CABOT OIL & GAS CORP
Form 10-Q
October 24, 2014
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UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549

FORM 10-Q

ý QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934.

For the quarterly period ended September 30, 2014

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

Commission file number 1-10447

CABOT OIL & GAS CORPORATION
(Exact name of registrant as specified in its charter)

DELAWARE	04-3072771
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification Number)

Three Memorial City Plaza
840 Gessner Road, Suite 1400, Houston, Texas 77024
(Address of principal executive offices including ZIP code)
(281) 589-4600
(Registrant’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 and (2) has been subject to such filing requirements for the past 90 days. Yes ý No o

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 ý No o

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

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

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

As of October 20, 2014, there were 413,019,880 shares of Common Stock, Par Value $.10 Per Share, outstanding.

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PART I. FINANCIAL INFORMATION
ITEM 1. Financial Statements
CABOT OIL & GAS CORPORATION
CONDENSED CONSOLIDATED BALANCE SHEET (Unaudited)

(In thousands, except share amounts)	September 30, 2014	December 31, 2013
ASSETS		
Current assets		
Cash and cash equivalents	$309,987	$23,400
Restricted cash	—	28,094
Accounts receivable, net	191,270	222,476
Inventories	13,731	17,468
Deferred income taxes	53,725	81,855
Other current assets	19,233	5,606
Total current assets	587,946	378,899
Properties and equipment, net (Successful efforts method)	5,130,213	4,546,227
Equity method investments	57,495	26,892
Other assets	31,610	29,062
	$5,807,264	$4,981,080
LIABILITIES AND STOCKHOLDERS' EQUITY		
Current liabilities		
Accounts payable	$379,787	$288,801
Accrued liabilities	44,843	87,513
Income taxes payable	8,161	31,591
Total current liabilities	432,791	407,905
Postretirement benefits	35,936	33,554
Long-term debt	1,612,000	1,147,000
Deferred income taxes	1,208,036	1,067,912
Asset retirement obligation	114,241	73,853
Other liabilities	37,789	46,254
Total liabilities	3,440,793	2,776,478
Commitments and contingencies		
Stockholders' equity		
Common stock:		
Authorized — 960,000,000 and 480,000,000 shares of $0.10 par value in 2014 and 2013, respectively		
Issued — 422,912,560 and 422,014,681 shares in 2014 and 2013, respectively	42,291	42,201
Additional paid-in capital	713,087	710,940
Retained earnings	1,929,026	1,627,805
Accumulated other comprehensive income (loss)	(19,199)	(8,361)
Less treasury stock, at cost:		
9,638,980 and 5,618,166 shares in 2014 and 2013, respectively	(298,734)	(167,983)
Total stockholders' equity	2,366,471	2,204,602
	$5,807,264	$4,981,080

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

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CABOT OIL & GAS CORPORATION
CONDENSED CONSOLIDATED STATEMENT OF OPERATIONS (Unaudited)

	Three Months Ended September 30,		Nine Months Ended September 30,	
(In thousands, except per share amounts)	2014	2013	2014	2013
OPERATING REVENUES				
Natural gas	$347,970	$341,901	$1,218,540	$1,004,085
Crude oil and condensate	82,563	84,209	228,047	220,090
Gain (loss) on derivative instruments	71,906	—	69,577	—
Brokered natural gas	6,501	7,165	27,794	26,302
Other	3,077	2,575	11,049	8,338
	512,017	435,850	1,555,007	1,258,815
OPERATING EXPENSES				
Direct operations	37,802	32,923	109,241	101,398
Transportation and gathering	85,966	60,803	247,707	159,672
Brokered natural gas	5,680	5,913	24,570	21,006
Taxes other than income	10,933	11,532	36,794	34,583
Exploration	8,812	3,891	19,963	12,444
Depreciation, depletion and amortization	154,013	168,980	458,995	469,022
General and administrative	19,579	24,697	61,342	82,009
	322,785	308,739	958,612	880,134
Earnings (loss) on equity method investments	1,063	278	1,819	614
Gain (loss) on sale of assets	46	4,421	(2,735)	4,601
INCOME FROM OPERATIONS	190,341	131,810	595,479	383,896
Interest expense	17,422	16,074	50,312	49,366
Income before income taxes	172,919	115,736	545,167	334,530
Income tax expense	72,131	45,847	218,928	132,703
NET INCOME	$100,788	$69,889	$326,239	$201,827
Earnings per share				
Basic	$0.24	$0.17	$0.78	$0.48
Diluted	$0.24	$0.17	$0.78	$0.48
Weighted-average common shares outstanding				
Basic	416,173	420,986	416,785	420,664
Diluted	418,093	423,453	418,468	422,824
Dividends per common share	$0.02	$0.02	$0.06	$0.04

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

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CABOT OIL & GAS CORPORATION
CONDENSED CONSOLIDATED STATEMENT OF COMPREHENSIVE INCOME (Unaudited)

	Three Months Ended September 30,		Nine Months Ended September 30,	
(In thousands)	2014	2013	2014	2013
Net income	$100,788	$69,889	$326,239	$201,827
Other comprehensive income (loss), net of taxes:				
Reclassification adjustment for settled cash flow hedge contracts(1)	12,965	(11,942)	69,337	(22,372)
Changes in fair value of cash flow hedge contracts(2)	—	(1,447)	(80,175)	31,417
Postretirement benefits:				
Amortization of net loss(3)	—	70	—	319
Total other comprehensive income (loss)	12,965	(13,319)	(10,838)	9,364
Comprehensive income (loss)	$113,753	$56,570	$315,401	$211,191

(1) Net of income taxes of $(8,592) and $7,742 for the three months ended September 30, 2014 and 2013, respectively, and $(45,951) and $14,504 for the nine months ended September 30, 2014 and 2013, respectively.

(2) Net of income taxes of $937 for the three months ended September 30, 2013 and $53,135 and $(20,366) for the nine months ended September 30, 2014 and 2013, respectively.

(3) Net of income taxes of $(46) and $(206) for the three and nine months ended September 30, 2013, respectively.

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

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CABOT OIL & GAS CORPORATION
CONDENSED CONSOLIDATED STATEMENT OF CASH FLOWS (Unaudited)

(In thousands)	Nine Months Ended September 30, 2014	2013
CASH FLOWS FROM OPERATING ACTIVITIES		
Net income	$326,239	$201,827
Adjustments to reconcile net income to cash provided by operating activities:		
Depreciation, depletion and amortization	458,995	469,022
Deferred income tax expense	181,439	107,235
(Gain) loss on sale of assets	2,735	(4,601)
Exploration expense	6,454	807
Unrealized (gain) loss on derivative instruments	(44,766)	—
Amortization of debt issuance costs	3,378	2,767
Stock-based compensation and other	13,304	36,684
Changes in assets and liabilities:		
Accounts receivable, net	30,418	(6,321)
Income taxes	(23,430)	(3,639)
Inventories	3,737	(6,665)
Other current assets	(147)	(1,547)
Accounts payable and accrued liabilities	(9,712)	(19,837)
Other assets and liabilities	607	228
Stock-based compensation tax benefit	(6,001)	(9,284)
Net cash provided by operating activities	943,250	766,676
CASH FLOWS FROM INVESTING ACTIVITIES		
Capital expenditures	(964,741)	(843,400)
Acquisitions	(15,826)	(128)
Proceeds from sale of assets	3,913	15,174
Restricted cash	28,094	—
Investment in equity method investments	(28,784)	(8,624)
Net cash used in investing activities	(977,344)	(836,978)
CASH FLOWS FROM FINANCING ACTIVITIES		
Borrowings from debt	1,802,000	585,000
Repayments of debt	(1,337,000)	(510,000)
Treasury stock repurchases	(119,767)	—
Dividends paid	(25,018)	(16,830)
Stock-based compensation tax benefit	6,001	9,284
Capitalized debt issuance costs	(5,626)	—
Other	91	44
Net cash provided by financing activities	320,681	67,498
Net increase (decrease) in cash and cash equivalents	286,587	(2,804)
Cash and cash equivalents, beginning of period	23,400	30,736
Cash and cash equivalents, end of period	$309,987	$27,932

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

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CABOT OIL & GAS CORPORATION
NOTES TO THE CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Unaudited)

1. Financial Statement Presentation

During interim periods, Cabot Oil & Gas Corporation (the Company) follows the same accounting policies disclosed in its Annual Report on Form 10-K for the year ended December 31, 2013 (Form 10-K) filed with the Securities and Exchange Commission (SEC). The interim financial statements should be read in conjunction with the notes to the consolidated financial statements and information presented in the Form 10-K. In management’s opinion, the accompanying interim condensed consolidated financial statements contain all material adjustments, consisting only of normal recurring adjustments, necessary for a fair statement. The results for any interim period are not necessarily indicative of the expected results for the entire year.

Certain reclassifications have been made to prior year statements to conform with the current year presentation. These reclassifications have no impact on previously reported net income.

With respect to the unaudited financial information of the Company as of September 30, 2014 and for the three and nine months ended September 30, 2014 and 2013, PricewaterhouseCoopers LLP reported that they have applied limited procedures in accordance with professional standards for a review of such information. However, their separate report dated October 24, 2014 appearing herein states that they did not audit and they do not express an opinion on that unaudited financial information. Accordingly, the degree of reliance on their report on such information should be restricted in light of the limited nature of the review procedures applied. PricewaterhouseCoopers LLP is not subject to the liability provisions of Section 11 of the Securities Act of 1933 for their report on the unaudited financial information because that report is not a “report” or a “part” of a registration statement prepared or certified by PricewaterhouseCoopers LLP within the meaning of Sections 7 and 11 of the Act.

Recent Accounting Pronouncements

In April 2014, the Financial Accounting Standards Board (FASB) issued Accounting Standards Update (ASU) No. 2014-08, Reporting Discontinued Operations and Disclosures of Disposals of Components of an Entity. The guidance applies prospectively to new disposals and new classifications of disposal groups as held for sale after the effective date. The guidance is effective for interim and annual periods beginning on or after December 15, 2014. The Company does not expect the adoption of this guidance to have a material impact on its financial position, results of operations or cash flows.

In May 2014, the FASB issued ASU No. 2014-09, Revenue from Contracts with Customers, as a new Topic, Accounting Standards Codification Topic 606. The new revenue recognition standard provides a five-step analysis of transactions to determine when and how revenue is recognized. The core principle of the guidance is that a company should recognize revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. This ASU is effective beginning in fiscal year 2017 and can be adopted either retrospectively or as a cumulative-effect adjustment as of the date of adoption. The Company is currently evaluating the effect that adopting this guidance will have on its financial position, results of operations or cash flows.

In August 2014, the FASB issued ASU No. 2014-15, Presentation of Financial Statements - Going Concern, as a new Sub-topic, Accounting Standards Codification Sub-topic 205.40. The new going concern standard codifies in generally accepted accounting principles (GAAP) management’s responsibility to evaluate whether there is substantial doubt about an entity’s ability to continue as a going concern and to provide related footnote disclosures. This ASU is effective for interim and annual periods beginning on or after December 15, 2016 and early adoption is permitted. The Company does not expect the adoption of this guidance to have a material impact on its financial position or results of operations.

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2. Properties and Equipment, Net

Properties and equipment, net are comprised of the following:

(In thousands)	September 30, 2014	December 31, 2013
Proved oil and gas properties	$7,405,851	$6,362,570
Unproved oil and gas properties	354,882	375,428
Gathering and pipeline systems	240,705	239,958
Land, buildings and other equipment	105,143	94,243
	8,106,581	7,072,199
Accumulated depreciation, depletion and amortization	(2,976,368)	(2,525,972)
	$5,130,213	$4,546,227

At September 30, 2014, the Company did not have any projects that had exploratory well costs that were capitalized for a period of greater than one year after drilling.

Subsequent Events

Acquisitions

In October 2014, the Company completed the acquisition of certain proved and unproved oil and gas properties in the Eagle Ford Shale in south Texas for approximately $210.0 million. Total cash consideration paid by the Company as of the closing date was approximately $186.2 million, subject to customary post-closing adjustments, which reflects the impact of customary purchase price adjustments and an adjustment for consents that the seller was unable to obtain for certain leaseholds prior to closing.

Divestitures

In October 2014, the Company completed the divestiture of certain proved and unproved oil and gas properties in east Texas to a third party for approximately $44.3 million. Total cash consideration received by the Company as of the closing date was approximately $39.9 million, subject to customary post-closing adjustments, which reflects the impact of customary purchase price adjustments. The net book value associated with the oil and gas properties held for sale as of September 30, 2014 was approximately $21.5 million and is included in properties and equipment, net in the Condensed Consolidated Balance Sheet.

3. Equity Method Investments

During the nine months ended September 30, 2014, the Company made contributions of approximately $28.8 million to its equity method investments ($26.6 million to Constitution Pipeline Company, LLC and $2.2 million to Meade Pipeline Co LLC (Meade)).

For further information regarding the Company's equity method investments, refer to Note 4 of the Notes to the Consolidated Financial Statements in the Form 10-K.

Meade Pipeline Co LLC

In February 2014, the Company acquired a 20% equity interest in Meade. Meade was formed to participate in the development and construction of a 177-mile pipeline (Central Penn Line) that will transport natural gas from Susquehanna County, Pennsylvania to an interconnect with Transcontinental Gas Pipe Line Company, LLC's (Transco) mainline in Lancaster County, Pennsylvania. The new pipeline will be constructed and operated by Transco and will be owned by Transco and Meade in proportion to their respective ownership percentages of approximately 61% and 39%, respectively. Under the terms of the Meade LLC agreement, the Company agreed to invest its proportionate share of Meade's anticipated costs associated with the new pipeline of $149 million, which is expected to occur over the next three to four years. The expected in-service date for the new pipeline is scheduled for the second half of 2017.

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4. Debt and Credit Agreements

The Company's debt and credit agreements consisted of the following:

(In thousands)	September 30, 2014	December 31, 2013
Long-Term Debt		
7.33% weighted-average fixed rate notes	$20,000	$20,000
6.51% weighted-average fixed rate notes	425,000	425,000
9.78% notes	67,000	67,000
5.58% weighted-average fixed rate notes	175,000	175,000
3.65% weighted-average fixed rate notes	925,000	—
Revolving credit facility	—	460,000
	$1,612,000	$1,147,000

Effective April 15, 2014, the lenders under the Company's revolving credit facility approved an increase in the Company's borrowing base from $2.3 billion to $3.1 billion as part of the annual redetermination under the terms of the revolving credit facility agreement. The commitments under the revolving credit facility remain unchanged at $1.4 billion. At September 30, 2014, the Company had no borrowings outstanding under its revolving credit facility and had $1.4 billion available for future borrowings. The Company's weighted-average effective interest rate for the three months ended September 30, 2014 and 2013 was approximately 2.2% and for the nine months ended September 30, 2014 and 2013 was approximately 2.2% and 2.3%, respectively.

The Company was in compliance with all restrictive financial covenants for both the revolving credit facility and fixed rate notes as of September 30, 2014.

3.65% Weighted-Average Fixed Rate Notes

In September 2014, the Company issued $925 million principal amount of senior unsecured fixed-rate notes to a group of 24 investors in a private placement. The notes have bullet maturities and were issued in three separate tranches as follows:

	Principal	Term	Maturity Date	Coupon	
Tranche 1	$100,000,000	7 years	September 2021	3.24	%
Tranche 2	$575,000,000	10 years	September 2024	3.67	%
Tranche 3	$250,000,000	12 years	September 2026	3.77	%

Interest on each series of the 3.65% weighted average fixed rate notes is payable semi annually. The Company may prepay all or any portion of the notes of each series on any date at a price equal to the principal amount thereof plus accrued and unpaid interest plus a make whole premium. The notes contain restrictions on the merger of the Company or any subsidiary with a third party other than under certain limited conditions. There are also various other restrictive covenants customarily found in such debt instruments. Those covenants include a required asset coverage ratio (present value of proved reserves to debt and other liabilities) of at least 1.75 to 1.0 and a minimum annual coverage ratio of operating cash flow to interest expense for the trailing four quarters of 2.8 to 1.0. The notes are also subject to customary events of default.

5. Derivative Instruments and Hedging Activities

The Company periodically enters into commodity derivatives to manage its exposure to price fluctuations on natural gas and crude oil production. The Company's credit agreement restricts the ability of the Company to enter into commodity derivatives other than to hedge or mitigate risks to which the Company has actual or projected exposure or as permitted under the Company's risk management policies and where such derivatives do not subject the Company to material speculative risks. All of the Company's derivatives are used for risk management purposes and are not held for trading purposes.

Through March 31, 2014, the Company elected to designate its commodity derivatives as cash flow hedges for accounting purposes. Effective April 1, 2014, the Company elected to discontinue hedge accounting for its commodity derivatives on a prospective basis. Accordingly, the change in the fair value of derivatives designated as hedges that are effective is recorded to accumulated other comprehensive income (loss) in stockholders' equity in the Condensed Consolidated Balance Sheet. The ineffective portion of the change in the fair value of derivatives designated as hedges and the change in fair

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value of realized cash settlements of derivatives not designated as hedges are recorded as a component of operating revenues in gain (loss) on derivative instruments in the Condensed Consolidated Statement of Operations.

As a result of discontinuing hedge accounting, the unrealized loss included in accumulated other comprehensive income (loss) as of April 1, 2014 of $73.4 million ($44.2 million net of tax) was frozen and will be reclassified into natural gas and crude oil and condensate revenues in the Condensed Consolidated Statement of Operations in future periods as the underlying hedge transactions occur. Through September 30, 2014, the Company has reclassified after-tax losses of $26.8 million that were previously frozen in accumulated other comprehensive income (loss) to natural gas and crude oil and condensate revenues in the Condensed Consolidated Statement of Operations. As of September 30, 2014, the Company expects to reclassify $17.4 million in after-tax losses associated with its commodity derivatives from accumulated other comprehensive income (loss) to natural gas and crude oil and condensate revenues in the Condensed Consolidated Statement of Operations over the next three months.

As of September 30, 2014, the Company had the following outstanding commodity derivatives:

				Collars				Swaps
				Floor		Ceiling		
Type of Contract	Volume		Contract Period	Range	Weighted-Average	Range	Weighted-Average	Weighted-Average
Natural gas	84.9	Bcf	Oct. 2014 - Dec. 2014	$3.60-$4.37	$ 4.13	$4.22-$4.80	$ 4.51	
Natural gas	26.8	Bcf	Oct. 2014 - Dec. 2014					$ 4.05
Natural gas	35.5	Bcf	Jan. 2015 - Dec. 2015	—	$ 3.86	$4.36-$4.43	$ 4.40	
Natural gas	35.5	Bcf	Jan. 2015 - Dec. 2015					$ 4.12
Crude oil	184.0	Mbbl	Oct. 2014 - Dec. 2014					$ 97.00

Natural gas prices are stated per Mcf and crude oil prices are stated per barrel.

Effect of Derivative Instruments on the Condensed Consolidated Balance Sheet

		Fair Values of Derivative Instruments			
		Derivative Assets		Derivative Liabilities	
(In thousands)	Balance Sheet Location	September 30, 2014	December 31, 2013	September 30, 2014	December 31, 2013
Derivatives Designated as Hedges					
Commodity contracts	Other current assets	$—	$ 3,019	$—	$ —
Commodity contracts	Accrued liabilities	—	—	—	13,912
Derivatives Not Designated as Hedges					
Commodity contracts	Other current assets	16,503	—	—	—
Commodity contracts	Accrued liabilities	—	—	102	—
Commodity contracts	Other liabilities	—	—	549	—
		$ 16,503	$ 3,019	$ 651	$ 13,912

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Offsetting of Derivative Assets and Liabilities in the Condensed Consolidated Balance Sheet

(In thousands)	September 30, 2014	December 31, 2013
Derivative Assets		
Gross amounts of recognized assets	$19,445	$13,792
Gross amounts offset in the statement of financial position	(2,942)	(10,773)
Net amounts of assets presented in the statement of financial position	16,503	3,019
Gross amounts of financial instruments not offset in the statement of financial position	238	373
Net amount	$16,741	$3,392
Derivative Liabilities		
Gross amounts of recognized liabilities	$3,593	$24,685
Gross amounts offset in the statement of financial position	(2,942)	(10,773)
Net amounts of liabilities presented in the statement of financial position	651	13,912
Gross amounts of financial instruments not offset in the statement of financial position	—	—
Net amount	$651	$13,912

Effect of Derivative Instruments on Accumulated Other Comprehensive Income (Loss)

The amount of gain (loss) recognized in accumulated other comprehensive income (loss) on derivatives (effective portion) is as follows:

	Three Months Ended September 30,		Nine Months Ended September 30,	
(In thousands)	2014	2013	2014	2013
Commodity contracts	$—	$(2,384)	$(133,310)	$51,783

The amount of gain (loss) reclassified from accumulated other comprehensive income (loss) into income (effective portion) is as follows:

	Three Months Ended September 30,		Nine Months Ended September 30,	
(In thousands)	2014 (1)	2013	2014 (1)	2013
Natural gas revenues	$(21,427)	$20,766	$(114,304)	$33,822
Crude oil and condensate revenues	(130)	(1,082)	(984)	3,054
	$(21,557)	$19,684	$(115,288)	$36,876

(1) The Company ceased hedge accounting effective April 1, 2014. For the three and nine months ended September 30, 2014, a loss of approximately $21.6 million and $44.5 million, respectively, were reclassified into income. These amounts were previously frozen in accumulated other comprehensive income (loss).

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Effect of Derivative Instruments on the Condensed Consolidated Statement of Operations

The amount of gain (loss) recognized in the Condensed Consolidated Statement of Operations on derivative instruments is as follows:

(In thousands)	Three Months Ended September 30, 2014	Three Months Ended September 30, 2013	Nine Months Ended September 30, 2014	Nine Months Ended September 30, 2013
Derivatives Designated as Hedges				
Realized				
Natural gas	$—	$20,766	$(70,557)	$33,822
Crude oil and condensate	—	(1,082)	(218)	3,054
	$—	$19,684	$(70,775)	$36,876
Derivatives Not Designated as Hedges				
Realized				
Natural gas	$(21,427)	$—	$(43,747)	$—
Crude oil and condensate	(130)	—	(766)	—
Gain (loss) on derivative instruments	40,073	—	24,811	—
Unrealized				
Gain (loss) on derivative instruments	31,833	—	44,766	—
	$50,349	$—	$25,064	$—
	$50,349	$19,684	$(45,711)	$36,876

For the three and nine months ended September 30, 2014 and 2013, respectively, there was no ineffectiveness recorded in the Condensed Consolidated Statement of Operations related to derivative instruments designated as hedges.

Additional Disclosures about Derivative Instruments and Hedging Activities

The use of derivative instruments involves the risk that the counterparties will be unable to meet their obligations under the agreements. The Company enters into derivative contracts with multiple counterparties in order to limit its exposure to individual counterparties. The Company also has netting arrangements with each of its counterparties that allow it to offset assets and liabilities from separate derivative contracts with that counterparty.

Certain counterparties to the Company's derivative instruments are also lenders under its revolving credit facility. The Company's revolving credit facility and derivative instruments contain certain cross default and acceleration provisions that may require immediate payment of its derivative liabilities in certain situations.

6. Fair Value Measurements

The Company follows the authoritative guidance for measuring fair value of assets and liabilities in its financial statements. For further information regarding the fair value hierarchy, refer to Note 7 of the Notes to the Consolidated Financial Statements in the Form 10-K.

Non-Financial Assets and Liabilities

The Company discloses or recognizes its non-financial assets and liabilities, such as impairments of oil and gas properties and other assets, at fair value on a nonrecurring basis. As none of the Company's non-financial assets and liabilities were impaired as of September 30, 2014 and 2013 and no other assets or liabilities were required to be recognized at fair value on a non-recurring basis, additional disclosures were not provided.

The estimated fair value of the Company's asset retirement obligation at inception is determined by utilizing the income approach by applying a credit-adjusted risk-free rate, which takes into account the Company's credit risk, the time value of money, and the current economic state, to the undiscounted expected abandonment cash flows. Given the unobservable nature of the inputs, the measurement of the asset retirement obligation was classified as Level 3 in the fair value hierarchy.

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Financial Assets and Liabilities

The following fair value hierarchy table presents information about the Company's financial assets and liabilities measured at fair value on a recurring basis:

(In thousands)	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	September 30, 2014
Assets				
Deferred compensation plan	$ 12,815	$ —	$ —	$ 12,815
Derivative contracts	—	1,578	17,867	19,445
Total assets	$ 12,815	$ 1,578	$ 17,867	$ 32,260
Liabilities				
Deferred compensation plan	$ 30,277	$ —	$ —	$ 30,277
Derivative contracts	—	1,216	2,377	3,593
Total liabilities	$ 30,277	$ 1,216	$ 2,377	$ 33,870

(In thousands)	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	December 31, 2013
Assets				
Deferred compensation plan	$ 12,507	$ —	$ —	$ 12,507
Derivative contracts	—	—	13,792	13,792
Total assets	$ 12,507	$ —	$ 13,792	$ 26,299
Liabilities				
Deferred compensation plan	$ 33,211	$ —	$ —	$ 33,211
Derivative contracts	—	6,983	17,702	24,685
Total liabilities	$ 33,211	$ 6,983	$ 17,702	$ 57,896

The Company's investments associated with its deferred compensation plan consist of mutual funds and deferred shares of the Company's common stock that are publicly traded and for which market prices are readily available.

The derivative instruments were measured based on quotes from the Company's counterparties. Such quotes have been derived using an income approach that considers various inputs including current market and contractual prices for the underlying instruments, quoted forward prices for natural gas and crude oil, basis differentials, volatility factors and interest rates, such as a LIBOR curve for a similar length of time as the derivative contract term as applicable. Estimates are verified using relevant NYMEX futures contracts and/or are compared to multiple quotes obtained from counterparties for reasonableness. The determination of the fair values presented above also incorporates a credit adjustment for non-performance risk. The Company measured the non-performance risk of its counterparties by reviewing credit default swap spreads for the various financial institutions with which it has derivative transactions, while non-performance risk of the Company is evaluated using a market credit spread provided by the Company's bank.

The most significant unobservable inputs relative to the Company's Level 3 derivative contracts are basis differentials and volatility factors. An increase (decrease) in these unobservable inputs would result in an increase (decrease) in fair value, respectively. The Company does not have access to the specific assumptions used in its counterparties' valuation models. Consequently, additional disclosures regarding significant Level 3 unobservable inputs were not provided.

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The following table sets forth a reconciliation of changes in the fair value of net financial assets (liabilities) classified as Level 3 in the fair value hierarchy:

	Nine Months Ended September 30,	
(In thousands)	2014	2013
Balance at beginning of period	$(3,910)	$41,159
Total gains (losses) (realized or unrealized):		
Realized and unrealized gains (losses) included in earnings	(33,804)	33,822
Included in other comprehensive income	(21,068)	24,287
Settlements	74,271	(33,822)
Transfers in and/or out of level 3	—	—
Balance at end of period	$15,489	$65,446
Change in unrealized gains (losses) relating to assets and liabilities still held at the end of the period	$40,467	$—

There were no transfers between Level 1 and Level 2 measurements for the three and nine months ended September 30, 2014 and 2013.

Fair Value of Other Financial Instruments

The estimated fair value of financial instruments is the amount at which the instrument could be exchanged currently between willing parties. The carrying amounts reported in the Condensed Consolidated Balance Sheet for cash and cash equivalents, accounts receivable and accounts payable approximate fair value due to the short-term maturities of these instruments.

The Company uses available market data and valuation methodologies to estimate the fair value of debt. The fair value of long-term debt is the estimated amount the Company would have to pay a third party to assume the debt, including a credit spread for the difference between the issue rate and the period end market rate. The credit spread is the Company's default or repayment risk. The credit spread (premium or discount) is determined by comparing the Company's fixed-rate notes and revolving credit facility to new issuances (secured and unsecured) and secondary trades of similar size and credit statistics for both public and private debt. The fair value of all fixed-rate notes and the revolving credit facility is based on interest rates currently available to the Company. The Company's long-term debt is valued using an income approach and classified as Level 3 in the fair value hierarchy due to the unobservable nature of the inputs.

The carrying amounts and fair values of long-term debt are as follows:

	September 30, 2014		December 31, 2013	
(In thousands)	Carrying Amount	Estimated Fair Value	Carrying Amount	Estimated Fair Value
Long-term debt	$1,612,000	$1,697,654	$1,147,000	$1,224,273

7. Asset Retirement Obligation

Activity related to the Company's asset retirement obligation is as follows:

(In thousands)	Nine Months Ended September 30, 2014
Balance at beginning of period	$75,853
Liabilities incurred	4,360
Liabilities settled	(411)
Liabilities divested	(899)
Change in estimate	33,810
Accretion expense	3,528

Balance at end of period	$116,241

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The change in estimate during 2014 is attributable to an increase in costs of materials and services. The increase in cost of materials and services is primarily due to more rigorous plugging and abandonment techniques associated with the Company's horizontal wells in certain areas of its operations and the lack of availability of service providers in areas with minimal activity.

As of both September 30, 2014 and December 31, 2013, approximately $2.0 million is included in accrued liabilities in the Condensed Consolidated Balance Sheet, which represents the current portion of the Company’s asset retirement obligation.

8. Commitments and Contingencies

Contractual Obligations

The Company has various contractual obligations in the normal course of its operations. Except for certain new and amended transportation agreements described below, there have been no material changes to the Company’s contractual obligations described under “Transportation and Gathering Agreements”, “Drilling Rig Commitments” and “Lease Commitments” as disclosed in Note 9 in the Notes to Consolidated Financial Statements included in the Form 10-K.

Transportation and Gathering Agreements

During the first nine months of 2014, the Company entered into or amended certain natural gas transportation agreements associated with the Company’s production in Pennsylvania. These agreements increased the Company’s future aggregate obligations under its transportation commitments by approximately $230.5 million over the next 13 years compared to those amounts disclosed in Note 9 in the Notes to Consolidated Financial Statements included in the Form 10-K.

Legal Matters

The Company is a defendant in various legal proceedings arising in the normal course of business. All known liabilities are accrued when management determines they are probable based on its best estimate of the potential loss. While the outcome and impact of these legal proceedings on the Company cannot be predicted with certainty, management believes that the resolution of these proceedings will not have a material effect on the Company’s financial position, results of operations or cash flows.

Contingency Reserves

When deemed necessary, the Company establishes reserves for certain legal proceedings. The establishment of a reserve is based on an estimation process that includes the advice of legal counsel and subjective judgment of management. While management believes these reserves to be adequate, it is reasonably possible that the Company could incur additional losses with respect to those matters in which reserves have been established. The Company believes that any such amount above the amounts accrued is not material to the Condensed Consolidated Financial Statements. Future changes in facts and circumstances not currently foreseeable could result in the actual liability exceeding the estimated ranges of loss and amounts accrued.

9. Postretirement Benefits

The components of net periodic benefit costs, included in general and administrative expense in the Condensed Consolidated Statement of Operations, were as follows:

	Three Months Ended September 30,		Nine Months Ended September 30,	
(In thousands)	2014	2013	2014	2013
Service cost	$456	$455	$1,368	$1,285
Interest cost	407	355	1,221	1,145
Amortization of net loss	—	116	—	525
	$863	$926	$2,589	$2,955

The guidance for retirement benefits provides that the net actuarial loss is not amortized if it is less than 10% of the postretirement obligation. Accordingly, the Company does not expect to amortize its net actuarial loss from accumulated other comprehensive income (loss) during 2014.

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10. Stock-based Compensation

General

Stock-based compensation expense during the first nine months of 2014 and 2013 was $15.1 million and $41.0 million, respectively, and is included in general and administrative expense in the Condensed Consolidated Statement of Operations. Stock-based compensation expense in the third quarter of 2014 and 2013 was $5.7 million and $12.2 million, respectively.

During the first nine months of 2014 and 2013, the Company realized a $6.0 million and $9.3 million tax benefit, respectively, related to the federal tax deduction in excess of book compensation cost for employee stock-based compensation. The Company is able to recognize this tax benefit only to the extent it reduces the Company’s income taxes payable.

Refer to Note 13 of the Notes to the Consolidated Financial Statements in the Form 10-K for further description of the various types of stock-based compensation awards and the applicable award terms.

Restricted Stock Awards

During the first nine months of 2014, 46,000 restricted stock awards were granted to employees with a weighted-average grant date per share value of $34.96. The fair value of restricted stock grants is based on the average of the high and low stock price on the grant date. The Company used an annual forfeiture rate assumption of 5.0% for purposes of recognizing stock-based compensation expense for restricted stock awards.

Restricted Stock Units

During the first nine months of 2014, 35,870 restricted stock units were granted to non-employee directors of the Company with a weighted-average grant date per unit value of $38.73. The fair value of these units is measured based on the average of the high and low stock price on grant date and compensation expense is recorded immediately. These units immediately vest and are issued when the director ceases to be a director of the Company.

Performance Share Awards

The performance period for the awards granted in 2014 commenced on January 1, 2014 and ends on December 31, 2016. The Company used an annual forfeiture rate assumption ranging from 0% to 5% for purposes of recognizing stock-based compensation expense for its performance share awards.

Performance Share Awards Based on Internal Performance Metrics

The fair value of performance award grants based on internal performance metrics is based on the average of the high and low stock price on the grant date and represents the right to receive up to 100% of the award in shares of common stock.

Employee Performance Share Awards. During the first nine months of 2014, 241,130 Employee Performance Share Awards were granted at a grant date per share value of $39.43. The performance metrics are set by the Company’s Compensation Committee and are based on the Company’s average production, average finding costs and average reserve replacement over a three-year performance period. Based on the Company’s probability assessment at September 30, 2014, it is considered probable that the criteria for these awards will be met.

Hybrid Performance Share Awards. During the first nine months of 2014, 123,257 Hybrid Performance Share Awards were granted at a grant date per share value of $39.43. The 2014 awards vest 25% on each of the first and second anniversary dates and 50% on the third anniversary, provided that the Company has $100 million or more of operating cash flow for the year preceding the vesting date, as set by the Company’s Compensation Committee. If the Company does not meet the performance metric for the applicable period, then the portion of the performance shares that would have been issued on that anniversary date will be forfeited. Based on the Company’s probability assessment at September 30, 2014, it is considered probable that the criteria for these awards will be met.

Performance Share Awards Based on Market Conditions

These awards have both an equity and liability component, with the right to receive up to the first 100% of the award in shares of common stock and the right to receive up to an additional 100% of the value of the award in excess of the equity component in cash. The Company calculates the fair value of these awards using a Monte Carlo simulation model. The equity component of these awards is valued on the grant date and is not marked to market, while the liability component of the awards is valued as of the end of each reporting period on a mark-to-market basis.

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TSR Performance Share Awards. During the first nine months of 2014, 184,885 TSR Performance Share Awards were granted and are earned, or not earned, based on the comparative performance of the Company's common stock measured against fourteen other companies in the Company's peer group over a three-year performance period.

The following assumptions were used to determine the grant date fair value of the equity component (February 20, 2014) and the period-end fair value of the liability component of the TSR Performance Share Awards:

	Grant Date	September 30, 2014
Fair value per performance share award	$32.04	$7.19 - $25.22
Assumptions:		
Stock price volatility	41.3 %	27.5% - 120.4%
Risk free rate of return	0.7 %	0.02% - 0.7%
Expected dividend yield	0.2 %	0.2 %

Supplemental Employee Incentive Plan

The Company recognized stock-based compensation expense of $0.2 million and $4.1 million for the three months ended September 30, 2014 and 2013, respectively, and $3.3 million and $9.2 million for the nine months ended September 30, 2014 and 2013, respectively, related to the Company's Supplemental Employee Incentive Plans, which is included in general and administrative expense in the Condensed Consolidated Statement of Operations. In August 2014, the Company paid $13.0 million associated with amounts that were previously deferred in accordance with the Company's Supplemental Employee Incentive Plan III. Refer to Note 13 of the Notes to the Consolidated Financial Statements in the Form 10-K for additional information on the provisions of the Plan.

The following assumptions were used to determine the period-end fair value of the Supplemental Employee Incentive Plan IV liability using a Monte Carlo model:

	September 30, 2014
Stock price volatility	33.9 %
Risk free rate of return	1.0 %
Annual salary increase rate	4.0 %
Annual turnover rate	4.6 %

11. Earnings per Common Share

Basic EPS is computed by dividing net income by the weighted-average number of common shares outstanding for the period. Diluted EPS is similarly calculated except that the common shares outstanding for the period is increased using the treasury stock method to reflect the potential dilution that could occur if outstanding stock appreciation rights were exercised and stock awards were vested at the end of the applicable period.

	Three Months Ended September 30,		Nine Months Ended September 30,	
(In thousands)	2014	2013	2014	2013
Weighted-average shares - basic	416,173	420,986	416,785	420,664
Dilution effect of stock appreciation rights and stock awards at end of period	1,920	2,467	1,683	2,160
Weighted-average shares - diluted	418,093	423,453	418,468	422,824
Weighted-average stock awards and shares excluded from diluted earnings per share due to the anti-dilutive effect	—	1	461	3

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12. Accumulated Other Comprehensive Income (Loss)

Changes in accumulated other comprehensive income (loss) by component, net of tax, were as follows:

(In thousands)	Net Gain (Loss) on Cash Flow Hedges	Postretirement Benefits	Total
Balance at December 31, 2013	$(6,551)	$(1,810)	$(8,361)
Other comprehensive income before reclassifications	(80,175)	—	(80,175)
Amounts reclassified from accumulated other comprehensive income	69,337	—	69,337
Net current-period other comprehensive income	(10,838)	—	(10,838)
Balance at September 30, 2014	$(17,389)	$(1,810)	$(19,199)

Amounts reclassified from accumulated other comprehensive income (loss) into the Condensed Consolidated Statement of Operations were as follows:

	Three Months Ended September 30,		Nine Months Ended September 30,		Affected Line Item in the Condensed
(In thousands)	2014	2013	2014	2013	Consolidated Statement of Operations
Net gain (loss) on cash flow hedges					
Commodity contracts	$(21,427)	$20,766	$(114,304)	$33,822	