CIMAREX ENERGY CO
Form 10-Q
August 07, 2013
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UNITED STATES
SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

(Mark One)

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

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

For the Quarterly Period ended June 30, 2013

Commission File No. 001-31446

CIMAREX ENERGY CO.

1700 Lincoln Street, Suite 1800

Denver, Colorado 80203-4518

(303) 295-3995

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

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

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

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

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

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

The number of shares of Cimarex Energy Co. common stock outstanding as of June 30, 2013 was 86,503,109.

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GLOSSARY

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

Bbls Barrels (of oil or natural gas liquids)

Bcf Billion cubic feet

Bcfe Billion cubic feet equivalent

Btu British thermal unit

MBbls Thousand barrels

Mcf Thousand cubic feet (of natural gas)

Mcfe Thousand cubic feet equivalent

MMBbls Million barrels

MMBtu Million British Thermal Units

MMcf Million cubic feet

MMcf/d Million cubic feet per day

MMcfe Million cubic feet equivalent

MMcfe/d Million cubic feet equivalent per day

Net Acres Gross acreage multiplied by Cimarex s working interest percentage

Net Production Gross production multiplied by Cimarex s net revenue interest

NGL or NGLs Natural gas liquids

Tcf Trillion cubic feet

Tcfe Trillion cubic feet equivalent

WTI West Texas Intermediate

One barrel of oil or NGL is the energy equivalent of six Mcf of natural gas

CAUTIONARY INFORMATION ABOUT FORWARD-LOOKING STATEMENTS

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

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

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PART I

ITEM 1 - Financial Statements

CIMAREX ENERGY CO.

Condensed Consolidated Balance Sheets

	June 30, 2013 (Unaudited)	December 31, 2012
	(In thousands, except share data)	
Assets		
Current assets:		
Cash and cash equivalents	$ 4,532	$ 69,538
Receivables, net	381,634	302,974
Oil and gas well equipment and supplies	66,902	81,029
Deferred income taxes	18,111	8,477
Derivative instruments	7,956	
Prepaid expenses	7,120	7,420
Other current assets	286	699
Total current assets	486,541	470,137
Oil and gas properties at cost, using the full cost method of accounting:		
Proved properties	12,097,102	11,258,748
Unproved properties and properties under development, not being amortized	567,178	645,078
	12,664,280	11,903,826
Less accumulated depreciation, depletion and amortization	(7,166,038)	(6,899,057)
Net oil and gas properties	5,498,242	5,004,769
Fixed assets, net	135,367	152,605
Goodwill	620,232	620,232
Derivative instruments	2,395	
Other assets, net	53,593	57,409
	$ 6,796,370	$ 6,305,152
Liabilities and Stockholders Equity		
Current liabilities:		
Accounts payable	$ 82,690	$ 103,653
Accrued liabilities	416,111	392,909
Derivative instruments	59	
Revenue payable	172,956	149,300
Total current liabilities	671,816	645,862
Long-term debt	892,000	750,000
Deferred income taxes	1,260,836	1,121,353
Other liabilities	292,721	313,201
Total liabilities	3,117,373	2,830,416
Stockholders equity:		
Preferred stock, $0.01 par value, 15,000,000 shares authorized, no shares issued		
Common stock, $0.01 par value, 200,000,000 shares authorized, 86,503,109 and 86,595,976 shares issued, respectively	865	866
Paid-in capital	1,948,381	1,939,628

Retained earnings		1,729,178		1,533,768
Accumulated other comprehensive income		573		474
		3,678,997		3,474,736
	$	6,796,370	$	6,305,152

See accompanying notes to consolidated financial statements.

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CIMAREX ENERGY CO.

Consolidated Statements of Income and Comprehensive Income

(Unaudited)

	For the Three Months Ended June 30, 2013	For the Three Months Ended June 30, 2012	For the Six Months Ended June 30, 2013	For the Six Months Ended June 30, 2012
	(In thousands, except per share data)			
Revenues:				
Gas sales	$ 126,547	$ 69,741	$ 227,668	$ 154,894
Oil sales	304,466	229,210	561,998	496,294
NGL sales	52,309	44,286	109,184	103,300
Gas gathering, processing and other	10,844	10,179	21,571	21,886
Gas marketing, net	(409)	(294)	(308)	(216)
	493,757	353,122	920,113	776,158
Costs and expenses:				
Depreciation, depletion and amortization	147,231	121,237	283,669	239,499
Asset retirement obligation	2,884	2,441	5,283	5,966
Production	69,433	62,494	138,819	130,119
Transportation and other operating	22,022	13,169	40,656	26,485
Gas gathering and processing	5,184	4,955	11,340	9,806
Taxes other than income	27,807	23,483	52,935	48,643
General and administrative	22,836	12,634	38,413	26,781
Stock compensation	3,507	4,684	7,112	9,218
Gain on derivative instruments, net	(13,660)	(10,078)	(12,057)	(5,990)
Other operating, net	2,365	2,719	5,297	5,059
	289,609	237,738	571,467	495,586
Operating income	204,148	115,384	348,646	280,572
Other (income) and expense:				
Interest expense	14,112	13,679	27,318	22,347
Capitalized interest	(7,387)	(9,119)	(16,582)	(16,923)
Loss on early extinguishment of debt		16,214		16,214
Other, net	(8,758)	(7,829)	(11,374)	(12,555)
Income before income tax	206,181	102,439	349,284	271,489
Income tax expense	76,616	38,137	129,792	101,080
Net income	$ 129,565	$ 64,302	$ 219,492	$ 170,409
Earnings per share to common stockholders:				
Basic				
Distributed	$ 0.14	$ 0.12	$ 0.28	$ 0.24
Undistributed	1.36	0.63	2.26	1.74
	$ 1.50	$ 0.75	$ 2.54	$ 1.98
Diluted				
Distributed	$ 0.14	$ 0.12	$ 0.28	$ 0.24
Undistributed	1.35	0.62	2.25	1.73
	$ 1.49	$ 0.74	$ 2.53	$ 1.97
Comprehensive income:				

Net income	$	129,565	$	64,302	$	219,492	$	170,409
Other comprehensive income:								
Change in fair value of investments, net of tax		19		(135)		99		264
Total comprehensive income	$	129,584	$	64,167	$	219,591	$	170,673

See accompanying notes to consolidated financial statements.

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CIMAREX ENERGY CO.

Condensed Consolidated Statements of Cash Flows

(Unaudited)

	For the Six Months Ended June 30, 2013	2012
	(In thousands)	
Cash flows from operating activities:		
Net income	$ 219,492	$ 170,409
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation, depletion and amortization	283,669	239,499
Asset retirement obligation	5,283	5,966
Deferred income taxes	129,792	101,080
Stock compensation	7,112	9,218
Derivative instruments, net	(10,292)	(5,990)
Loss on early extinguishment of debt		16,214
Changes in non-current assets and liabilities	5,790	5,115
Other, net	(2,116)	1,955
Changes in operating assets and liabilities:		
(Increase) decrease in receivables, net	(55,060)	107,834
(Increase) decrease in other current assets	14,840	(4,910)
(Decrease) in accounts payable and accrued liabilities	(28,724)	(71,458)
Net cash provided by operating activities	569,786	574,932
Cash flows from investing activities:		
Oil and gas expenditures	(776,138)	(758,608)
Sales of oil and gas assets	14,407	1,273
Sales of other assets	31,157	408
Other expenditures	(25,475)	(26,087)
Net cash used by investing activities	(756,049)	(783,014)
Cash flows from financing activities:		
Net increase (decrease) in bank debt	142,000	(55,000)
Increase in other long-term debt		750,000
Decrease in other long-term debt		(363,595)
Financing costs incurred		(12,692)
Dividends paid	(22,448)	(18,869)
Issuance of common stock and other	1,705	2,764
Net cash provided by financing activities	121,257	302,608
Net change in cash and cash equivalents	(65,006)	94,526
Cash and cash equivalents at beginning of period	69,538	2,406
Cash and cash equivalents at end of period	$ 4,532	$ 96,932

See accompanying notes to consolidated financial statements.

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Notes to Consolidated Financial Statements

June 30, 2013

(Unaudited)

1. Basis of Presentation

The accompanying unaudited financial statements have been prepared by Cimarex Energy Co. pursuant to rules and regulations of the Securities and Exchange Commission (SEC). Accordingly, certain disclosures required by accounting principles generally accepted in the United States and normally included in annual reports on Form 10-K have been omitted. Although management believes that our disclosures in these interim financial statements are adequate, they should be read in conjunction with the financial statements, summary of significant accounting policies, and footnotes included in our 2012 Annual Report on Form 10-K.

In the opinion of management, the accompanying financial statements reflect all adjustments necessary to present fairly our financial position, results of operations, and cash flows for the periods shown. Certain amounts in prior years financial statements have been reclassified to conform to the 2012 financial statement presentation. We have evaluated subsequent events through the date of this filing.

Oil and Gas Properties

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

At June 30, 2013, the calculated value of the ceiling limitation exceeded the carrying value of our oil and gas properties subject to the test, and no impairment was necessary. However, our ceiling limitation has declined since December 31, 2012. A significant component of the decrease is related to decreases in the 12-month average trailing prices for oil and NGLs, which have reduced proved reserve values. If pricing conditions decline, or if there is a negative impact on one or more of the other components of the calculation, we may incur a full cost ceiling impairment related to our oil and gas properties in future quarters.

Use of Estimates

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

Accounts Receivable, Accounts Payable, and Accrued Liabilities

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

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CIMAREX ENERGY CO.

Notes to Consolidated Financial Statements (Continued)

June 30, 2013

(Unaudited)

(in thousands)		June 30, 2013		December 31, 2012
Receivables, net of allowance				
Trade	$	87,114	$	55,528
Oil and gas sales		281,962		239,106
Gas gathering, processing, and marketing		12,347		7,901
Other		211		439
Receivables, net	$	381,634	$	302,974
Accounts payable				
Trade	$	58,225	$	88,168
Gas gathering, processing, and marketing		24,465		15,485
Accounts payable	$	82,690	$	103,653
Accrued liabilities				
Exploration and development	$	175,233	$	155,002
Taxes other than income		23,119		29,179
Other		217,759		208,728
Accrued liabilities	$	416,111	$	392,909

Recently Issued Accounting Standards

No significant accounting standards applicable to Cimarex have been issued during the quarter ended June 30, 2013.

2. Derivative Instruments/Hedging

We periodically enter into derivative instruments to mitigate a portion of our potential exposure to a decline in commodity prices and the corresponding negative impact on cash flow available for reinvestment. While the use of these instruments limits the downside risk of adverse price changes, their use may also limit future revenues from favorable price changes.

The following tables summarize our outstanding contracts as of June 30, 2013. We have elected not to account for these derivatives as cash flow hedges.

Oil Contracts

Period		Type	Volume/Day	Index(1)	Weighted Average Price Floor	Ceiling	Swap	Fair Value (in thousands)
Jul 13	Dec 13	Collars	6,000 Bbls	WTI	$ 85.00	$ 102.31		$ (18)
Jul 13	Dec 13	Swaps	6,000 Bbls	WTI			$ 96.13	$ 1,110

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

Gas Contracts

Period		Type	Volume/Day	Index(1)	Weighted Average Price Floor	Ceiling	Fair Value (in thousands)
Jul 13	Dec 14	Collars	80,000 MMBtu	PEPL	$ 3.51	$ 4.57	$ 9,200

(1) PEPL refers to Panhandle Eastern Pipe Line, Tex/OK Mid-Continent Index as quoted in Platt s Inside FERC.

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

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Notes to Consolidated Financial Statements (Continued)

June 30, 2013

(Unaudited)

index price is between the floor and ceiling prices. For a swap contract, the counterparty is required to make a payment to us if the settlement price for any settlement period is less than the swap price. We are required to make a payment to the counterparty if the settlement price for the settlement period is greater than the swap price.

Depending on changes in oil and gas futures markets and management s view of underlying supply and demand trends, we may increase or decrease our current hedging positions.

The following table summarizes the realized and unrealized gains and (losses) from settlements and changes in fair value of our derivative contracts as presented in our accompanying financial statements.

	Three Months Ended June 30,		Six Months Ended June 30,	
(in thousands)	**2013**	**2012**	**2013**	**2012**
Settlements gains (losses):				
Natural gas contracts	$	$	$	$
Oil contracts	1,039		1,765	
Total settlements gains (losses)	1,039		1,765	
Unrealized gains (losses) on fair value change:				
Natural gas contracts	9,199		9,199	
Oil contracts	3,422	10,078	1,093	5,990
Total unrealized gains (losses) on fair value change	12,621	10,078	10,292	5,990
Gain (loss) on derivative instruments, net	$ 13,660	$ 10,078	$ 12,057	$ 5,990

Our derivative contracts are carried at their fair value on our balance sheet using Level 2 inputs. We estimate the fair value using internal risk-adjusted discounted cash flow calculations. Cash flows are based on published forward commodity price curves for the underlying commodity as of the date of the estimate. For collars, we estimate the option value of the contract floors and ceilings using an option pricing model which takes into account market volatility, market prices, and contract terms.

The fair value of our derivative instruments in an asset position includes a measure of counterparty credit risk and the fair value of instruments in a liability position includes a measure of our own nonperformance risk. These credit risks are based on current published credit default swap rates.

Due to the volatility of commodity prices, the estimated fair value of our derivative instruments is subject to fluctuation from period to period, which could result in significant differences between the current estimated fair value and the ultimate settlement price. The following table presents the estimated fair value of our derivative assets and liabilities as of June 30, 2013. All of our derivative contracts entered into prior to January 1, 2013 were settled as of December 31, 2012. Our derivatives are presented on a gross basis.

June 30, 2013:

(in thousands)	**Balance Sheet Location**		**Asset**		**Liability**
Oil contracts	Current assets Derivative instruments	$	1,151	$	
Natural gas contracts	Current assets Derivative instruments	$	6,805	$	
Natural gas contracts	Noncurrent assets Derivative instruments	$	2,395	$	
Oil contracts	Current liabilities Derivative instruments	$		$	59
		$	10,351	$	59

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Notes to Consolidated Financial Statements (Continued)

June 30, 2013

(Unaudited)

Because we elect not to account for our current derivative contracts as cash flow hedges, we recognize all realized settlements and unrealized changes in fair value in earnings. Cash settlements of our derivative contracts are included in cash flows from operating activities in our statements of cash flows.

We are exposed to financial risks associated with these contracts from nonperformance by our counterparties. Counterparty risk is also a component of our estimated fair value calculations. We have mitigated our exposure to any single counterparty by contracting with a number of financial institutions, each of which has a high credit rating and is a member of our bank credit facility. Our member banks do not require us to post collateral for our hedge liability positions.

3. Fair Value Measurements

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

The following tables provide fair value measurement information for certain assets and liabilities as of June 30, 2013 and December 31, 2012:

June 30, 2013: **(in thousands)**	**Carrying Amount**	**Fair Value**
Financial Assets (Liabilities):		
Bank debt	$ (142,000)	$ (142,000)
5.875% Notes due 2022	$ (750,000)	$ (780,000)
Derivative instruments assets	$ 10,351	$ 10,351
Derivative instruments liabilities	$ (59)	$ (59)

December 31, 2012: **(in thousands)**	**Carrying Amount**	**Fair Value**

Financial (Liabilities):		
5.875% Notes due 2022	$ (750,000)	$ (825,750)

Assessing the significance of a particular input to the fair value measurement requires judgment, including the consideration of factors specific to the asset or liability. The following methods and assumptions were used to estimate the fair value of the assets and liabilities in the table above.

Debt (Level 1)

The fair value of our bank debt at June 30, 2013 was estimated to approximate the carrying amount because the floating rate interest paid on such debt was set for periods of three months or less.

The fair value for our 5.875% fixed rate notes was based on their last traded value before period end.

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Notes to Consolidated Financial Statements (Continued)

June 30, 2013

(Unaudited)

Derivative Instruments (Level 2)

The fair value of our derivative instruments was estimated using internal discounted cash flow calculations. Cash flows are based on the stated contract prices and current and published forward commodity price curves, adjusted for volatility. The cash flows are risk adjusted relative to nonperformance for both our counterparties and our liability positions. Please see Note 2 for further information on the fair value of our derivative instruments.

Other Financial Instruments

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

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

We routinely assess the recoverability of all material accounts receivable to determine their collectability. We accrue a reserve to the allowance for doubtful accounts when, based on the judgment of management, it is probable that a receivable will not be collected and the amount of the reserve may be reasonably estimated. At June 30, 2013 and December 31, 2012, the allowance for doubtful accounts was $6.5 million.

4. Capital Stock

Authorized capital stock consists of 200 million shares of common stock and 15 million shares of preferred stock. At June 30, 2013, there were no shares of preferred stock outstanding. A summary of our common stock activity for the six months ended June 30, 2013 follows:

(in thousands)	
Issued and outstanding as of December 31, 2012	86,596
Restricted shares issued under compensation plans, net of reacquired stock and cancellations	(136)
Option exercises, net of cancellations	43
Issued and outstanding as of June 30, 2013	86,503

Dividends

In May 2013, the Board of Directors declared a cash dividend of $0.14 per share. The dividend is payable on September 3, 2013 to stockholders of record on August 15, 2013. Future dividend payments will depend on our level of earnings, financial requirements, and other factors considered relevant by the Board of Directors.

5. Stock-based Compensation

Our 2011 Equity Incentive Plan (the 2011 Plan) was approved by stockholders in May 2011 and our previous plan was terminated at that time. Outstanding awards under the previous plan were not impacted. The 2011 Plan provides for grants of stock options, restricted stock, restricted stock units,

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CIMAREX ENERGY CO.

Notes to Consolidated Financial Statements (Continued)

June 30, 2013

(Unaudited)

performance stock and performance stock units. A total of 5.3 million shares of common stock may be issued under the 2011 Plan.

We have recognized non-cash stock-based compensation cost as follows:

	Three Months Ended June 30,		Six Months Ended June 30,	
(in thousands)	**2013**	**2012**	**2013**	**2012**
Restricted stock	$ 6,017	$ 6,729	$ 11,923	$ 13,550
Stock options	707	632	1,415	1,425
	6,724	7,361	13,338	14,975
Less amounts capitalized to oil and gas properties	(3,217)	(2,677)	(6,226)	(5,757)
Compensation expense	$ 3,507	$ 4,684	$ 7,112	$ 9,218

Historical amounts may not be representative of future amounts as additional awards may be granted.

Restricted Stock and Units

The following tables provide information about restricted stock awards granted during the three and six months ended June 30, 2013 and 2012.

	Three Months Ended June 30, 2013		Three Months Ended June 30, 2012	
	Number of Shares	**Weighted Average Grant-Date Fair Value**	**Number of Shares**	**Weighted Average Grant-Date Fair Value**
Performance-based stock awards		$	238,770	$ 51.95
Service-based stock awards	49,036	$ 70.92	37,598	$ 56.17
Total restricted stock awards	49,036	$ 70.92	276,368	$ 52.52

	Six Months Ended June 30, 2013	Six Months Ended June 30, 2012

	Number of Shares		Weighted Average Grant-Date Fair Value	Number of Shares		Weighted Average Grant-Date Fair Value
Performance-based stock awards		$		238,770	$	51.95
Service-based stock awards	49,036	$	70.92	56,098	$	57.59
Total restricted stock awards	49,036	$	70.92	294,868	$	53.02

From time to time performance-based awards are granted to eligible executives and are subject to market condition-based vesting determined by our stock price performance relative to a defined peer group s stock price performance. After three years of continued service, an executive will be entitled to vest in 50% to 100% of the award. In accordance with Internal Revenue Code Section 162(m), certain of the amounts awarded may not be deductible for tax purposes. Service-based stock awards granted to other eligible employees and non-employee directors have vesting schedules of three to five years.

Compensation cost for the performance-based stock awards is based on the grant-date fair value of the award utilizing a Monte Carlo simulation model. Compensation cost for the service-based vesting restricted shares is based upon the grant-date market value of the award. Such costs are recognized ratably over the applicable vesting period.

The following table reflects the non-cash compensation cost related to our restricted stock:

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CIMAREX ENERGY CO.

Notes to Consolidated Financial Statements (Continued)

June 30, 2013

(Unaudited)

	Three Months Ended June 30,				Six Months Ended June 30,			
(in thousands)	**2013**		**2012**		**2013**		**2012**	
Performance-based stock awards	$	2,568	$	4,082	$	5,253	$	7,671
Service-based stock awards		3,449		2,647		6,670		5,879
		6,017		6,729		11,923		13,550
Less amounts capitalized to oil and gas properties		(2,954)		(2,439)		(5,738)		(5,169)
Restricted stock compensation expense	$	3,063	$	4,290	$	6,185	$	8,381

Unrecognized compensation cost related to unvested restricted shares at June 30, 2013 was $45.1 million, which we expect to recognize over a weighted average period of approximately 2.1 years.

The following table provides information on restricted stock and unit activity as of June 30, 2013 and changes during the year. A restricted unit held by an employee represents a right to an unrestricted share of common stock upon completion of defined vesting and holding periods. A restricted unit held by a non-employee director represents an election to defer payment of director fees until the time specified by the director in his deferred compensation agreement. The remaining outstanding restricted units shown below represent restricted units held by a non-employee director who has elected to defer payment of common stock represented by the units until termination of his service on the Board of Directors.

	Restricted Stock	**Restricted Units**
Outstanding as of January 1, 2013	1,838,736	33,838
Vested	(218,175)	
Converted to stock		(25,000)
Granted	49,036	
Canceled	(108,680)	
Outstanding as of June 30, 2013	1,560,917	8,838
Vested included in outstanding	N/A	8,838

Stock Options

Options granted under our 2011 and previous plans expire seven to ten years from the grant date and have service-based vesting schedules of three to five years. The plans provide that all grants have an exercise price of the average of the high and low prices of our common stock as reported by the New York Stock Exchange on the date of grant. No options were granted during the first six months of 2013 and 2012.

Compensation cost related to stock options is based on the grant-date fair value of the award, recognized ratably over the applicable vesting period. We estimate the fair value using the Black-Scholes option-pricing model. Expected volatilities are based on the historical volatility of our common stock. We also use historical data to estimate the probability of option exercise, expected years until exercise and potential forfeitures. We use U.S. Treasury bond rates in effect at the grant date for our risk-free interest rates.

Non-cash compensation cost related to our stock options is reflected in the following table:

	Three Months Ended June 30,		Six Months Ended June 30,	
(in thousands)	**2013**	**2012**	**2013**	**2012**
Stock option awards	$ 707	$ 632	$ 1,415	$ 1,425
Less amounts capitalized to oil and gas properties	(263)	(238)	(488)	(588)
Stock option compensation expense	$ 444	$ 394	$ 927	$ 837

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CIMAREX ENERGY CO.

Notes to Consolidated Financial Statements (Continued)

June 30, 2013

(Unaudited)

As of June 30, 2013, there was $3.3 million of unrecognized compensation cost related to non-vested stock options. We expect to recognize that cost pro rata over a weighted-average period of approximately 1.5 years.

Information about outstanding stock options is summarized below:

	Options	Weighted Average Exercise Price	Weighted Average Remaining Term	Aggregate Intrinsic Value (in thousands)
Outstanding as of January 1, 2013	687,459	$ 54.51		
Exercised	(43,156)	$ 39.53		
Canceled	(1,665)	$ 86.00		
Forfeited	(8,172)	$ 73.43		
Outstanding as of June 30, 2013	634,466	$ 55.21	5.4 Years	$ 8,587
Exercisable as of June 30, 2013	330,083	$ 50.75	5.1 Years	$ 5,738

The following table provides information regarding the options exercised:

(dollars in thousands)	Six Months Ended June 30, 2013	2012
Number of options exercised	43,156	58,071
Cash received from option exercises	$ 1,705	$ 2,764
Intrinsic value of options exercised	$ 1,407	$ 1,605

The following summary reflects the status of non-vested stock options as of June 30, 2013 and changes during the year:

	Options	Weighted Average Grant-Date Fair Value	Weighted Average Exercise Price
Non-vested as of January 1, 2013	317,062	$ 23.22	$ 60.58
Vested	(4,507)	$ 28.96	$ 74.34
Forfeited	(8,172)	$ 29.10	$ 73.43

Non-vested as of June 30, 2013	304,383	$	22.98	$	60.04

6. Asset Retirement Obligations

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

The following table reflects the components of the change in the carrying amount of the asset retirement obligation for the six months ended June 30, 2013:

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CIMAREX ENERGY CO.

Notes to Consolidated Financial Statements (Continued)

June 30, 2013

(Unaudited)

(in thousands)		
Asset retirement obligation at January 1, 2013	$	185,138
Liabilities incurred		2,443
Liability settlements and disposals		(28,360)
Accretion expense		4,136
Revisions of estimated liabilities		(6,524)
Asset retirement obligation at June 30, 2013		156,833
Less current obligation		(48,156)
Long-term asset retirement obligation	$	108,677

7. Long-Term Debt

Debt at June 30, 2013 and December 31, 2012 consisted of the following:

(in thousands)		**June 30, 2013**		**December 31, 2012**
Bank debt	$	142,000	$	
5.875% Senior Notes due 2022		750,000		