

NATURAL GAS SERVICES GROUP INC
Form 10-Q
November 06, 2007

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

FORM 10-Q

**(X) QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF
THE SECURITIES EXCHANGE ACT OF 1934
For the quarterly period ended September 30, 2007**

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)

Colorado
(State or other jurisdiction of
incorporation or organization)

75-2811855
(I.R.S. Employer
Identification No.)

2911 SCR 1260
Midland, Texas 79706
(Address of principal executive offices)

(432) 563-3974
(Issuer's telephone number, including area code)

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

Yes No

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

Large Accelerated Filer Accelerated Filer Non Accelerated Filer

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

Yes No

APPLICABLE ONLY TO CORPORATE ISSUERS

Indicate the number of shares outstanding of each of the issuer's classes of common equity, as of the latest practicable date.

| Class | Outstanding at October 31, 2007 |
|-------------------------------|--|
| Common Stock, \$.01 par value | 12,081,334 |

NATURAL GAS SERVICES GROUP, INC.

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| | December 31, 2006 | September 30, 2007 |
|---|----------------------|-----------------------|
| ASSETS | | |
| Current Assets: | | |
| Cash and cash equivalents | \$ 4,391 | \$ 2,022 |
| Short-term investments | 25,052 | 22,899 |
| Trade accounts receivable, net of doubtful accounts of \$110 each period | 8,463 | 7,747 |
| Inventory, net of allowance for obsolescence of \$347 each period | 16,943 | 21,122 |
| Prepaid expenses and other | 321 | 530 |
| Total current assets | 55,170 | 54,320 |
| Rental equipment, net of accumulated depreciation of \$11,320 and \$15,299, respectively | 59,866 | 70,782 |
| Property and equipment, net of accumulated depreciation of \$3,679 and \$4,557, respectively | 6,714 | 6,254 |
| Goodwill, net of accumulated amortization \$325 each period | 10,039 | 10,039 |
| Intangibles, net of accumulated amortization of \$819 and \$1,063, respectively | 3,650 | 3,406 |
| Other assets | 113 | 56 |
| Total assets | \$ 135,552 | \$ 144,857 |
| LIABILITIES AND STOCKHOLDERS' EQUITY | | |
| Current Liabilities: | | |
| Current portion of long-term debt | \$ 3,442 | \$ 3,378 |
| Current portion subordinated notes-related parties | 1,000 | 1,000 |
| Accounts payable | 2,837 | 3,807 |
| Accrued liabilities | 2,077 | 3,297 |
| Current portion of tax liability | 1,056 | 373 |
| Deferred income | 225 | 246 |
| Total current liabilities | 10,637 | 12,101 |
| Long-term debt, less current portion | 12,950 | 10,417 |
| Subordinated notes-related parties, less current portion | 1,000 | — |
| Deferred income tax payable | 9,764 | 11,970 |
| Total liabilities | 34,351 | 34,488 |
| Stockholders' Equity: | | |
| Common stock, 30,000 shares authorized, par value \$0.01; 12,046 and 12,072 shares issued and outstanding, respectively | 120 | 121 |
| Additional paid-in capital | 82,560 | 83,063 |
| Retained earnings | 18,521 | 27,185 |
| Total stockholders' equity | 101,201 | 110,369 |
| Total liabilities and stockholders' equity | \$ 135,552 | \$ 144,857 |

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See accompanying notes to these condensed consolidated financial statements.

Table of Contents**NATURAL GAS SERVICES GROUP, INC.****CONDENSED CONSOLIDATED INCOME STATEMENTS***(in thousands, except earnings per share)**(unaudited)*

| | Three months ended September 30, | | Nine months ended September 30, | |
|--|-------------------------------------|-----------|------------------------------------|-----------|
| | 2006 | 2007 | 2006 | 2007 |
| Revenue: | | | | |
| Sales, net | \$ 10,880 | \$ 10,574 | \$ 28,509 | \$ 30,239 |
| Service and maintenance income | 209 | 220 | 749 | 729 |
| Rental income | 6,041 | 7,857 | 16,908 | 22,019 |
| Total revenue | 17,130 | 18,651 | 46,166 | 52,987 |
| Operating costs and expenses: | | | | |
| Cost of sales, exclusive of depreciation stated separately below | 8,351 | 6,894 | 22,472 | 20,856 |
| Cost of service and maintenance, exclusive of depreciation stated separately below | 170 | 132 | 567 | 456 |
| Cost of rentals, exclusive of depreciation stated separately below | 2,240 | 3,161 | 6,513 | 8,885 |
| Selling, general and administrative expense | 1,182 | 1,311 | 3,824 | 3,773 |
| Depreciation and amortization | 1,497 | 1,921 | 4,135 | 5,448 |
| Total operating costs and expenses | 13,440 | 13,419 | 37,511 | 39,418 |
| Operating income | 3,690 | 5,232 | 8,655 | 13,569 |
| Other income (expense): | | | | |
| Interest expense | (385) | (281) | (1,308) | (879) |
| Other income | 447 | 346 | 1,015 | 1,062 |
| Total other income (expense) | 62 | 65 | (293) | 183 |
| Income before provision for income taxes | 3,752 | 5,297 | 8,362 | 13,752 |
| Provision for income taxes | 1,388 | 1,960 | 3,094 | 5,088 |
| Net income | 2,364 | 3,337 | 5,268 | 8,664 |
| Earnings per share: | | | | |
| Basic | \$ 0.20 | \$ 0.28 | \$ 0.47 | \$ 0.72 |
| Diluted | \$ 0.20 | \$ 0.28 | \$ 0.47 | \$ 0.72 |
| Weighted average shares outstanding: | | | | |
| Basic | 11,960 | 12,072 | 11,199 | 12,067 |
| Diluted | 12,046 | 12,091 | 11,264 | 12,086 |

See accompanying notes to these condensed consolidated financial statements.

Table of Contents**NATURAL GAS SERVICES GROUP, INC.****CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS***(in thousands of dollars)**(unaudited)*

| | Nine Months Ended September 30, | |
|--|------------------------------------|-----------------|
| | 2006 | 2007 |
| CASH FLOWS FROM OPERATING ACTIVITIES: | | |
| Net income | \$ 5,268 | \$ 8,664 |
| Adjustments to reconcile net income to net cash provided by operating activities: | | |
| Depreciation and amortization | 4,135 | 5,448 |
| Deferred taxes | 2,215 | 2,259 |
| Employee stock options expensed | 218 | 292 |
| Gain on sale of property and equipment | (17) | (1) |
| Changes in current assets and liabilities: | | |
| Trade and other receivables | (1,823) | 716 |
| Inventory and work in progress | (298) | (4,179) |
| Prepaid expenses and other | 106 | (209) |
| Accounts payable and accrued liabilities | 1,475 | 2,190 |
| Current tax liability | — | (683) |
| Deferred income | 33 | 21 |
| Other | (94) | 30 |
| NET CASH PROVIDED BY OPERATING ACTIVITIES | 11,218 | 14,548 |
| CASH FLOWS FROM INVESTING ACTIVITIES: | | |
| Purchase of property and equipment | (21,583) | (15,676) |
| Purchase of short-term investments | (37,905) | (2,347) |
| Redemption of short-term investments | 8,700 | 4,500 |
| Proceeds from sale of assets | 32 | 44 |
| NET CASH USED IN INVESTING ACTIVITIES | (50,756) | (13,479) |
| CASH FLOWS FROM FINANCING ACTIVITIES: | | |
| Proceeds from long-term debt | 68 | — |
| Proceeds from line of credit | 1,375 | — |
| Repayments of long-term debt | (8,695) | (3,597) |
| Repayments of line of credit | (1,675) | — |
| Proceeds from exercise of stock options and warrants | 226 | 159 |
| Proceeds from sale of stock, net of transaction costs | 47,163 | — |
| NET CASH PROVIDED BY (USED IN) FINANCING ACTIVITIES | 38,462 | (3,438) |
| NET CHANGE IN CASH | (1,076) | (2,369) |
| CASH AND CASH EQUIVALENTS AT BEGINNING OF PERIOD | | |
| | 3,271 | 4,391 |
| CASH AND CASH EQUIVALENTS AT END OF PERIOD | \$ 2,195 | \$ 2,022 |

**SUPPLEMENTAL DISCLOSURE OF CASH FLOW
INFORMATION:**

| | | | | |
|-------------------|----|-------|----|-------|
| Interest paid | \$ | 1,146 | \$ | 942 |
| Income taxes paid | \$ | 879 | \$ | 3,546 |

See accompanying notes to these condensed consolidated financial statements.

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NATURAL GAS SERVICES GROUP, INC.

NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(1) Basis of Presentation and Summary of Significant Accounting Policies

The accompanying unaudited condensed consolidated financial statements present the condensed consolidated results of our company taken from our books and records. In our opinion, such information includes all adjustments, consisting of only normal recurring adjustments, which are necessary to make our financial position at September 30, 2007 and September 30, 2006 and the results of our operations for the three and nine month periods ended September 30, 2007 and September 30, 2006 not misleading. As permitted by the rules and regulations of the Securities and Exchange Commission (SEC) the accompanying condensed consolidated financial statements do not include all disclosures normally required by accounting principles generally accepted in the United States of America. These condensed consolidated financial statements should be read in conjunction with the financial statements included in our Annual Report on Form 10-K/A for the year ended December 31, 2006 on file with the SEC. In our opinion, the condensed consolidated financial statements are a fair presentation of the financial position, results of operations and cash flows for the periods presented.

The results of operations for the three and nine month periods ended September 30, 2007 are not necessarily indicative of the results of operations to be expected for the full fiscal year ending December 31, 2007.

Unless otherwise noted, amounts reported in tables are in thousands, except per share data and stock option data.

On June 25, 2007, we entered into Articles of Merger with our wholly owned subsidiary, Screw Compression Systems, Inc. (SCS). On June 30, 2007, all of the issued and outstanding shares of common stock for SCS, all of which we held, were cancelled without consideration and SCS was merged into our company. The purpose of the merger was to consolidate and simplify our internal accounting and tax reporting functions. There was no impact to the consolidated financial statement for this merger.

Short-Term investments

Short-term investments consist primarily of government and corporate bonds with original maturities of ninety days to one year.

Revenue recognition

Revenue from the sales of custom and fabricated compressors, and flare systems is recognized upon shipment of the equipment to customers. 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 term of the respective rental agreements based upon the classification of the rental agreement. 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.

Recently Issued Accounting Pronouncements

In July 2006 the FASB issued FASB Interpretation ("FIN") No. 48, *Accounting for Uncertainty in Income Taxes – an interpretation of FASB Statement 109*. FIN 48 clarifies the accounting for uncertainty in income taxes recognized in an enterprise's financial statements in accordance with FASB Statement No. 109, *Accounting for Income Taxes*. FIN 48 prescribes a comprehensive model for recognizing, measuring, presenting and disclosing, in the financial

statements, tax positions taken or expected to be taken on a tax return. FIN 48 is effective for fiscal years beginning after December 15, 2006. We adopted FIN 48 on January 1, 2007, and its adoption did not have a material impact on our consolidated financial position and results of operations. See Note 5 for additional information regarding income taxes.

In September 2006, the FASB issued Statement of Financial Accounting Standards ("SFAS") No. 157, *Fair Value Measurements*, which defines fair value, establishes a framework for measuring fair value in GAAP, and expands disclosures about fair value measurements. This Statement applies under other accounting pronouncements that require or permit fair value measurements and is effective for fiscal years beginning after November 15, 2007. We are currently evaluating the impact of adopting this Statement.

In February 2007, the FASB issued Statement of Financial Accounting Standards ("SFAS") No. 159, *The Fair Value Option for Financial Assets and Financial Liabilities-Including an amendment of FASB Statement No. 115* ("SFAS 159"). SFAS 159 permits entities to measure eligible assets and liabilities at fair value. Unrealized gains and losses on items for which the fair value option has been elected are reported in earnings. SFAS 159 is effective for fiscal years beginning after November 15, 2007. We are currently evaluating the impact of adopting this Statement.

Table of Contents**NATURAL GAS SERVICES GROUP, INC.****NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS****(2) Stock-Based Compensation**

Effective January 1, 2006, we adopted the fair value recognition provisions of Statement of Financial Accounting Standard 123(R) "*Share-Based Payment*" ("SFAS 123(R)") using the modified prospective transition method. In addition, the Securities and Exchange Commission issued Staff Accounting Bulletin No. 107 "*Share-Based Payment*" ("SAB 107") in March, 2006, which provides supplemental SFAS 123(R) application guidance based on the views of the SEC. Under the modified prospective transition method, compensation cost recognized in the quarterly periods ended September 30, 2006 and 2007 included: (a) compensation cost for all share-based payments granted prior to, but not yet vested as of January 1, 2006, based on the grant date fair value estimated in accordance with the original provisions of SFAS No. 123, and (b) compensation cost for all share-based payments granted beginning January 1, 2006, based on the grant date fair value estimated in accordance with the provisions of SFAS 123(R).

A summary of stock option activity under our 1998 Stock Option plan as of September 30, 2007 and changes during the nine months ended September 30, 2007 is presented below.

| | Number of Stock Options | Weighted Average Exercise Price | Weighted Average Remaining Contractual Life (years) | Aggregate Intrinsic Value (in thousands) |
|---------------------------------|----------------------------------|--|---|--|
| Outstanding, December 31, 2006 | 174,170 | \$ 9.63 | 8.22 | \$ 744 |
| Granted | 7,500 | 15.60 | | |
| Exercised | (21,168) | 5.67 | | |
| Forfeited or expired | (4,334) | 12.15 | | |
| Outstanding, September 30, 2007 | 156,168 | \$ 10.39 | 7.79 | \$ 1,060 |
| Exercisable, September 30, 2007 | 102,168 | \$ 8.99 | 7.20 | \$ 836 |

We granted employee stock options on August 13, 2007. There were no options granted during the nine months ended September 30, 2006. The total intrinsic value or the difference between the exercise price and the market price on the date of exercise, of stock options exercised during the three and nine months ended September 30, 2007, were approximately \$6 thousand and \$176 thousand, respectively. We received cash from the exercise of stock options of approximately \$5 thousand and \$120 thousand during the three and nine months ended September 30, 2007, respectively. We realized an income tax net deduction of approximately \$1 thousand and \$52 thousand from stock options exercised during the three and nine months ended September 30, 2007, respectively.

Table of Contents**NATURAL GAS SERVICES GROUP, INC.**

The following table summarizes information about the stock options outstanding at September 30, 2007:

| Range of Exercise Prices | Number of Stock Options | Stock Options Outstanding | | Stock Options Exercisable | | |
|--------------------------|-------------------------|---|---------------------------------|---------------------------|---------------------------------|--|
| | | Weighted Average Remaining Contractual Life (years) | Weighted Average Exercise Price | Number of Stock Options | Weighted Average Exercise Price | |
| \$ 0.00 – 5.58 | 28,000 | 5.24 | \$ 4.17 | 28,000 | \$ 4.17 | |
| 5.59 – 9.44 | 66,668 | 7.63 | 8.95 | 51,668 | 8.87 | |
| 9.44 – 16.96 | 61,500 | 9.11 | 14.77 | 22,500 | 15.26 | |
| \$ 0.00 – 16.96 | 156,168 | 7.79 | \$ 10.39 | 102,168 | \$ 8.99 | |

A summary of the status of our unvested stock options as of September 30, 2007 and changes during the nine months ended September 30, 2007 is presented below.

| | Number of Stock Options | Weighted Average Grant Date Fair Value |
|--------------------------------|-------------------------|--|
| Unvested at December 31, 2006 | 85,838 | \$ 9.32 |
| Granted | 7,500 | 5.71 |
| Vested | (35,671) | 10.11 |
| Forfeited | (3,667) | 5.12 |
| Unvested at September 30, 2007 | 54,000 | \$ 8.57 |

As of September 30, 2007, there was approximately \$261 thousand of unrecognized compensation cost related to unvested stock options. Such cost is expected to be recognized over a weighted-average period of one year. Total compensation expense for stock options was \$73 thousand and \$99 thousand for the three months ended September 30, 2006 and 2007, respectively. Total compensation expense for stock options was \$146 thousand and \$292 thousand for the nine months ended September 30, 2006 and 2007, respectively. An income tax benefit was recognized of approximately \$27 thousand and \$37 thousand for the three months ended September 30, 2006 and 2007, respectively. An income tax benefit was recognized of approximately \$81 thousand and \$108 thousand for the nine months ended September 30, 2006 and 2007, respectively.

(3) Inventory

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Inventory, net of allowance for obsolescence of \$347 thousand at December 31, 2006 and September 30, 2007, consisted of the following amounts:

| | December 31, 2006 | September 30, 2007 |
|-----------------|-------------------------|--------------------------|
| Raw materials | \$ 12,154 | \$ 15,511 |
| Finished goods | 1,084 | 772 |
| Work in process | 3,705 | 4,839 |
| | \$ 16,943 | \$ 21,122 |

Table of Contents**NATURAL GAS SERVICES GROUP, INC.****NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS****(4) Earnings per Share**

The following table reconciles the numerators and denominators of the basic and diluted earnings per share computation.

| | Three months Ended September 30, | | Nine months Ended September 30, | |
|---|-------------------------------------|----------|------------------------------------|----------|
| | 2006 | 2007 | 2006 | 2007 |
| Numerator: | | | | |
| Net income | \$ 2,364 | \$ 3,337 | \$ 5,268 | \$ 8,664 |
| Denominator for basic net income per common share: | | | | |
| Weighted average common shares outstanding | 11,960 | 12,072 | 11,199 | 12,067 |
| Denominator for diluted net income per share: | | | | |
| Weighted average common shares outstanding | 11,960 | 12,072 | 11,199 | 12,067 |
| Dilutive effect of stock options and warrants | 86 | 19 | 65 | 19 |
| Diluted weighted average shares | 12,046 | 12,091 | 11,264 | 12,086 |
| Earnings per common share: | | | | |
| Basic | \$ 0.20 | \$ 0.28 | \$ 0.47 | \$ 0.72 |
| Diluted | \$ 0.20 | \$ 0.28 | \$ 0.47 | \$ 0.72 |

(5) Income Taxes

We adopted the provisions of FIN 48, Accounting for Uncertainty in Income Taxes, on January 1, 2007. We had no material unrecognized income tax assets or liabilities at the date of adoption or during the three and nine months ended September 30, 2007.

Our policy regarding income tax interest and penalties is to expense those items as general and administrative expense but to identify them for tax purposes. During the three and nine months ended September 30, 2007, there were no income tax interest and penalty items in the income statement, or as a liability on the balance sheet.

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 2003. We are not currently involved in any income tax examinations.

Table of Contents**NATURAL GAS SERVICES GROUP, INC.****NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS****(6) Segment Information**

FAS No. 131, *Disclosures About Segments of an Enterprise and Related Information*, establishes standards for public companies relating to the reporting of financial and descriptive information about their operating segments in financial statements. Operating segments are components of an enterprise about which separate financial information is available that is evaluated regularly by chief operating decision makers in how to allocate resources and in assessing performance.

We identify our segments based upon major revenue sources as follows:

For the three months ended September 30, 2007:

| | Service & | | | | |
|---------------------------------|--------------|-------------|----------|------------|------------|
| | Sales | Maintenance | Rental | Corporate | Total |
| Revenue | \$ 10,574 | \$ 220 | \$ 7,857 | \$ - | \$ 18,651 |
| Operating costs and expenses | 6,894 | 132 | 3,161 | 3,232 | 13,419 |
| Operating income | \$ 3,680 | \$ 88 | \$ 4,696 | \$ (3,232) | \$ 5,232 |
| *Segment Assets | \$ - | \$ - | \$ - | \$ 144,857 | \$ 144,857 |

For the three months ended September 30, 2006:

| | Service & | | | | |
|---------------------------------|--------------|-------------|----------|------------|------------|
| | Sales | Maintenance | Rental | Corporate | Total |
| Revenue | \$ 10,880 | \$ 209 | \$ 6,041 | \$ - | \$ 17,130 |
| Operating costs and expenses | 8,351 | 170 | 2,240 | 2,679 | 13,440 |
| Operating income | \$ 2,529 | \$ 39 | \$ 3,801 | \$ (2,679) | \$ 3,690 |
| *Segment Assets | \$ - | \$ - | \$ - | \$ 134,039 | \$ 134,039 |

For the nine months ended September 30, 2007:

| | Service & | | | | |
|---------------------------------|--------------|-------------|-----------|------------|------------|
| | Sales | Maintenance | Rental | Corporate | Total |
| Revenue | \$ 30,239 | \$ 729 | \$ 22,019 | \$ - | \$ 52,987 |
| Operating costs and expenses | 20,856 | 456 | 8,885 | 9,221 | 39,418 |
| Operating income | \$ 9,383 | \$ 273 | \$ 13,134 | \$ (9,221) | \$ 13,569 |
| *Segment Assets | \$ - | \$ - | \$ - | \$ 144,857 | \$ 144,857 |

For the nine months ended September 30, 2006:

| | Service & | | | | |
|---------|--------------|-------------|-----------|-----------|-----------|
| | Sales | Maintenance | Rental | Corporate | Total |
| Revenue | \$ 28,509 | \$ 749 | \$ 16,908 | \$ - | \$ 46,166 |
| | 22,472 | 567 | 6,513 | 7,959 | 37,511 |

Operating costs
and expenses

| | | | | | |
|------------------|----------|--------|-----------|------------|------------|
| Operating income | \$ 6,037 | \$ 182 | \$ 10,395 | \$ (7,959) | \$ 8,655 |
| *Segment Assets | \$ - | \$ - | \$ - | \$ 134,039 | \$ 134,039 |

* Management does not track assets by segment

(7) Legal Proceedings

From time to time, we are a party to various legal proceedings in the ordinary course of our business. We are not currently a party to any material pending legal proceedings. We have not been a party to any bankruptcy, receivership, reorganization, adjustment or similar proceeding.

(8) Subsequent Event

We are pursuing the purchase of an existing manufacturing facility in Midland, Texas. This facility would expand our current manufacturing capabilities. We will relocate our corporate office to a professional building located in the downtown area of Midland, Texas.

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NATURAL GAS SERVICES GROUP, INC.

Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations

The discussion and analysis of our financial condition and results of operations are based on, and should be read in conjunction with, our condensed consolidated financial statements and the related notes included elsewhere in this report and in our December 31, 2006 Form 10-K/A Report filed with the SEC. All amounts reported in tables are in thousands of dollars unless otherwise noted.

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 9 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 one month in advance and include maintenance of the rented compressors. As of September 30, 2007, we had 1,136 natural gas compressors totaling 132,147 horsepower rented to 92 third parties, compared to 909 natural gas compressors totaling 105,213 horsepower rented to 85 third parties at September 30, 2006.

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 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 components in the fabrication of compressor units for sale or rental. We also sell the finished component products to other compressor fabricators. We design, fabricate, sell, install and service flare stacks and related ignition and control devices for onshore and offshore incineration of natural 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, Tulsa, Oklahoma 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. As of September 30, 2007, we had written maintenance agreements with third parties relating to 46 compressors. Maintenance agreements typically have terms of nine months to one year and require payment of a monthly fee.

The oil and 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 the corresponding changes in commodity prices. As demand and prices increase, oil and gas producers increase their capital expenditures for drilling, development and production activities. The increased capital expenditures generally result in greater revenues

and profits for services 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 coalbed methane, gas shales and tight gas, which typically requires more compression than production from conventional natural gas reservoirs.

Demand for our products and service was strong throughout 2006 and the first nine months of 2007. We believe demand will remain strong throughout the remainder of 2007 and 2008 due to high oil and natural gas prices and increased demand for natural gas. Because of these market fundamentals for natural gas, we believe the long-term trend of activity in our markets is favorable. However, these factors could be more than offset by other developments affecting the worldwide supply and demand for natural gas.

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For fiscal year 2007, our forecasted capital expenditures are \$24 to \$27 million, primarily for additions to our compressor rental fleet. We believe that the proceeds from our public offering of common stock in March 2006, together with funds available to us under our bank credit facility and cash flows from operations will be sufficient to satisfy our capital and liquidity requirements through the remainder of 2007. We may further require additional capital to fund any unanticipated expenditures, including any acquisitions of other businesses. Additional capital may not be available to us when we need it or on acceptable terms.

Results of Operations***Three months ended September 30, 2006, compared to the three months ended September 30, 2007.***

The table below shows our revenues and percentage of total revenues for each of our segments for the three months ended September 30, 2006 and September 30, 2007.

| | Revenue | | | |
|----------------------------|--|------|-----------|------|
| | Three months Ended September 30, 2006 | | 2007 | |
| Sales | \$ 10,880 | 64% | \$ 10,574 | 57% |
| Service and Maintenance | 209 | 1% | 220 | 1% |
| Rental | 6,041 | 35% | 7,857 | 42% |
| Total | \$ 17,130 | 100% | \$ 18,651 | 100% |

Total revenue increased from \$17.1 million to \$18.7 million, or 8.9%, for the three months ended September 30, 2007, compared to the same period ended September 30, 2006. This was mainly the result of increased rental revenue of 30.1%, service and maintenance revenue of 5.3%, the total being offset by a decrease in sales revenue of 2.8%. This decrease was due to the sales of \$1.5 million of rental equipment to an existing customer during the three months ended September 30, 2006. Excluding the sales of rental equipment, the compressor unit sales actually increased \$1.2 million, or 12.8%, for the three months ended September 30, 2007 compared to the same period ended September 30, 2006.

Rental revenue increased from \$6.0 million to \$7.9 million, or 30.1%, for the three months ended September 30, 2007, compared to the same period ended September 30, 2006. This increase was the result of additional units added to our rental fleet and rented to third parties. We ended the period with 1,277 compressor packages in its rental fleet, up from 1,052 units at September 30, 2006. The rental fleet has a utilization of 89.0% as of September 30, 2007.

Sales revenue decreased from \$10.9 million to \$10.6 million, or 2.8%, for the three months ended September 30, 2007, compared to the same period ended September 30, 2006. This apparent decrease was due to the inflated sales of \$1.5 million of rental equipment to an existing customer during the three months ended September 30, 2006. Excluding the sales of rental equipment, the compressor unit sales actually increased \$1.2 million, or 12.8%, for the three months ended September 30, 2007 compared to the same period ended September 30, 2006. Sales from outside sources included: (1) compressor unit sales, (2) flare sales, (3) parts sales, (4) compressor rebuilds and (5) rental unit sales.

Service and maintenance revenue increased from \$209 thousand to \$220 thousand, or 5.3%, for the three months ended September 30, 2007, compared to the same period ended September 30, 2006. This increase was mainly the result of additional activity in our New Mexico area.

The overall operating margin percentage increased to 28.1% for the three months ended September 30, 2007, from 21.5% for the same period ended September 30, 2006. This was mainly the result of improvements in our sales margins were 23.2% for the third quarter of 2006 compared to 34.8% in third quarter of 2007. The improvement in margins resulted from refinements in our quote process and and the use of more frequent overhead calculations.

Selling, general and administrative expenses increased from \$1.2 million to \$1.3 million, or 10.9%, for the three months ended September 30, 2007, as compared to the same period ended September 30, 2006. This increase was mainly the result of increase in the officer salaries category because we filled some vacancies.

Depreciation and amortization expense increased from \$1.5 million to \$1.9 million, or 28.3%, for the three months ended September 30, 2007, compared to the same period ended September 30, 2006. This increase is the result of 225 new gas compressor rental units added to the rental fleet from September 30, 2006 to September 30, 2007, thus increasing the depreciable base.

Table of Contents**NATURAL GAS SERVICES GROUP, INC.**

Other income net of other expense decreased \$101 thousand for the three months ended September 30, 2007, compared to the same period ended September 30, 2006. This decrease is mainly the result of reduced interest income from our short-term investments. Short-term investments declined from the use of funds to build rental equipment, which has been and remains the intended purpose.

Interest expense decreased 27.0% for the three months ended September 30, 2007, compared to the same period ended September 30, 2006, mainly due to decreased loan balances financing rental equipment. The loan balances decreased from the amortization of the debt. There were no additional borrowings during the quarter ended September 30, 2007.

Provision for income tax increased from \$1.4 million to \$2.0 million, or 41.2%, for the three months ended September 30, 2007, compared to the same period ended September 30, 2006. This increase is the result of an increase in taxable income.

Nine months ended September 30, 2006, compared to the nine months ended September 30, 2007.

The table below shows our revenues and percentage of total revenues of each of our segments for the nine months ended September 30, 2006 and September 30, 2007.

| | Revenue | | | |
|----------------------------|---|------|-----------|------|
| | Nine months Ended September 30, 2006 | | 2007 | |
| Sales | \$ 28,509 | 62% | \$ 30,239 | 57% |
| Service and Maintenance | 749 | 1% | 729 | 1% |
| Rental | 16,908 | 37% | 22,019 | 42% |
| Total | \$ 46,166 | 100% | \$ 52,987 | 100% |

Total revenue increased from \$46.2 million to \$53.0 million, or 14.8%, for the nine months ended September 30, 2007, compared to the same period ended September 30, 2006. This was mainly the result of increased rental revenue of 30.2%, sales revenue of 6.1%, the total being offset by a decrease in service and maintenance revenue of 2.7%.

Rental revenue increased from \$16.9 million to \$22.0 million, or 30.2%, for the nine months ended September 30, 2007, compared to the same period ended September 30, 2006. This increase was the result of additional units added to our rental fleet and rented to third parties. We ended the period with 1,277 compressor packages in its rental fleet, up from 1,052 units at September 30, 2006. The rental fleet has a utilization of 89.0% as of September 30, 2007.

Sales revenue increased from \$28.5 million to \$30.2 million, or 6.1%, for the nine months ended September 30, 2007, compared to the same period ended September 30, 2006. Sales revenue for the nine months ended September 30, 2006 included \$4.2 million in sales of rental equipment to an existing rental customer. Excluding the rental equipment sales, actual unit sales increased \$5.9 million, or 23.8%, for the nine months ended September 30, 2007, compared to the same period ended September 30, 2006. Sales from outside sources included: (1) compressor unit sales, (2) flare sales, (3) parts sales, (4) compressor rebuilds and (5) rental unit sales.

Service and maintenance revenue decreased from \$749 thousand to \$729 thousand, or 2.7%, for the nine months ended September 30, 2007, compared to the same period ended September 30, 2006. This decrease was expected because the company does not intend to pursue third party service work.

The overall operating margin percentage increased to 25.6% for the nine months ended September 30, 2007, from 18.8% for the same period ended September 30, 2006. This was mainly the result of refinements in the quote process and more frequent overhead calculations. The overall operating margin increased from 21.2% for the nine months ended September 30, 2006 compared to 31.0% for same period ended September 30, 2007.

Selling, general and administrative expenses remained flat at \$3.8 million for the nine months ended September 30, 2007, compared to the same period ended September 30, 2006. This was expected because late in 2006 we had a reduction in our sales force from resignations, therefore our commissions expense did not increase with sales.

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NATURAL GAS SERVICES GROUP, INC.

Depreciation and amortization expense increased 31.8% from \$4.1 million to \$5.4 million for the nine months ended September 30, 2007, compared to the same period ended September 30, 2006. This increase was the result of 225 new gas compressor rental units being added to the rental fleet from September 30, 2006 to September 30, 2007, thus increasing the depreciable base.

Other income net of other expense increased by \$47 thousand for the nine months ended September 30, 2007, compared to the same period ended September 30, 2006. This increase is mainly the result of additional interest income from our short-term investment account.

Interest expense decreased 32.8% for the nine months ended September 30, 2007, compared to the same period ended September 30, 2006, mainly due to decreased loan balances financing rental equipment. Our loan balances decreased from the amortization of debt. There were no additional borrowings during the nine months ended September 30, 2007.

Provision for income tax increased from \$3.1 million to \$5.1 million, or 64.4%, for the nine months ended September 30, 2007, compared to the same period ended September 30, 2006. This increase is the result of an increase in taxable income.

Critical Accounting Policies and Practices

A discussion of our critical accounting policies is included in our Form 10-K/A for the year ended December 31, 2006. There have been no significant changes in the nine months ended September 30, 2007.

Recently Issued Accounting Pronouncements

In July 2006 the FASB issued FASB Interpretation ("FIN") No. 48, *Accounting for Uncertainty in Income Taxes – an interpretation of FASB Statement 109*. FIN 48 clarifies the accounting for uncertainty in income taxes recognized in an enterprise's financial statements in accordance with FASB Statement No. 109, *Accounting for Income Taxes*. FIN 48 prescribes a comprehensive model for recognizing, measuring, presenting and disclosing in the financial statements tax positions taken or expected to be taken on a tax return. FIN 48 is effective for fiscal years beginning after December 15, 2006. We adopted FIN 48 on January 1, 2007, and its adoption did not have a material impact on our consolidated financial position and results of operations.

In September 2006, the FASB issued Statement of Financial Accounting Standards ("SFAS") No. 157, *Fair Value Measurements*, which defines fair value, establishes a framework for measuring fair value in GAAP, and expands disclosures about fair value measurements. This Statement applies under other accounting pronouncements that require or permit fair value measurements and is effective for fiscal years beginning after November 15, 2007. We are currently evaluating the impact of adopting this Statement.

In February 2007, the FASB issued Statement of Financial Accounting Standards ("SFAS") No. 159, *The Fair Value Option for Financial Assets and Financial Liabilities-Including an amendment of FASB Statement No. 115* ("SFAS 159"). SFAS 159 permits entities to measure eligible assets and liabilities at fair value. Unrealized gains and losses on items for which the fair value option has been elected are reported in earnings. SFAS 159 is effective for fiscal years beginning after November 15, 2007. We are currently evaluating the impact of adopting this Statement.

Table of Contents**NATURAL GAS SERVICES GROUP, INC.****Liquidity and Capital Resources**

The following represents our working capital position as of December 31, 2006 and September 30, 2007.

| | December 31, 2006 | September 30, 2007 |
|--|-------------------|--------------------|
| Current Assets: | | |
| Cash & cash equivalents | \$ 4,391 | \$ 2,022 |
| Short-term investments | 25,052 | 22,899 |
| Trade accounts receivable | 8,463 | 7,747 |
| Inventory | 16,943 | 21,122 |
| Prepaid expenses and other | 321 | 530 |
| Total current assets | \$ 55,170 | \$ 54,320 |
| Current Liabilities: | | |
| Current portion of long-term debt | \$ 4,442 | \$ 4,378 |
| Accounts payable & accrued liabilities | 4,914 | 7,104 |
| Current portion of tax liability | 1,056 | 373 |
| Deferred income | 225 | 246 |
| Total current liabilities | \$ 10,637 | \$ 12,101 |
| Total working capital | \$ 44,533 | \$ 42,219 |

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 from financing were primarily used to service debt and fund the manufacture and fabrication of additional units for our rental fleet of natural gas compressors.

For the nine months ended September 30, 2007, we invested \$15.7 million in equipment for our rental fleet and service vehicles. We financed this activity with cash flow from operations and public offering proceeds. In addition, we have repaid \$3.6 million of our existing debt.

Cash flows

At September 30, 2007, we had cash, cash equivalents and short-term investments of \$24.9 million compared to \$29.4 million at December 31, 2006. We had working capital of \$42.2 million at September 30, 2007 compared to \$44.5 million at December 31, 2006. At September 30, 2007, our total debt was \$14.8 million of which \$4.4 million was classified as current compared to \$18.4 million and \$4.4 million, respectively at December 31, 2006. We had positive net cash flow from operating activities of \$14.5 million during the first nine months of 2007 compared to \$11.2 million for the first nine months of 2006. This was primarily from net income of \$8.7 million and an increase in accounts payable and accrued liabilities of \$2.2 million, offset by an increase in inventory of \$4.2 million and the add back of depreciation and amortization of \$5.4 million during the nine months ended September 30, 2007.

Accounts receivable decreased \$716 thousand to \$7.7 million at September 30, 2007 as compared to \$8.5 million at December 31, 2006. At the end of the third quarter of 2007, the average of aged accounts receivable decreased to 41 days outstanding compared to 49 days outstanding at the end of year December 31, 2006.

Inventory increased \$4.2 million to \$21.1 million as of September 30, 2007, as compared to \$16.9 million as of December 31, 2006. This increase is mainly the result of an increase in raw materials and work in progress associated with the production of third party compressor sales and rental units. Our service facilities inventories have increased as the result of an increase in our rental fleet.

Long-term debt decreased \$3.6 million to \$14.8 million at September 30, 2007, compared to \$18.4 million at December 31, 2006. The current portion of long-term debt remained at \$4.4 million for both September 30, 2007 and December 31, 2006.

Table of Contents**NATURAL GAS SERVICES GROUP, INC.***Subordinated Debt-Related Parties*

We have subordinated debt, which is included in the current portion of long-term debt. The \$3.0 million principal amount of this debt is in the form of promissory notes issued to the three stockholders of Screw Compression Systems, Inc., or "SCS", who are currently employed by us, as part of the consideration for the acquisition of SCS, a former subsidiary. The principal of each note is payable in three equal annual installments, which commenced on January 3, 2006. Accrued and unpaid interest on the unpaid principal balance of each note is payable on the same dates as, and in addition to, the installments of principal. To secure payment of these notes, our bank lender issued letters of credit for the benefit of the holders in the aggregate amount \$2.0 million. On February 3, 2007, the face amount of the letter of credit was reduced by one-half and is currently \$1.0 million. On January 3, 2007, we paid the second installment of the annual payments in the amount of \$1.0 million in principal. The current balance of these notes is \$1.0 million.

Contractual Obligations and Commitments

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

| | Obligation Due in Periods (in thousands of dollars) | | | | | | Total |
|---|--|----------|----------|----------|----------|------------|-----------|
| | 2007 ⁽¹⁾ | 2008 | 2009 | 2010 | 2011 | Thereafter | |
| Credit facility (secured) | \$ 845 | \$ 3,378 | \$ 3,378 | \$ 3,378 | \$ 2,816 | \$ - | \$ 13,795 |
| Interest on credit facility ⁽²⁾ | 259 | 884 | 591 | 338 | 106 | - | 2,178 |
| Subordinated debt | - | 1,000 | - | - | - | - | 1,000 |
| Facilities and office leases | 41 | 56 | 8 | 7 | 7 | 19 | 138 |
| Purchase obligations | - | - | - | - | - | - | - |
| Total | \$ 1,145 | \$ 5,318 | \$ 3,977 | \$ 3,723 | \$ 2,929 | \$ 19 | \$ 17,111 |

(1) For the three months remaining in 2007.

(2) Assumes no change in the interest rate.

Merger and Consolidation-Screw Compression Systems, Inc.

On June 25, 2007, we entered into Articles of Merger with our wholly owned subsidiary, SCS. On June 30, 2007, all of the issued and outstanding shares of common stock for SCS, all of which we held, were cancelled without consideration and SCS was merged into our company. The purpose of the merger was to consolidate and simplify our internal accounting and tax reporting functions.

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 September 30, 2007, the off-balance sheet arrangements and transactions that we have

entered into include an un-drawn letter of credit and operating lease agreements. We do not believe that these arrangements are reasonably likely to materially affect our liquidity or availability of, or requirements for, capital resources.

Special Note Regarding Forward-Looking Statements

Please refer to and read “Special Note Regarding Forward-Looking Statements” in our Annual Report on Form 10-K/A for the fiscal year ended December 31, 2006.

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NATURAL GAS SERVICES GROUP, INC.

Item 3. Quantitative and Qualitative Disclosures about Market Risk

Commodity Risk

Our commodity risk exposure is the pricing applicable to oil and natural gas 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 oil and natural gas 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, short-term investments, accounts receivable, accounts payable, bank borrowings, and notes. The carrying amounts of cash and cash equivalents, accounts receivable and accounts payable approximate fair value due to the highly liquid nature of these short-term instruments. The fair value of the bank borrowings approximate the carrying amounts as of September 30, 2007, and were determined based upon interest rates currently available to us for borrowings with similar terms.

Customer Credit Risk

We are exposed to the risk of financial non-performance by customers. Our ability to collect on sales to our customers is dependent on the liquidity of our customer base. To manage customer credit risk, we monitor credit ratings of customers and seek to minimize exposure to any one customer where other customers are readily available. 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.

Item 4. Controls and Procedures

Under the supervision and with the participation of certain members of Natural Gas Services Group, Inc's management, the chief executive officer and the vice-president of accounting evaluated the effectiveness of the design and operation of the disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e) of the Securities Exchange Act of 1934, as amended (the "Exchange Act")) for Natural Gas Services Group, Inc. as of the end of the period covered by this report. Based on this evaluation, the chief executive officer and vice-president of accounting concluded that, as of the end of the period covered by this report, Natural Gas Services Group, Inc's disclosure controls and procedures were effective to ensure that information required to be disclosed by Natural Gas Services Group, Inc. in the reports that it files under the Exchange Act is collected, processed and disclosed within the time periods specified in the SEC's rules and forms.

There were no changes in Natural Gas Services Group, Inc's internal controls during the period covered by this report that have materially affected or are reasonably likely to materially affect Natural Gas Services Group, Inc's internal controls over financial reporting. In addition, to the knowledge of the chief executive officer and vice-president of accounting there were no changes in other factors that could significantly affect these controls subsequent to the date of the most recent evaluation made by the chief executive officer and the vice-president of accounting.

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NATURAL GAS SERVICES GROUP, INC.

PART II – OTHER INFORMATION

Item 1. Legal Proceedings

From time to time, we are a party to various legal proceedings in the ordinary course of our business. We are not currently a party to any material pending legal proceedings. We have not been a party to any bankruptcy, receivership, reorganization, adjustment or similar proceeding.

Item 1A. Risk Factors

Please refer to and read “Risk Factors” in our Annual Report on Form 10-K/A for the fiscal year ended December 31, 2006, one of which has been updated as set forth below.

Our current debt level is high and may negatively impact our current and future financial stability.

As of September 30, 2007, we had an aggregate of approximately \$14.8 million of outstanding indebtedness, not including outstanding letters of credit in the aggregate face amount of \$1.0 million, and accounts payable and accrued expenses of approximately \$7.1 million. As a result of our significant indebtedness, 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 significant leverage could make us more vulnerable to economic downturns.

Interest rate risk

Our Loan Agreement provides for a fixed interest rate of 7.5% for our term loan facility and our revolving line of credit facility. Consequently, our exposure to interest rates relate primarily to interest earned on short-term investments and paying above market rates, if such rates are below the fixed rate, on our bank borrowings. As of September 30, 2007, we were not using any derivatives to manage interest rate risk.

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NATURAL GAS SERVICES GROUP, INC.

Item 6. Exhibits

The following exhibits are filed herewith or incorporated herein by reference, as indicated:

| <u>Exhibit No.</u> | <u>Description</u> |
|--------------------|---|
| 3.1 | Articles of Incorporation, as amended (Incorporated by reference to Exhibit 3.1 of the 10QSB 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 | Form of warrant certificate (Incorporated by reference to Exhibit 4.1 of the Registrant's Registration Statement on Form SB-2, No. 333-88314) |
| 4.2 | Form of warrant agent agreement (Incorporated by reference to Exhibit 4.2 of the Registrant's Registration Statement on Form SB-2, No. 333-88314) |
| 4.3 | Form of representative's option for the purchase of common stock (Incorporated by reference to Exhibit 4.4 of the Registrant's Registration Statement on Form SB-2, No. 333-88314) |
| 4.4 | Form of representative's option for the purchase of warrants (Incorporated by reference to Exhibit 4.5 of the Registrant's Registration Statement on Form SB-2, No. 333-88314) |
| 4.5 | Stockholders Agreement, dated January 3, 2005 among Paul D. Hensley, Tony Vohjesus, Jim Hazlett and Natural Gas Services Group, Inc. (Incorporated by reference to Exhibit 4.3 of the Registrant's Form 8-K Report, dated January 3, 2005, as filed with the Securities and Exchange Commission on January 7, 2005) |
| | Executive Compensation Plans and Arrangements (Exhibits 10.1, 10.14, 10.15, 10.16, 10.23, 10.24, 10.26 and 10.27). |
| 10.1 | 1998 Stock Option Plan, as amended (Incorporated by reference to Exhibit 10.1 of the Registrant's Form 8-K Report dated September 20, 2006 as filed with the SEC on September 26, 2006) |
| 10.2 | Form of Series A 10% Subordinated Notes due December 31, 2006 (Incorporated by reference to Exhibit 10.8 of the Registrant's Registration Statement on Form SB-2, No. 333-88314) |
| 10.3 | Form of Five-Year Warrants to Purchase Common Stock (Incorporated by reference to Exhibit 10.9 of the Registrant's Registration Statement on Form SB-2, No. 333-88314) |
| 10.4 | Warrants issued to Berry-Shino Securities, Inc. (Incorporated by reference to Exhibit 10.10 of the Registrant's Registration Statement on Form SB-2, No. 333-88314) |
| 10.5 | Warrants issued to Neidiger, Tucker, Bruner, Inc. (Incorporated by reference to Exhibit 10.11 of the Registrant's Registration Statement on Form SB-2, No. 333-88314) |
| 10.6 | Form of warrant issued in March 2001 for guaranteeing debt (Incorporated by reference to Exhibit 10.12 of the Registrant's Registration Statement on Form SB-2, No. 333-88314) |

10.7 Form of warrant issued in April 2002 for guaranteeing debt (Incorporated by reference to Exhibit 10.13 of the Registrant's Registration Statement on Form SB-2, No. 333-88314)

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NATURAL GAS SERVICES GROUP, INC.

| <u>Exhibit No.</u> | <u>Description</u> |
|--------------------|--|
| 10.8 | Lease Agreement, dated March 1, 2004, between the Registrant and the City of Midland, Texas (Incorporated by reference to Exhibit 10.19 of the Registrant's Form 10-QSB for the fiscal quarter ended September 30, 2004) |
| 10.9 | Second Amended and Restated Loan Agreement, dated November 3, 2003, between the Registrant and Western National Bank (Incorporated by reference to Exhibit 10.20 of the Registrant's Form 10-QSB for the fiscal quarter ended September 30, 2004) |
| 10.10 | Securities Purchase Agreement, dated July 20, 2004, between the Registrant and CBarney Investments, Ltd. (Incorporated by reference to Exhibit 4.1 of the Registrant's Current Report on Form 8-K dated July 20, 2004 and filed with the Securities and Exchange Commission on July 27, 2004) |
| 10.11 | Stock Purchase Agreement, dated October 18, 2004, by and among the Registrant, Screw Compression Systems, Inc., Paul D. Hensley, Jim Hazlett and Tony Vohjesus (Incorporated by reference to Exhibit 4.1 of the Registrant's Current Report on Form 8-K dated October 18, 2004 and filed with the Securities and Exchange Commission on October 21, 2004) |
| 10.12 | Third Amended and Restated Loan Agreement dated as of January 3, 2005, among Natural Gas Services Group, Inc., Screw Compression Systems, Inc. and Western National Bank (Incorporated by reference to Exhibit 10.1 of the Registrant's Current Report on Form 8-K, dated January 3, 2005, and filed with the Securities and Exchange Commission on January 7, 2005) |
| 10.13 | Employment Agreement between Paul D. Hensley and Natural Gas Services Group, Inc., (Incorporated by reference to Exhibit 10.1 of the Registrants Form 8-K Report, dated January 3, 2005, as filed with the Securities and Exchange Commission on January 7, 2005) |
| 10.14 | Employment Agreement between William R. Larkin and Natural Gas Services Group, Inc., (Incorporated by reference to Exhibit 10.25 of the Registrant's Form 10-KSB for the fiscal year ended December 31, 2004, and filed with the Securities and Exchange Commission on March 30, 2005) |
| 10.15 | Promissory Note, dated January 3, 2005, in the original principal amount of \$2.1 million made by Natural Gas Services Group, Inc. payable to Paul D. Hensley (Incorporated by reference to Exhibit 10.26 of the Registrant's Form 10-KSB for the fiscal year ended December 31, 2004, and filed with the Securities and Exchange Commission on March 30, 2005) |
| 10.16 | Fourth Amended and Restated Loan Agreement (Incorporated by reference to Exhibit 10.1 of the Registrant's Current Report on Form 8-K, dated March 14, 2005, and filed with the Securities and Exchange Commission on March 18, 2005) |
| 10.17 | Modification Agreement, dated as of January 3, 2005, by and between Natural Gas Services Group, Inc. and Western National Bank (Incorporated by reference to Exhibit 10.2 of the Registrant's Current Report on Form 8-K, dated January 3, 2005, and filed with the Securities and Exchange Commission on January 7, 2005) |
| 10.18 | Guaranty Agreement, dated as of January 3, 2005, made by Natural Gas Service Group, Inc., for the benefit of Western National Bank (Incorporated by reference to Exhibit 10.3 of the Registrant's Current Report on Form 8-K, dated January 3, 2005, and filed with the Securities and Exchange Commission on January 7, 2005) |

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- 10.19 Guaranty Agreement, dated as of January 3, 2005, made by Screw Compression Systems, Inc., for the benefit of Western National Bank (Incorporated by reference to Exhibit 10.4 of the Registrant's Current Report on Form 8-K, dated January 3, 2005, and filed with the Securities and Exchange Commission on January 7, 2005)
- 10.20 Fifth Amended and Restated Loan Agreement (Incorporated by reference to Exhibit 10.2 of the Registrant's Form 8-K dated January 3, 2006 and filed with the Securities and Exchange Commission January 6, 2006)
- 10.21 First Modification to Fourth Amended and Restated Loan Agreement (Incorporated by reference Exhibit 10.1 of the Registrant's Form 8-K dated May 1, 2005 and filed with Securities and Exchange Commission May 13, 2005)

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NATURAL GAS SERVICES GROUP, INC.

| <u>Exhibit No.</u> | <u>Description</u> |
|--------------------|--|
| 10.22 | Employment Agreement between Stephen C. Taylor and Natural Gas Services Group, Inc., (Incorporated by reference to Exhibit 10.1 of the Registrant's Form 8-K Report, dated August 24, 2005, and filed with the Securities and Exchange Commission on August 30, 2005) |
| 10.23 | Employment Agreement between James R. Hazlett and Natural Gas Services Group, Inc., (Incorporated by reference to Exhibit 10.1 of the Registrant's Form 8-K Report, dated September 14, 2005, and filed with the Securities and Exchange Commission on November 14, 2005) |
| 10.24 | Stockholders Agreement, dated January 3, 2005 among Paul D. Hensley, Tony Vohjesus, Jim Hazlett and Natural Gas Services Group, Inc. (Incorporated by reference to Exhibit 4.3 of the Registrant's Form 8-K Report, dated January 3, 2005, and filed with the Securities and Exchange Commission on January 7, 2005) |
| 10.25 | Promissory Note, dated January 3, 2005, in the original principal amount of \$300 thousand made by Natural Gas Services Group, Inc. payable to Jim Hazlett (Incorporated by reference to Exhibit 10.3 of the Registrant's Form 8-K Report, dated September 14, 2005, and filed with the Securities and Exchange Commission on November 14, 2005) |
| 10.26 | Retirement Agreement, dated December 14, 2005, between Wallace C. Sparkman and Natural Gas Services Group, Inc. (Incorporated by reference to Exhibit 10.1 of the Registrant's Form 8-K Report, dated December 14, 2005, and filed with the Securities and Exchange Commission on December 15, 2005) |
| 10.27 | Sixth Amended and Restated Loan Agreement, dated as of January 3, 2006 (Incorporated by reference to Exhibit 10.3 of the Registrant's Current Report on Form 8-K, dated January 3, 2006, and filed with the Securities and Exchange Commission on January 6, 2006) |
| 10.28 | Guaranty Agreement dated as of January 3, 2006, and made by Screw Compression Systems, Inc. for the benefit of Western National Bank (Incorporated by reference to Exhibit 10.4 of the Registrant's Current Report on Form 8-K, dated January 3, 2006, and filed with the Securities and Exchange Commission on January 6, 2006) |
| 10.29 | Seventh Amended and Restated Loan Agreement (Incorporated by reference to Exhibit 10.1 of the Registrant's Form 8-K dated October 26, 2006 and filed with the Securities and Exchange Commission on November 1, 2006) |
| 14.0 | Code of Ethics (Incorporated by reference to Exhibit 14.0 of the Registrant's Form 10-KSB for the fiscal year ended December 31, 2004, and filed with the Securities and Exchange Commission on March 30, 2005) |
| 21.0 | Subsidiaries (Incorporated by reference to Exhibit 21.0 of the Registrant's Form 10-KSB for the fiscal year ended December 31, 2004, and filed with the Securities and Exchange Commission on March 30, 2005) |
| *31.1 | <u>Certifications</u> |
| *31.2 | <u>Certifications</u> |
| *32.1 | <u>Certification required by Section 906 of the Sarbanes-Oxley Act of 2002</u> |

*32.2

Certification required by Section 906 of the Sarbanes-Oxley Act of 2002

* Filed herewith.

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NATURAL GAS SERVICES GROUP, INC.

SIGNATURES

Pursuant to the requirements 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.

/s/Stephen C. Taylor
Stephen C. Taylor
President and Chief Executive
Officer

/s/ Earl R. Wait
Earl R. Wait
Principal Accounting Officer and
Treasurer

November 6, 2007

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NATURAL GAS SERVICES GROUP, INC.

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 10QSB 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 | Form of warrant certificate (Incorporated by reference to Exhibit 4.1 of the Registrant's Registration Statement on Form SB-2, No. 333-88314) |
| 4.2 | Form of warrant agent agreement (Incorporated by reference to Exhibit 4.2 of the Registrant's Registration Statement on Form SB-2, No. 333-88314) |
| 4.3 | Form of representative's option for the purchase of common stock (Incorporated by reference to Exhibit 4.4 of the Registrant's Registration Statement on Form SB-2, No. 333-88314) |
| 4.4 | Form of representative's option for the purchase of warrants (Incorporated by reference to Exhibit 4.5 of the Registrant's Registration Statement on Form SB-2, No. 333-88314) |
| 4.5 | Stockholders Agreement, dated January 3, 2005 among Paul D. Hensley, Tony Vohjesus, Jim Hazlett and Natural Gas Services Group, Inc. (Incorporated by reference to Exhibit 4.3 of the Registrant's Form 8-K Report, dated January 3, 2005, as filed with the Securities and Exchange Commission on January 7, 2005) |
| | Executive Compensation Plans and Arrangements (Exhibits 10.1, 10.14, 10.15, 10.16, 10.23, 10.24, 10.26 and 10.27). |
| 10.1 | 1998 Stock Option Plan, as amended (Incorporated by reference to Exhibit 10.1 of the Registrant's Form 8-K Report dated September 20, 2006 as filed with the SEC on September 26, 2006) |
| 10.2 | Form of Series A 10% Subordinated Notes due December 31, 2006 (Incorporated by reference to Exhibit 10.8 of the Registrant's Registration Statement on Form SB-2, No. 333-88314) |
| 10.3 | Form of Five-Year Warrants to Purchase Common Stock (Incorporated by reference to Exhibit 10.9 of the Registrant's Registration Statement on Form SB-2, No. 333-88314) |
| 10.4 | Warrants issued to Berry-Shino Securities, Inc. (Incorporated by reference to Exhibit 10.10 of the Registrant's Registration Statement on Form SB-2, No. 333-88314) |
| 10.5 | Warrants issued to Neidiger, Tucker, Bruner, Inc. (Incorporated by reference to Exhibit 10.11 of the Registrant's Registration Statement on Form SB-2, No. 333-88314) |
| 10.6 | Form of warrant issued in March 2001 for guaranteeing debt (Incorporated by reference to Exhibit 10.12 of the Registrant's Registration Statement on Form SB-2, No. 333-88314) |
| 10.7 | |

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Form of warrant issued in April 2002 for guaranteeing debt (Incorporated by reference to Exhibit 10.13 of the Registrant's Registration Statement on Form SB-2, No. 333-88314)

10.8 Lease Agreement, dated March 1, 2004, between the Registrant and the City of Midland, Texas (Incorporated by reference to Exhibit 10.19 of the Registrant's Form 10-QSB for the fiscal quarter ended September 30, 2004)

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NATURAL GAS SERVICES GROUP, INC.

| <u>Exhibit No.</u> | <u>Description</u> |
|--------------------|--|
| 10.9 | Second Amended and Restated Loan Agreement, dated November 3, 2003, between the Registrant and Western National Bank (Incorporated by reference to Exhibit 10.20 of the Registrant's Form 10-QSB for the fiscal quarter ended September 30, 2004) |
| 10.10 | Securities Purchase Agreement, dated July 20, 2004, between the Registrant and CBarney Investments, Ltd. (Incorporated by reference to Exhibit 4.1 of the Registrant's Current Report on Form 8-K dated July 20, 2004 and filed with the Securities and Exchange Commission on July 27, 2004) |
| 10.11 | Stock Purchase Agreement, dated October 18, 2004, by and among the Registrant, Screw Compression Systems, Inc., Paul D. Hensley, Jim Hazlett and Tony Vohjesus (Incorporated by reference to Exhibit 4.1 of the Registrant's Current Report on Form 8-K dated October 18, 2004 and filed with the Securities and Exchange Commission on October 21, 2004) |
| 10.12 | Third Amended and Restated Loan Agreement dated as of January 3, 2005, among Natural Gas Services Group, Inc., Screw Compression Systems, Inc. and Western National Bank (Incorporated by reference to Exhibit 10.1 of the Registrant's Current Report on Form 8-K, dated January 3, 2005, and filed with the Securities and Exchange Commission on January 7, 2005) |
| 10.13 | Employment Agreement between Paul D. Hensley and Natural Gas Services Group, Inc. (Incorporated by reference to Exhibit 10.1 of the Registrants Form 8-K Report, dated January 3, 2005, as filed with the Securities and Exchange Commission on January 7, 2005) |
| 10.14 | Employment Agreement between William R. Larkin and Natural Gas Services Group, Inc. (Incorporated by reference to Exhibit 10.25 of the Registrant's Form 10-KSB for the fiscal year ended December 31, 2004, and filed with the Securities and Exchange Commission on March 30, 2005) |
| 10.15 | Promissory Note, dated January 3, 2005, in the original principal amount of \$2.1 million made by Natural Gas Services Group, Inc. payable to Paul D. Hensley (Incorporated by reference to Exhibit 10.26 of the Registrant's Form 10-KSB for the fiscal year ended December 31, 2004, and filed with the Securities and Exchange Commission on March 30, 2005) |
| 10.16 | Fourth Amended and Restated Loan Agreement (Incorporated by reference to Exhibit 10.1 of the Registrant's Current Report on Form 8-K, dated March 14, 2005, and filed with the Securities and Exchange Commission on March 18, 2005) |
| 10.17 | Modification Agreement, dated as of January 3, 2005, by and between Natural Gas Services Group, Inc. and Western National Bank (Incorporated by reference to Exhibit 10.2 of the Registrant's Current Report on Form 8-K, dated January 3, 2005, and filed with the Securities and Exchange Commission on January 7, 2005) |
| 10.18 | Guaranty Agreement, dated as of January 3, 2005, made by Natural Gas Service Group, Inc., for the benefit of Western National Bank (Incorporated by reference to Exhibit 10.3 of the Registrant's Current Report on Form 8-K, dated January 3, 2005, and filed with the Securities and Exchange Commission on January 7, 2005) |
| 10.19 | Guaranty Agreement, dated as of January 3, 2005, made by Screw Compression Systems, Inc., for the benefit of Western National Bank (Incorporated by reference to Exhibit 10.4 of the Registrant's Current Report on Form 8-K, dated January 3, 2005, and filed with the Securities and Exchange Commission on January 7, 2005) |

- 10.20 Fifth Amended and Restated Loan Agreement (Incorporated by reference to Exhibit 10.2 of the Registrant's Form 8-K dated January 3, 2006 and filed with the Securities and Exchange Commission January 6, 2006)
- 10.21 First Modification to Fourth Amended and Restated Loan Agreement (Incorporated by reference Exhibit 10.1 of the Registrant's Form 8-K dated May 1, 2005 and filed with Securities and Exchange Commission May 13, 2005)
- 10.22 Employment Agreement between Stephen C. Taylor and Natural Gas Services Group, Inc. (Incorporated by reference to Exhibit 10.1 of the Registrant's Form 8-K Report, dated August 24, 2005, and filed with the Securities and Exchange Commission on August 30, 2005)

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NATURAL GAS SERVICES GROUP, INC.

| <u>Exhibit No.</u> | <u>Description</u> |
|--------------------|--|
| 10.23 | Employment Agreement between James R. Hazlett and Natural Gas Services Group, Inc. (Incorporated by reference to Exhibit 10.1 of the Registrant's Form 8-K Report, dated September 14, 2005, and filed with the Securities and Exchange Commission on November 14, 2005) |
| 10.24 | Stockholders Agreement, dated January 3, 2005 among Paul D. Hensley, Tony Vohjesus, Jim Hazlett and Natural Gas Services Group, Inc. (Incorporated by reference to Exhibit 4.3 of the Registrant's Form 8-K Report, dated January 3, 2005, and filed with the Securities and Exchange Commission on January 7, 2005) |
| 10.25 | Promissory Note, dated January 3, 2005, in the original principal amount of \$300 thousand made by Natural Gas Services Group, Inc. payable to Jim Hazlett (Incorporated by reference to Exhibit 10.3 of the Registrant's Form 8-K Report, dated September 14, 2005, and filed with the Securities and Exchange Commission on November 14, 2005) |
| 10.26 | Retirement Agreement, dated December 14, 2005, between Wallace C. Sparkman and Natural Gas Services Group, Inc. (Incorporated by reference to Exhibit 10.1 of the Registrant's Form 8-K Report, dated December 14, 2005, and filed with the Securities and Exchange Commission on December 15, 2005) |
| 10.27 | Sixth Amended and Restated Loan Agreement, dated as of January 3, 2006 (Incorporated by reference to Exhibit 10.3 of the Registrant's Current Report on Form 8-K, dated January 3, 2006, and filed with the Securities and Exchange Commission on January 6, 2006) |
| 10.28 | Guaranty Agreement dated as of January 3, 2006, and made by Screw Compression Systems, Inc. for the benefit of Western National Bank (Incorporated by reference to Exhibit 10.4 of the Registrant's Current Report on Form 8-K, dated January 3, 2006, and filed with the Securities and Exchange Commission on January 6, 2006) |
| 10.29 | Seventh Amended and Restated Loan Agreement (Incorporated by reference to Exhibit 10.1 of the Registrant's Form 8-K dated October 26, 2006 and filed with the Securities and Exchange Commission on November 1, 2006) |
| 14.0 | Code of Ethics (Incorporated by reference to Exhibit 14.0 of the Registrant's Form 10-KSB for the fiscal year ended December 31, 2004, and filed with the Securities and Exchange Commission on March 30, 2005) |
| 21.0 | Subsidiaries (Incorporated by reference to Exhibit 21.0 of the Registrant's Form 10-KSB for the fiscal year ended December 31, 2004, and filed with the Securities and Exchange Commission on March 30, 2005) |
| *31.1 | <u>Certifications</u> |
| *31.2 | <u>Certifications</u> |
| *32.1 | <u>Certification required by Section 906 of the Sarbanes-Oxley Act of 2002</u> |
| *32.2 | <u>Certification required by Section 906 of the Sarbanes-Oxley Act of 2002</u> |

* Filed herewith.

