16,390</b>
<b>CASH AND CASH EQUIVALENTS AT END OF PERIOD</b>	<b>\$ 6,181</b>	<b>\$ 24,443</b>	<b>\$ 28,086</b>
<b>SUPPLEMENTAL DISCLOSURE OF CASH FLOW INFORMATION:</b>			
Interest paid	\$ 10	\$ 56	\$ 18
Income taxes paid	\$ 4,108	\$ 2,590	\$ 267
<b>NON-CASH TRANSACTIONS</b>			
Transfer of rental equipment to inventory	\$ 131	\$ 207	\$ 8,690
Property and equipment purchases included in accounts payable	\$ 218	\$ 251	\$ 31

See accompanying notes to these financial statements.

**NATURAL GAS SERVICES GROUP INC.  
NOTES TO FINANCIAL STATEMENTS**

**1. Summary of Significant Accounting Policies**

***Organization and Principles of Consolidation***

These notes apply to the financial statements of Natural Gas Services Group, Inc. (the "Company", "NGSG", "Natural Gas Services Group", "we" or "our") (a Colorado corporation). Natural Gas Services Group, Inc. was formed on December 17, 1998 for the purposes of combining the operations of certain manufacturing, service and leasing entities.

***Nature of Operations***

Natural Gas Services Group, Inc. is a leading provider of small to medium horsepower compression equipment to the natural gas industry. We focus primarily on the non-conventional natural gas production business in the United States (such as coal bed methane, gas shale, tight gas and oil shale). We manufacture, fabricate and rent natural gas compressors that enhance the production of natural gas wells. NGSG provides maintenance services for its natural gas compressors. In addition, we sell custom fabricated natural gas compressors to meet customer specifications dictated by well pressures, production characteristics and particular applications. We also manufacture and sell flare systems for oil and natural gas plant and production facilities.

***Use of Estimates***

The preparation of our financial statements in conformity with accounting principles generally accepted in the United States of America requires our management to make estimates and assumptions that affect the amounts reported in these financial statements and accompanying notes. Actual results could differ from those estimates. Significant estimates include fixed asset lives, bad debt allowance and the allowance for inventory obsolescence. It is at least reasonably possible these estimates could be revised in the near term and the revisions could be material.

***Cash Equivalents***

For purposes of reporting cash flows, we consider all short-term investments with an original maturity of three months or less to be cash equivalents.

***Accounts Receivable***

Our trade receivables consist of customer obligations for the sale of compressors and flare systems due under normal trade terms, and operating leases for the use of our natural gas compressors. The receivables are not collateralized except as provided for under lease agreements. However, we typically require deposits of as much as 50% for large custom contracts. We extend credit based on management's assessment of the customer's financial condition, receivable aging, customer disputes and general business and economic conditions. The allowance for doubtful accounts was \$507,000 and \$436,000 at December 31, 2014 and 2013, respectively. Management believes that the allowance is adequate; however, actual write-offs may exceed the recorded allowance.

***Revenue Recognition***

Revenue from the sales of custom and fabricated compressors, and flare systems is recognized when title passes to the customer, the customer assumes risks and rewards of ownership, collectability is reasonably assured and delivery occurs as directed by our customer. Exchange and rebuilt compressor revenue is recognized when both the replacement compressor has been delivered and the rebuild assessment has been completed. Revenue from compressor service and retrofitting services is recognized upon providing services to the customer. Maintenance agreement revenue is recognized as services are rendered. Rental revenue is recognized over the terms of the respective rental agreements. Deferred income represents payments received before a product is shipped. Revenue from the sale of rental units is included in sales revenue when equipment is shipped or title is transferred to the customer.



### ***Major Customers and Concentration of Credit Risk***

Sales and rental income to Devon Energy Production, Inc. ("Devon") and EOG Resources, Inc. ("EOG") in 2014 amounted to 18% and 15% of revenue, respectively. Sales and rental income to EOG and Devon in 2013 amounted to 18% and 15% of revenue, respectively. Sales and rental income to EOG and Devon in 2012 amounted to 32% and 12% of revenue. No other single customer accounted for more than 10% of our revenues in 2014, 2013 or 2012. EOG, Promatcon and Oxy amounted to 20%, 18% and 14% of our accounts receivable as of December 31, 2014. EOG and Devon amounted to 18% and 14% of our accounts receivable as of December 31, 2013, respectively. No other customers amounted to more than 10% of our accounts receivable as of December 31, 2014 and 2013.

### ***Inventory***

Inventory is valued at the lower of cost or market. The cost of inventories is determined by the weighted average method. A reserve is recorded against inventory balances for estimated obsolescence. This reserve is based on specific identification and historical experience and totaled \$225,000 and \$128,000 at December 31, 2014 and 2013, respectively. There were no new completed compressor units at December 31, 2014 or at December 31, 2013 available for sale or for use in our rental fleet. At December 31, 2014 and 2013, inventory consisted of the following (in thousands):

	2014	2013
Raw materials	\$ 25,984	\$ 20,524
Work in process	6,640	6,308
Total	<u>\$ 32,624</u>	<u>\$ 26,832</u>

### ***Property and Equipment***

Property and equipment is recorded at cost less accumulated depreciation. Depreciation is computed using the straight-line method over the estimated useful lives of the assets, which range from three to forty years. Rental equipment has an estimated useful life of fifteen years.

Gains and losses resulting from sales and dispositions of property and equipment are included in current operations. Maintenance and repairs are charged to operations as incurred.

### ***Goodwill***

Goodwill represents the cost in excess of fair value of the identifiable net assets acquired. Goodwill is tested for impairment annually or whenever events indicate impairment may have occurred. The annual goodwill impairment test is performed in the fourth quarter of each year. We experienced no impairment of goodwill at December 31, 2014 and 2013.

## *Intangibles*

At December 31, 2014, NGSB had intangible assets, which relate to developed technology and a trade name. The carrying amount net of accumulated amortization at December 31, 2014 and 2013 was \$1.9 million and \$2.0 million respectively. Developed technology is amortized on a straight-line basis with a useful life of 20 years, with a weighted average remaining life of approximately ten years as of December 31, 2014. Amortization expense recognized in each of the years ending December 31, 2014, 2013, and 2012 was \$125,000, \$130,000 and \$125,000 respectively. Estimated amortization expense for the years 2015-2024 is \$125,000 per year. NGSB has an intangible asset with a gross carrying value of \$654,000 at December 31, 2014 related to the trade name of SCS which was acquired in our acquisition of Screw Compression Systems in January 2005. This asset is not being amortized as it has been deemed to have an indefinite life.

The following table represents the identified intangible assets by major asset class (in thousands):

	<b>December 31, 2014</b>				<b>December 31, 2013</b>		
	Useful Life (years)	Gross Carrying Value	Accumulated Amortization	Net Book Value	Gross Carrying Value	Accumulated Amortization	Net Book Value
Developed Technology	20	2,505	1,257	1,248	2,505	1,132	1,373
Trade Name	Indefinite	654	—	654	654	—	654
<b>Total</b>		<b>\$ 3,159</b>	<b>\$ 1,257</b>	<b>\$ 1,902</b>	<b>\$ 3,159</b>	<b>\$ 1,132</b>	<b>\$ 2,027</b>

Our policy is to periodically review intangibles for impairment through an assessment of the estimated future cash flows related to such assets. In the event that assets are found to be carried at amounts in excess of estimated undiscounted future cash flows, then the assets will be adjusted for impairment to a level commensurate with a discounted cash flow analysis of the underlying assets. Based upon our analysis, we experienced no impairment of intangible assets at December 31, 2014 or 2013.

## *Warranty*

We accrue amounts for estimated warranty claims based upon current and historical product warranty costs and any other related information known. The warranty reserve was \$0 and \$28,000 for December 31, 2014 and 2013, respectively, and is included in accrued liabilities on the balance sheet.

## *Financial Instruments and Concentrations of Credit Risk*

We invest our cash primarily in deposits and money market funds with commercial banks. At times, cash balances at banks and financial institutions may exceed federally insured amounts.

## *Per Share Data*

Basic earnings per common share is computed using the weighted average number of common shares outstanding during the period. Diluted earnings per common share is computed using the weighted average number of common stock and common stock equivalent shares outstanding during the period. There were no anti-dilutive securities in 2014, 2013, and 2012.

The following table sets forth the computation of basic and diluted earnings per share (in thousands, except per share amounts):

	<b>Year Ended December 31,</b>		
	<b>2014</b>	<b>2013</b>	<b>2012</b>
<b>Numerator:</b>			
Net income	\$ 14,128	\$ 14,390	\$ 12,685
<b>Denominator for basic net income per common share:</b>			
Weighted average common shares outstanding	12,434	12,324	12,220
<b>Denominator for diluted net income per share:</b>			
Weighted average common shares outstanding	12,434	12,324	12,220
Dilutive effect of stock options and restricted shares	287	226	100
Diluted weighted average shares	12,721	12,550	12,320
<b>Earnings per common share:</b>			
Basic	\$ 1.14	\$ 1.17	\$ 1.04
Diluted	\$ 1.11	\$ 1.15	\$ 1.03

### ***Income Taxes***

Deferred tax assets and liabilities are recognized for the future tax consequences attributable to temporary differences between the financial statement carrying amounts of assets and liabilities and their respective tax bases, and operating losses and tax credit carry-forwards. Deferred tax assets and liabilities are measured using enacted tax rates expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or settled.

ASC Topic 740 prescribes a recognition threshold and measurement attribute for the financial statement recognition and measurement of a tax position taken or expected to be taken in a tax return. In order to record any financial statement benefit, we are required to determine, based on technical merits of the position, whether it is more likely than not (a likelihood of more than 50 percent) that a tax position will be sustained upon examination, including resolution of any related appeals or litigation processes. If that step is satisfied, then we must measure the tax position to determine the amount of benefit to recognize in the financial statements. The tax position is measured at the largest amount of the benefit that is greater than 50 percent likely of being realized upon ultimate settlement. We have no uncertain tax positions as of December 31, 2014 or 2013.

### ***Fair Value Measurement***

Fair value is defined as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date under current market conditions. Topic 820 established a fair value hierarchy, which requires an entity to maximize the use of observable inputs when measuring fair value. These inputs are categorized as follows:

Level 1- quoted prices in an active market for identical assets or liabilities;

Level 2- quoted prices in an active market for similar assets or liabilities, inputs other than quoted prices that are observable for similar assets or liabilities, inputs derived principally from or corroborated by observable market data by correlation or other means; and

Level 3- valuation methodology with unobservable inputs that are significant to the fair value measurement.

Management believes that the fair value of our cash and cash equivalents, trade receivables, accounts payable and line of credit at December 31, 2014 and 2013 approximate their carrying values due to the short-term nature of the instruments or the use of prevailing market interest rates.

## Segments and Related Information

ASC 280-10-50, "Operating Segments", define the characteristics of an operating segment as a) being engaged in business activity from which it may earn revenue and incur expenses, b) being reviewed by the company's chief operating decision maker (CODM) for decisions about resources to be allocated and assess its performance and c) having discrete financial information. Although we indeed look at our products to analyze the nature of our revenue, other financial information, such as certain costs and expenses, net income and EBITDA are not captured or analyzed by these categories. Our CODM does not make resource allocation decisions or assess the performance of the business based on these categories, but rather in the aggregate. Based on this, Management believes that it operates in one business segment.

In their analysis of product lines as potential operating segments, Management also considered ASC 280-10-50-11, "Aggregation Criteria", which allows for the aggregation of operating segments if the segments have similar economic characteristics and if the segments are similar in each of the following areas:

- The nature of the products and services;
- The nature of the production processes;
- The type or class of customer for their products and services;
- The methods used to distribute their products or provide their services; and
- The nature of the regulatory environment, if applicable.

We are engaged in the business of designing and manufacturing compressors and flares. Our compressors and flares are sold and rented to our customers. In addition, we provide service and maintenance on compressors in our fleet and to third parties. These business activities are similar in all geographic areas. Our manufacturing process is essentially the same for the entire Company and is performed in house at our facilities in Midland, Texas and Tulsa, Oklahoma. Our customers primarily consist of entities in the business of producing natural gas. The maintenance and service of our products is consistent across the entire Company and is performed via an internal fleet of vehicles. The regulatory environment is similar in every jurisdiction in that the most impacting regulations and practices are the result of federal energy policy. In addition, the economic characteristics of each customer arrangement are similar in that we maintain policies at the corporate level.

## Recently Issued Accounting Pronouncements

On May 28, 2014, the FASB issued Accounting Standards Update (ASU) No. 2014-09, Revenue from Contracts with Customers (Topic 606), as part of a joint project with the International Accounting Standards Board (IASB) to clarify revenue-recognition principles and develop a common revenue standard for U.S. GAAP and International Financial Reporting Standards (IFRS). ASU No. 2014-09 finalizes Proposed ASU Nos. 1820-100, 2011-230 and 2011-250 and is expected, among other things, to remove inconsistencies and weaknesses in revenue requirements and improve comparability of revenue recognition practices across entities, industries, jurisdictions and capital markets. In particular, the amendments in this ASU will be added to the FASB Accounting Standards Codification (FASB ASC) as Topic 606, Revenue from Contracts with Customers, and will supersede the revenue recognition requirements in FASB ASC 605, Revenue Recognition, as well as some cost guidance in FASB ASC Subtopic 605-35, Revenue Recognition-Construction-Type and Production-Type Contracts. The core principle of this ASU is that an entity should recognize revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. To achieve this core principle, the guidance provides that an entity should apply the following steps: (1) identify the contract(s) with a customer; (2) identify the performance obligation in the contract; (3) determine the transaction price; (4) allocate the transaction price to the performance obligations in the contract; and (5) recognize revenue when, or as, the entity satisfies a performance obligation. For public entities, the amendments in ASU No. 2014-09 are effective for annual reporting periods beginning after December 15, 2016, including interim periods within that reporting period, and early application is prohibited. Additionally, an entity should apply the amendments either retrospectively to each prior reporting period presented or retrospectively with the cumulative effect of initially applying this ASU recognized at the date of initial application. If an entity elects the latter, transition method, then it must also provide the additional disclosures in reporting periods that include the date of initial application of (1) the amount by which each financial statement line item is affected in the current reporting period, as compared to the guidance that was in effect before the change, and (2) an explanation of the reasons for significant changes. The new standard will be effective during our first quarter ending March 31, 2017. We are currently evaluating the new standard to determine which reporting option allows us to report the most meaningful information and are still evaluating the potential impact this new standard may have on our financial statements.

## 2. Rental Activity

We rent natural gas compressor packages to entities in the petroleum industry. These rental arrangements are classified as operating leases and generally have original terms of six months to two years and continue on a month-to-month basis thereafter. Future minimum rent payments for arrangements not on a month-to-month basis at December 31, 2014 are as follows :

Years Ending December 31, (in thousands)		
2015	\$	9,835
2016		1,306
Thereafter		—
Total	\$	11,141

### 3. Property and Equipment

Property and equipment consists of the following at December 31, 2014 and 2013 (in thousands):

	Useful Lives (Years)	2014	2013
Land and building	30	\$ 5,636	\$ 5,636
Leasehold improvements	39	793	770
Office equipment and furniture	5	1,376	1,434
Software	5	573	573
Machinery and equipment	7	2,847	2,635
Vehicles	3	6,967	6,073
Total		18,192	17,121
Less accumulated depreciation		(10,830)	(9,692)
Total		\$ 7,362	\$ 7,429

Depreciation expense for property and equipment and the compressors described in Note 2 was \$21.4 million, \$18.0 million and \$15.6 million for the years ended December 31, 2014, 2013 and 2012, respectively.

### 4. Credit Facility

We have a senior secured revolving credit agreement with JP Morgan Chase Bank, N.A (the "Amended Credit Agreement") aggregate commitment \$30 million, subject to collateral availability. We also have a right to request from the lender, on an uncommitted basis, an increase of up to \$20 million on the aggregate commitment (which could potentially increase the commitment amount to \$50 million).

*Borrowing Base.* At any time before the maturity of the Amended Credit Agreement, we may draw, repay and re-borrow amounts available under the borrowing base up to the maximum aggregate availability discussed above. Generally, the borrowing base equals the sum of (a) 80% of our eligible accounts receivable plus (b) 50% of the book value of our eligible general inventory (not to exceed 50% of the commitment amount at the time) plus (c) 75% of the book value of our eligible equipment inventory. JPMorgan Chase Bank (the "Lender") may adjust the borrowing base components if material deviations in the collateral are discovered in future audits of the collateral. We had \$29.6 million borrowing base availability at December 31, 2014 under the terms of our Amended Credit Agreement.

*Interest and Fees.* Under the terms of the Amended Credit Agreement, we have the option of selecting the applicable variable rate for each revolving loan, or portion thereof, of either (a) LIBOR multiplied by the Statutory Reserve Rate (as defined in the Amended Credit Agreement), with respect to this rate, for Eurocurrency funding, plus the Applicable Margin ("LIBOR-based"), or (b) CB Floating Rate, which is the Lender's Prime Rate less the Applicable Margin; provided, however, that no more than three LIBOR-based borrowings under the agreement may be outstanding at any one time. For purposes of the LIBOR-based interest rate, the Applicable Margin is 1.50%. For purposes of the CB Floating Rate, the Applicable Margin is 1.25%.

Accrued interest is payable monthly on outstanding principal amounts, provided that accrued interest on LIBOR-based loans is payable at the end of each interest period, but in no event less frequently than quarterly. In addition, fees and expenses are payable in connection with our requests for letters of credit (generally equal to the Applicable Margin for LIBOR-related borrowings multiplied by the face amount of the requested letter of credit) and administrative and legal costs.

*Maturity*. The maturity date of the Amended Credit Agreement is December 31, 2017, at which time all amounts borrowed under the agreement will be due and outstanding letters of credit must be cash collateralized. The agreement may be terminated early upon our request or the occurrence of an event of default.

*Security*. The obligations under the Amended Credit Agreement are secured by a first priority lien on all of our inventory and accounts and leases receivables, along with a first priority lien on a variable number of our leased compressor equipment the book value of must be maintained at a minimum of 2.00 to 1.00 commitment coverage ratio (such ratio being equal to (i) the amount of the borrowing base as of such date to (ii) the amount of the commitment as of such date.)

*Covenants*. The Amended Credit Agreement contains customary representations and warranties, as well as covenants which, among other things, limit our ability to incur additional indebtedness and liens; enter into transactions with affiliates; make acquisitions in excess of certain amounts; pay dividends; redeem or repurchase capital stock or senior notes; make investments or loans; make negative pledges; consolidate, merge or effect asset sales; or change the nature of our business. In addition, we also have certain financial covenants that require us to maintain a leverage ratio less than or equal to 2.50 to 1.00 as of the last day of each fiscal quarter.

*Events of Default and Acceleration*. The Amended Credit Agreement contains customary events of default for credit facilities of this size and type, and includes, without limitation, payment defaults; defaults in performance of covenants or other agreements contained in the loan documents; inaccuracies in representations and warranties; certain defaults, termination events or similar events; certain defaults with respect to any other Company indebtedness in excess of \$50,000; certain bankruptcy or insolvency events; the rendering of certain judgments in excess of \$150,000; certain ERISA events; certain change in control events and the defectiveness of any liens under the secured revolving credit facility. Obligations under the Amended Credit Agreement may be accelerated upon the occurrence of an event of default.

As of December 31, 2014, we were in compliance with all covenants in our Amended Credit Agreement. A default under our Credit Agreement could trigger the acceleration of our bank debt so that it is immediately due and payable. Such default would likely limit our ability to access other credit. At December 31, 2014 our balance on the line of credit was \$417,000. Our weighted average interest rate for the year ended December 31, 2014 was 1.40%.

## **5. Other Long-term Liabilities**

At December 31, 2012, we had a long-term liability of \$275,000 to Midland Development Corporation. The liability was fully satisfied during the quarter ended March 31, 2013. As a result of our performance under the agreement, a payment to Midland Development Corporation of \$52,000 was made to settle the liability, resulting in a gain of \$223,000, which is included in the other income line, in our statement of income for the year ended December 31, 2013.

In addition, we entered into a purchase agreement with a vendor on July 30, 2008 pursuant to which we agreed to purchase up to \$4.8 million of our paint and coating requirements exclusively from the vendor. In connection with the execution of the agreement, the vendor paid us a \$300,000 fee which is considered to be a discount toward future purchases from the vendor. The \$300,000 payment we received is recorded as a long-term liability and will decrease as the purchase commitment is fulfilled. The long-term liability remaining for the purchase commitment was \$155,000 and \$197,000 as of December 31, 2014 and 2013, respectively.

## 6. Income Taxes

The provision for income taxes for the years ended December 31, 2014, 2013 and 2012, consists of the following (in thousands):

	<b>2014</b>	<b>2013</b>	<b>2012</b>
Current provision:			
Federal	\$ 995	\$ 69	\$ 332
State	195	330	222
Total current provision	<u>1,190</u>	<u>399</u>	<u>554</u>
Deferred provision:			
Federal	6,840	7,723	6,972
Total deferred provision	<u>6,840</u>	<u>7,723</u>	<u>6,972</u>
Total provision	<u>\$ 8,030</u>	<u>\$ 8,122</u>	<u>\$ 7,526</u>

The income tax effects of temporary differences that give rise to significant portions of deferred income tax assets and (liabilities) as of December 31, 2014 and 2013, are as follows (in thousands):

	<b>2014</b>	<b>2013</b>
Deferred income tax assets:		
Stock Compensation	\$ 1,249	\$ 916
Other	80	45
Total deferred income tax assets	<u>\$ 1,329</u>	<u>\$ 961</u>
Deferred income tax liabilities:		
Property and equipment	\$ (58,610)	(51,377)
Goodwill and other intangible assets	(1,023)	(1,048)
Total deferred income tax liabilities	<u>(59,633)</u>	<u>(52,425)</u>
Net deferred income tax liabilities	<u>\$ (58,304)</u>	<u>\$ (51,464)</u>

The effective tax rate for the years ended December 31, 2014, 2013 and 2012, differs from the statutory rate as follows:

	<b>2014</b>	<b>2013</b>	<b>2012</b>
Statutory rate	34.0%	34.0%	34.0%
State and local taxes	1.5%	1.7%	0.7%
Other	0.7%	0.4%	2.5%
Effective rate	<u>36.2%</u>	<u>36.1%</u>	<u>37.2%</u>

Our policy regarding income tax interest and penalties is to expense those items as general and administrative expense. During the years ended December 31, 2014, 2013 and 2012, there were no significant income tax interest or penalty items in the statement of income.

We had a federal net operating loss carry forward of \$3.2 million as of December 31, 2012, which was utilized in the year ended December 31, 2013. We file income tax returns in the U.S. federal jurisdiction and various state jurisdictions. With few exceptions, we are no longer subject to U.S. federal or state income tax examination by tax authorities for years before 2009.

## 7. Stockholders' Equity

### *Preferred Stock*

We have a total of 5.0 million authorized preferred shares with rights and preferences as designated by the Board of Directors. As of December 31, 2014 and 2013, there were no issued or outstanding preferred shares.

## 8. Stock-Based Compensation

### *Restricted Stock*

On June 16, 2009, at our annual meeting of shareholders, our shareholders adopted the 2009 Restricted Stock/Unit Plan. On June 3, 2014, at our annual meeting of shareholders, our shareholders approved a proposed amendment to the Plan to add additional 500,000 shares of common stock to the Plan, thereby authorizing the issuance of up to 800,000 shares of common stock under the Plan. On March 20, 2014, the Compensation Committee awarded 15,000 shares of restricted common stock to each of G. Larry Lawrence, our CFO, and James Hazlett our Vice President of Technical Services, subject to the approval at our June 2014 annual meeting of shareholders of a proposal to increase the number of shares reserved for issuance under our 2009 restricted Stock/Unit Plan. As the proposal was approved by shareholders at the 2014 annual meeting, we issued the restricted shares to Messrs. Hazlett and Lawrence which vest one year from the grant date. We also awarded and issued 13,152 shares of restricted common stock to our Board of Directors as partial payment for 2014 Directors' fees. The restricted stock issued to our Directors vests over one year, in quarterly installments, beginning March 31, 2015. In accordance with the Company's employment agreement with Stephen Taylor, the Company's Chief Executive Officer, the Compensation Committee reviewed his performance in determining the issuance of restricted common stock. Based on this review which included consideration of the Company's 2013 performance, Mr. Taylor, was awarded 49,420 restricted shares on January 23, 2014, which vest one year from the date of grant. Compensation expense related to the restricted shares was approximately \$2,818,000, \$1,485,000 and \$978,000 for the years ended December 31, 2014, 2013, and 2012, respectively. As of December 31, 2014, there was a total of approximately \$608,000 of unrecognized compensation expense related to the nonvested portion of these restricted shares. This expense is expected to be recognized within one year. As of December 31, 2014, 423,717 shares were still available for issuance under the 2009 Restricted Stock/Unit Plan.

A summary of all restricted stock activity as of December 31, 2014 and changes during the year then ended is presented below.

	Number of Shares	Weighted Average Grant Date Fair Value	Weighted Average Remaining Contractual Life (years)	Aggregate Intrinsic Value <i>(in thousands)</i>
Outstanding, December 31, 2013	103,618	\$ 18.94	9.07	\$ 2,857
Granted	92,572	29.18	—	2,701
Vested	(96,952)	19.21	—	2,935
Canceled/Forfeited	—	—	—	—
Outstanding, December 31, 2014	99,238	\$ 28.22	9.00	\$ 2,286

### *Stock Option Plan*

Our 1998 Stock Option Plan (the "Plan"), which is stockholder approved, permits the grant of stock options to its employees for up to 550,000 shares of common stock. On June 16, 2009, at our annual meeting of shareholders, our shareholders approved a proposed amendment to the Plan to add additional 200,000 shares of common stock to the Plan, thereby authorizing the issuance of up to 750,000 shares of common stock under the Plan. We believe that such awards better align the interests of our employees with our stockholders. Option awards are generally granted with an exercise price equal to the market price of our stock at the date of grant; those option awards generally vest based on three years of continuous service and have ten-year contractual terms. Certain option and share awards provide for accelerated vesting if there is a change in control of the Company (as defined in the Plan). The last date that grants can be made under the Plan is March 1, 2016. As of December 31, 2014, 186,419 shares were still available for issue under the Plan.

The fair value of each option award is estimated on the date of grant using the Black-Scholes option valuation model that uses the assumptions noted in the following table. The risk-free rate for periods within the contractual life of the option is based on the U.S. Treasury yield curve in effect at the time of grant. The expected life of options granted is based on the vesting period and historical exercise and post-vesting employment termination behavior for similar grants. We use historical data to estimate



option exercise and employee termination within the valuation model; separate groups of employees that have similar historical exercise behavior are considered separately for valuation purposes.

**Weighted average Black -Scholes fair value assumption during the years ended December 31, are as follows:**

	<b>2014</b>	<b>2013</b>	<b>2012</b>
Risk free rate	1.96%	1.02%	0.98%
Expected life	6 years	6 years	5 years
Expected volatility	58.44%	60.39%	62.37%
Expected dividend yield	—	—	—

A summary of all option activity as of December 31, 2014 and changes during the year then ended is presented below.

	Number of Stock Options	Weighted Average Exercise Price	Weighted Average Remaining Contractual Life (years)	Aggregate Intrinsic Value <i>(in thousands)</i>
Outstanding, December 31, 2013	378,852	\$ 15.61	5.23	\$ 4,533
Granted	60,000	30.06		
Exercised	(3,500)	17.13		48
Canceled/Forfeited	(3,083)	22.13		24
Expired	—	—		
Outstanding, December 31, 2014	432,269	\$ 17.55	10.10	\$ 2,786
Exercisable, December 31, 2014	340,435	\$ 15.34	8.99	\$ 2,622

We granted three options to purchase a total of 60,000 shares to non-executive employees in March, July and October 2014 at an exercise price of \$30.41, \$33.36 and \$23.30, respectively with a three year vesting period.

The weighted average grant date fair value of options granted during the years 2014, 2013, and 2012 was \$16.56, \$10.30, and \$8.22 respectively. The total intrinsic value, or the difference between the exercise price and the market price on the date of exercise, of options exercised during the years ended December 31, 2014, 2013, and 2012 was approximately \$48,000, \$458,000, and \$151,000 respectively. Cash received from stock options exercised during the years ended December 31, 2014, 2013, and 2012 was \$59,000, \$829,000, and \$180,000, respectively.

The following table summarizes information about our stock options outstanding at December 31, 2014:

Range of Exercise Prices	Options Outstanding			Options Exercisable	
	Shares	Weighted Average Remaining Contractual Life (years)	Weighted Average Exercise Price	Shares	Weighted Average Exercise Price
\$0.01-9.43	71,352	1.97	\$ 8.72	71,352	\$ 8.72
\$9.44-15.60	70,000	4.06	\$ 12.51	64,166	\$ 12.30
\$15.61-18.75	146,917	5.60	\$ 17.81	119,917	\$ 17.60
\$18.76-33.36	144,000	6.03	\$ 24.12	85,000	\$ 20.00
	432,269	4.89	\$ 17.55	340,435	\$ 15.34

The summary of the status of our unvested stock options as of December 31, 2014 and changes during the year then ended is presented below.

Unvested stock options:	Shares	Weighted Average Grant Date Fair Value
Unvested at December 31, 2013	63,082	\$ 9.87
Granted	60,000	\$ 16.56
Vested	(28,915)	\$ 9.80
Cancelled/Forfeited	(2,333)	\$ 12.87
Unvested at December 31, 2014	<u>91,834</u>	<u>\$ 14.19</u>

We recognized stock compensation expense from stock options vesting of \$426,000, \$198,000, and \$440,000 for the years ended December 31, 2014, 2013 and 2012, respectively. As of December 31, 2014, there was approximately \$808,000 of total unamortized compensation cost related to unvested stock options. We expect to recognize such cost over a weighted-average period of 3.0 years.

## 9. Commitments and Contingencies

### 401(k) Plan

We offer a 401(k) Plan to all employees that have reached the age of eighteen and have completed six months of service. The participants may contribute up to 100% of their salary subject to IRS limitations. Employer contributions are subject to Board discretion and are subject to a vesting schedule of 20% each year after the first year and 100% after six years. We contributed \$296,000, \$294,000, and \$283,000 to the 401(k) Plan in 2014, 2013 and 2012, respectively.

### Rented Facilities, Vehicles and Equipment

We lease certain of our facilities and equipment under operating leases with terms generally ranging from month-to-month to five years. Most leases contain renewal options. Remaining future minimum rental payments due under these leases are as follows:

Years Ending December 31, (in thousands)		
2015	\$	301
2016		268
2017		243
2018		113
2019		15
Total	\$	940

Rent expense under such leases was \$380,000, \$358,000, and \$453,000 for the years ended December 31, 2014, 2013 and 2012, respectively.

### Legal Proceedings

From time to time, we are a party to various legal proceedings in the ordinary course of our business. While management is unable to predict the ultimate outcome of these actions, it believes that any ultimate liability arising from these actions will not have a material effect on our financial position, results of operations or cash flow. We are not currently a party to any bankruptcy, receivership, reorganization, adjustment or similar proceeding, and we are not aware of any other threatened litigation.

## 10. Quarterly Financial Data (in thousands, except per share data) – Unaudited

2014	Q1	Q2	Q3	Q4	Total
Total revenue	\$ 22,322	\$ 21,952	\$ 25,599	\$ 27,101	\$ 96,974
Operating income	4,362	5,085	5,840	6,699	21,986
Net income	2,856	3,385	3,883	4,004	14,128
Net income per share - Basic	0.23	0.27	0.31	0.32	1.14
Net income per share - Diluted	0.23	0.27	0.30	0.32	1.11

2013	Q1	Q2	Q3	Q4	Total
Total revenue	\$ 23,983	\$ 20,258	\$ 21,865	\$ 23,142	\$ 89,248
Operating income	6,138	5,844	5,088	4,950	22,020
Net income	3,994	3,844	3,394	3,158	14,390
Net income per share - Basic	0.33	0.31	0.28	0.25	1.17
Net income per share - Diluted	0.32	0.31	0.27	0.25	1.15

Amounts may not add due to rounding differences.

\*\*\*\*\*  
INDEX TO EXHIBITS

<u>Exhibit No.</u>	<u>Description</u>
3.1	Articles of Incorporation, as amended (Incorporated by reference to Exhibit 3.1 of the 10-QSB filed and dated November 10, 2004)
3.2	Bylaws (Incorporated by reference to Exhibit 3.4 of the Registrant's Registration Statement on Form SB-2, No. 333-88314)
4.1	Non-Statutory Stock Option Agreement (Incorporated by reference to Exhibit 10.2 to Form 8-K filed with the SEC on August 30, 2005)
4.2	Form of Senior Indenture (Incorporated by reference to Exhibit 4.1 of the Registrant's Registration Statement on Form S-3 (No. 333-161346) and filed on August 14, 2009)
10.1	Lease Agreement, dated March 26, 2008, between WNB Tower, LTD and Natural Gas Services Group, Inc. (Incorporated by reference to Exhibit 10.15 of the Registrant's Form 10-K for the fiscal year ended December 31, 2008 and filed with the Securities and Exchange Commission on March 9, 2009)
10.2	2009 Restricted Stock/Unit Plan (Incorporated by reference to Exhibit 10.1 of the Registrant's Current Report on Form 8-K dated September 18, 2009 and filed with the Securities and Exchange Commission on September 18, 2009.)
10.3	1998 Stock Option Plan, as amended (Incorporated by reference to Exhibit 10.2 of the Registrant's Current Report on Form 8-K dated September 18, 2009 and filed with the Securities and Exchange Commission on September 18, 2009.)

- 10.4 Lease Agreement, dated December 11, 2008, between Klement-Wes Partnership, LTD and Natural Gas Services Group, Inc. and commencing on January 1, 2009
- 10.5 Credit Agreement between Natural Gas Services Group, Inc. and JPMorgan Chase Bank, N.A., dated December 10, 2010 (Incorporated by reference to Exhibit 10.1 of the Registrant's Current Report on Form 8-K filed with the Securities and Exchange Commission on November 24, 2014.)
- 10.6 Third Amendment of Credit Agreement between Natural Gas Services Group, Inc. and JPMorgan Chase Bank, N.A., dated November 19, 2014 (Incorporated by reference to Exhibit 10.1 of the Registrant's Current report on Form 8-K filed with the Securities and Exchange Commission on January 9, 2012.)
- 10.7 Security Agreement between Natural Gas Services Group, Inc. and JPMorgan Chase Bank, N.A., dated December 10, 2010 (Incorporated by reference to Exhibit 10.2 of the Registrant's Current Report on Form 8-K filed with the Securities and Exchange Commission on December 16, 2011.)
- 10.8 First Amendment of Security Agreement between Natural Gas Services Group, Inc. and JPMorgan Chase Bank, N.A., dated December 31, 2011 (Incorporated by reference to Exhibit 10.2 of the Registrant's Current report on Form 8-K filed with the Securities and Exchange Commission on January 9, 2012.)
- 10.9 Promissory Note in the aggregate amount of \$30,000,000 issued to JPMorgan Chase Bank, N.A., dated December 31, 2014, in connection with the revolving credit line under the Credit Agreement with JPMorgan Chase Bank, N.A. (Incorporated by reference to Exhibit 10.2 of the Registrant's Current Report on Form 8-K filed with the Securities and Exchange Commission on November 24, 2014.)
- 10.10 Employment Agreement between Natural Gas Services Group, Inc. and Stephen C. Taylor dated October 23, 2013 (Incorporated by reference to Exhibit 10.1 of the Registrant's Current Report on Form 8-K filed with the Securities and Exchange Commission on October 25, 2013)
- \*23.1 Consent of BDO USA, LLP
- \*31.1 Certification of Chief Executive Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002
- \*31.2 Certification of Principal Accounting Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002
- \*32.1 Certification of Chief Executive Officer pursuant to Section 906 of the Sarbanes-Oxley Act of 2002
- \*32.2 Certification of Principal Accounting Officer pursuant to Section 906 of the Sarbanes-Oxley Act of 2002
- 101.INS XBRL Instance Document
- 101.SCH XBRL Taxonomy Extension Schema Document
- 101.CAL XBRL Taxonomy Extension Calculation Linkbase Document
- 101.DEF XBRL Taxonomy Extension Definition Linkbase Document
- 101.LAB XBRL Taxonomy Extension Label Linkbase Document
- 101.PRE XBRL Taxonomy Extension Presentation Linkbase Document

\* Filed herewith.

## Certifications

I, Stephen C. Taylor, certify that:

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

Dated: March 13, 2015

Natural Gas Services Group, Inc.

By: /s/ Stephen C. Taylor

Stephen C. Taylor,  
President, CEO and Chairman of the Board of Directors  
(Principal Executive Officer)

## Certifications

I, G. Larry Lawrence, certify that:

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

Dated: March 13, 2015

Natural Gas Services Group, Inc.

By: /s/ G. Larry Lawrence

G. Larry Lawrence

Vice President, Chief Financial Officer

(Principal Accounting Officer)

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

In connection with the Annual Report of Natural Gas Services Group, Inc. (the “Company”) on Form 10-K for the period ended December 31, 2014 as filed with the Securities and Exchange Commission on the date hereof (the “Report”), I, Stephen C. Taylor, Chief Executive Officer of the Company, certify, pursuant to 18 U.S.C. §1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, that:

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

Dated: March 13, 2015

Natural Gas Services Group, Inc.

By: /s/ Stephen C. Taylor  
Stephen C. Taylor,  
President, CEO and Chairman of the Board of Directors  
(Principal Executive Officer)

The foregoing certification is being furnished solely to accompany the Report pursuant to 18 U.S.C. § 1350, and is not being filed for purposes of Section 18 of the Securities Exchange Act of 1934, as amended, and is not to be incorporated by reference into any filing of the Company, whether made before or after the date hereof, regardless of any general incorporation language in such filing.



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

In connection with the Annual Report of Natural Gas Services Group, Inc. (the “Company”) on Form 10-K for the period ended December 31, 2014 as filed with the Securities and Exchange Commission on the date hereof (the “Report”), I, G. Larry Lawrence, Chief Financial Officer of the Company, certify, pursuant to 18 U.S.C. §1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, that:

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

Dated: March 13, 2015

Natural Gas Services Group, Inc.

By: /s/ G. Larry Lawrence  
G. Larry Lawrence,  
Vice President and Chief Financial Officer  
(Principal Accounting Officer)

The foregoing certification is being furnished solely to accompany the Report pursuant to 18 U.S.C. § 1350, and is not being filed for purposes of Section 18 of the Securities Exchange Act of 1934, as amended, and is not to be incorporated by reference into any filing of the Company, whether made before or after the date hereof, regardless of any general incorporation language in such filing.

**Consent of Independent Registered Public Accounting Firm**

Natural Gas Services Group, Inc.  
Midland, Texas

We hereby consent to the incorporation by reference in the Registration Statements on Form S-8 (Nos. 333-196578, 333-147311, 333-110954, 333-160068, 333-160063 and 333-153874) and Form S-3 (No. 333-184672) of Natural Gas Services Group, Inc. of our reports dated March 13, 2015, relating to the financial statements and the effectiveness of Natural Gas Services Group, Inc.'s internal control over financial reporting, which appear in this Annual Report on Form 10-K.

/s/ BDO USA, LLP

Houston, Texas  
March 13, 2015



## EXECUTIVE OFFICERS & DIRECTORS

### **Stephen C. Taylor**

Chairman of the Board, President  
and Chief Executive Officer

### **G. Larry Lawrence**

Vice President and Chief Financial  
Officer

### **James R. Hazlett**

Vice President – Technical Services

### **David L. Bradshaw**

Director, Oil and Gas Investor,  
Former Chairman and CEO,  
Tipperary Corporation

### **John W. Chisholm**

Director, Founder, Wellogix, Inc.;  
President, CEO, Chairman of the  
Board, Flotek Industries

### **Charles G. Curtis**

Director, Retired, Former President  
and Chief Executive  
Officer of Curtis One Inc. dba  
Roll Stair

### **William F. Hughes**

Director, Co-Owner, The  
Whole Wheatery, LLC

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### **Independent Auditors**

BDO USA, LLP  
333 Clay St., Suite 4700  
Houston, Texas 77002

### **Annual Meeting of Shareholders**

June 18, 2015  
8:30 A.M. CDT  
Petroleum Club of Midland  
501 West Wall Street  
Midland, Texas 79701

### **Legal Counsel**

David A. Thayer  
Jones & Keller, P.C.  
1999 Broadway, Suite #3150  
Denver, Colorado 80202

### **Investor Relations**

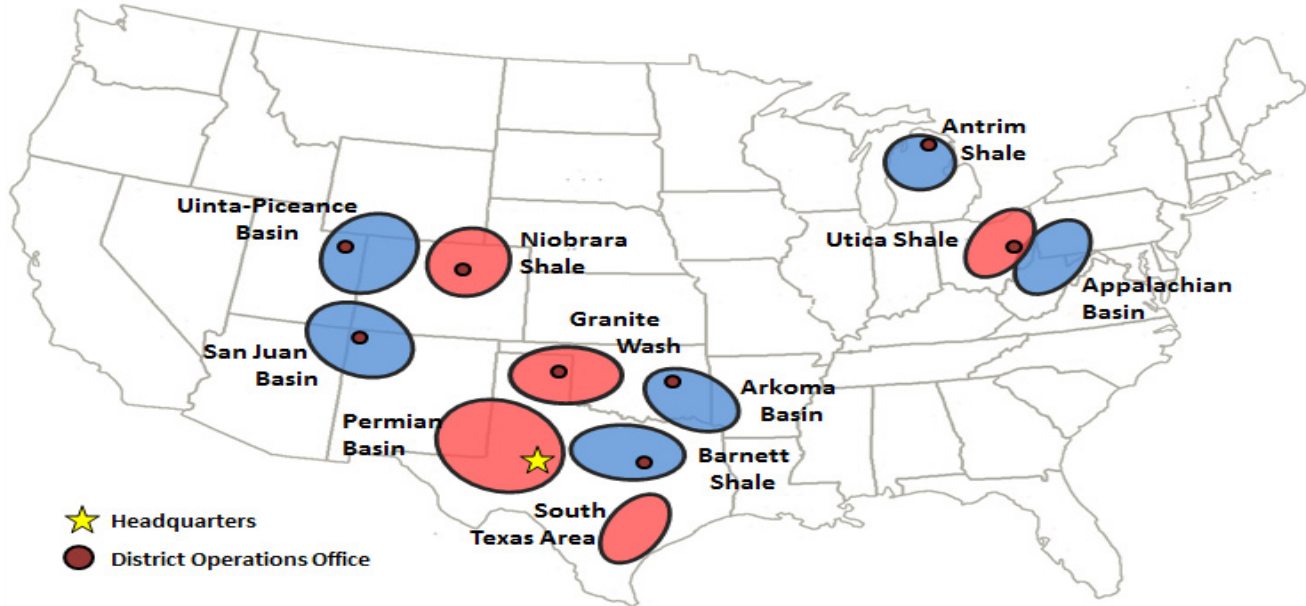
Alicia M. Dada  
Natural Gas Services Group  
Investor Relations Coordinator

### **Transfer Agent & Registrar**

Computershare Trust Company,  
Inc., Golden, Colorado



**NATURAL GAS SERVICES GROUP, INC.**  
RENTAL OPERATIONS MAP



**About Natural Gas Services Group, Inc.**

Headquartered in Midland, TX, Natural Gas Services Group (NGS) maintains a growing rental fleet of high quality rotary screw and reciprocating wellhead compressors in the 50-500 horsepower range. At the end of 2014 the rental fleet totaled 2879 compressor units...the largest rental compressor fleet in the U.S. dedicated to the small-medium horsepower, wellhead market. Repair and maintenance services for rental fleet units is provided through a network of district offices in Midland, Bridgeport and Godley, TX, Farmington, NM, Vernal, UT, Tulsa, OK, Loveland, CO and Lewiston, MI. Rental compressor fabrication facilities are located in Midland, TX. NGS designs, fabricates and sells custom engineered rotary screw and reciprocating compressor packages through our Engineered Products line in Tulsa, OK. This custom equipment ranges up to 2,500 horsepower per unit and can be natural gas engine or electric motor driven. NGS also designs, manufactures and fabricates a proprietary reciprocating compressor product line. The CIP (Cylinders in Plane) reciprocating compressor is a unique and efficient, small horsepower design that is utilized in our rental fleet and sold to compressor packagers, distributors and end-users throughout North America. Additionally, the Company designs, fabricates, sells, installs and services technologically advanced and patented industrial flare and combustion systems through our Flare King product line for use in onshore and offshore oil and natural gas production facilities. NGS is a public company, and has been listed on the New York Stock Exchange (NYSE:NGS) since 2008.

**Headquarters**

508 West Wall Street,  
Suite 550  
Midland, Texas 79701  
(432) 262-2700  
(432) 262-2701 fax  
[www.ngsgi.com](http://www.ngsgi.com)

**Michigan**

3690 CR 491  
Lewiston, Michigan 49756  
(989) 786-3788  
(989) 786-5182 fax

**Utah**

374 South 800 E  
Vernal, Utah 84078  
(435) 789-3280

**New Mexico**

3900 N. 1st  
Bloomfield, New Mexico 87413  
(505) 632-4566  
(505) 632-1364 fax

**Texas**

Bldg 107 PR 1420  
Bridgeport, Texas 76426  
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(940) 683-5113 fax

4721 N. Hwy 171  
Cleburne, Texas 76033  
(817) 645-5559  
(817) 645-6809 fax

**Oklahoma**

575 Bird Creek Avenue  
Catoosa, Oklahoma 74015  
(918) 266-3330  
(918) 971-1818 fax

**West Texas**

12301 W. CR 125  
Odessa, Texas 79765  
(432) 262-2700  
(432) 561-5480 fax

**Colorado**

3555 S. Lincoln Ave  
Loveland, CO 80537  
(970) 683-5322  
(970) 667-4257 fax