

MURPHY OIL CORP /DE
Form 10-Q
November 02, 2016

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

For the quarterly period ended September 30, 2016

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 1-8590

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MURPHY OIL CORPORATION

(Exact name of registrant as specified in its charter)

Delaware
(State or other jurisdiction of incorporation or organization)

71-0361522
(I.R.S. Employer Identification Number)

300 Peach Street, P.O. Box 7000,
El Dorado, Arkansas
(Address of principal executive offices)

71731-7000
(Zip Code)

(870) 862-6411
(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 (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 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

Number of shares of Common Stock, \$1.00 par value, outstanding at September 30, 2016 was 172,200,075.

MURPHY OIL CORPORATION

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PART I – FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS

Murphy Oil Corporation and Consolidated Subsidiaries

CONSOLIDATED BALANCE SHEETS (unaudited)

(Thousands of dollars)

	September 30, 2016	December 31, 2015
ASSETS		
Current assets		
Cash and cash equivalents	\$ 753,093	283,183
Canadian government securities with maturities greater than 90 days at the date of acquisition	117,938	173,288
Accounts receivable, less allowance for doubtful accounts of \$1,605 in 2016 and 2015	400,532	522,672
Inventories, at lower of cost or market		
Crude oil	11,196	25,583
Materials and supplies	151,107	141,205
Prepaid expenses	90,401	212,962
Deferred income taxes	50,879	51,183
Assets held for sale	29,978	38,340
Total current assets	1,605,124	1,448,416
Property, plant and equipment, at cost less accumulated depreciation, depletion and amortization of \$12,425,414 in 2016 and \$11,924,193 in 2015	8,440,336	9,818,365
Deferred charges and other assets	348,555	227,031
Total assets	\$ 10,394,015	11,493,812
LIABILITIES AND STOCKHOLDERS' EQUITY		
Current liabilities		
Current maturities of long-term debt	\$ 20,444	18,881
Accounts payable and accrued liabilities	876,664	1,643,632
Income taxes payable	13,817	4,819
Liabilities associated with assets held for sale	3,276	7,297
Total current liabilities	914,201	1,674,629
Long-term debt, including capital lease obligation	2,973,888	3,040,594
Deferred income taxes	50,244	239,811
Asset retirement obligations	748,576	793,474

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Deferred credits and other liabilities	621,518	438,576
Stockholders' equity		
Cumulative Preferred Stock, par \$100, authorized 400,000 shares, none issued	—	—
Common Stock, par \$1.00, authorized 450,000,000 shares, issued 195,055,724 shares in 2016 and 2015	195,056	195,056
Capital in excess of par value	921,675	910,074
Retained earnings	5,836,567	6,212,201
Accumulated other comprehensive loss	(571,031)	(704,542)
Treasury stock, 22,855,649 shares of Common Stock in 2016 and 23,021,013 shares of Common Stock in 2015, at cost	(1,296,679)	(1,306,061)
Total stockholders' equity	5,085,588	5,306,728
Total liabilities and stockholders' equity	\$ 10,394,015	11,493,812

See Notes to Consolidated Financial Statements, page 7.

The Exhibit Index is on page 35.

Murphy Oil Corporation and Consolidated Subsidiaries

CONSOLIDATED STATEMENTS OF OPERATIONS (unaudited)

(Thousands of dollars, except per share amounts)

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2016	2015	2016	2015
REVENUES				
Sales and other operating revenues	\$ 486,276	665,589	1,326,587	2,133,360
Gain (loss) on sale of assets	(730)	60	3,101	154,183
Interest and other income	14,987	49,300	38,602	87,443
Total revenues	500,533	714,949	1,368,290	2,374,986
COSTS AND EXPENSES				
Lease operating expenses	119,663	183,826	435,296	643,736
Severance and ad valorem taxes	9,592	14,265	35,668	54,099
Exploration expenses, including undeveloped lease amortization	19,866	58,149	83,910	251,842
Selling and general expenses	55,523	71,791	196,143	237,934
Depreciation, depletion and amortization	255,900	433,706	797,288	1,318,123
Impairment of assets	–	2,300,974	95,088	2,300,974
Accretion of asset retirement obligations	11,043	11,918	35,514	35,437
Interest expense	40,088	32,009	107,207	91,945
Interest capitalized	(869)	(1,864)	(3,318)	(5,072)
Other expense (benefit)	6,486	18,192	(1,446)	81,804
Total costs and expenses	517,292	3,122,966	1,781,350	5,010,822
Loss from continuing operations before income taxes	(16,759)	(2,408,017)	(413,060)	(2,635,836)
Income tax benefit	(2,176)	(820,935)	(201,897)	(963,298)
Loss from continuing operations	(14,583)	(1,587,082)	(211,163)	(1,672,538)
Loss from discontinued operations, net of income taxes	(1,593)	(8,344)	(885)	(11,163)
NET LOSS	\$ (16,176)	(1,595,426)	(212,048)	(1,683,701)
PER COMMON SHARE – BASIC				
Loss from continuing operations	\$ (0.08)	(9.22)	(1.23)	(9.55)
Loss from discontinued operations	(0.01)	(0.04)	(0.01)	(0.07)
Net loss	\$ (0.09)	(9.26)	(1.24)	(9.62)
PER COMMON SHARE – DILUTED				
Loss from continuing operations	\$ (0.08)	(9.22)	(1.23)	(9.55)
Loss from discontinued operations	(0.01)	(0.04)	(0.01)	(0.07)
Net loss	\$ (0.09)	(9.26)	(1.24)	(9.62)
Average Common shares outstanding				

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Basic	172,199,350	172,205,433	172,164,683	175,047,295
Diluted	172,199,350	172,205,433	172,164,683	175,047,295

See Notes to Consolidated Financial Statements, page 7.

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Murphy Oil Corporation and Consolidated Subsidiaries

CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME (LOSS) (unaudited)

(Thousands of dollars)

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2016	2015	2016	2015
Net loss	\$ (16,176)	(1,595,426)	(212,048)	(1,683,701)
Other comprehensive income (loss), net of tax				
Net gain (loss) from foreign currency translation	(37,369)	(195,440)	124,522	(462,054)
Retirement and postretirement benefit plans	2,515	3,116	7,544	9,105
Deferred loss on interest rate hedges reclassified to interest expense	482	482	1,445	1,445
Other comprehensive income (loss)	(34,372)	(191,842)	133,511	(451,504)
COMPREHENSIVE LOSS	\$ (50,548)	(1,787,268)	(78,537)	(2,135,205)

See Notes to Consolidated Financial Statements, page 7.

Murphy Oil Corporation and Consolidated Subsidiaries

CONSOLIDATED STATEMENTS OF CASH FLOWS (unaudited)

(Thousands of dollars)

	Nine Months Ended September 30,	
	2016	2015
OPERATING ACTIVITIES		
Net loss	\$ (212,048)	(1,683,701)
Adjustments to reconcile net loss to net cash provided by continuing operations activities:		
Loss from discontinued operations	885	11,163
Depreciation, depletion and amortization	797,288	1,318,123
Impairment of assets	95,088	2,300,974
Amortization of deferred major repair costs	3,794	5,450
Dry hole costs	15,226	120,459
Amortization of undeveloped leases	35,828	62,331
Accretion of asset retirement obligations	35,514	35,437
Deferred and noncurrent income tax benefits	(345,157)	(975,120)
Pretax gains from disposition of assets	(3,101)	(154,183)
Net (increase) decrease in noncash operating working capital	(152,618) 1	97,026
Other operating activities, net	9,651	(41,431)
Net cash provided by continuing operations activities	280,350	1,096,528
INVESTING ACTIVITIES		
Property additions and dry hole costs	(781,668) 2	(1,975,069)
Proceeds from sales of property, plant and equipment	1,154,623	423,842
Purchase of investment securities ³	(651,218)	(865,251)
Proceeds from maturity of investment securities ³	712,863	852,394
Other investing activities, net	(7,229)	(19,538)
Net cash provided (required) by investing activities	427,371	(1,583,622)
FINANCING ACTIVITIES		
Borrowings of debt	541,444	885,000
Repayments of debt	(600,000)	(450,000)
Capital lease obligation payments	(7,808)	(7,156)
Purchase of treasury stock	—	(250,000)
Withholding tax on stock-based incentive awards	(1,138)	(8,976)
Issue cost of debt facility	(13,971)	—
Cash dividends paid	(163,586)	(184,789)
Other financing activities, net	(20)	(153)
Net cash required by financing activities	(245,079)	(16,074)
CASH FLOWS FROM DISCONTINUED OPERATIONS		
Operating activities	2,830	(4,866)
Investing activities	—	5,343
Changes in cash included in current assets held for sale	(2,830)	179,774

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Net increase in cash and cash equivalents of discontinued operations	–	180,251
Effect of exchange rate changes on cash and cash equivalents	7,268	8,276
Net increase (decrease) in cash and cash equivalents	469,910	(314,641)
Cash and cash equivalents at January 1	283,183	1,193,308
Cash and cash equivalents at September 30	\$ 753,093	878,667

12016 balance includes payments for deepwater rig contract exit of \$266.6 million.

2Includes costs of \$206.7 million associated with acquisition of Kaybob Duvernay and Placid Montney.

3Investments are Canadian government securities with maturities greater than 90 days at the date of acquisition.

See Notes to Consolidated Financial Statements, page 7.

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Murphy Oil Corporation and Consolidated Subsidiaries

CONSOLIDATED STATEMENTS OF STOCKHOLDERS' EQUITY (unaudited)

(Thousands of dollars)

	Nine Months Ended September 30,	
	2016	2015
Cumulative Preferred Stock – par \$100, authorized 400,000 shares, none issued	\$ –	–
Common Stock – par \$1.00, authorized 450,000,000 shares, issued 195,055,724 shares at September 30, 2016 and September 30, 2015		
Balance at beginning of period	195,056	195,040
Exercise of stock options	–	16
Balance at end of period	195,056	195,056
Capital in Excess of Par Value		
Balance at beginning of period	910,074	906,741
Exercise of stock options, including income tax benefits	–	(73)
Restricted stock transactions and other	(10,078)	(38,260)
Stock-based compensation	21,918	33,925
Other	(239)	(92)
Balance at end of period	921,675	902,241
Retained Earnings		
Balance at beginning of period	6,212,201	8,728,032
Net loss for the period	(212,048)	(1,683,701)
Cash dividends	(163,586)	(184,789)
Balance at end of period	5,836,567	6,859,542
Accumulated Other Comprehensive Loss		
Balance at beginning of period	(704,542)	(170,255)
Foreign currency translation gain (loss), net of income taxes	124,522	(462,054)
Retirement and postretirement benefit plans, net of income taxes	7,544	9,105
Deferred loss on interest rate hedges reclassified to interest expense, net of income taxes	1,445	1,445
Balance at end of period	(571,031)	(621,759)
Treasury Stock		
Balance at beginning of period	(1,306,061)	(1,086,124)
Purchase of treasury shares	–	(250,000)

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Sale of stock under employee stock purchase plans	389	322
Awarded restricted stock, net of forfeitures	8,993	29,176
Balance at end of period – 22,855,649 shares of Common Stock in 2016 and 22,303,782 shares of Common Stock in 2015, at cost	(1,296,679)	(1,306,626)
Total Stockholders' Equity	\$ 5,085,588	6,028,454

See Notes to Consolidated Financial Statements, page 7.

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

These notes are an integral part of the financial statements of Murphy Oil Corporation and Consolidated Subsidiaries (Murphy/the Company) on pages 2 through 6 of this Form 10-Q report.

Note A – Nature of Business and Interim Financial Statements

NATURE OF BUSINESS – Murphy Oil Corporation is an international oil and gas company that conducts its business through various operating subsidiaries. The Company produces oil and natural gas in the United States, Canada and Malaysia and conducts oil and natural gas exploration activities worldwide. The Company sold its interest in a Canadian synthetic oil operation in the second quarter of 2016. The Company acquired 70% interest in Duvernay Shale and a 30% interest in liquids rich Montney properties during the second quarter 2016.

INTERIM FINANCIAL STATEMENTS – In the opinion of Murphy's management, the unaudited financial statements presented herein include all accruals necessary to present fairly the Company's financial position at September 30, 2016 and December 31, 2015, and the results of operations, cash flows and changes in stockholders' equity for the interim periods ended September 30, 2016 and 2015, in conformity with accounting principles generally accepted in the United States of America (U.S.). In preparing the financial statements of the Company in conformity with accounting principles generally accepted in the U.S., management has made a number of estimates and assumptions related to the reporting of assets, liabilities, revenues, and expenses and the disclosure of contingent assets and liabilities. Actual results may differ from the estimates.

Financial statements and notes to consolidated financial statements included in this Form 10-Q report should be read in conjunction with the Company's 2015 Form 10-K report, as certain notes and other pertinent information have been abbreviated or omitted in this report. Financial results for the nine-month period ended September 30, 2016 are not necessarily indicative of future results.

Note B – Property, Plant and Equipment

Under U.S. generally accepted accounting principles for companies that use the successful efforts method of accounting, exploratory well costs should continue to be capitalized when the well has found a sufficient quantity of reserves to justify its completion as a producing well and the company is making sufficient progress assessing the reserves and the economic and operating viability of the project.

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At September 30, 2016, the Company had total capitalized exploratory well costs pending the determination of proved reserves of \$128.2 million. The following table reflects the net changes in capitalized exploratory well costs during the

nine-month periods ended September 30, 2016 and 2015.

(Thousands of dollars)	2016	2015
Beginning balance at January 1	\$ 130,514	120,455
Additions pending the determination of proved reserves	847	89,197
Other adjustments	(3,205)	–
Balance at September 30	\$ 128,156	209,652

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Contd.)

Note B – Property, Plant and Equipment (Contd.)

The following table provides an aging of capitalized exploratory well costs based on the date the drilling was completed for each individual well and the number of projects for which exploratory well costs have been capitalized. The projects are aged based on the last well drilled in the project.

(Thousands of dollars)	September 30, 2016			2015		
	Amount	No. of Wells	No. of Projects	Amount	No. of Wells	No. of Projects
Aging of capitalized well costs:						
Zero to one year	\$ 10,563	2	2	\$ 52,249	5	3
One to two years	53,101	3	3	32,192	2	1
Two to three years	31,627	2	–	27,842	2	–
Three years or more	32,865	4	–	97,369	4	2
	\$ 128,156	11	5	\$ 209,652	13	6

Of the \$117.6 million of exploratory well costs capitalized more than one year at September 30, 2016, \$64.5 million is in Brunei, \$31.4 million is in Vietnam and \$21.7 million is in Malaysia. In all geographical areas, either further appraisal or development drilling is planned and/or development studies/plans are in various stages of completion.

In April 2016, a Canadian subsidiary of the Company signed a purchase and sale agreement for the sale of its five percent, non-operated working interest in Syncrude Canada Ltd. (“Syncrude”) asset to Suncor Energy Inc. (“Suncor”), subject to closing adjustments. The sale was completed in June 2016 and the Company received net cash proceeds of \$739.1 million. The Company recorded an after-tax gain of \$71.7 million in the second quarter of 2016 associated with the Syncrude divestiture.

In April 2016, a Canadian subsidiary of the Company completed its transaction to divest natural gas processing and sales pipeline assets that support Murphy’s Montney natural gas fields in the Tupper area of northeastern British Columbia. Total cash consideration received by Murphy upon closing of the transaction was \$414.1 million. A gain on sale of approximately \$187 million is being deferred and recognized over the next 20 years in the Canadian operating segment. The Company has amortized \$3.4 million of the deferred gain during 2016. The remaining deferred gain is included as a component of deferred credits and other liabilities on the Company’s Consolidated Balance Sheet.

In a separate transaction, the same Canadian subsidiary signed a definitive agreement to acquire a 70 percent operated working interest (WI) of Athabasca Oil Corporation's (Athabasca) production, acreage, infrastructure and facilities in the Kaybob Duvernay lands, and a 30 percent non-operated WI of Athabasca's production, acreage, infrastructure and facilities in the liquids rich Montney lands in Alberta, the majority of which is unproved. Under the terms of the joint venture the total consideration amounts to approximately \$375 million, of which Murphy paid \$206.7 million in cash at closing, subject to normal closing adjustments, and the remaining \$168.0 million in the form of a carried interest for a period of up to five years. The transaction closed in the second quarter of 2016.

During the first quarter of 2016, declines in crude oil and natural gas prices from year end 2015 provided indications of possible impairments in certain of the company's producing properties. As a result of management's assessments, the Company recognized pretax non-cash impairments charges of \$95.1 million in the nine-month period ended September 30, 2016, to reduce the carrying value to their estimated fair value for its Terra Nova field offshore Canada and its Western Canada onshore heavy oil producing properties. The fair values were determined by internal discounted cash flow models using estimates of future production, prices from futures exchanges, estimates of future costs, and a discount rate believed to be consistent with those used by principal market participants in the region.

During the third quarter 2015, declines in future oil and gas prices provided indications of possible impairments in certain of the Company's producing properties. As a result of management's assessments, during the third quarter of 2015, the Company recognized a pretax noncash impairment charge of approximately \$2.3 billion to reduce the carrying value of certain producing properties in the Gulf of Mexico, Western Canada and Malaysia to their estimated fair value. The fair values were determined by internal discounted cash flow models using estimates of future production, prices from futures exchanges, estimates of future costs, and a discount rate believed to be consistent with those used by principal market participants in the applicable region.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Contd.)

Note B – Property, Plant and Equipment (Contd.)

During 2015, the Company completed the second phase of the sale of 30% of its oil and gas assets in Malaysia and received net cash proceeds of \$417.2 million. The Company recorded an after-tax gain of \$218.8 million on the sale of the final 10% portion of the total 30% sold.

Note C – Discontinued Operations

The Company has accounted for its U.K. refining and marketing operations as discontinued operations for all periods presented. The Company completed its agreement to sell the remaining U.K. downstream assets at the end of the second quarter of 2015. The 2015 nine-month period includes an adjustment to the impairment recognized as a result of the final sale of the U.K. downstream assets.

The results of operations associated with discontinued operations for the three-month and nine-month periods ended September 30, 2016 and 2015 were as follows:

	Three Months Ended September 30,		Nine Months Ended September 30,	
(Thousands of dollars)	2016	2015	2016	2015
Revenues (costs)	\$ (1,345)	(1,342)	(510)	381,154
Loss before income taxes	\$ (1,593)	(8,366)	(885)	(8,029)
Income tax (benefit) expense	–	(22)	–	3,134
Loss from discontinued operations	\$ (1,593)	(8,344)	(885)	(11,163)

The following table presents the carrying value of the major categories of assets and liabilities of U.K. refining and marketing operations reflected as held for sale on the Company's Consolidated Balance Sheets at September 30, 2016 and December 31, 2015.

(Thousands of dollars)	September 30, 2016	December 31, 2015
Current assets		
Cash	\$ 5,097	7,927
Accounts receivable	9,001	12,037
Other	15,880	18,376
Total current assets held for sale	\$ 29,978	38,340
Current liabilities		
Accounts payable	\$ 915	2,433
Accrued compensation and severance	-	2,179
Refinery decommissioning cost	2,361	2,685
Total current liabilities associated with assets held for sale	\$ 3,276	7,297

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Contd.)

Note D – Financing Arrangements and Debt

In August 2016 the Company reduced its existing \$2.0 billion unsecured revolving credit facility (“2011 facility”) to \$630 million and entered into a separate \$1.2 billion senior unsecured guaranteed credit facility (“2016 facility”) with a major banking consortium that expires in August 2019. Facility fees of 0.5% are charged annually on the full \$1.2 billion commitment. The Company incurred transaction costs of approximately \$14.0 million to place the 2016 facility which are included in financing activities in the Consolidated Statement of Cash Flows. At September 30, 2016, the Company had no outstanding borrowings under either credit facility, however, there was approximately \$88 million of issued letters of credit under the 2016 facility. The 2016 facility is unsecured, with guarantees from certain domestic and foreign subsidiaries. Should the Company make substantial asset sales, the facility size would be automatically reduced to a minimum of \$1.0 billion. Borrowings under the 2016 facility are subject to varying interest rates ranging from LIBOR plus 250 basis points to LIBOR plus 450 basis points. The terms of the 2016 facility include covenants that impose certain restrictions on the Company. These financial covenants include a minimum adjusted EBITDAX of 2.5 times consolidated interest expense, consolidated debt not to exceed 3.75 times adjusted EBITDAX and minimum liquidity from U.S. and Canadian entities equal to or greater than \$500 million. Also beginning March 31, 2017, if the Company’s total leverage ratio exceeds 3.25 times the Company’s trailing twelve month consolidated adjusted EBITDAX, as defined in the 2016 facility, the facility will become secured, subject to limitations set forth in the Company’s existing notes. The existing unsecured 2011 facility, which expires in June 2017, includes a financial covenant under which the Company may not have total debt in excess of 60% of its total capital employed (debt borrowed plus stockholders’ equity). As of September 30, 2016, the Company was in compliance with all financial covenants contained in both credit facilities. The Company also has a shelf registration statement on file with the U.S. Securities and Exchange Commission that permits the offer and sale of debt and/or equity securities through October 2018.

In August 2016, the Company sold \$550 million of new notes that bear interest at the rate of 6.875% and mature on August 15, 2024. The new notes pay interest semi-annually on February 15 and August 15 of each year. The initial interest payment is to be made on February 15, 2017. The proceeds of the \$550 million notes were used for general corporate purposes.

The Company and its partners are parties to a 25-year lease of production equipment at the Kakap field offshore Malaysia. The lease has been accounted for as a capital lease, and payments under the agreement are to be made over a 15-year period through September 2028. Current maturities and long-term debt on the Consolidated Balance Sheet included \$20.4 million and \$202.7 million, respectively, associated with this lease at September 30, 2016.

Note E – Cash Flow Disclosures

Additional disclosures regarding cash flow activities are provided below.

(Thousands of dollars)	Nine Months Ended	
	September 30,	
	2016	2015
Net (increase) decrease in operating working capital other than cash and cash equivalents:		
Decrease in accounts receivable	\$ 75,841	389,413
Increase in inventories	(15,768)	(16,607)
Decrease (increase) in prepaid expenses	122,399	(87,051)
Decrease in deferred income tax assets	720	4,863
Decrease in accounts payable and accrued liabilities	(376,310)	(134,458)
Increase (decrease) in current income tax liabilities	40,500	(59,134)
Net (increase) decrease in noncash operating working capital	\$ (152,618)	97,026
Supplementary disclosures:		
Cash income taxes paid (refunded), net	\$ (3,911)	111,897
Interest paid, net of amounts capitalized	52,287	60,766
Non-cash investing activities:		
Asset retirement costs capitalized	\$ 13,959	55,258
Decrease in capital expenditure accrual	179,203	374,720

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Contd.)

Note F – Employee and Retiree Benefit Plans

The Company has defined benefit pension plans that are principally noncontributory and cover most full-time employees. All pension plans are funded except for the U.S. and Canadian nonqualified supplemental plans and the U.S. directors' plan. All U.S. tax qualified plans meet the funding requirements of federal laws and regulations. Contributions to foreign plans are based on local laws and tax regulations. The Company also sponsors health care and life insurance benefit plans, which are not funded, that cover most active and retired U.S. employees. Additionally, most U.S. retired employees are covered by a life insurance benefit plan. The health care benefits are contributory; the life insurance benefits are noncontributory.

The table that follows provides the components of net periodic benefit expense for the three-month and nine-month periods ended September 30, 2016 and 2015.

(Thousands of dollars)	Three Months Ended September 30,			
	Pension Benefits		Other Postretirement Benefits	
	2016	2015	2016	2015
Service cost	\$ 2,610	5,898	674	826
Interest cost	5,913	8,972	1,109	1,192
Expected return on plan assets	(6,626)	(10,471)	–	–
Amortization of prior service cost	323	187	(21)	(21)
Amortization of transitional asset	–	402	2	2
Recognized actuarial loss	3,617	3,885	38	193
Net periodic benefit expense	\$ 5,837	8,873	1,802	2,192
(Thousands of dollars)	Nine Months Ended September 30,			
	Pension Benefits		Other Postretirement Benefits	
	2016	2015	2016	2015
Service cost	\$ 8,533	15,751	2,022	2,482
Interest cost	20,386	24,893	3,324	3,576
Expected return on plan assets	(21,709)	(27,882)	–	–
Amortization of prior service cost	963	580	(62)	(62)
Amortization of transitional asset	–	947	4	5
Recognized actuarial loss	10,864	11,667	113	578
	19,037	25,956	5,401	6,579

Special termination benefits	–	8,606	(19)	–
Curtailments	822	306	–	–
Net periodic benefit expense	\$ 19,859	34,868	5,382	6,579

Curtailment expense for the nine months ended September 30, 2016 shown in the table above, relates to restructuring activities in the U.S. undertaken by the Company in the first quarter 2016. Termination and curtailment expenses for the nine months ended September 30, 2015 relate to restructuring activities in the U.S. undertaken by the Company in the second quarter 2015. During the nine-month period ended September 30, 2016, the Company made contributions of \$10.0 million to its defined benefit pension and postretirement benefit plans. Remaining required funding in 2016 for the Company's defined benefit pension and postretirement benefit plans is anticipated to be \$2.9 million.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Contd.)

Note G – Incentive Plans

The costs resulting from all share-based payment transactions are recognized as an expense in the Consolidated Statements of Operations using a fair value-based measurement method over the periods that the awards vest.

The 2012 Annual Incentive Plan (2012 Annual Plan) authorizes the Executive Compensation Committee (the Committee) to establish specific performance goals associated with annual cash awards that may be earned by officers, executives and other key employees. Cash awards under the 2012 Annual Plan are determined based on the Company's actual financial and operating results as measured against the performance goals established by the Committee. The 2012 Long-Term Incentive Plan (2012 Long-Term Plan) authorizes the Committee to make grants of the Company's Common Stock and other stock-based incentives to employees. These grants may be in the form of stock options (nonqualified or incentive), stock appreciation rights (SAR), restricted stock, restricted stock units (RSU), performance units, performance shares, dividend equivalents and other stock-based incentives. The 2012 Long-Term Plan expires in 2022. A total of 8,700,000 shares are issuable during the life of the 2012 Long-Term Plan, with annual grants limited to 1% of Common shares outstanding. The Company has an Employee Stock Purchase Plan that permits the issuance of up to 980,000 shares through September 30, 2017. The Company also has a Stock Plan for Non-Employee Directors that permits the issuance of restricted stock and stock options or a combination thereof to the Company's Directors.

In February 2016, the Committee granted stock options for 862,000 shares at an exercise price of \$17.57 per share. The Black-Scholes valuation for these awards was \$5.03 per option. The Committee also granted 394,000 performance-based RSU and 417,500 time-based RSU in February and April 2016. The fair value of the performance-based RSU, using a Monte Carlo valuation model, ranged from \$12.21 to \$16.34 per unit. The fair values of time-based RSU was estimated based on the fair market value of the Company's stock on the date of grant, which ranged from \$17.57 to 24.075 per share. Additionally, the Committee granted 708,200 SAR and 507,470 units of cash-settled RSU (RSU-C) to certain employees in 2016. The SAR and RSU-C are to be settled in cash, net of applicable income taxes, and are accounted for as liability-type awards. The initial fair value of these SAR was equivalent to the stock options granted, while the initial value of RSU-C was equivalent to equity-settled restricted stock units granted. Also in February 2016, the Committee granted 85,679 shares of time-based RSU to the Company's Directors under the Non-employee Director Plan. These shares vest on the third anniversary of the date of grant. The estimated fair value of these awards was \$19.26 per unit on date of grant.

Amounts recognized in the financial statements with respect to share-based plans are as follows:

(Thousands of dollars)	Nine Months Ended September 30,	
	2016	2015
Compensation charged against income before tax benefit	\$ 35,948	30,722
Related income tax benefit recognized	11,796	9,046

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Contd.)

Note H – Earnings per Share

Net loss was used as the numerator in computing both basic and diluted income per Common share for the three-month and nine-month periods ended September 30, 2016 and 2015. The following table reconciles the weighted-average shares outstanding used for these computations.

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2016	2015	2016	2015
(Weighted-average shares)				
Basic method	172,199,350	172,205,433	172,164,683	175,047,295
Dilutive stock options*	—	—	—	—
Diluted method	172,199,350	172,205,433	172,164,683	175,047,295

*Due to a net loss recognized by the Company for the three-month and nine-month periods ended September 30, 2016 and 2015, no unvested stock awards were included in the computation of diluted earnings per share because the effect would have been anti-dilutive.

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2016	2015	2016	2015
Antidilutive stock options excluded from diluted shares	5,884,201	5,807,453	5,822,036	5,770,731
Weighted average price of these options	\$ 49.00	53.13	49.82	53.25

Note I – Income Taxes

The Company's effective income tax rate is calculated as the amount of income tax expense (benefit) divided by income (loss) before income taxes. For the three-month and nine-month periods in 2016 and 2015, the Company's effective income tax rates were as follows:

	2016	2015
Three months ended September 30	13.0%	34.1%
Nine months ended September 30	48.9%	36.6%

The effective tax rates for most periods differ from the U.S. statutory tax rate of 35% due to several factors, including: the effects of income generated in foreign tax jurisdictions, certain of which have income tax rates that are higher than the U.S. Federal rate; U.S. state tax expense; and certain expenses, including exploration and other expenses in certain foreign jurisdictions, for which no income tax benefits are available or are not presently being recorded due to a lack of reasonable certainty of adequate future revenue against which to utilize these expenses as deductions. Conversely, the effective tax rates for most periods where losses are incurred generally are lower than U.S. statutory tax rate of 35% due to similar reasons. The effective tax rate for the three-month period ended September 30, 2016 was less than the U.S. statutory tax rate primarily due to expenses in foreign jurisdictions for which no tax benefits were recognized. The effective tax rate for the nine-month period ended September 30, 2016 was above the U.S. statutory tax rate primarily due to deferred tax benefits recognized related to the Canadian asset dispositions and income tax benefits on investments in foreign areas. The effective tax rate for the three-month period ended September 30, 2015 was less than the U.S. statutory tax rate primarily due to a deferred tax expense associated with an enacted increase in the statutory tax rate in Alberta. The effective tax rate for the nine-month period ended September 30, 2015 was above the U.S. statutory tax rate primarily due to a deferred tax benefit associated with the sale of Malaysian assets, partially offset by expenses in foreign jurisdictions for which no tax benefits were recognized and the enacted increase in statutory rate in Alberta.

The Company's tax returns in multiple jurisdictions are subject to audit by taxing authorities. These audits often take years to complete and settle. Although the Company believes that recorded liabilities for unsettled issues are adequate, additional gains or losses could occur in future years from resolution of outstanding unsettled matters. As of September 30, 2016, the earliest years remaining open for audit and/or settlement in our major taxing jurisdictions are as follows: United States – 2011; Canada – 2008; Malaysia – 2009; and United Kingdom – 2014.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Contd.)

Note J – Financial Instruments and Risk Management

Murphy often uses derivative instruments to manage certain risks related to commodity prices, foreign currency exchange rates and interest rates. The use of derivative instruments for risk management is covered by operating policies and is closely monitored by the Company's senior management. The Company does not hold any derivatives for speculative purposes and it does not use derivatives with leveraged or complex features. Derivative instruments are traded primarily with creditworthy major financial institutions or over national exchanges, such as the New York Mercantile Exchange (NYMEX). The Company has a risk management control system to monitor commodity price risks and any derivatives obtained to manage a portion of such risks. For accounting purposes, the Company has not designated commodity and foreign currency derivative contracts as hedges, and therefore, it recognizes all gains and losses on these derivative contracts in its Consolidated Statements of Operations. Certain interest rate derivative contracts were accounted for as hedges and the net payment upon settlement recording the fair value of these contracts was deferred in Accumulated Other Comprehensive Loss. This deferred cost is being reclassified to Interest Expense in the Consolidated Statements of Operations over the period until the associated notes mature in 2022.

Commodity Purchase Price Risks

The Company is subject to commodity price risk related to crude oil, natural gas liquids and natural gas it produces and sells. The Company had open derivative contracts at September 30, 2016 and 2015. The impact from marking to market these commodity derivative contracts increased the loss before income taxes by \$3.9 million for the nine-month period ended September 30, 2016 and reduced the loss before income taxes by \$7.4 million for the nine-month period ended September 30, 2015.

Open West Texas Intermediate (WTI) contracts were as follows:

	Volumes	Swap Prices
At September 30, 2016	(barrels per day)	
October – December 2016	25,000	\$50.67 per barrel
January – December 2017	16,000	\$50.34 per barrel
At September 30, 2015		
October – December 2015	15,000	\$63.30 per barrel

Foreign Currency Exchange Risks

The Company is subject to foreign currency exchange risk associated with operations in countries outside the U.S. At September 30, 2016 and 2015 short-term derivative instruments were outstanding in Canada for approximately \$25.2 million and \$6.2 million, respectively, to manage the currency risks of certain U.S. dollar accounts receivable associated with sale of Canadian crude oil. The impact from marking to market these foreign currency derivative contracts was insignificant for the nine-month periods ended September 30, 2016 and 2015, respectively.

After signing an agreement to sell its five percent non-operated working interest in Syncrude, the Company's Canadian subsidiary entered into forward sales contracts for C\$1.0 billion at a fixed rate to lock in the U.S. dollar value of the proceeds and protect the Company from exposure to weakening of the Canadian dollar. Upon completion of the sale and settlement of the forward sale contracts, the Company recognized income of approximately \$26.8 million in the second quarter of 2016 due to weakening of the Canadian dollar subsequent to entering into the contracts.

At September 30, 2016 and December 31, 2015, the fair value of derivative instruments not designated as hedging instruments are presented in the following table.

(Thousands of dollars)	September 30, 2016		December 31, 2015	
	Asset (Liability) Derivatives		Asset (Liability) Derivatives	
	Balance Sheet Location	Fair Value	Balance Sheet Location	Fair Value
Commodity	Accounts receivable	\$ 192	Accounts receivable	\$ 89,358
Foreign exchange	Accounts receivable	142	Accounts payable	(29)

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Contd.)

Note J – Financial Instruments and Risk Management (Contd.)

For the three-month and nine-month periods ended September 30, 2016 and 2015, the gains and losses recognized in the Consolidated Statements of Operations for derivative instruments not designated as hedging instruments are presented in the following table.

(Thousands of dollars)		Gain (Loss)			
		Three Months Ended		Nine Months Ended	
Type of Derivative Contract	Statement of Operations Location	September 30,		September 30,	
Commodity	Sales and other operating revenues	2016	2015	2016	2015
Foreign exchange	Interest and other income	\$ 11,871	39,392	(22,678)	46,811
		143	33	26,929	47
		\$ 12,014	39,425	4,251	46,858

Interest Rate Risks

In 2011 the Company entered into a series of derivative contracts known as forward starting interest rate swaps to manage interest rate risk associated with \$350 million of 10-year notes that were sold in May 2012. These interest rate swaps matured in May 2012. Under hedge accounting rules, the Company deferred the net cost associated with these contracts to match the payment of interest on these notes through 2022. During each of the nine-month periods ended September 30, 2016 and 2015, \$1.5 million of the deferred loss on the interest rate swaps was charged to Interest expense in the Consolidated Statement of Operations. The remaining loss deferred on these matured contracts at September 30, 2016 was \$10.8 million, which was recorded, net of income taxes of \$5.8 million, in Accumulated Other Comprehensive Loss in the Consolidated Balance Sheet. The Company expects to charge approximately \$0.7 million of this deferred loss to Interest expense in the Consolidated Statement of Operations during the remaining three months of 2016.

Fair Values – Recurring

The Company carries certain assets and liabilities at fair value in its Consolidated Balance Sheets. The fair value hierarchy is based on the quality of inputs used to measure fair value, with Level 1 being the highest quality and Level 3 being the lowest quality. Level 1 inputs are quoted prices in active markets for identical assets or liabilities. Level 2 inputs are observable inputs other than quoted prices included within Level 1. Level 3 inputs are

unobservable inputs which reflect assumptions about pricing by market participants.

The carrying value of assets and liabilities recorded at fair value on a recurring basis at September 30, 2016 and December 31, 2015 are presented in the following table.

(Thousands of dollars)	September 30, 2016				December 31, 2015			
	Level 1	Level 2	Level 3	Total	Level 1	Level 2	Level 3	Total
Assets:								
Foreign currency exchange derivative contracts	\$ –	142	–	142	–	–	–	–
Commodity derivative contracts	–	192	–	192	–	89,358	–	89,358
	\$ –	334	–	334	–	89,358	–	89,358
Liabilities:								
Nonqualified employee savings plans	\$ 13,637	–	–	13,637	12,971	–	–	12,971
Foreign currency exchange derivative contracts	–	–	–	–	–	29	–	29
	\$ 13,637	–	–	13,637	12,971	29	–	13,000

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Contd.)

Note J – Financial Instruments and Risk Management (Contd.)

The fair value of WTI crude oil derivative contracts was determined based on active market quotes for WTI crude oil at the balance sheet date. The fair value of foreign exchange derivative contracts in each year was based on market quotes for similar contracts at the balance sheet dates. The income effect of changes in the fair value of crude oil derivative contracts is recorded in Sales and Other Operating Revenues in the Consolidated Statements of Operations while the effects of changes in fair value of foreign exchange derivative contracts is recorded in Interest and Other Income. The nonqualified employee savings plan is an unfunded savings plan through which participants seek a return via phantom investments in equity securities and/or mutual funds. The fair value of this liability was based on quoted prices for these equity securities and mutual funds. The income effect of changes in the fair value of the nonqualified employee savings plan is recorded in Selling and General Expenses in the Consolidated Statements of Operations. The Company offsets certain assets and liabilities related to derivative contracts when the legal right of offset exists. There were no offsetting positions recorded at September 30, 2016 and December 31, 2015.

Fair Values – Nonrecurring

As a result of significantly lower commodity prices during the nine-month periods ended September 30, 2016 and 2015, the Company recognized \$95.1 million and \$2.3 billion, respectively, in pretax noncash impairment charges related to producing properties. The fair value information associated with these impaired properties is presented in the following tables.

	September 30, 2016			Net Book Value Prior to Impairment	Total Pretax (Noncash) Impairment Loss
	Fair Value				
	Level 1	Level 2	Level 3		
(Thousands of dollars)					
Assets:					
Impaired proved properties					
Canada	\$ –	–	71,967	167,055	95,088

September 30, 2015

Total

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	Fair Value			Net Book	Pretax
	Level 1	Level 2	Level 3	Value Prior to Impairment	(Noncash) Impairment Loss
(Thousands of dollars)					
Assets:					
Impaired proved properties					
Gulf of Mexico	\$ -	-	216,602	361,402	144,800
Western Canada	-	-	23,526	707,100	683,574
Malaysia	-	-	1,208,900	2,681,500	1,472,600
	\$ -	-	1,449,028	3,750,002	2,300,974

The fair values were determined by internal discounted cash flow models using estimates of future production, prices from futures exchanges, estimates of future costs and a discount rate believed to be consistent with those used by principal market participants in the applicable region.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Contd.)

Note K – Accumulated Other Comprehensive Loss

The components of Accumulated Other Comprehensive Loss on the Consolidated Balance Sheets at December 31, 2015 and September 30, 2016 and the changes during the nine-month period ended September 30, 2016 are presented net of taxes in the following table.

(Thousands of dollars)	Foreign Currency Translation Gains (Losses) ¹	Retirement and Postretirement Benefit Plan Adjustments ¹	Deferred Loss on Interest Rate Derivative Hedges ¹	Total ¹
Balance at December 31, 2015	\$ (513,004)	(179,260)	(12,278)	(704,542)
Components of other comprehensive income:				
Before reclassifications to income	124,522	(3)	–	124,519
Reclassifications to income	–	7,547	2 1,445	3 8,992
Net other comprehensive income	124,522	7,544	1,445	133,511
Balance at September 30, 2016	\$ (388,482)	(171,716)	(10,833)	(571,031)

¹All amounts are presented net of income taxes.

²Reclassifications before taxes of \$11,602 for the nine-month period ended September 30, 2016 are included in the computation of net periodic benefit expense. See Note G for additional information. Related income taxes of \$4,055 for the nine-month period ended September 30, 2016 are included in Income tax expense.

³Reclassifications before taxes of \$2,222 for the nine-month period ended September 30, 2016 are included in Interest expense. Related income taxes of \$777 for the nine-month period ended September 30, 2016 are included in Income tax expense.

Note L – Environmental and Other Contingencies

The Company's operations and earnings have been and may be affected by various forms of governmental action both in the United States and throughout the world. Examples of such governmental action include, but are by no means limited to: tax increases and retroactive tax claims; royalty and revenue sharing increases; import and export controls; price controls; currency controls; allocation of supplies of crude oil and petroleum products and other goods; expropriation of property; restrictions and preferences affecting the issuance of oil and gas or mineral leases; restrictions on drilling and/or production; laws and regulations intended for the promotion of safety and the protection and/or remediation of the environment; governmental support for other forms of energy; and laws and regulations

affecting the Company's relationships with employees, suppliers, customers, stockholders and others. Because governmental actions are often motivated by political considerations and may be taken without full consideration of their consequences, and may be taken in response to actions of other governments, it is not practical to attempt to predict the likelihood of such actions, the form the actions may take or the effect such actions may have on the Company.

Murphy and other companies in the oil and gas industry are subject to numerous federal, state, local and foreign laws and regulations dealing with the environment. Violation of federal or state environmental laws, regulations and permits can result in the imposition of significant civil and criminal penalties, injunctions and construction bans or delays. A discharge of hazardous substances into the environment could, to the extent such event is not insured, subject the Company to substantial expense, including both the cost to comply with applicable regulations and claims by neighboring landowners and other third parties for any personal injury and property damage that might result.

The Company currently owns or leases, and has in the past owned or leased, properties at which hazardous substances have been or are being handled. Although the Company has used operating and disposal practices that were standard in the industry at the time, hazardous substances may have been disposed of or released on or under the properties owned or leased by the Company or on or under other locations where these wastes have been taken for disposal. In addition, many of these properties have been operated by third parties whose treatment and disposal or release of hydrocarbons or other wastes were

not under Murphy's control. Under existing laws the Company could be required to remove or remediate previously disposed wastes (including wastes disposed of or released by prior owners or operators), to clean up contaminated property (including contaminated groundwater) or to perform remedial plugging operations to prevent future contamination. Certain of these historical properties are in various stages of negotiation, investigation, and/or cleanup and the Company is investigating the extent of any such liability and the availability of applicable defenses. The Company has retained certain liabilities related

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Contd.)

Note L – Environmental and Other Contingencies(Contd.)

to environmental matters at formerly owned U.S. refineries that were sold in 2011. The Company also obtained insurance covering certain levels of environmental exposures related to past operations of these refineries. The Company believes costs related to these sites will not have a material adverse effect on Murphy's net income, financial condition or liquidity in a future period.

During 2015, the Company's subsidiary in Canada identified a leak or leaks at an infield condensate transfer pipeline at the Seal field in a remote area of Alberta. The pipeline was immediately shut down and the Company's emergency response plan was activated. In cooperation with local governmental regulators, and with the assistance of qualified consultants, an investigation and remediation plan is progressing as planned and the Company's insurers have been notified. The Company has not yet established a complete estimate of the costs to remediate the site. Based on the assessments done to date, the Company recorded \$43.9 million in other expense during 2015 associated with the estimated costs of remediating the site. The Company has spent \$32.8 million to date associated with this event. Further refinements in the estimated total cost to remediate the site are anticipated in future periods, including possible fines from regulators and insurance recoveries. It is possible that the ultimate net remediation costs to the Company associated with the condensate leak or leaks will exceed the amount of expense recorded through September 30, 2016.

There is the possibility that environmental expenditures could be required at currently unidentified sites, and new or revised regulations could require additional expenditures at known sites. However, based on information currently available to the Company, the amount of future remediation costs incurred at known or currently unidentified sites is not expected to have a material adverse effect on the Company's future net income, cash flows or liquidity.

Murphy and its subsidiaries are engaged in a number of other legal proceedings, all of which Murphy considers routine and incidental to its business. Based on information currently available to the Company, the ultimate resolution of these matters is not expected to have a material adverse effect on the Company's net income, financial condition or liquidity in a future period.

Note M – Commitments

The Company has entered into forward sales contracts to mitigate the price risk for a portion of its 2016 to 2020 natural gas sales volumes in Western Canada. The natural gas sales contracts call for deliveries during the last three

months of 2016 of approximately 99 million cubic feet per day (MMCFD) at C\$3.00 per MCF, 79 MMCFD at C\$2.83 per MCF from January 2017 to December 2017 and 59 MMCFD at C\$2.81 per MCF from January 2018 through December 2020. In October 2016, the Company entered into an additional 20 MMCFD of natural gas sales contracts for the January 2017 through December 2020 period at C\$3.12 per MCF. These natural gas contracts have been accounted for as normal sales for accounting purposes.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Contd.)

Note N – Business Segments