CONTANGO OIL & GAS CO
Form 10-Q
May 04, 2018
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UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

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

For the quarterly period ended March 31, 2018

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 001-16317

CONTANGO OIL & GAS COMPANY

(Exact name of registrant as specified in its charter)

DELAWARE	95-4079863
(State or other jurisdiction of incorporation or organization)	(IRS Employer Identification No.)
717 TEXAS AVENUE, SUITE 2900	77002

HOUSTON, TEXAS
(Address of principal executive offices) (Zip Code)

(713) 236-7400

(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 website, 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, a smaller reporting company, or an emerging growth company. See the definitions of "large accelerated filer", "accelerated filer", "smaller reporting company" and "emerging growth company" in Rule 12b-2 of the Exchange Act. (Check one):

Large accelerated filer	Accelerated filer
Non-accelerated filer	Smaller reporting company
Emerging growth company	

If an emerging growth company, indicate by check mark if the registrant has elected not to use the extended transition period for complying with any new or revised financial accounting standards provided pursuant to Section 13(a) of the Exchange Act.

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

The total number of shares of common stock, par value $0.04 per share, outstanding as of May 1, 2018 was 25,662,238.

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CONTANGO OIL & GAS COMPANY AND SUBSIDIARIES

QUARTERLY REPORT ON FORM 10-Q

FOR THE THREE MONTHS ENDED MARCH 31, 2018

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All references in this Quarterly Report on Form 10-Q to the "Company", "Contango", "we", "us" or "our" are to Contango Oil Gas Company and its subsidiaries.

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Item 1. Consolidated Financial Statements

CONTANGO OIL & GAS COMPANY AND SUBSIDIARIES

CONSOLIDATED BALANCE SHEETS

(in thousands, except shares)

	March 31, 2018	December 31, 2017
	(unaudited)	
CURRENT ASSETS:		
Cash and cash equivalents	$ —	$ —
Accounts receivable, net	13,701	13,059
Prepaid expenses	952	1,892
Current derivative asset	736	822
Total current assets	15,389	15,773
PROPERTY, PLANT AND EQUIPMENT:		
Natural gas and oil properties, successful efforts method of accounting:		
Proved properties	1,180,083	1,239,662
Unproved properties	36,150	35,243
Other property and equipment	1,272	1,272
Accumulated depreciation, depletion and amortization	(876,972)	(930,220)
Total property, plant and equipment, net	340,533	345,957
OTHER NON-CURRENT ASSETS:		
Investments in affiliates	19,170	18,464
Long-term derivative asset	328	—
Deferred tax asset	424	424
Other	716	835
Total other non-current assets	20,638	19,723
TOTAL ASSETS	$ 376,560	$ 381,453
CURRENT LIABILITIES:		
Accounts payable and accrued liabilities	$ 42,610	$ 46,755
Current derivative liability	2,047	1,765
Current asset retirement obligations	1,592	2,017
Total current liabilities	46,249	50,537
NON-CURRENT LIABILITIES:		
Long-term debt	78,660	85,380
Long-term derivative liability	778	300
Asset retirement obligations	20,455	20,388
Other long term liabilities	3,528	248
Total non-current liabilities	103,421	106,316
Total liabilities	149,670	156,853
COMMITMENTS AND CONTINGENCIES (NOTE 12)		

SHAREHOLDERS’ EQUITY:		
Common stock, $0.04 par value, 50 million shares authorized, 31,079,584 shares issued and 25,695,797 shares outstanding at March 31, 2018, 30,873,470 shares issued and 25,505,715 shares outstanding at December 31, 2017	1,231	1,223
Additional paid-in capital	303,943	302,527
Treasury shares at cost (5,383,787 shares at March 31, 2018 and 5,367,755 shares at December 31, 2017)	(128,654)	(128,583)
Retained earnings	50,370	49,433
Total shareholders’ equity	226,890	224,600
TOTAL LIABILITIES AND SHAREHOLDERS’ EQUITY	$ 376,560	$ 381,453

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

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CONTANGO OIL & GAS COMPANY AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF OPERATIONS

(in thousands, except per share amounts)

	Three Months Ended March 31,	
	2018	2017
	(unaudited)	
REVENUES:		
Oil and condensate sales	$ 8,811	$ 5,542
Natural gas sales	8,609	11,140
Natural gas liquids sales	3,017	2,742
Total revenues	20,437	19,424
EXPENSES:		
Operating expenses	6,927	6,833
Exploration expenses	469	91
Depreciation, depletion and amortization	10,485	11,771
Impairment and abandonment of oil and gas properties	3,327	30
General and administrative expenses	6,726	6,596
Total expenses	27,934	25,321
OTHER INCOME (EXPENSE):		
Gain from investment in affiliates, net of income taxes	707	1,784
Gain from sale of assets	9,447	2,940
Interest expense	(1,409)	(759)
Gain (loss) on derivatives, net	(1,032)	3,096
Other income (expense)	879	(88)
Total other income	8,592	6,973
NET INCOME BEFORE INCOME TAXES	1,095	1,076
Income tax provision	(158)	(191)
NET INCOME	$ 937	$ 885
NET INCOME PER SHARE:		
Basic	$ 0.04	$ 0.04
Diluted	$ 0.04	$ 0.04
WEIGHTED AVERAGE COMMON SHARES OUTSTANDING:		
Basic	24,793	24,607
Diluted	24,841	24,641

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

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CONTANGO OIL & GAS COMPANY AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF CASH FLOWS

(in thousands)

	Three Months Ended March 31, 2018	2017
	(unaudited)	
CASH FLOWS FROM OPERATING ACTIVITIES:		
Net income	$ 937	$ 885
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation, depletion and amortization	10,485	11,771
Impairment of natural gas and oil properties	3,097	—
Exploration recovery	—	(232)
Gain on sale of assets	(9,447)	(2,940)
Gain from investment in affiliates	(707)	(1,784)
Stock-based compensation	1,424	1,456
Unrealized loss (gain) on derivative instruments	519	(3,275)
Changes in operating assets and liabilities:		
Decrease (increase) in accounts receivable & other receivables	(642)	4,840
Decrease in prepaids	940	991
Increase (decrease) in accounts payable & advances from joint owners	(6,053)	3,869
Decrease in other accrued liabilities	(1,921)	(973)
Increase in income taxes payable, net	158	188
Other	3,279	61
Net cash provided by operating activities	$ 2,069	$ 14,857
CASH FLOWS FROM INVESTING ACTIVITIES:		
Natural gas and oil exploration and development expenditures	$ (16,244)	$ (20,807)
Additions to furniture & equipment	—	(14)
Sale of oil & gas properties	20,965	670
Net cash provided by (used) in investing activities	$ 4,721	$ (20,151)
CASH FLOWS FROM FINANCING ACTIVITIES:		
Borrowings under credit facility	$ 74,832	$ 54,963
Repayments under credit facility	(81,551)	(49,595)
Purchase of treasury stock	(71)	(74)
Net cash provided by (used in) financing activities	$ (6,790)	$ 5,294
NET CHANGE IN CASH AND CASH EQUIVALENTS	$ —	$ —
CASH AND CASH EQUIVALENTS, BEGINNING OF PERIOD	—	—
CASH AND CASH EQUIVALENTS, END OF PERIOD	$ —	$ —

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

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CONTANGO OIL & GAS COMPANY AND SUBSIDIARIES

CONSOLIDATED STATEMENT OF SHAREHOLDERS' EQUITY

(in thousands, except number of shares)

Ex

	Common Stock Shares (unaudited)	Amount	Additional Paid-in Capital	Treasury Stock	Retained Earnings	Total Shareholders' Equity
Balance at December 31, 2017	25,505,715	$ 1,223	$ 302,527	$ (128,583)	$ 49,433	$ 224,600
Treasury shares at cost	(16,032)	—	—	(71)	—	(71)
Restricted shares activity	206,114	8	(8)	—	—	—
Stock-based compensation	—	—	1,424	—	—	1,424
Net income	—	—	—	—	937	937
Balance at March 31, 2018	25,695,797	$ 1,231	$ 303,943	$ (128,654)	$ 50,370	$ 226,890

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

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CONTANGO OIL & GAS COMPANY AND SUBSIDIARIES

NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited)

1. Organization and Business

Contango Oil & Gas Company (collectively with its subsidiaries, "Contango" or the "Company") is a Houston, Texas based, independent oil and natural gas company. The Company's business is to maximize production and cash flow from its offshore properties in the shallow waters of the Gulf of Mexico ("GOM") and onshore properties in Texas and Wyoming and to use that cash flow to explore, develop, exploit, increase production from and acquire crude oil and natural gas properties in the onshore West Texas, the Texas Gulf Coast and the Rocky Mountain regions of the United States.

The following table lists the Company's primary producing areas as of March 31, 2018:

Location	Formation
Gulf of Mexico	Offshore Louisiana - water depths less than 300 feet
Madison and Grimes counties, Texas	Woodbine (Upper Lewisville)
Pecos County, Texas	Southern Delaware Basin (Wolfcamp)
Other Texas Gulf Coast	Conventional and smaller unconventional formations
Zavala and Dimmit counties, Texas	Buda / Austin Chalk
Weston County, Wyoming	Muddy Sandstone
Sublette County, Wyoming	Jonah Field (1)

(1) Through a 37% equity investment in Exaro Energy III LLC ("Exaro"). Production associated with this investment is not included in the Company's reported production results for the quarter ended March 31, 2018.

The Company's 2018 capital program has focused, and will continue to focus, on the development of the Company's 16,500 gross operated acres (6,800 net) in the Southern Delaware Basin. Additionally, the Company will continue to identify opportunities for cost efficiencies in all areas of its operations, maintain core leases and continue to identify new resource potential opportunities internally and, where appropriate, through acquisition. Acquisition efforts will typically be focused on areas in which the Company can leverage its geographic and geological expertise to exploit identified drilling opportunities and where the Company can develop an inventory of additional drilling prospects that the Company believes will enable it to grow production and add reserves. The Company will continuously monitor the commodity price environment, including its stability and forecast, and, if warranted, make adjustments to its strategy as the year progresses.

2. Summary of Significant Accounting Policies

The accounting policies followed by the Company are set forth in the notes to the Company's audited consolidated financial statements included in its Annual Report on Form 10-K for the year ended December 31, 2017 (the "2017 Form 10-K") filed with the Securities and Exchange Commission ("SEC"). Please refer to the notes to the financial statements included in the 2017 Form 10-K for additional details of the Company's financial condition, results of operations and cash flows. No material items included in those notes have changed except as a result of normal transactions in the interim or as disclosed within this report.

Basis of Presentation

The accompanying unaudited consolidated financial statements have been prepared in conformity with accounting principles generally accepted in the United States of America ("GAAP") for interim financial information, pursuant to the rules and regulations of the SEC, including instructions to Quarterly Reports on Form 10-Q and Article 10 of Regulation S-X. Accordingly, they do not include all the information and footnotes required by GAAP for complete annual financial statements. In the opinion of management, all adjustments considered necessary for a fair statement of the unaudited consolidated financial statements have been included. All such adjustments are of a normal recurring nature. The consolidated financial statements should be read in conjunction with the 2017 Form 10-K. The consolidated results of operations for the quarter ended March 31, 2018 are not necessarily indicative of the results that may be expected for the year ending December 31, 2018.

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The Company's consolidated financial statements include the accounts of Contango Oil & Gas Company and its subsidiaries, after elimination of all material intercompany balances and transactions. All wholly owned subsidiaries are consolidated. The investment in Exaro by our wholly owned subsidiary, Contaro Company ("Contaro") is accounted for using the equity method of accounting, and therefore, the Company does not include its share of individual operating results, reserves or production in those reported for the Company's consolidated results.

Oil and Gas Properties - Successful Efforts

The Company's application of the successful efforts method of accounting for the Company's natural gas and oil exploration and production activities requires judgments as to whether particular wells are developmental or exploratory, since exploratory costs and the costs related to exploratory wells that are determined to not have proved reserves must be expensed whereas developmental costs are capitalized. The results from a drilling operation can take considerable time to analyze, and the determination that commercial reserves have been discovered requires both judgment and application of industry experience. Wells may be completed that are assumed to be productive and actually deliver natural gas and oil in quantities insufficient to be economic, which may result in the abandonment of the wells at a later date. On occasion, wells are drilled which have targeted geologic structures that are both developmental and exploratory in nature, and in such instances an allocation of costs is required to properly account for the results. Delineation seismic costs incurred to select development locations within a productive natural gas and oil field are typically treated as development costs and capitalized, but often these seismic programs extend beyond the proved reserve areas and therefore management must estimate the portion of seismic costs to expense as exploratory. The evaluation of natural gas and oil leasehold acquisition costs included in unproved properties requires management's judgment of exploratory costs related to drilling activity in a given area. Drilling activities in an area by other companies may also effectively condemn leasehold positions.

Impairment of Long-Lived Assets

Pursuant to GAAP, when circumstances indicate that proved properties may be impaired, the Company compares expected undiscounted future cash flows on a field by field basis to the unamortized capitalized cost of the asset. If the estimated future undiscounted cash flows based on the Company's estimate of future reserves, natural gas and oil prices, operating costs and production levels from oil and natural gas reserves, are lower than the unamortized capitalized cost, then the capitalized cost is reduced to fair value. The factors used to determine fair value include, but are not limited to, estimates of proved, probable and possible reserves, future commodity prices, the timing of future production and capital expenditures and a discount rate commensurate with the risk reflective of the lives remaining for the respective oil and gas properties. Additionally, the Company may use appropriate market data to determine fair value. During the quarter ended March 31, 2018, the Company recognized $2.3 million in non-cash proved impairment charges related to its Vermilion 170 offshore property. No impairment of proved properties was recognized during the quarter ended March 31, 2017.

Unproved properties are reviewed quarterly to determine if there has been impairment of the carrying value, with any such impairment charged to expense in the period. The Company recognized impairment expense of approximately $0.8 million for the quarter ended March 31, 2018, related to impairment of certain non-core unproved properties due to expiring leases. The Company recognized no impairment of unproved properties for the quarter ended March 31, 2017.

Net Income Per Common Share

Basic net income per common share is computed by dividing the net income attributable to common stock by the weighted average number of common shares outstanding for the period. Diluted net income per common share reflects the potential dilution that could occur if securities or other contracts to issue common stock were exercised or converted into common stock. Potentially dilutive securities, including unexercised stock options, Performance Stock Units and unvested restricted stock, have not been considered when their effect would be antidilutive. For the quarter ended March 31, 2018, the Company excluded 670,210 potentially dilutive securities, as they were antidilutive. For the quarter ended March 31, 2017, the Company excluded 917,737 potentially dilutive securities, as they were antidilutive.

Subsidiary Guarantees

Contango Oil & Gas Company, as the parent company (the “Parent Company”), has filed a registration statement on Form S-3 with the SEC to register, among other securities, debt securities that the Parent Company may

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issue from time to time. Any such debt securities would likely be guaranteed on a full and unconditional basis by each of the Company's current subsidiaries and any future subsidiaries specified in any future prospectus supplement (each a "Subsidiary Guarantor"). Each of the Subsidiary Guarantors is wholly owned by the Parent Company, either directly or indirectly. The Parent Company has no assets or operations independent of the Subsidiary Guarantors, and there are no significant restrictions upon the ability of the Subsidiary Guarantors to distribute funds to the Parent Company. The Parent Company has one wholly owned subsidiary that is inactive and not a Subsidiary Guarantor. Finally, the Parent Company's wholly owned subsidiaries do not have restricted assets that exceed 25% of net assets as of the most recent fiscal year end that may not be transferred to the Parent Company in the form of loans, advances or cash dividends by such subsidiary without the consent of a third party.

Revenue Recognition

Adoption of ASC 606

During the quarter ended March 31, 2018 the Company adopted Accounting Standards Codification 606 – Revenue from Contracts with Customers ("ASC 606"). The Company adopted ASC 606 using the modified retrospective method which allows the Company to apply the new standard to all new contracts entered into after December 31, 2017 and all existing contracts for which all (or substantially all) of the revenue has not been recognized under legacy revenue guidance prior to December 31, 2017. The Company identified no material impact on its historical revenues upon initial application of ASC 606, and as such has not recognized any cumulative catch-up effect to the opening balance of the Company's shareholders' equity as of January 1, 2018. ASC 606 supersedes previous revenue recognition requirements in ASC 605 and includes a five-step revenue recognition model to depict the transfer of goods or services to customers in an amount that reflects the consideration to which the Company expects to be entitled in exchange for those goods or services.

Revenue from Contracts with Customers

Sales of oil, condensate, natural gas and natural gas liquids ("NGLs") are recognized at the time control of the products are transferred to the customer. Based upon the Company's current purchasers' past experience and expertise in the market, collectability is probable, and there have not been payment issues with the Company's purchasers over the past year or currently. Generally, the Company's gas processing and purchase agreements indicate that the processors take control of the gas at the inlet of the plant and that control of residue gas is returned to the Company at the outlet of the plant. The midstream processing entity gathers and processes the natural gas and remits proceeds to the Company for the resulting sales of NGLs. The Company delivers oil and condensate to the purchaser at a contractually agreed-upon delivery point at which the purchaser takes custody, title, and risk of loss of the product.

When sales volumes exceed the Company's entitled share, a production imbalance occurs. If production imbalance exceeds the Company's share of the remaining estimated proved natural gas reserves for a given property, the Company records a liability. Production imbalances have not had and currently do not have a material impact on the financial statements, and this did not change with the adoption of ASC 606.

Transaction Price Allocated to Remaining Performance Obligations

Generally, the Company's contracts have an initial term of one year or longer but continue month to month unless written notification of termination in a specified time period is provided by either party to the contract. The Company has used the practical expedient in ASC 606 which states that the Company is not required to disclose that transaction price allocated to remaining performance obligations if the variable consideration is allocated entirely to a wholly unsatisfied performance obligation. Future volumes are wholly unsatisfied, and disclosure of the transaction price allocated to remaining performance obligation is not required.

Contract Balances

The Company receives purchaser statements from the majority of the Company's customers but there are a few contracts where the Company prepares the invoice. Payment is unconditional upon receipt of the statement or invoice. Accordingly, the Company's product sales contracts do not give rise to contract assets or liabilities under ASC 606. The majority of the Company's contract pricing provisions are tied to a market index, with certain adjustments based on,

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among other factors, whether a well delivers to a gathering or transmission line, quality of the oil or natural gas, and supply and demand conditions. The price of these commodities fluctuates to remain competitive with supply.

Prior Period Performance Obligations

The Company records revenue in the month production is delivered to the purchaser. Settlement statements may not be received for 30 to 90 days after the date production is delivered, and therefore the Company is required to estimate the amount of production delivered to the purchaser and the price that will be received for the sale of the product. Differences between the Company's estimates and the actual amounts received for product sales are generally recorded in the following month that payment is received. Any differences between the Company's revenue estimates and actual revenue received historically have not been significant. The Company has internal controls in place for its revenue estimation accrual process.

Impact of Adoption of ASC 606

The Company has reviewed all of the Company's natural gas, NGLs, residue gas, condensate and crude oil sales contracts to assess the impact of the provisions of ASC 606. Based upon the Company's review, there were no required changes to the recording of residue gas or condensate and crude oil contracts. Certain NGL and natural gas contracts would require insignificant changes to the recording of transportation, gathering and processing fees as net to revenue or as an expense. The Company concluded that these minor changes were not material to its operating results on a quantitative or qualitative basis. Therefore, there was no impact to our operating results for the quarter ended March 31, 2018. Going forward, the Company is modifying procedures to its existing internal controls relating to revenue by reviewing for any significant increase in sales level, primarily on gas processing or gas purchasing contracts, on a quarterly basis to monitor the significance of gross revenue versus net revenue and expenses under ASC 606. As under previous revenue guidance, the Company will continue to review all new or modified revenue contracts on a quarterly basis for proper treatment.

Recent Accounting Pronouncements

In January 2018, the Financial Accounting Standards Board ("FASB") issued Accounting Standards Update ("ASU") 2018-01 – Leases (Topic 842): Land Easement Practical Expedient for Transition to Topic 842. The amendments in this update permit an entity to elect an optional transition practical expedient to not evaluate under Topic 842 land easements (right of way payments) that exist or expired before the entity's adoption of Topic 842 and that were not previously accounted for as leases under Topic 840. Right of way payments do not have a material impact on the Company's results of operations and the Company plans to elect the practical expedient to evaluate right of way payments prospectively on adoption of Topic 842.

In February 2016, the FASB issued ASU No. 2016-02: Leases (Topic 842) (ASU 2016 02). The main objective of ASU 2016-02 is to increase transparency and comparability among organizations by recognizing lease assets and lease liabilities on the balance sheet and disclosing key information about leasing arrangements. The main difference between previous GAAP and Topic 842 is the recognition of lease assets and lease liabilities by lessees for those leases classified as operating leases. ASU 2016-02 requires lessees to recognize assets and liabilities arising from leases on the balance sheet. In transition, lessees and lessors are required to recognize and measure leases at the beginning of the earliest period presented using a modified retrospective approach. For public entities, ASU 2016-02 is effective for financial statements issued for fiscal years beginning after December 15, 2018, including interim periods within those fiscal years; early application is permitted. The Company will continue to assess the impact this may have on its financial position, results of operations and cash flows.

3. Acquisitions and Dispositions

On March 28, 2018, the Company sold its operated Eagle Ford Shale assets located in Karnes County, Texas for a cash purchase price of $21.0 million. The Company recorded a net gain of $9.4 million.

Effective February 1, 2017, the Company sold to a third party all of its assets in the North Bob West area and its operated assets in the Escobas area, both located in Southeast Texas, for a cash purchase price of $650,000. The Company recorded a net gain of $2.9 million after removal of the asset retirement obligations associated with the sold properties.

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4. Fair Value Measurements

Pursuant to Accounting Standards Codification 820, Fair Value Measurements and Disclosures (ASC 820), the Company's determination of fair value incorporates not only the credit standing of the counterparties involved in transactions with the Company resulting in receivables on the Company's consolidated balance sheets, but also the impact of the Company's nonperformance risk on its own liabilities. ASC 820 defines fair value as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date (exit price). ASC 820 establishes a fair value hierarchy that prioritizes the inputs to valuation techniques used to measure fair value. The hierarchy assigns the highest priority to unadjusted quoted prices in active markets for identical assets or liabilities (Level 1) and the lowest priority to unobservable inputs (Level 3). Level 2 measurements are inputs that are observable for assets or liabilities, either directly or indirectly, other than quoted prices included within Level 1. The Company utilizes market data or assumptions that market participants would use in pricing the asset or liability, including assumptions about risk and the risks inherent in the inputs to the valuation technique. These inputs can be readily observable, market corroborated, or generally unobservable. The Company classifies fair value balances based on the observability of those inputs.

The following table sets forth, by level within the fair value hierarchy, the Company’s financial assets and liabilities that were accounted for at fair value as of March 31, 2018. As required by ASC 820, a financial instrument's level within the fair value hierarchy is based on the lowest level of input that is significant to the fair value measurement. The Company's assessment of the significance of a particular input to the fair value measurement requires judgment and may affect the valuation of fair value assets and liabilities and their placement within the fair value hierarchy levels. There have been no transfers between Level 1, Level 2 or Level 3.

Fair value information for financial assets and liabilities was as follows as of March 31, 2018 (in thousands):

	Total	Fair Value Measurements Using		
	Carrying Value	Level 1	Level 2	Level 3
Derivatives				
Commodity price contracts - assets	$ 1,064	$ —	$ 1,064	$ —
Commodity price contracts - liabilities	$ (2,825)	$ —	$ (2,825)	$ —

Derivatives listed above are recorded in “Current derivative asset or liability” and “Long-term derivative asset or liability” on the Company’s consolidated balance sheet and include swaps and costless collars that are carried at fair value. The Company records the net change in the fair value of these positions in "Gain (loss) on derivatives, net" in the Company's consolidated statements of operations. The Company is able to value the assets and liabilities based on observable market data for similar instruments, which resulted in the Company reporting its derivatives as Level 2. This observable data includes the forward curves for commodity prices based on quoted markets prices and implied volatility factors related to changes in the forward curves. See Note 5 - "Derivative Instruments" for additional discussion of derivatives.

As of March 31, 2018, the Company's derivative contracts were with certain members of its credit facility lenders which are major financial institutions with investment grade credit ratings which are believed to have minimal credit risk. As such, the Company is exposed to credit risk to the extent of nonperformance by the counterparties in the derivative contracts discussed above; however, the Company does not anticipate such nonperformance.

Estimates of the fair value of financial instruments are made in accordance with the requirements of ASC 825, Financial Instruments. The estimated fair value amounts are determined at discrete points in time based on relevant market information. These estimates involve uncertainties and cannot be determined with precision. The estimated fair value of cash, accounts receivable and accounts payable approximates their carrying value due to their short-term nature. The estimated fair value of the Company's credit facility with the Royal Bank of Canada and other lenders (the “RBC Credit Facility”) approximates carrying value because the facility interest rate approximates current market rates and is reset at least every six months. See Note 9 - "Long-Term Debt" for further information.

Impairments

Contango tests proved oil and natural gas properties for impairment when events and circumstances indicate a decline in the recoverability of the carrying value of such properties, such as a downward revision of the reserve

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estimates or lower commodity prices. The Company estimates the undiscounted future cash flows expected in connection with the oil and gas properties on a field by field basis and compares such future cash flows to the unamortized capitalized costs of the properties. If the estimated future undiscounted cash flows are lower than the unamortized capitalized cost, the capitalized cost is reduced to its fair value. The factors used to determine fair value include, but are not limited to, estimates of proved, probable and possible reserves, future commodity prices, the timing of future production and capital expenditures and a discount rate commensurate with the risk reflective of the lives remaining for the respective oil and gas properties. Additionally, the Company may use appropriate market data to determine fair value. Because these significant fair value inputs are typically not observable, impairments of long-lived assets are classified as a Level 3 fair value measure.

Unproved properties are reviewed quarterly to determine if there has been impairment of the carrying value, with any such impairment charged to expense in the period.

Asset Retirement Obligations

The initial measurement of asset retirement obligations at fair value is calculated using discounted cash flow techniques and based on internal estimates of future retirement costs associated with oil and gas properties. The factors used to determine fair value include, but are not limited to, estimated future plugging and abandonment costs and expected lives of the related reserves. As there is no corroborating market activity to support the assumptions used, the Company has designated these liabilities as Level 3.

5. Derivative Instruments

The Company is exposed to certain risks relating to its ongoing business operations, such as commodity price risk. Derivative contracts are typically utilized to hedge the Company's exposure to price fluctuations and reduce the variability in the Company's cash flows associated with anticipated sales of future oil and natural gas production. The Company typically hedges a substantial, but varying, portion of anticipated oil and natural gas production for future periods. The Company believes that these derivative arrangements, although not free of risk, allow it to achieve a more predictable cash flow and to reduce exposure to commodity price fluctuations. However, derivative arrangements limit the benefit of increases in the prices of crude oil, natural gas and natural gas liquids sales. Moreover, because its derivative arrangements apply only to a portion of its production, the Company’s strategy provides only partial protection against declines in commodity prices. Such arrangements may expose the Company to risk of financial loss in certain circumstances. The Company continuously reevaluates its hedging programs in light of changes in production, market conditions and commodity price forecasts.

As of March 31, 2018, the Company’s natural gas and oil derivative positions consisted of “swaps” and “costless collars”. Swaps are designed so that the Company receives or makes payments based on a differential between fixed and variable prices for crude oil and natural gas. A costless collar consists of a purchased put option and a sold call option, which establishes a minimum and maximum price, respectively, that the Company will receive for the volumes under the contract.

It is the Company's policy to enter into derivative contracts only with counterparties that are creditworthy institutions deemed by management as competent and competitive market makers. The Company does not post collateral, nor is it exposed to potential margin calls, under any of these contracts as they are secured under the RBC Credit Facility. See Note 9 - "Long-Term Debt" for further information regarding the RBC Credit Facility.

The Company has elected not to designate any of its derivative contracts for hedge accounting. Accordingly, derivatives are carried at fair value on the consolidated balance sheets as assets or liabilities, with the changes in the fair value included in the consolidated statements of operations for the period in which the change occurs. The Company records the net change in the mark-to-market valuation of these derivative contracts, as well as all payments and receipts on settled derivative contracts, in "Gain (loss) on derivatives, net" on the consolidated statements of operations.

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The following derivative instruments were in place at March 31, 2018 (fair value in thousands):

Commodity	Period	Derivative	Volume/Month	Price/Unit	Fair Value
Natural Gas	Apr 2018 - July 2018	Swap	370,000 MMBtus	$ 3.07 (1)	462
Natural Gas	Aug 2018 - Oct 2018	Swap	70,000 MMBtus	$ 3.07 (1)	48
Natural Gas	Nov 2018 - Dec 2018	Swap	320,000 MMBtus	$ 3.07 (1)	77
Oil	Apr 2018 - June 2018	Swap	20,000 Bbls	$ 56.40 (2)	(653)
Oil	July 2018 - Oct 2018	Collar	20,000 Bbls	$ 52.00 - 56.85 (2)	(737)
Oil	Nov 2018 - Dec 2018	Collar	15,000 Bbls	$ 52.00 - 56.85 (2)	(241)
Oil	Apr 2018 - Dec 2018	Collar	2,000 Bbls	$ 52.00 - 58.76 (3)	(100)
Oil	Apr 2018 - July 2018	Collar	6,000 Bbls	$ 58.00 - 68.00 (2)	(35)
Oil	Nov 2018 - Dec 2018	Collar	5,000 Bbls	$ 58.00 - 68.00 (2)	(5)
Oil	Jan 2019 - Dec 2019	Collar	4,000 Bbls	$ 52.00 - 59.45 (3)	(105)
Oil	Jan 2019 - Dec 2019	Collar	7,000 Bbls	$ 50.00 - 58.00 (2)	(472)
		Total net fair value of derivative instruments			$ (1,761)

(1) Based on Henry Hub NYMEX natural gas prices.
(2) Based on Argus Louisiana Light Sweet crude oil prices.
(3) Based on West Texas Intermediate crude oil prices.

The following summarizes the fair value of commodity derivatives outstanding on a gross and net basis as of March 31, 2018 (in thousands):

	Gross	Netting (1)	Total
Assets	$ 1,064	$ —	$ 1,064
Liabilities	$ (2,825)	$ —	$ (2,825)

(1) Represents counterparty netting under agreements governing such derivatives.

The following summarizes the fair value of commodity derivatives outstanding on a gross and net basis as of December 31, 2017 (in thousands):

	Gross	Netting (1)	Total
Assets	$ 1,188	$ (1,188)	$ —
Liabilities	$ (2,431)	$ 1,188	$ (1,243)

(1) Represents counterparty netting under agreements governing such derivatives.

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The following table summarizes the effect of derivative contracts on the consolidated statements of operations for the quarters ended March 31, 2018 and 2017 (in thousands):

	Three Months Ended March 31,	
	2018	2017
Crude oil contracts	$ (588)	$ 170
Natural gas contracts	75	(349)
Realized loss	$ (513)	$ (179)
Crude oil contracts	$ (284)	$ 524
Natural gas contracts	(235)	2,751
Unrealized gain (loss)	$ (519)	$ 3,275
Gain (loss) on derivatives, net	$ (1,032)	$ 3,096

6. Stock-Based Compensation

The Company recognized approximately $1.4 million and $1.5 million in stock compensation expense during the quarters ended March 31, 2018 and 2017, respectively, for equity awards granted to its officers, employees and directors. As of March 31, 2018, an additional $5.3 million of compensation expense remained to be recognized over the remaining weighted-average vesting period of 1.9 years. This includes expense related to restricted stock, Performance Stock Units (“PSUs”) and stock options.

Restricted Stock

During the quarter ended March 31, 2018, the Company granted 225,782 shares of restricted common stock, which vest over three years, to executive officers as part of their overall compensation package. The weighted average fair value of the restricted shares granted during the quarter ended March 31, 2018, was $3.57 with a total fair value of approximately $0.8 million with no adjustment for an estimated weighted average forfeiture rate. During the quarter ended March 31, 2018, 19,668 restricted shares were forfeited by former employees. The aggregate intrinsic value of restricted shares forfeited during the quarter ended March 31, 2018 was approximately $164 thousand. Approximately 1.2 million shares remained available for grant under the Amended and Restated 2009 Incentive Compensation Plan as of March 31, 2018, assuming PSUs are settled at 100% of target.

During the quarter ended March 31, 2017, the Company granted 30,000 shares of restricted common stock, which vest over three years, to a newly hired employee as part of his overall compensation package. The weighted average fair value of the restricted shares granted during the quarter ended March 31, 2017, was $7.78 with a total fair value of approximately $0.2 million after adjustment for an estimated weighted average forfeiture rate of 5.8%. During the quarter ended March 31, 2017, 24,244 restricted shares were forfeited by former employees. The aggregate intrinsic value of restricted shares forfeited during the quarter ended March 31, 2017 was approximately $256 thousand.

Performance Stock Units

During the quarter ended March 31, 2018, the Company granted 190,782 PSUs to executive officers as part of their overall compensation package, at a weighted average fair value of $7.69 per unit. During the quarter ended March 31, 2017, the Company granted 30,000 PSUs to a new employee, at a weighted average fair value of $8.32 per unit. All fair value prices were determined using the Monte Carlo simulation model. During the quarters ended March 31, 2018 and 2017, 16,900 and 23,800 PSUs were forfeited by former employees, respectively. PSUs represent the opportunity to receive shares of the Company's common stock at the time of settlement. The number of shares to be awarded upon settlement of these PSUs may range from 0% to 300% of the number of PSUs awarded contingent upon the achievement of certain share price appreciation targets as compared to a peer group index. The PSUs vest and settlement is determined after a three year period.

Compensation expense associated with PSUs is based on the grant date fair value of a single PSU as determined using the Monte Carlo simulation model which utilizes a stochastic process to create a range of potential future outcomes given a variety of inputs. As it is contemplated that the PSUs will be settled with shares of the Company's common stock after three years, the PSU awards are accounted for as equity awards and the fair value is calculated on the grant date. The simulation model calculates the payout percentage based on the stock price performance over the

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performance period. The concluded fair value is based on the average achievement percentage over all the iterations. The resulting fair value expense is amortized over the life of the PSU award.

Stock Options

Under the fair value method of accounting for stock options, cash flows from the exercise of stock options resulting from tax benefits in excess of recognized cumulative compensation cost (excess tax benefits) are classified as financing cash flows. For the quarters ended March 31, 2018 and 2017, there was no excess tax benefit recognized.

Compensation expense related to stock option grants are recognized over the stock option's vesting period based on the fair value at the date the options are granted. The fair value of each option is estimated as of the date of grant using the Black-Scholes options-pricing model. No stock options were granted during the quarters ended March 31, 2018 or 2017.

During the quarter ended March 31, 2018, no stock options were exercised or forfeited. During the quarter ended March 31, 2017, no stock options were exercised and stock options for 14,586 shares of common stock were forfeited by former employees.

7. Other Financial Information

The following table provides additional detail for accounts receivable, prepaid expenses and other, and accounts payable and accrued liabilities which are presented on the consolidated balance sheets (in thousands):

	March 31, 2018	December 31, 2017
Accounts receivable:		
Trade receivables	$ 7,407	$ 6,565
Receivable for Alta Resources Distribution	1,993	1,993
Joint interest billings	3,896	4,030
Income taxes receivable	424	