CIMAREX ENERGY CO
Form 10-Q
November 03, 2016
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UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

(Mark One)

Quarterly Report Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934

Transition Report Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934

For the Quarterly Period ended September 30, 2016

Commission File No. 001-31446

CIMAREX ENERGY CO.

1700 Lincoln Street, Suite 3700

Denver, Colorado 80203

(303) 295-3995

Incorporated in the State of Delaware	Employer Identification No. 45-0466694

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes No

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes No

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

Large accelerated filer	Accelerated filer	Non-accelerated filer (Do not check if a smaller reporting company)	Smaller reporting company

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

The number of shares of Cimarex Energy Co. common stock outstanding as of September 30, 2016 was 94,964,174.

CIMAREX ENERGY CO.

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GLOSSARY

Bbl/d—Barrels (of oil or natural gas liquids) per day

Bbls—Barrels (of oil or natural gas liquids)

Bcf—Billion cubic feet

Bcfe—Billion cubic feet equivalent

Btu—British thermal unit

MBbls—Thousand barrels

Mcf—Thousand cubic feet (of natural gas)

Mcfe—Thousand cubic feet equivalent

MMBbl/MMBbls—Million barrels

MMBtu—Million British thermal units

MMcf—Million cubic feet

MMcf/d—Million cubic feet per day

MMcfe—Million cubic feet equivalent

MMcfe/d—Million cubic feet equivalent per day

Net Acres—Gross acreage multiplied by working interest percentage

Net Production—Gross production multiplied by net revenue interest

NGL or NGLs—Natural gas liquids

Tcf—Trillion cubic feet

Tcfe—Trillion cubic feet equivalent

Energy equivalent is determined using the ratio of one barrel of crude oil, condensate or NGL to six Mcf of natural gas

CAUTIONARY INFORMATION ABOUT FORWARD-LOOKING STATEMENTS

Throughout this Form 10-Q, we make statements that may be deemed “forward-looking” statements within the meaning of Section 27A of the Securities Act of 1933, as amended, and Section 21E of the Securities and Exchange Act of 1934, as amended. These forward-looking statements include, among others, statements concerning our outlook with regard to timing and amount of future production of oil and gas, price realizations, amounts, nature and timing of capital expenditures for exploration and development, plans for funding operations and capital expenditures, drilling of wells, operating costs and other expenses, marketing of oil, gas, and NGLs and other statements of expectations, beliefs, future plans and strategies, anticipated events or trends, and similar expressions concerning matters that are not historical facts. The forward-looking statements in this report are subject to risks and uncertainties that could cause actual results to differ materially from those expressed in or implied by the statements.

These risks and uncertainties include, but are not limited to, fluctuations in the price we receive for our oil and gas production, full cost ceiling impairments to the carrying values of our oil and gas properties, reductions in the quantity of oil and gas sold due to decreased industry-wide demand and/or curtailments in production from specific properties or areas due to mechanical, transportation, marketing, weather or other problems, operating and capital expenditures that are either significantly higher or lower than anticipated because the actual cost of identified projects varied from original estimates and/or from the number of exploration and development opportunities being greater or fewer than currently anticipated, and increased financing costs due to a significant increase in interest rates. In addition, exploration and development opportunities that we pursue may not result in economic, productive oil and gas properties. There are also numerous uncertainties inherent in estimating quantities of proved reserves, projecting future rates of production and the timing of development expenditures. These and other risks and uncertainties affecting us are discussed in greater detail in this report and in our other filings with the Securities and Exchange Commission.

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PART I

ITEM 1 - Financial Statements

CIMAREX ENERGY CO.

Condensed Consolidated Balance Sheets

(Unaudited)

	September 30, 2016	December 31, 2015
	(in thousands, except share data)	
Assets		
Current assets:		
Cash and cash equivalents	$ 698,696	$ 779,382
Receivables, net	226,983	225,398
Oil and gas well equipment and supplies	34,909	54,579
Derivative instruments	1,147	10,745
Prepaid expenses	3,453	7,036
Other current assets	1,315	790
Total current assets	966,503	1,077,930
Oil and gas properties at cost, using the full cost method of accounting:		
Proved properties	16,013,316	15,546,948
Unproved properties and properties under development, not being amortized	447,071	440,166
	16,460,387	15,987,114
Less — accumulated depreciation, depletion, amortization and impairment	(13,756,311)	(12,710,968)
Net oil and gas properties	2,704,076	3,276,146
Fixed assets, net	214,448	230,009
Goodwill	620,232	620,232
Derivative instruments	3	501
Other assets, net	33,485	38,468
	$ 4,538,747	$ 5,243,286
Liabilities and Stockholders' Equity		
Current liabilities:		
Accounts payable	$ 53,428	$ 66,815
Accrued liabilities	258,551	247,508
Derivative instruments	21,573	—
Revenue payable	107,766	95,744
Total current liabilities	441,318	410,067
Long-term debt:		
Principal	1,500,000	1,500,000
Less—unamortized debt issuance costs	(12,629)	(14,380)
Long-term debt, net	1,487,371	1,485,620
Deferred income taxes	87,523	352,705
Other liabilities	189,253	197,216

Total liabilities	2,205,465	2,445,608
Commitments and contingencies		
Stockholders' equity:		
Preferred stock, $0.01 par value, 15,000,000 shares authorized, no shares issued	—	—
Common stock, $0.01 par value, 200,000,000 shares authorized, 94,964,174 and 94,820,570 shares issued, respectively	950	948
Paid-in capital	2,774,804	2,762,976
Retained earnings (Accumulated deficit)	(443,480)	33,313
Accumulated other comprehensive income	1,008	441
Total stockholders' equity	2,333,282	2,797,678
	$ 4,538,747	$ 5,243,286

See accompanying notes to consolidated financial statements.

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CIMAREX ENERGY CO.

Consolidated Statements of Operations and Comprehensive Income (Loss)

(Unaudited)

	For the Three Months Ended September 30,		For the Nine Months Ended September 30,	
	2016	2015	2016	2015
	(in thousands, except per share data)			
Revenues:				
Oil sales	$ 166,079	$ 192,501	$ 445,657	$ 647,850
Gas sales	109,278	114,649	268,501	331,985
NGL sales	50,464	40,159	135,755	135,236
Gas gathering and other	9,824	8,754	25,276	26,165
Gas marketing, net	72	(8)	1	104
	335,717	356,055	875,190	1,141,340
Costs and expenses:				
Impairment of oil and gas properties	89,816	1,180,649	719,142	2,751,535
Depreciation, depletion and amortization	109,344	185,654	361,320	619,883
Asset retirement obligation	2,033	2,615	6,081	6,393
Production	52,976	69,334	180,891	222,145
Transportation, processing, and other operating	48,706	46,290	139,585	129,645
Gas gathering and other	7,905	8,429	23,477	28,599
Taxes other than income	15,974	19,717	43,879	67,678
General and administrative	20,118	20,413	55,439	50,405
Stock compensation	5,764	4,737	18,782	14,880
(Gain) loss on derivative instruments, net	(9,758)	(1,968)	23,050	(1,968)
Other operating, net	179	60	293	844
	343,057	1,535,930	1,571,939	3,890,039
Operating income (loss)	(7,340)	(1,179,875)	(696,749)	(2,748,699)
Other (income) and expense:				
Interest expense	20,931	21,416	62,560	63,969
Capitalized interest	(5,421)	(7,100)	(15,958)	(25,087)
Other, net	(3,828)	(2,375)	(7,489)	(9,814)
Income (loss) before income tax	(19,022)	(1,191,816)	(735,862)	(2,777,767)
Income tax expense (benefit)	(6,204)	(428,532)	(266,623)	(999,327)
Net income (loss)	$ (12,818)	$ (763,284)	$ (469,239)	$ (1,778,440)
Earnings (loss) per share to common stockholders:				
Basic	$ (0.14)	$ (8.21)	$ (5.04)	$ (19.14)
Diluted	$ (0.14)	$ (8.21)	$ (5.04)	$ (19.14)
Dividends per share	$ 0.08	$ 0.16	$ 0.24	$ 0.48
Comprehensive income (loss):				

Net income (loss)	$ (12,818)	$ (763,284)	$ (469,239)	$ (1,778,440)
Other comprehensive income (loss):				
Change in fair value of investments, net of tax	287	(609)	567	(800)
Total comprehensive income (loss)	$ (12,531)	$ (763,893)	$ (468,672)	$ (1,779,240)

See accompanying notes to consolidated financial statements.

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CIMAREX ENERGY CO.

Condensed Consolidated Statements of Cash Flows

(Unaudited)

	For the Nine Months Ended September 30, 2016	2015
	(in thousands)	
Cash flows from operating activities:		
Net income (loss)	$ (469,239)	$ (1,778,440)
Adjustments to reconcile net income (loss) to net cash provided by operating activities:		
Impairment of oil and gas properties	719,142	2,751,535
Depreciation, depletion and amortization	361,320	619,883
Asset retirement obligation	6,081	6,393
Deferred income taxes	(265,508)	(1,014,264)
Stock compensation	18,782	14,880
(Gain) loss on derivative instruments	23,050	(1,968)
Settlements on derivative instruments	9,718	—
Changes in non-current assets and liabilities	4,121	16,343
Other, net	2,931	3,494
Changes in operating assets and liabilities:		
Receivables, net	(1,723)	151,783
Other current assets	23,034	29,634
Accounts payable and other current liabilities	(2,378)	(222,727)
Net cash provided by operating activities	429,331	576,546
Cash flows from investing activities:		
Oil and gas expenditures	(485,114)	(771,029)
Sales of oil and gas assets	19,013	38,343
Sales of other assets	5,718	1,057
Other capital expenditures	(24,013)	(58,085)
Net cash used by investing activities	(484,396)	(789,714)
Cash flows from financing activities:		
Proceeds from sale of common stock	—	752,100
Financing and underwriting fees	(1)	(22,663)
Dividends paid	(30,243)	(43,211)
Proceeds from exercise of stock options and other	4,623	20,392
Net cash provided by (used in) financing activities	(25,621)	706,618
Net change in cash and cash equivalents	(80,686)	493,450
Cash and cash equivalents at beginning of period	779,382	405,862
Cash and cash equivalents at end of period	$ 698,696	$ 899,312

See accompanying notes to consolidated financial statements.

CIMAREX ENERGY CO.

Notes to Consolidated Financial Statements

September 30, 2016

(Unaudited)

1. Basis of Presentation

The accompanying unaudited financial statements have been prepared by Cimarex Energy Co. ("Cimarex," "we" or "us") pursuant to rules and regulations of the Securities and Exchange Commission (SEC). Accordingly, certain disclosures required by accounting principles generally accepted in the United States and normally included in Annual Reports on Form 10-K have been omitted. Although management believes that our disclosures in these interim financial statements are adequate, they should be read in conjunction with the financial statements, summary of significant accounting policies and footnotes included in our Annual Report on Form 10-K for the year ended December 31, 2015.

In the opinion of management, the accompanying financial statements reflect all adjustments necessary to present fairly our financial position, results of operations, and cash flows for the periods and as of the dates shown. We have evaluated subsequent events through the date of this filing.

Use of Estimates

Areas of significance requiring the use of management's judgments include the estimation of proved oil and gas reserves, the use of proved reserves in calculating depletion, depreciation and amortization (DD&A), estimates of future net revenues in computing ceiling test limitations and estimates of future abandonment obligations used in recording asset retirement obligations and the assessment of goodwill. Estimates and judgments also are required in determining allowance for bad debt, impairments of undeveloped properties and other assets, purchase price allocation, valuation of deferred tax assets, fair value measurements and contingencies.

Oil and Gas Well Equipment and Supplies

Our oil and gas well equipment and supplies are valued at the lower of cost or net realizable value, where net realizable value is a defined estimated selling price. An analysis of our oil and gas well equipment and supplies was performed and no impairment was required. However, the continued industry-wide decline in drilling operations has put downward pressure on the price of oil and gas well equipment and supplies. Declines in future periods could cause us to recognize impairments on these assets. An impairment would not affect cash flow from operating activities, but would adversely affect our net income (loss) and stockholders' equity.

Oil and Gas Properties

We use the full cost method of accounting for our oil and gas operations. Accounting rules require us to perform a quarterly ceiling test calculation to test our oil and gas properties for possible impairment. If the net capitalized cost of our oil and gas properties subject to amortization (the carrying value) exceeds the ceiling limitation, the excess is charged to expense. The ceiling limitation is equal to the sum of the present value discounted at 10% of estimated future net cash flows from proved reserves, the cost of properties not being amortized, the lower of cost or estimated fair value of unproven properties included in the costs being amortized and all related tax effects. Estimated future net cash flows are determined by commodity prices and proved reserve quantities.

At September 30, 2016, the carrying value of our oil and gas properties subject to the test exceeded the calculated value of the ceiling limitation, and we recognized an impairment of $89.8 million ($57.1 million, net of tax). Year-to-date 2016 impairments totaled $719.1 million ($456.9 million, net of tax). These impairments resulted primarily from the continued impact of decreases in the 12-month average trailing prices for oil, natural gas and NGLs utilized in determining the future net cash flows from proved reserves. If pricing conditions stay at current levels or decline, or if there is a negative impact on one or more of the other components of the calculation, we may incur full cost ceiling impairments in future quarters. The ceiling calculation is not intended to be indicative of the fair market value of our proved reserves or future results. Impairment charges do not affect cash flow from operating activities, but do adversely affect our net income (loss) and various components of our balance sheet. Any recorded impairment of oil and gas properties is not reversible at a later date.

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Notes to Consolidated Financial Statements

September 30, 2016

(Unaudited)

Accounts Receivable, Accounts Payable and Accrued Liabilities

The components of our accounts receivable, accounts payable and accrued liabilities are shown below:

(in thousands)	September 30, 2016	December 31, 2015
Receivables, net of allowance		
Trade	$ 46,749	$ 81,888
Oil and gas sales	170,025	136,537
Gas gathering, processing, and marketing	10,197	6,935
Other	12	38
Receivables, net	$ 226,983	$ 225,398
Accounts payable		
Trade	$ 33,471	$ 53,384
Gas gathering, processing, and marketing	19,957	13,431
Accounts payable	$ 53,428	$ 66,815
Accrued liabilities		
Exploration and development	$ 56,032	$ 56,721
Taxes other than income	17,924	17,545
Other	184,595	173,242
Accrued liabilities	$ 258,551	$ 247,508

Recently Issued Accounting Standards

In May 2014, the Financial Accounting Standards Board (FASB) issued Accounting Standards Update (ASU) 2014-09, Revenue from Contracts with Customers (Topic 606). In July 2015, the FASB deferred the effective date by one year to annual reporting periods beginning after December 15, 2017, including interim periods within that reporting period. Early adoption is permitted, but not before the original effective date of reporting periods beginning after December 15, 2016. We do not intend to early adopt this standard. At this time we do not expect that the adoption of this standard will have a material effect on our consolidated financial statements and related disclosures.

In February 2016, the FASB issued ASU 2016-02, which requires lease assets and lease liabilities for most leases to be recognized on the balance sheet and disclosing key information about leasing arrangements. The standard is effective for reporting periods beginning after December 15, 2018, with early adoption permitted. We are currently evaluating the impact of this new guidance on our consolidated financial statements and related disclosures. We anticipate that we will not early adopt this standard.

In March 2016, the FASB issued ASU 2016-09, which will change how companies account for certain aspects of the accounting for share-based payment transactions, including the income tax consequences, classification of awards as either equity or liabilities and classification on the statement of cash flows. The standard is effective for reporting periods beginning after December 15, 2016. Early adoption is permitted but all of the guidance must be adopted in the same period. We are currently evaluating the impact of this new guidance on our consolidated financial statements and related disclosures. We do not intend to early adopt this standard.

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Notes to Consolidated Financial Statements

September 30, 2016

(Unaudited)

2.Long-Term Debt

Debt at September 30, 2016 and December 31, 2015 consisted of the following:

	September 30, 2016		December 31, 2015	
(in thousands)	Principal	Unamortized Debt Issuance Costs	Principal	Unamortized Debt Issuance Costs
5.875% Senior Notes, due May 1, 2022	$ 750,000	$ 6,005	$ 750,000	$ 6,978
4.375% Senior Notes, due June 1, 2024	750,000	6,624	750,000	7,402
Total long-term debt	$ 1,500,000	$ 12,629	$ 1,500,000	$ 14,380

At September 30, 2016 and December 31, 2015, we had no bank debt outstanding. All of our long-term debt is senior unsecured debt and is, therefore, pari passu with other unsecured debt with respect to the payment of both principal and interest.

Bank Debt

We have a senior unsecured revolving credit facility (Credit Facility) that matures October 16, 2020. The Credit Facility has aggregate commitments of $1.0 billion, with our option to increase aggregate commitments to $1.25 billion at any time. There is no borrowing base subject to the discretion of the lenders based on the value of our proved reserves under the Credit Facility. As of September 30, 2016, we had letters of credit outstanding under the Credit Facility of $2.5 million, leaving an unused borrowing availability of $997.5 million.

At our option, borrowings under the Credit Facility may bear interest at either (a) LIBOR plus 1.125 – 2.0% based on the credit rating for our senior unsecured long-term debt, or (b) a base rate (as defined in the credit agreement) plus 0.125 – 1.0%, based on the credit rating for our senior unsecured long-term debt. Unused borrowings are subject to a commitment fee of 0.125 – 0.35%, based on the credit rating for our senior unsecured long-term debt.

The Credit Facility contains representations, warranties, covenants and events of default that are customary for investment grade, senior unsecured bank credit agreements, including a financial covenant for the maintenance of a defined total debt-to-capital ratio of no greater than 65%. As of September 30, 2016, we were in compliance with all of the financial and non-financial covenants.

At September 30, 2016 and December 31, 2015, we had $4.7 million and $5.7 million, respectively, of unamortized debt issuance costs associated with our Credit Facility, which were recorded as deferred assets and included in Other assets, net in our balance sheet. These costs are being amortized to interest expense ratably over the life of the Credit Facility.

Senior Notes

Each of our senior notes is governed by an indenture containing certain covenants, events of default and other restrictive provisions with which we were in compliance as of September 30, 2016. Interest on each of the senior notes is payable semi-annually. The effective interest rate on the 4.375% notes and the 5.875% notes, including the debt issuance cost, is 4.50% and 6.04%, respectively.

3.Derivative Instruments/Hedging

We periodically use derivative instruments to mitigate volatility in commodity prices. While the use of these instruments limits the downside risk of adverse price changes, their use may also limit future revenues from favorable price changes. Depending on changes in oil and gas futures markets and management's view of underlying supply and demand trends, we may increase or decrease our hedging positions. We may hedge up to 50% of our oil and natural gas production.

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CIMAREX ENERGY CO.

Notes to Consolidated Financial Statements

September 30, 2016

(Unaudited)

The following tables summarize our outstanding derivative contracts as of September 30, 2016:

	First Quarter	Second Quarter	Third Quarter	Fourth Quarter	Total
Oil Collars:					
2016:					
Three-Way Collars WTI (1)					
Volume (Bbls)	—	—	—	276,000	276,000
Wtd Avg Price - Lower Floor	$ —	$ —	$ —	$ 40.00	$ 40.00
Wtd Avg Price - Upper Floor	$ —	$ —	$ —	$ 50.00	$ 50.00
Wtd Avg Price - Ceiling	$ —	$ —	$ —	$ 60.00	$ 60.00
Collars WTI (1)					
Volume (Bbls)	—	—	—	1,288,000	1,288,000
Wtd Avg Price - Floor	$ —	$ —	$ —	$ 41.25	$ 41.25
Wtd Avg Price - Ceiling	$ —	$ —	$ —	$ 50.24	$ 50.24
2017:					
Collars WTI (1)					
Volume (Bbls)	1,260,000	1,274,000	920,000	460,000	3,914,000
Wtd Avg Price - Floor	$ 41.25	$ 41.25	$ 43.75	$ 45.00	$ 42.28
Wtd Avg Price - Ceiling	$ 50.24	$ 50.24	$ 53.34	$ 54.42	$ 51.46

(1) WTI refers to West Texas Intermediate price as quoted on the New York Mercantile Exchange.

	First Quarter	Second Quarter	Third Quarter	Fourth Quarter	Total
Gas Collars:					
2016:					
PEPL (1)					
Volume (MMBtu)	—	—	—	8,280,000	8,280,000
Wtd Avg Price - Floor	$ —	$ —	$ —	$ 2.42	$ 2.42
Wtd Avg Price - Ceiling	$ —	$ —	$ —	$ 2.93	$ 2.93
Perm EP (1)					
Volume (MMBtu)	—	—	—	6,440,000	6,440,000
Wtd Avg Price - Floor	$ —	$ —	$ —	$ 2.47	$ 2.47

Wtd Avg Price - Ceiling	$ —	$ —	$ —	$ 2.96	$ 2.96
2017:					
PEPL (1)					
Volume (MMBtu)	7,200,000	7,280,000	5,520,000	2,760,000	22,760,000
Wtd Avg Price - Floor	$ 2.38	$ 2.38	$ 2.47	$ 2.68	$ 2.44
Wtd Avg Price - Ceiling	$ 2.94	$ 2.94	$ 3.02	$ 3.13	$ 2.98
Perm EP (1)					
Volume (MMBtu)	6,300,000	6,370,000	3,680,000	1,840,000	18,190,000
Wtd Avg Price - Floor	$ 2.47	$ 2.47	$ 2.51	$ 2.73	$ 2.51
Wtd Avg Price - Ceiling	$ 3.01	$ 3.01	$ 3.04	$ 3.15	$ 3.03

(1) PEPL refers to Panhandle Eastern Pipe Line, Tex/OK Mid-Continent Index as quoted in Platt's Inside FERC. Perm EP refers to El Paso Natural Gas Company, Permian Basin Index as quoted in Platt's Inside FERC.

CIMAREX ENERGY CO.

Notes to Consolidated Financial Statements

September 30, 2016

(Unaudited)

A three-way collar is a combination of three options: lower floor (sold put), upper floor (bought put) and ceiling (sold call). If the published index price is below the lower floor, we receive the difference between the two floors. If the index price is between the two floors, we receive the difference between the upper floor and the index price. If the index price is between the upper floor and the ceiling, we do not receive or pay any amounts. If the index price is above the ceiling, we pay the excess over the ceiling price.

Under a collar agreement, we receive the difference between the published index price and a floor price if the index price is below the floor. We pay the difference between the ceiling price and the index price if the index price is above the contracted ceiling price. No amounts are paid or received if the index price is between the floor and the ceiling price.

We have elected not to account for our derivatives as cash flow hedges. Therefore, we recognize settlements and changes in the assets or liabilities relating to our open derivative contracts in earnings. Cash settlements of our contracts are included in cash flows from operating activities in our statements of cash flows.

The following table presents the aggregate net (gain) loss from settlements and changes in fair value of our derivative contracts and the (gains) losses only from settlements during the periods shown below.

	Three Months Ended September 30,		Nine Months Ended September 30,	
(in thousands)	2016	2015	2016	2015
(Gain) loss on derivative instruments, net	$ (9,758)	$ (1,968)	$ 23,050	$ (1,968)
Settlement (gains) losses	$ (791)	$ —	$ (9,718)	$ —

Our derivative contracts are carried at their fair value on our balance sheet using Level 2 inputs and are subject to enforceable master netting arrangements, which allow us to offset recognized asset and liability fair value amounts on contracts with the same counterparty. Our policy is to not offset asset and liability positions in our accompanying balance sheets.

CIMAREX ENERGY CO.

Notes to Consolidated Financial Statements

September 30, 2016

(Unaudited)

The following tables present the amounts and classifications of our derivative assets and liabilities as of September 30, 2016 and December 31, 2015, as well as the potential effect of netting arrangements on contracts with the same counterparty.

September 30, 2016:

(in thousands)	Balance Sheet Location	Asset	Liability
Oil contracts	Current assets — Derivative instruments	$ 662	$ —
Natural gas contracts	Current assets — Derivative instruments	485	—
Natural gas contracts	Non-current assets — Derivative instruments	3	—
Oil contracts	Current liabilities — Derivative instruments	—	15,166
Natural gas contracts	Current liabilities — Derivative instruments	—	6,407
Oil contracts	Non-current liabilities — Other liabilities	—	1,026
Natural gas contracts	Non-current liabilities — Other liabilities	—	73
Total gross amounts presented in accompanying balance sheet		1,150	22,672
Less: gross amounts not offset in the accompanying balance sheet		(1,150)	(1,150)
Net amount:		$ —	$ 21,522

December 31, 2015:

(in thousands)	Balance Sheet Location	Asset	Liability
Oil contracts	Current assets — Derivative instruments	$ 6,774	$ —
Natural gas contracts	Current assets — Derivative instruments	3,971	—
Natural gas contracts	Non-current assets — Derivative instruments	501	—
Total gross amounts presented in accompanying balance sheet		11,246	—
Less: gross amounts not offset in the accompanying balance sheet		—	—
Net amount:		$ 11,246	$ —

We are exposed to financial risks associated with our derivative contracts from non-performance by our counterparties. We mitigate our exposure to any single counterparty by contracting with a number of financial institutions, each of which have a high credit rating and is a member of our bank credit facility. Our member banks do not require us to post collateral for our hedge liability positions. Because some of the member banks have discontinued hedging activities, in the future we may hedge with counterparties outside our bank group to obtain competitive terms and to spread counterparty risk.

4.Fair Value Measurements

Fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date (exit price). The FASB has established a fair value hierarchy that prioritizes the inputs to valuation techniques used to measure fair value. This hierarchy consists of three broad levels. Level 1 inputs are the highest priority and consist of unadjusted quoted prices in active markets for identical assets and liabilities. Level 2 are inputs other than quoted prices that are observable for the asset or liability, either directly or indirectly. Level 3 are unobservable inputs for an asset or liability.

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The following table provides fair value measurement information for certain assets and liabilities as of September 30, 2016 and December 31, 2015:

	September 30, 2016		December 31, 2015	
(in thousands)	Book Value	Fair Value	Book Value	Fair Value
Financial Assets (Liabilities):				
5.875% Notes due 2022	$ (750,000)	$ (791,235)	$ (750,000)	$ (723,750)
4.375% Notes due 2024	$ (750,000)	$ (792,180)	$ (750,000)	$ (683,318)
Derivative instruments — assets	$ 1,150	$ 1,150	$ 11,246	$ 11,246
Derivative instruments — liabilities	$ (22,672)	$ (22,672)	$ —	$ —

Assessing the significance of a particular input to the fair value measurement requires judgment, including the consideration of factors specific to the asset or liability. The fair value (Level 1) of our 4.375% and 5.875% fixed rate notes was based on their last traded value before period end. The fair value of our derivative instruments (Level 2) was estimated using option pricing models. These models use certain variables including forward price and volatility curves and the strike prices for the instruments. The fair value estimates are adjusted relative to non-performance risk as appropriate. See Note 3 for further information on the fair value of our derivative instruments.

Other Financial Instruments

The carrying amounts of our cash, cash equivalents, accounts receivable, accounts payable, and accrued liabilities approximate fair value because of the short-term maturities and/or liquid nature of these assets and liabilities.

Most of our accounts receivable balances are uncollateralized and result from transactions with other companies in the oil and gas industry. Concentration of customers may impact our overall credit risk because our customers may be similarly affected by changes in economic or other conditions within the industry.

We routinely assess the recoverability of all material accounts receivable to determine their collectability. We accrue a reserve to the allowance for doubtful accounts when it is probable that a receivable will not be collected and the amount of the reserve may be reasonably estimated. At September 30, 2016 and December 31, 2015, the allowance for doubtful accounts was $1.6 million and $1.8 million, respectively.

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5.Capital Stock

Authorized capital stock consists of 200 million shares of common stock and 15 million shares of preferred stock. At September 30, 2016, there were no shares of preferred stock outstanding. A summary of our common stock activity for the nine months ended September 30, 2016 follows:

(in thousands)	
Issued and outstanding as of December 31, 2015	94,821
Issuance of service-based restricted stock awards	208
Restricted stock forfeited and retired	(26)
Common stock reacquired and retired	(100)
Option exercises, net of cancellations	61
Issued and outstanding as of September 30, 2016	94,964

Dividends

In August 2016, the Board of Directors declared a cash dividend of $0.08 per share. The dividend is payable on December 1, 2016, to stockholders of record on November 15, 2016. Dividends declared are recorded as a reduction of retained earnings to the extent retained earnings are available at the close of the period prior to the date of the declared dividend. Dividends in excess of retained earnings are recorded as a reduction of additional paid-in capital. For the dividends declared in May and August 2016, all of the dividends declared ($15.2 million) were recorded as a reduction of additional paid-in capital. Future dividend payments will depend on our level of earnings, financing requirements, and other factors considered relevant by the Board of Directors.

6.Stock-based Compensation

We have recognized stock-based compensation cost as shown below. Expense associated with stock compensation will fluctuate based on the grant-date fair value of awards, the number of awards and the timing of the awards. Historical amounts may not be representative of future amounts as the value of future awards may vary from historical amounts.

	Three Months Ended	Nine Months Ended

	September 30,		September 30,	
(in thousands)	2016	2015	2016	2015
Restricted stock awards				
Performance stock awards	$ 5,465	$ 4,984	$ 18,374	$ 14,627
Service-based stock awards	4,624	1,902	13,540	10,700
	10,089	6,886	31,914	25,327
Stock option awards	571	855	1,974	2,141
Total stock compensation cost	10,660	7,741	33,888	27,468
Less amounts capitalized to oil and gas properties	(4,896)	(3,004)	(15,106)	(12,588)
Compensation expense	$ 5,764	$ 4,737	$ 18,782	$ 14,880

The increases in 2016 stock compensation are primarily related to performance awards granted in December 2015, a portion of which have been amortized over the 2016 periods.

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7.Asset Retirement Obligations

We recognize the fair value of liabilities for retirement obligations associated with tangible long-lived assets in the period in which there is a legal obligation associated with the retirement of such assets and the amount can be reasonably estimated. The associated asset retirement costs are capitalized as part of the carrying amount of the long-lived asset. This liability includes costs related to the plugging and abandonment of wells, the removal of facilities and equipment, and site restorations. Subsequent to initial measurement, the asset retirement liability is required to be accreted each period. If the fair value of a recorded asset retirement obligation changes, a revision is recorded to both the asset retirement obligation and the asset retirement capitalized cost. Capitalized costs are included as a component of the DD&A calculations.

The following table reflects the components of the change in the carrying amount of the asset retirement obligation for the nine months ended September 30, 2016:

(in thousands)	
Asset retirement obligation at January 1, 2016	$ 164,105
Liabilities incurred	2,234
Liability settlements and disposals	(20,316)
Accretion expense	5,732
Revisions of estimated liabilities	2,735
Asset retirement obligation at September 30, 2016	154,490
Less current obligation	(9,033)
Long-term asset retirement obligation	$ 145,457

During the first nine months of 2016, the liability settlements and disposals included $12.5 million related to properties that were sold.

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8.Earnings (loss) per Share

The calculations of basic and diluted net earnings (loss) per common share under the two-class method are presented below:

(in thousands, except per share data)	Three Months Ended September 30, 2016	Three Months Ended September 30, 2015	Nine Months Ended September 30, 2016	Nine Months Ended September 30, 2015
Basic:				
Net income (loss)	$ (12,818)	$ (763,284)	$ (469,239)	$ (1,778,440)
Participating securities' share in earnings (1)	—	—	—	—
Net income (loss) applicable to common stockholders	$ (12,818)	$ (763,284)	$ (469,239)	$ (1,778,440)
Diluted:				
Net income (loss)	$ (12,818)	$ (763,284)	$ (469,239)	$ (1,778,440)
Participating securities' share in earnings (1)	—	—	—	—
Net income (loss) applicable to common stockholders	$ (12,818)	$ (763,284)	$ (469,239)	$ (1,778,440)
Shares:				
Basic shares outstanding	93,221	92,969	93,221	92,969
Dilutive effect of stock options (2)	—	—	—	—
Fully diluted common stock	93,221	92,969	93,221	92,969
Excluded (2)	2,065	1,915	2,065	1,915
Earnings (loss) per share to common stockholders (3):				
Basic	$ (0.14)	$ (8.21)	$ (5.04)	$ (19.14)
Diluted	$ (0.14)	$ (8.21)	$ (5.04)	$ (19.14)

(1) Participating securities are not included in undistributed earnings when a loss exists.
(2) Inclusion of certain shares would have an anti-dilutive effect.
(3) Earnings (loss) per share are based on actual figures rather than the rounded figures presented.

9.Income Taxes

The components of our provision for income taxes are as follows:

	Three Months Ended September 30,		Nine Months Ended September 30,	
(in thousands)	2016	2015	2016	2015
Current taxes (benefit)	$ (1,115)	$ 14,937	$ (1,115)	$ 14,937
Deferred taxes (benefit)	(5,089)	(443,469)	(265,508)	(1,014,264)
	$ (6,204)	$ (428,532)	$ (266,623)	$ (999,327)
Combined Federal and State effective income tax rate	32.6 %	36.0 %	36.2 %	36.0 %

At December 31, 2015, we had a U.S. net tax operating loss carryforward of $891.3 million, which would expire in tax years 2031 through 2035. We believe that the carryforward will be utilized before it expires. The

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amount of U.S. net tax operating loss carryforward that will be recorded to equity when utilized to reduce taxes payable is $77.2 million. We also had an alternative minimum tax credit carryforward of approximately $6.0 million.

At September 30, 2016, we had no unrecognized tax benefits that would impact our effective tax rate and have made no provisions for interest or penalties related to uncertain tax positions. The tax years 2013 through 2015 remain open to examination by the Internal Revenue Service of the United States. We file tax returns with various state taxing authorities, which remain open to examination for tax years 2011 through 2015.

Our provision for income taxes differed from the U.S. statutory rate of 35% primarily due to state income taxes and non-deductible expenses.

10.Commitments and Contingencies

Commitments

We have commitments of $200.9 million to finish drilling and completing wells in progress at September 30, 2016. We also have various commitments for drilling rigs. The total minimum commitments under these agreements are $1.9 million.

At September 30, 2016, we had firm sales contracts to deliver approximately 50.2 Bcf of natural gas over the next 25 months. If this gas is not delivered, our financial commitment would be approximately $134.9 million. This commitment will fluctuate due to price volatility and actual volumes delivered. However, we believe no financial commitment will be due based on our current proved reserves and production levels from which we can fulfill these obligations.

In connection with gas gathering and processing agreements, we have volume commitments over the next ten years. If no gas is delivered, the maximum amount that would be payable under these commitments would be approximately $227.8 million. However, we believe no financial commitment will be due based on our current proved reserves and production levels from which we can fulfill these obligations.

We have minimum volume delivery commitments in connection with agreements to reimburse connection costs to various pipelines. The maximum amount that would be payable if no gas is delivered would be approximately $16.0 million. Of this total, we have accrued a liability of $9.6 million. Due to reduced drilling activity in 2015 and 2016, we may have additional liabilities associated with these delivery commitments in the future.

We have other various transportation, delivery and facilities commitments in the normal course of business, which approximate $31.6 million. We anticipate meeting these obligations.

We have various commitments for office space and equipment under operating lease arrangements totaling $99.0 million.

All of the noted commitments were routine and made in the ordinary course of our business.

Litigation

We have various litigation matters related to the ordinary course of our business. We assess the probability of estimable amounts related to those matters in accordance with guidance established by the FASB and adjust our accruals accordingly. Though some of the related claims may be significant, we believe the resolution of them, individually or in the aggregate, would not have a material adverse effect on our financial condition or results of operations after consideration of current accruals.

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11.Supplemental Disclosure of Cash Flow Information