

TEXCOM, INC. AND SUBSIDIARIES

CONSOLIDATED FINANCIAL STATEMENTS

**As of December 31, 2013 and 2012
and for the Years Ended December 31, 2013 and 2012**

TEXCOM, INC. AND SUBSIDIARIES
CONSOLIDATED FINANCIAL STATEMENTS
As of and for the Years Ended December 31, 2013 and 2012

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Report of Independent Registered Public Accounting Firm

To the Board of Directors of
TexCom, Inc. and Subsidiaries
Houston, Texas

We have audited the consolidated balance sheets of TexCom, Inc. and Subsidiaries (the “Company”) as of December 31, 2013 and 2012, and the related consolidated statements of operations, changes in equity (deficit), and cash flows for the years then ended. 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 each audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. The Company is not required to have, nor were we engaged to perform, an audit of its internal control over financial reporting. Our audits included consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Company’s internal control over financial reporting. Accordingly, we express no such opinion. An audit also 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 consolidated financial statements referred to above present fairly, in all material respects, the consolidated financial position of TexCom, Inc. and Subsidiaries as of December 31, 2013 and 2012, and the consolidated results of their operations and their cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.

/s/ GBH CPAs, PC

GBH CPAs, PC
www.gbhcpas.com
Houston, Texas

March 31, 2014

TEXCOM, INC. AND SUBSIDIARIES
CONSOLIDATED BALANCE SHEETS

	December 31, 2013	December 31, 2012
Assets		
Current assets:		
Cash and cash equivalents	\$ 791,716	\$ 807,022
Restricted cash	-	1,809,000
Accounts receivable, net	2,887,004	1,772,043
Prepaid expenses and other current assets	235,121	64,320
Current portion of deferred income tax asset	50,000	320,000
Total current assets	3,963,841	4,772,385
Property and equipment, net	6,039,908	3,586,538
Equity in net assets of affiliate	705,152	707,793
Intangible assets, net	1,107,991	199,771
Goodwill	533,894	396,722
Deferred income tax asset, net of current portion	2,590,000	2,330,000
Other assets	234,054	602,168
Total assets	\$ 15,174,840	\$ 12,595,377
Liabilities and Equity		
Current liabilities:		
Accounts payable and accrued liabilities	\$ 1,908,422	\$ 2,315,057
Derivative liability	157,035	89,786
Line of credit	529,843	882,378
Current portion of long-term debt	1,800,012	1,591,858
Total current liabilities	4,395,312	4,879,079
Other long-term liabilities	457,956	233,595
Long-term debt, net of current portion	4,796,644	5,796,658
Total liabilities	9,649,912	10,909,332
Equity:		
Series A convertible preferred stock, \$0.001 par value, 5,000,000 shares authorized, 2,028,750 shares issued and outstanding	2,029	2,029
Non-designated preferred stock, \$1.00 par value, 15,000,000 shares authorized, no shares issued and outstanding	-	-
Common stock, \$0.001 par value, 100,000,000 shares authorized, 64,453,389 and 63,878,389 shares issued and outstanding, respectively	64,453	63,878
Additional paid-in capital	13,037,481	13,030,556
Accumulated deficit	(8,677,129)	(12,555,843)
Total TexCom equity	4,426,834	540,620
Noncontrolling interest	1,098,094	1,145,425
Total equity	5,524,928	1,686,045
Total liabilities and equity	\$ 15,174,840	\$ 12,595,377

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

TEXCOM, INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF OPERATIONS
FOR THE YEARS ENDED DECEMBER 31, 2013 AND 2012

	For the Years Ended December 31,	
	2013	2012
Revenues	\$ 15,888,922	\$ 11,527,251
Cost of revenues, excluding royalties, depreciation and amortization	4,540,735	2,778,168
Royalties	3,364,341	2,715,564
Depreciation and amortization	601,265	445,080
Total cost of revenues	8,506,341	5,938,812
 Gross profit	 7,382,581	 5,588,439
Selling, general, and administrative expenses	2,265,018	2,091,945
Loss on sale of assets	34,127	-
 Operating income	 5,083,436	 3,496,494
Other income (expense)		
Interest expense	(737,043)	(1,989,828)
Enhanced payments to shareholders	-	(65,627)
Equity in loss of affiliate	(2,641)	(98,235)
Gain (loss) on change in fair value of derivative liability	(67,249)	83,165
 Income before income taxes	 4,276,503	 1,425,969
Income tax benefit (expense)	(10,000)	2,650,000
 Net income	 4,266,503	 4,075,969
 Income attributable to noncontrolling interest	 (387,789)	 (303,119)
 Net income attributable to TexCom shareholders	 \$ 3,878,714	 \$ 3,772,850
 Income per common share – basic	 \$ 0.05	 \$ 0.05
 Income per common share – diluted	 \$ 0.05	 \$ 0.05
 Weighted average common shares outstanding – basic	 63,900,444	 63,581,724
 Weighted average common shares outstanding – diluted	 63,900,444	 64,145,379

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

TEXCOM, INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENT OF CHANGES IN EQUITY (DEFICIT)
FOR THE TWO YEARS ENDED DECEMBER 31, 2013 AND 2012

	Preferred Stock		Common Stock		Additional Paid-in Capital	Accumulated Deficit	Noncontrolling Interest	Total
	Shares	Amount	Shares	Amount				
Balances at December 31, 2011 (Restated)	2,028,750	\$ 2,029	62,940,154	\$ 62,940	\$ 12,834,711	\$ (16,328,693)	\$ 972,486	\$ (2,456,527)
Shares issued for cash	-	-	588,235	588	99,412	-	-	100,000
Share-based compensation	-	-	100,000	100	74,795	-	-	74,895
Exercise of warrants	-	-	250,000	250	21,638	-	-	21,888
Payment of dividends	-	-	-	-	-	-	(130,180)	(130,180)
Net income	-	-	-	-	-	3,772,850	303,119	4,075,969
Balances at December 31, 2012	2,028,750	\$ 2,029	63,878,389	\$ 63,878	\$ 13,030,556	\$ (12,555,843)	\$ 1,145,425	\$ 1,686,045
Payable recorded to settle stock offering costs	-	-	-	-	(50,000)	-	-	(50,000)
Exercise of warrants	-	-	575,000	575	56,925	-	-	57,500
Payment of dividends	-	-	-	-	-	-	(435,120)	(435,120)
Net income	-	-	-	-	-	3,878,714	387,789	4,266,503
Balances at December 31, 2013	<u>2,028,750</u>	<u>\$ 2,029</u>	<u>64,453,389</u>	<u>\$ 64,453</u>	<u>\$ 13,037,481</u>	<u>\$ (8,677,129)</u>	<u>\$ 1,098,094</u>	<u>\$ 5,524,928</u>

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

TEXCOM, INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF CASH FLOWS
FOR THE YEARS ENDED DECEMBER 31, 2013 AND 2012

	For the Years Ended December 31,	
	2013	2012
Cash flows from operating activities:		
Net income	\$ 4,266,503	\$ 4,075,969
Adjustments to reconcile net income to cash from operating activities:		
Depreciation and amortization	601,265	445,080
Bad debt expense	2,832	73,544
Amortization of deferred financing costs	286,059	540,764
Stock-based compensation	-	22,000
Equity in loss of affiliate	2,641	98,235
Loss on disposition of equipment	34,127	-
Loss (gain) on change in fair value of derivative liabilities	67,249	(83,165)
Deferred income tax expense (benefit)	10,000	(2,650,000)
Changes in operating assets and liabilities:		
Accounts receivable	(1,117,793)	(219,582)
Prepaid expenses and other current assets	(21,976)	(46,500)
Accounts payable and accrued liabilities	(344,399)	(179,310)
Other long-term liabilities	(46,082)	(35,587)
Net cash provided by operating activities	<u>3,740,426</u>	<u>2,041,448</u>
Cash flows from investing activities:		
Investment in affiliates	-	(82,833)
Net proceeds from restricted cash	1,809,000	(1,647,379)
Proceeds from sale of equipment	20,000	-
Purchases of property and equipment	(2,795,947)	(711,306)
Other assets – deposit paid	(13,690)	-
Acquisition of ALMAC	(1,200,000)	-
Net cash used in investing activities	<u>(2,180,637)</u>	<u>(2,441,518)</u>
Cash flows from financing activities:		
Proceeds from long-term debt, third party	-	6,862,378
Net change in line of credit	(352,535)	882,378
Proceeds from issuance of note payable	906,920	-
Principal repayments on long-term debt	(1,751,860)	(7,274,967)
Principal repayments on long-term debt, related party	-	(475,554)
Payment of dividends to noncontrolling interest	(435,120)	(130,180)
Proceeds from issuances of common stock	57,500	121,888
Net cash used in financing activities	<u>(1,575,095)</u>	<u>(14,057)</u>
Net change in cash and cash equivalents	(15,306)	(414,127)
Cash and cash equivalents, beginning of year	<u>807,022</u>	<u>1,221,149</u>
Cash and cash equivalents, end of year	<u>\$ 791,716</u>	<u>\$ 807,022</u>
Supplemental cash flows information:		
Cash paid for interest	<u>\$ 481,970</u>	<u>\$ 1,435,549</u>
Cash paid for income tax	<u>\$ -</u>	<u>\$ -</u>
Non-cash investing and financing activities:		
Payable for purchase of equipment	<u>\$ 104,793</u>	<u>\$ 73,615</u>
Estimate of asset retirement obligations	<u>\$ 25,000</u>	<u>\$ -</u>
Contingent liability accrued for acquisition of subsidiary	<u>\$ 238,000</u>	<u>\$ -</u>
Payable recorded to settle stock offering costs	<u>\$ 50,000</u>	<u>\$ -</u>

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

TEXCOM, INC. AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
For the Years Ended December 31, 2013 and 2012

NOTE 1 – DESCRIPTION OF BUSINESS AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Business and Basis of Presentation

TexCom, Inc. (“TexCom” or the “Company”) was incorporated under the laws of the State of Texas on December 9, 2003. In 2012, the Company converted from a Texas corporation to a Nevada corporation.

The Company was organized to pursue investment opportunities in certain energy related businesses and develop them to their logical and full commercial potential. The Company is a provider of environmental services to the oil and gas industry, currently engaged in the business of disposing of waste generated by exploration and production operations. Among these wastes are non-hazardous oilfield wastes (“NOW”) and naturally occurring radioactive materials (“NORM”). The Company’s controlled subsidiaries, M.B. Environmental Services, LLC (“MBES”) and Eagle Ford Environmental Services, LLC (“EFES”), operate two wells for disposal of NOW and NORM and two for disposal of NOW, all located in Texas. The Company’s wholly owned TexCom Environmental Services, LLC (“TES”) provides consulting, remediation services. TES was formed with the assets and ongoing business that were purchased from ALMAC Environmental Services, Inc. (“ALMAC”), in July 2013, for \$1.2 million and an estimated earnout valued at \$238,000. The acquired fixed assets were valued at \$270,828, the customer relationships at \$760,000, the workforce at \$270,000 and a goodwill at \$137,172 was recorded. See notes 2, 6 and 8.

The consolidated financial statements include the accounts of the Company and its wholly owned and majority-owned subsidiaries. All material intercompany transactions and balances have been eliminated. The Company owns 83.2% of M.B. Energy Services, Inc. (“MBSI”) which fully owns MBES. The Company’s twenty percent (20%) interest in Texcom Gulf Disposal, LLC (“TGD”) is accounted for under the equity method.

Use of Estimates and Assumptions

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reported periods. Actual results could materially differ from those estimates.

Summary of Significant Accounting Policies

Cash and Cash Equivalents – The Company considers any highly liquid financial instruments purchased with an original maturity of three months or less to be cash equivalents.

Restricted Cash – During the year ended December 31, 2013, we drew down \$1,809,000 of restricted cash to construct a second well at our site in the Eagle Ford Shale area. At December 31, 2013 and 2012, there was \$0 and \$1,809,000, respectively, of restricted cash. The funds were part of the debt that was originated on November 30, 2012. See Note 6.

Accounts Receivable and Allowance for Doubtful Accounts – Accounts receivable are stated at the amount the Company expects to collect. Accounts receivable represents receivables, net of allowances for doubtful accounts. The allowance for doubtful accounts reflects our best estimate of probable losses inherent in the accounts receivable balance. We determine the allowance based on historical experience and other currently available information. When a specific account is deemed uncollectible, the account is written off against the allowance. As of December 31, 2013 and 2012, the allowance for doubtful accounts was \$155,710 and \$158,812, respectively.

Equity Method of Accounting – Investments in corporate entities over which the Company can exert significant influence (but not control) are accounted for using the equity method. Under the equity method, the investment is recorded initially at cost. Subsequent adjustments are made through recognition in the income statement for the Company’s share of post-acquisition profits and losses and through recognition in stockholders’ equity for other post-acquisition changes in the investee’s net assets. Dividends received reduce the investment account. The equity method requires the Company to record its investment in the investee as a one-line asset and to reflect its proportionate share of the investee’s net income/loss on one line in the statement of operations.

TEXCOM, INC. AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
For the Years Ended December 31, 2013 and 2012

NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Property and Equipment – Property and equipment are stated at cost. Depreciation is computed over the estimated useful lives of the related assets using the straight-line method for financial reporting purposes.

Expenditures for normal repairs and maintenance are charged to expense as incurred. Significant renewals and improvements are capitalized. The costs and related accumulated depreciation of assets retired or otherwise disposed of are eliminated from the accounts, and any resulting gain or loss is recognized in the year of disposal.

Impairment of Long-Lived Assets – Management reviews long-lived assets for impairment whenever events or changes in circumstances indicate that the carrying amount may not be realizable or at a minimum annually during the fourth quarter of the year. If an evaluation is required, the estimated future undiscounted cash flows associated with the asset are compared to the asset's carrying value to determine if an impairment of such asset is necessary. The effect of any impairment would be to expense the difference between the fair value of such asset and its carrying value.

Goodwill and Other Intangible Assets – We apply a fair value-based impairment test to the net book value of goodwill and indefinite-lived intangible assets on an annual basis and, if certain events or circumstances indicate that an impairment loss may have been incurred, on an interim basis.

Key Assumptions - The key assumptions in our impairment tests include (1) our projected revenues, expenses and cash flows, (2) an estimated weighted average cost of capital, (3) assumed discount rates depending on the asset and (4) a tax rate. These assumptions are consistent with those hypothetical market participants would use. Since we are required to make estimates and assumptions when evaluating goodwill and indefinite-lived intangible assets for impairment, the actual amounts may differ materially from these estimates.

Changes in assumptions or circumstances could result in impairment. Factors which could cause impairment include, but are not limited to, (1) negative trends in our market capitalization, (2) a decline in prices for oil and natural gas, (3) a decrease in drilling activity, (4) interruption to our operations, (5) changes to the regulatory environment and (6) consolidation of competitors in the disposal industry.

Goodwill – As of December 31, 2013 and 2012, our goodwill balance was \$533,894 and \$396,722, respectively. In evaluating goodwill for impairment, we estimate the fair value of our reporting unit by considering market capitalization and other factors if it is more likely than not that the fair value of our reporting unit is less than its carrying value. If the reporting unit's fair value exceeds its carrying value, no further testing is required. If, however, the reporting unit's carrying value exceeds its fair value, we then determine the amount of the impairment charge, if any. We recognize an impairment charge if the carrying value of the reporting unit's goodwill exceeds its estimated fair value.

Intangible Assets – Intangible assets with definite useful lives are recorded on the basis of cost and are amortized on a straight-line basis over their estimated useful lives. The Company uses a useful life of 20 years for permits and 5 years for customer relationship. The Company evaluates the remaining useful life of intangible assets annually to determine whether events and circumstances warrant a revision to the remaining amortization period. If the estimate of the intangible asset's remaining useful life is changed, the remaining carrying amount of the intangible asset will be amortized prospectively over that revised remaining useful life. At December 31, 2013 and 2012, no revision to the remaining amortization period of the intangible assets was made.

TEXCOM, INC. AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
For the Years Ended December 31, 2013 and 2012

NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Asset Retirement Obligation – The Company recognizes the fair value of all liabilities where the Company has an obligation to close or remediate property upon its abandonment or the end of its useful life. The amount recognized as a liability is capitalized as part of the cost of the asset to which it relates and amortized to expense ratably over its useful life. The Company's asset retirement obligations are associated with its oil and gas and industrial wastewater disposal wells.

Derivatives – All derivatives are recorded at fair value on the balance sheet. Fair values for securities traded in the open market and derivatives are based on quoted market prices. Where market prices are not readily available, fair values are determined using market based pricing models incorporating readily observable market data and requiring judgment and estimates.

Income Taxes – The Company uses the asset and liability method in accounting for income taxes. Under this method, deferred tax assets and liabilities are determined based on differences between financial reporting and income tax carrying amounts of assets and liabilities and are measured using the enacted tax rates and laws that will be in effect when the differences are expected to reverse. The Company reviews deferred tax assets for a valuation allowance based upon whether it is more likely than not that the deferred tax asset will be fully realized. A valuation allowance, if necessary, is provided against deferred tax assets, based upon management's assessment as to their realization.

Fair Value of Financial Instruments – 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. A fair value hierarchy has been established for valuation inputs that gives the highest priority to quoted prices in active markets for identical assets or liabilities and the lowest priority to unobservable inputs. The fair value hierarchy is as follows:

- Level 1 Inputs – Unadjusted quoted prices in active markets for identical assets or liabilities that the reporting entity has the ability to access at the measurement date.
- Level 2 Inputs – Inputs other than quoted prices included in Level 1 that are observable for the asset or liability, either directly or indirectly. These might include quoted prices for similar assets or liabilities in active markets, quoted prices for identical or similar assets or liabilities in markets that are not active, inputs other than quoted prices that are observable for the asset or liability (such as interest rates, volatilities, prepayment speeds, credit risks, etc.) or inputs that are derived principally from or corroborated by market data by correlation or other means.
- Level 3 Inputs – Unobservable inputs for determining the fair values of assets or liabilities that reflect an entity's own assumptions about the assumptions that market participants would use in pricing the assets or liabilities.

Financial instruments consist of cash and cash equivalents, accounts receivable, collateralized receivables, accounts payable and secured borrowings.

TEXCOM, INC. AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
For the Years Ended December 31, 2013 and 2012

NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Earnings Per Common Share – The Company provides basic and diluted earnings per common share information for each period presented. The basic earnings per common share is computed by dividing the net income available to common stockholders by the weighted average number of common shares outstanding during the reporting period. Diluted earnings per common share is computed by dividing the net income available to common stockholders by the weighted average number of common shares outstanding plus dilutive securities. The dilutive effect of outstanding stock options and warrants is reflected in diluted earnings per share by application of the treasury stock method. The dilutive effect of Series A Preferred Stock is reflected in diluted earnings per share by application of the if-converted method.

Revenue Recognition – Revenues from waste disposal activities are recognized when the Company takes delivery of the waste product at its disposal well location, the price is fixed or determinable, and collection is reasonably assured.

Stock-Based Compensation – The cost of employee services received in exchange for stock is measured based on the grant-date fair value (with limited exceptions). That cost is to be recognized over the period during which an employee is required to provide service in exchange for the award (usually the vesting period). The fair value of immediately vested shares is determined by reference to quoted prices for similar shares, and the fair value of shares issued subject to a service period is estimated using an option-pricing model. Excess tax benefits, for which no valuation allowance is required, are recognized as additions to paid-in-capital.

The Company also makes stock awards to non-employees for goods and services acquired by the Company. These awards are generally recorded at the market price of the shares issued on the date the shares are issued.

Concentration of Credit Risk – Financial instruments which subject the Company to concentrations of credit risk include cash and cash equivalents, accounts receivable, and notes payable to third parties. The Company maintains its cash and cash equivalents with major financial institutions selected based upon management's assessment of the institutions' financial stability. Balances periodically exceed the federally insured limits. The Company has not experienced any losses on deposits. Accounts receivable generally arise from sales of services to customers operating in the United States of America. Collateral is generally not required for credit granted. The Company provides allowances for potential credit losses when necessary. A substantial portion of the Company's notes payable are with a single lender at December 31, 2013.

Subsequent Events – The Company's management reviewed all material events from December 31, 2013 through the issuance date of this report for disclosure consideration.

Recent Accounting Pronouncements – Management does not expect the adoption of any other recently issued accounting pronouncements to have a significant effect on the Company's financial position or results of operation.

Reclassifications – Certain prior period amounts have been reclassified to conform to current period presentation.

TEXCOM, INC. AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
For the Years Ended December 31, 2013 and 2012

NOTE 2 – BUSINESS COMBINATION

On July 1, 2013, the Company completed the acquisition of certain assets of ALMAC. The Company accounted for the assets and ownership interests in accordance with the provisions of ASC 805, Business Combinations. Pursuant to the purchase agreement, the Company paid \$1,200,000, consisting of \$1,000,000 cash at closing and \$200,000 recorded as a payable to the sellers, which was paid during 2013. In addition, the Company agreed to pay up to \$1,600,000 as contingent consideration, based on the subsidiary’s quarterly earnings for the next four years. The Company has calculated an estimated present value of the contingent consideration of \$254,456 at December 31, 2013, which includes accretion of \$16,456 since the acquisition date.

The acquisition price was allocated to the assets acquired based upon their estimated fair values. The following table summarizes the estimated fair values of the assets acquired at the date of acquisition. The Company did not assume any liabilities. The estimated fair values of assets acquired were determined based on management’s best estimates. Estimates and assumptions are subject to change upon management’s final review. The Company is still reviewing the final value of the assets acquired and is expecting to complete its final assessment no later than one year from the acquisition date.

Assets acquired:	
Current assets	\$ -
Fixed assets	270,828
Customer relationships	760,000
Workforce	270,000
Goodwill	<u>137,172</u>
Total assets acquired	<u>\$ 1,438,000</u>
Consideration:	
Cash	\$ 1,200,000
Contingent liability	<u>238,000</u>
Total consideration	<u>\$ 1,438,000</u>

NOTE 3 – INVESTMENTS IN AFFILIATES

In 2005, the Company created a wholly owned subsidiary, TexCom Gulf Disposal, LLC (“TGD”) to develop an injection well it owned in Texas. In various transactions in 2008 and 2009, the Company transferred 80% of its interest in TGD to Montgomery County Environmental Solutions, LLC (“MCES”), an unrelated third party, that agreed to provide the working capital necessary to complete the application for a Class I Industrial Wastewater Disposal Permit, from the Texas Commission on Environmental Quality, (the “TCEQ”), and construct the surface facilities needed to place the disposal business in commercial operation. MCES together with its shareholders is now a 30% owner of the Company.

The Company does not guarantee any obligations of TGD, but may be obligated to partially fund the operations of TGD in order to maintain its 20% interest. When the controlling interest was transferred to MCES, TexCom began to account for TGD using the equity method rather than consolidating the entity. At that time, TexCom’s investment in the net assets of TGD exceeded its share of the net assets recorded in the financial statements of TGD by approximately \$612,000.

For the years ended December 31, 2013 and 2012, the Company recorded equity losses of affiliates of \$2,641 and \$15,402, respectively, related to its investment in TGD.

In 2011, the Company entered into an agreement to acquire a 25% interest in Providence Environmental Solutions, Ltd. (“PES”), a foreign entity, for \$400,000. The Company is not obligated to provide further funding and has no other liabilities in connection with PES. Due to the nature of the foreign investment, no value has been assigned to the investment and the Company reported a loss in affiliates related to PES of \$82,833 for the year ending December 31, 2012. The Company has not contributed any money or sustained any losses since March 2012.

TEXCOM, INC. AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
For the Years Ended December 31, 2013 and 2012

NOTE 4 – PROPERTY AND EQUIPMENT

Property and equipment consisted of the following at December 31, 2013 and December 31, 2012:

	<u>Lives</u>	<u>December 31, 2013</u>	<u>December 31, 2012</u>
Building & improvements	10 – 30 years	\$ 308,117	\$ 308,117
Equipment, furniture & fixtures	5 – 10 years	651,802	628,801
Disposal wells	10 years	581,501	581,501
Transportation equipment	7 years	358,829	94,444
Leasehold improvements	10 years	5,320,427	2,844,728
Land		<u>47,484</u>	<u>47,484</u>
Subtotal		7,268,160	4,505,075
Less: accumulated depreciation		<u>(1,228,252)</u>	<u>(918,537)</u>
Property and equipment, net		<u>\$ 6,039,908</u>	<u>\$ 3,586,538</u>

All of the leasehold improvements are related to our location in the Eagle Ford shale area. The value of leasehold improvements includes \$192,675 and \$161,988 of capitalized interest at December 31, 2013 and 2012, respectively.

Depreciation expense was \$479,485 and \$426,300 for the years ended December 31, 2013 and 2012, respectively.

NOTE 5 – INTANGIBLE ASSETS

Intangible assets consisted of the following at December 31, 2013 and 2012:

	<u>December 31, 2013</u>	<u>December 31, 2012</u>
Disposal permit and customer lists	\$ 1,257,901	\$ 1,257,901
Customer relationships	760,000	-
Workforce	270,000	-
Less: accumulated amortization	<u>(1,179,910)</u>	<u>(1,058,130)</u>
Intangible assets, net	<u>\$ 1,107,991</u>	<u>\$ 199,771</u>

Amortization expense was \$121,780 and \$18,780 for the years ended December 31, 2013 and 2012, respectively.

TEXCOM, INC. AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
For the Years Ended December 31, 2013 and 2012

NOTE 6 – NOTES PAYABLE AND LINE OF CREDIT

Notes payable consisted of payables to financial institutions and other third parties as the following at December 31, 2013 and 2012:

	December 31, 2013	December 31, 2012
\$7,400,000 note payable, bearing interest at Prime + 3% (6.25% at December 31, 2013 and 2012), subject to a maximum rate of 18% and minimum of 6.25%, payable in 60 monthly installments of \$123,334 plus interest, secured by a first-position lien on all assets of the Company.	\$ 5,796,658	\$ 7,276,666
\$960,000 note payable, bearing interest at Prime + 3% (6.25% at December 31, 2013), subject to a maximum rate of 18% and minimum of 6.25%, payable in 36 monthly installments of \$26,667 plus interest, secured by a first-position lien on all assets of the Company.	799,998	-
Various notes payable bearing interest ranging from 8.8% to 17.0% per annum and maturing in January and February 2013.	-	111,850
Total notes payable	6,596,656	7,388,516
Less: amounts due within one year	(1,800,012)	(1,591,858)
Long-term portion of notes payable	\$ 4,796,644	\$ 5,796,658

In November 2012, the Company refinanced the majority of its debt and augmented its working capital through a relationship with a new bank. The Company obtained \$7,400,000 in a term loan and a separate revolving line of credit equal to 80% of eligible trade accounts receivable, subject to a maximum of \$2,000,000. At December 31, 2013, there was \$661,777 line of credit available. The Company incurred \$590,517 of financing costs associated with the financing. The \$464,875 related to the term loan is amortized using the effective-interest-rate method over the life of the five-year term loan. The \$125,642 related to the line of credit was amortized equally over twelve months.

On July 1, 2013, the Company issued a note to borrow \$960,000 for the acquisition of the assets of ALMAC Environmental Services, Inc. The note bears interest at the Prime Rate plus 3% with a minimum rate of 6.25% and is secured by all the assets purchased and all assets of the Company. Principal on the note is payable in 36 monthly installments of \$26,667 plus interest. The Company incurred \$53,080 of financing costs associated with the financing, which is amortized using the effective-interest-rate method over the life of the three-year term loan.

Future minimum payments under existing third-party notes payable for the twelve months ending each of the following periods are as follows:

For the year ending December 31,	Amount
2014	\$ 1,800,012
2015	1,800,012
2016	1,639,998
2017	1,356,634
2018	-
Total	\$ 6,596,656

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NOTE 6 – NOTES PAYABLE AND LINE OF CREDIT (CONTINUED)

Revolving line of credit payable to third party consisted of the following at December 31, 2013 and 2012:

	December 31, 2013	December 31, 2012
\$2,000,000 revolving line of credit, bearing interest at Prime + 2% (5.25% at December 31, 2013), subject to a maximum rate of 18% and minimum of 5.25%, secured by a first-position lien on all assets of the Company.	\$ 529,843	\$ 882,378

Both the two term loans and the line of credit require that the Company maintain the three following:

1. Debt service coverage ratio (calculated as EBITDA less current taxes plus non-cash stock expenses divided by current maturities of long-term debt plus current interest) of at least 1.5.
2. Maximum funded debt to EBITDA of no more than 3.0.
3. A tangible net worth of \$1,000,000 or greater.

Pursuant to the notes agreement, no dividends shall be paid by the Company without the consent of the lender of the two term loans except as to certain shareholders of M.B. Energy Services, Inc.

At December 31, 2013, the Company was in compliance with all covenants.

For the years ended December 31, 2013 and 2012, the Company recognized \$286,059 and \$24,659 of expense related to the amortization of the two term loans and the line of credit, respectively.

NOTE 7 – DERIVATIVE INSTRUMENTS

The Company determined that the warrants associated with the purchase of the Eagle Ford shale area disposal well qualified for accounting treatment as a financial derivative, because the warrant agreement requires that the exercise price and number of shares be adjusted if the Company sells or issues stock or common-stock equivalents at a price that is less than the warrant's strike price. The fair value of \$112,020 on these warrants valued in August 2011, the date of issuance, was classified as a derivative liability. At December 31, 2011, the Company revalued the derivative at \$172,951, resulting in a loss of \$60,931. At December 31, 2012, the Company again revalued the derivative at \$89,786, resulting in a gain of \$83,165 for the year then ended. At December 31, 2013, the Company again revalued the derivative at \$157,035, resulting in a loss of \$67,249 for the year then ended. After adjustments for price resets, the warrant provides for the purchase of 1,800,643 shares at an exercise price of \$0.16 per share, expiring in August 2015.

The Company uses a lattice model to value the derivative based on a probability weighted discounted cash flow model. This model is based on future projections of the various potential outcomes. The following assumptions were made in valuing the derivative at December 31, 2013 and 2012:

- The stock price will fluctuate with an annual volatility ranging from 110% to 561% at December 31, 2013 and from 143% to 642% at December 31, 2012.
- The holder will exercise the warrant at a target price of the higher of 2.0 times the reset price or 5 times the stock price.
- The holder will exercise at maturity if the market value exceeds the exercise price.
- The Company will raise capital through sales of common stock quarterly during the next twelve months at prices equal to the market value.

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NOTE 8 – OTHER LONG-TERM LIABILITIES

	December 31, 2013	December 31, 2012
Asset retired obligations	\$ 100,000	\$ 75,000
Production payment of Eagle Ford well	158,595	204,678
Contingent consideration related to the acquisition of ALMAC	254,456	-
Subtotal	513,051	279,678
Current portion of production payment of Eagle Ford well	(55,095)	(46,083)
Long-term portion of other long-term liabilities	<u>\$ 457,956</u>	<u>\$ 233,595</u>

The Company's asset retirement obligations, totaling \$100,000 at December 31, 2013 and \$75,000 at December 31, 2012, are related to its expected costs for the plugging of its four oil and gas waste disposal injection wells. The balances are included in other long-term liabilities on the consolidated balance sheets.

As part of the August 2011 acquisition of the disposal well in the Eagle Ford shale area, the Company agreed to pay \$0.03 for every barrel of disposed liquid, up to a maximum of \$350,000. Accordingly, the Company calculated the present value of the future payments at \$240,265 and recorded a liability. For the years ended December 31, 2013 and 2012, the Company paid \$46,082 and \$34,345, respectively, for disposed liquid. The present value of the estimated remaining payments is \$158,595.

As part of the July 2013 acquisition of the assets of ALMAC Environmental Services, Inc., the Company agreed to pay the sellers contingent consideration based on TES pre-tax net income ("PNI") for the next four years. The payments will equal 75% of the amount by which PNI exceeds \$1.2 million. The Company estimated the present value of the payments to be \$238,000. The balances are included in other long-term liabilities on the consolidated balance sheets. As of December 31, 2013, total TES PNI has not exceeded \$1.2 million, and nothing has been paid to the sellers. The sellers are now Company employees.

NOTE 9 – INCOME TAXES

The components of income tax expense (benefit) for the years ended December 31, 2013 and 2012 are as follows:

	2013	2012
Current income tax expense (benefit)	\$ -	\$ -
Deferred income tax expense (benefit)	10,000	(2,650,000)
Total income tax expense (benefit)	<u>\$ 10,000</u>	<u>\$ (2,650,000)</u>

The difference between the income tax benefit and the amount that would result if the U.S. Federal statutory rate of 34% were applied to pre-tax income for the years ended December 31, 2013 and 2012 is as follows:

	2013		2012	
	Amount	%	Amount	%
Income tax at federal statutory rate	\$ 1,460,000	34.0 %	\$ 480,000	34.0 %
Change in valuation allowance	(1,620,000)	(37.7) %	(3,300,000)	(233.8) %
Other adjustments	170,000	(4.0) %	170,000	12.0 %
Effective tax	<u>\$ 10,000</u>	<u>0.3 %</u>	<u>\$ (2,650,000)</u>	<u>(187.8) %</u>

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NOTE 9 – INCOME TAXES (CONTINUED)

Deferred income taxes reflect the net tax effects of temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for income tax purposes. Significant components of the Company’s deferred tax assets and liabilities at December 31, 2013 and 2012 are as follows:

	<u>December 31, 2013</u>	<u>December 31, 2012</u>
Deferred tax assets:		
Net operating losses	\$ 2,200,000	\$ 2,930,000
Equity in net assets of affiliate	40,000	150,000
Intangibles and other assets	880,000	1,040,000
Other differences in tax basis	300,000	510,000
Total deferred tax assets	<u>3,420,000</u>	<u>4,630,000</u>
Deferred tax liabilities:		
Change in accounting method for tax purposes	130,000	260,000
Property and equipment	650,000	100,000
Total deferred tax liabilities	<u>780,000</u>	<u>360,000</u>
Net deferred tax assets	2,640,000	4,270,000
Valuation allowance	-	(1,620,000)
Deferred tax assets, net	2,640,000	2,650,000
Less: current portion of deferred tax assets	(50,000)	(320,000)
Long-term portion of deferred tax assets	<u>\$ 2,590,000</u>	<u>\$ 2,330,000</u>

The Company fully reserved its U.S. net deferred tax assets in 2011 due to the uncertainty of future taxable income. In 2012, based on all available evidence, management believes that it is more likely than not that the Company’s deferred tax assets related to net operating losses (“NOLs”) will be realized. Accordingly, the Company reduced its related valuation allowance in 2012. In 2013, based on all available evidence, management believes that it is more likely than not that the Company will realize the benefit from the additional tax basis resulting from the 2009 acquisition of membership interests and shares of MBES. Accordingly, the Company reduced its related valuation allowance in 2013 to zero. The benefits from the reductions were recorded as tax benefits in accordance with accounting standards for income taxes.

As of December 31, 2013, for U.S. federal income tax reporting purposes, the Company has approximately \$6,500,000 of unused NOLs available for carry forward to future years. The benefit from the carry forward of such NOLs will begin expiring during the year ending December 31, 2027. Because United States tax laws limit the time during which NOL carry forwards may be applied against future taxable income, the Company may be unable to take full advantage of its NOL for federal income tax purposes should the Company generate taxable income. Further, the benefit from utilization of NOLs carry forwards could be subject to limitations due to material ownership changes that could occur in the Company as it continues to raise additional capital.

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NOTE 10 – EQUITY TRANSACTIONS

Preferred Stock

The Company's Articles of Incorporation authorize the issuance of 20,000,000 shares of preferred stock with a par value of \$0.001 per share. In 2006, the Board of Directors adopted a Statement of Designations Establishing Series A Convertible Preferred Stock. Initially, 5,000,000 of the 20,000,000 shares authorized have been designated Series A Convertible Preferred Stock, par value \$0.001 per share. The shares are entitled to a dividend of \$0.20 per share payable on October 1 of each year commencing October 1, 2006, when and if declared by the Board of Directors. If not paid, the dividends accumulate and no dividends, whether in cash, stock or other property, and no distributions may be made on any class of stock of the Company ranking junior to the Series A Convertible Preferred Stock until dividends are no longer in arrears. Furthermore, the Company may not redeem, purchase or otherwise acquire any stock ranking junior to the Series A Convertible Preferred until dividends are no longer in arrears. The Company is in arrears to the extent of \$2,941,688 (\$1.45 per share) and \$2,535,938 (\$1.25 per share) in dividends on the Series A Convertible Preferred Stock as of December 31, 2013 and 2012, respectively.

The Series A Convertible Preferred shares are convertible into 2 shares of common stock, par value \$0.001. The conversion rate is subject to anti-dilution provisions in certain circumstances set out in the Statement of Designations. Holders of the Series A Convertible Preferred shares are entitled to vote on all matters subject to a vote of holders of Common Stock. Each share of Series A Convertible Preferred is entitled to two votes.

Series A Convertible Preferred shares have a liquidation preference of \$2.00 plus dividends in arrears in the event of a dissolution, liquidation or winding up of the Company. There are no preemptive rights attached to the Series A Convertible Preferred shares. Any shares of Series A Convertible Preferred stock reacquired by the Company will be returned to the status of authorized but unissued, undesignated as to series and subject to later issuance.

Common Stock

The Company is authorized to issue up to 100,000,000 shares of common stock. Each share of common stock has a par value of \$0.001.

As of December 31, 2013 and 2012, the Board of Directors of the Company has reserved a total of 6,503,379 and 7,928,379 shares of common stock for the contingent issuances in connection with the following securities:

	December 31, 2013	December 31, 2012
Convertible preferred stock	4,057,500	4,057,500
Warrants issued to employees	-	800,000
Warrants issued to non-employees	2,445,879	3,070,879
Total shares reserved for contingent issuances	<u>6,503,379</u>	<u>7,928,379</u>

During the year ended December 31, 2013, the Company had the following common stock activities:

- 575,000 shares of common stock were issued to investors who exercised their warrants at an exercise price \$0.10.
- The Company agreed to pay a \$50,000 finder's fee related to shares issued in 2011.

During the year ended December 31, 2012, the Company had the following common stock activities:

- 588,235 shares of common stock were sold to a third party for \$100,000.
- 100,000 shares of common stock were issued to a third party for services. These shares were valued at their fair value of \$22,000.
- Warrants to purchase 645,236 shares were granted to a third party at an exercise price of \$0.16 per share. These warrants were valued at their fair value of \$52,895.
- An investor exercised his warrants to purchase 250,000 shares for \$21,888.

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NOTE 11 – SHARE-BASED PAYMENTS

Warrants Granted to Employees:

A summary of activities in employee warrants and the related information is as follows:

	Shares	Weighted Average Exercise Price	Remaining Contractual Term (years)	Intrinsic Value
Outstanding balance, December 31, 2011	1,950,000	\$ 0.46	0.84	\$ -
Granted	-	-		
Expired	(1,150,000)	0.46		
Forfeited	-	-		
Outstanding balance, December 31, 2012	800,000	0.26	0.42	-
Granted	-	-		
Expired	(800,000)	0.26		
Forfeited	-	-		
Outstanding balance, December 31, 2013	-	-	-	-

During the years ended December 31, 2013 and 2012, there were no warrants granted to employees.

Warrants Granted to Non-Employees:

A summary of activities in non-employee warrants and the related information is as follows:

	Shares	Weighted Average Exercise Price	Remaining Contractual Term (years)	Intrinsic Value
Outstanding balance, December 31, 2011	2,775,643	\$ 0.15	\$ 2.87	\$ 86,886
Granted	645,236	0.16		
Exercised	(250,000)	0.09		
Expired	(100,000)	0.15		
Forfeited	-	-		
Outstanding balance, December 31, 2012	3,070,879	0.15	2.76	-
Granted	-	-		
Exercised	(575,000)	0.10		
Expired	(50,000)	0.29		
Forfeited	-	-		
Outstanding balance, December 31, 2013 (Fully vested and exercisable)	2,445,879	\$ 0.16	2.22	\$ 72,153

There were no warrants issued during the year ended December 31, 2013.

During the year ended December 31, 2012, warrants to purchase 645,236 shares were granted to a third party at an exercise price of \$0.16 per share. These warrants have a term of five years and vested immediately. Fair value of \$52,895 was calculated using the Black-Scholes option-pricing model. Variables used in the Black-Scholes option-pricing model include: (1) discount rate of 0.61%, (2) warrant life of five years from grant date, (3) expected volatility of 110% and, (4) zero expected dividends. The warrant's value is recorded as deferred financing cost and is being amortized as part of the costs related to the term loan and line of credit. See Note 6 for details of the amortization.

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NOTE 12 – COMMITMENTS AND CONTINGENCIES

Operating Leases

MBES has entered into an operating agreement for a transfer station dock in Louisiana, which it subleases to another party. The primary lease began May 1, 1997, with an initial term of ten years and options to renew for five additional five-year periods and has been consistently renewed. The sublease began on May 1, 2013 with an initial term of five years and options to renew for two additional terms, with rent equal to the basic rent plus \$30,000 per month, escalating at 3.5% each year.

The Company has a corporate office lease in Houston, Texas which runs through December 2015, and a land lease in the Eagle Ford shale area that runs through June 2027. Total amounts paid to these non-cancellable real estate leases were \$114,784 and \$101,506 in the years ended December 31, 2013 and 2012, respectively.

Future minimum lease obligations for the non-cancellable leases for next five years are as follows:

Year	Amount
2014	\$ 102,090
2015	106,496
2016	36,000
2017	36,000
2018 and after	342,000
Total	\$ 622,586

Royalty Agreements

MBES has entered into an operations agreement with a company from which it purchased the land on which its disposal well in Chambers County, Texas is located. As per the agreement, the Company is required to pay a minimum royalty of \$8,000 per month (adjusted for increases in the Consumer Price Index (“CPI”) since 2000) or 7% of monthly gross revenue, whichever is greater, for so long as the property is used for oilfield waste disposal. Included in the accompanying consolidated statements of operations for the years ended December 31, 2013 and 2012 are \$570,566 and \$577,104 of royalty expense, respectively. Upon termination of the Operations Agreement, the prior landowner has an option to purchase the property for \$30,000 (adjusted for increases in the CPI since 1998).

Under the Matador Loan agreement that was paid off in 2011, the Company is obligated to pay a royalty of 20% of gross cash received on MBES gross revenue and on all gross proceeds from disposal revenue in Texas and neighboring states, excluding revenue related to EFES. The royalty payment continues in perpetuity after the payment of the Matador Loan. During the years ended December 31, 2013 and 2012, the Company incurred royalty expense of \$1,761,542 and \$1,698,896, respectively. The royalty agreement further prohibits the Company, its affiliate and its controlling persons from operating Class II waste-disposal facilities in Texas and neighboring states.

The Company also acquired the lease of 45 acres in the Eagle Ford shale area on which the disposal well and related facilities are located, including the right to drill additional wells on the property, for a lease fee of \$3,000 per month, plus a royalty of \$0.08 for every barrel of disposed fluid, and a 20% royalty of all skim oil sold. The lease expires on June 30, 2027. During the years ended December 31, 2013 and 2012, the Company incurred royalty expense of \$1,032,233 and \$440,562, respectively.

Enhanced Payments to Noncontrolling Interest Shareholders

In December 2009, the Company agreed to remit certain payments (“the Enhanced Payments”) to the remaining MBSI noncontrolling interest shareholders equal to 10.39% of the payments on the Matador Loan. In December 2012, the Company reached an agreement with those shareholders to pay \$568,766 to cover all outstanding Enhanced Payments, together with interest of \$175,005. During the year ended December 31, 2012, the Company paid \$341,260, leaving a liability of \$227,506 that was paid in March 2013.

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NOTE 13 – CONCENTRATIONS

The Company derives the majority of its revenues and net income from operating disposal wells in two locations in Texas. Revenues are derived primarily from three activities in the oil and gas industry: 1) cleaning wells and pipelines, which yields NORM; 2) drilling wastes, which primarily yield NOW and skim oil; and 3) pumping oil from existing wells, which primarily yields NOW and limited skim oil.

Any relaxation of regulatory rules concerning disposal of NORM or NOW could negatively impact the Company's ability to generate revenues.

As of December 31, 2013 and 2012, five customers accounted for 58% and 35% of the Company's outstanding accounts receivable, respectively.

For the years ended December 31, 2013 and 2012, the Company generated 43% and 28% of total revenues from its five largest customers, respectively.

NOTE 14 – EARNINGS PER COMMON SHARES

The following table illustrates the computation of basic and diluted EPS for the years ended December 31, 2013 and 2012.

	2013	2012
Basic earnings per share		
Numerator:		
Net income attributable to TexCom stockholders	\$ 3,878,714	\$ 3,772,850
Less: Preferred stock dividends	(405,750)	(405,750)
Income available to common stockholders	\$ 3,472,964	\$ 3,367,100
Denominator:		
Weighted-average shares outstanding	63,900,444	63,581,724
Basic earnings per share	\$ 0.05	\$ 0.05
Diluted earnings per share		
Numerator:		
Income available to common stockholders	\$ 3,472,964	\$ 3,367,100
Denominator:		
Weighted-average shares outstanding	63,900,444	63,581,724
Effect of dilutive securities:		
Warrants	-	563,655
Adjusted weighted-average shares	63,900,444	64,145,379
Diluted earnings per share	\$ 0.05	\$ 0.05

Potentially dilutive securities include stock options and warrants to purchase 2,445,879 shares of common stock and Series A Preferred Stock convertible to 4,057,500 common stock were excluded from the computation of dilutive earnings per share for year 2013 because their effect would have been antidilutive.

Potentially dilutive securities include stock options and warrants to purchase 850,000 shares of common stock and Series A Preferred Stock convertible to 4,057,500 common stock were excluded from the computation of dilutive earnings per share for year 2012 because their effect would have been antidilutive.

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NOTE 15 – RELATED PARTY TRANSACTIONS

During the year ended December 31, 2013, the Company invoiced \$206,000 to an entity controlled by Bob May, the Company's Chief Executive Officer, for disposal of waste. All amounts were billed at the Company's standard rates and were paid in full by December 31, 2013.

See Note 8 concerning amounts owing to the sellers of ALMAC's assets, who are now Company employees.

NOTE 16 – SUBSEQUENT EVENT

Subsequent to December 31, 2013, an investor partially exercised the warrants giving rise to the derivative. Of the 1,800,643 warrants available, 1,500,000 were exercised, resulting in the issuance of 492,713 common shares in a cashless exercise for stock valued at \$121,750.

