MURPHY OIL CORP /DE
Form 10-Q
August 05, 2014
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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**

For the quarterly period ended June 30, 2014

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

MURPHY OIL CORPORATION

(Exact name of registrant as specified in its charter)

Delaware	**71-0361522**
(State or other jurisdiction of	**(I.R.S. Employer**
incorporation or organization)	**Identification Number)**

200 Peach Street

P.O. Box 7000, El Dorado, Arkansas	**71731-7000**
(Address of principal executive offices)	**(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. x 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). x 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	x	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 x No

Number of shares of Common Stock, $1.00 par value, outstanding at June 30, 2014 was **177,571,522.**

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MURPHY OIL CORPORATION

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PART I FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS

Murphy Oil Corporation and Consolidated Subsidiaries

CONSOLIDATED BALANCE SHEETS

(Thousands of dollars)

	(Unaudited) June 30, 2014	December 31, 2013
ASSETS		
Current assets		
Cash and cash equivalents	$ 661,086	750,155
Canadian government securities with maturities greater than 90 days at the date of acquisition	427,372	374,842
Accounts receivable, less allowance for doubtful accounts of $1,609 in 2014 and 2013	1,053,122	999,872
Inventories, at lower of cost or market		
Crude oil	38,119	40,077
Materials and supplies	251,375	254,118
Prepaid expenses	125,046	83,856
Deferred income taxes	59,619	61,991
Assets held for sale	617,194	943,732
Total current assets	3,232,933	3,508,643
Property, plant and equipment, at cost less accumulated depreciation, depletion and amortization of $9,318,710 in 2014 and $8,540,239 in 2013	14,196,884	13,481,055
Goodwill	40,083	40,259
Deferred charges and other assets	101,883	98,123
Assets held for sale	302,151	381,404
Total assets	$ 17,873,934	17,509,484
LIABILITIES AND STOCKHOLDERS EQUITY		
Current liabilities		
Current maturities of long-term debt	$ 35,100	26,249
Accounts payable and accrued liabilities	2,257,458	2,335,712
Income taxes payable	302,028	222,930
Liabilities associated with assets held for sale	255,935	639,140
Total current liabilities	2,850,521	3,224,031
Long-term debt, including capital lease obligation	3,786,494	2,936,563
Deferred income taxes	1,507,484	1,466,100
Asset retirement obligations	905,467	852,488
Deferred credits and other liabilities	331,144	339,028
Liabilities associated with assets held for sale	93,927	95,544
Stockholders equity		
Cumulative Preferred Stock, par $100, authorized 400,000 shares, none issued	0	0
Common Stock, par $1.00, authorized 450,000,000 shares, issued 195,017,103 shares in 2014 and 194,920,155 shares in 2013	195,017	194,920
Capital in excess of par value	886,292	902,633
Retained earnings	8,231,331	8,058,792
Accumulated other comprehensive income	172,531	172,119

Treasury stock, 17,445,581 shares of Common Stock in 2014 and 11,513,642 shares of Common Stock in 2013, at cost	(1,086,274)	(732,734)
Total stockholders equity	8,398,897	8,595,730
Total liabilities and stockholders equity	$ 17,873,934	17,509,484

See Notes to Consolidated Financial Statements, page 7.

The Exhibit Index is on page 36.

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Murphy Oil Corporation and Consolidated Subsidiaries

CONSOLIDATED STATEMENTS OF INCOME (unaudited)

(Thousands of dollars, except per share amounts)

	Three Months Ended June 30, 2014	Three Months Ended June 30, 2013*	Six Months Ended June 30, 2014	Six Months Ended June 30, 2013*
REVENUES				
Sales and other operating revenues	$ 1,357,905	1,315,600	2,639,113	2,614,526
Interest and other income (loss)	(8,884)	16,386	(3,692)	8,398
Total revenues	1,349,021	1,331,986	2,635,421	2,622,924
COSTS AND EXPENSES				
Lease operating expenses	285,865	251,775	548,120	588,998
Severance and ad valorem taxes	28,893	20,334	55,219	35,397
Exploration expenses, including undeveloped lease amortization	134,812	88,772	273,278	197,265
Selling and general expenses	95,000	86,904	187,026	168,371
Depreciation, depletion and amortization	458,993	381,384	855,242	744,526
Impairment of assets	0	21,587	0	21,587
Accretion of asset retirement obligations	12,327	11,961	24,392	23,857
Interest expense	33,769	29,593	66,655	56,621
Interest capitalized	(5,053)	(14,478)	(13,921)	(27,866)
Other expense	(178)	0	636	0
Total costs and expenses	1,044,428	877,832	1,996,647	1,808,756
Income from continuing operations before income taxes	304,593	454,154	638,774	814,168
Income tax expense	161,925	194,265	326,820	371,596
Income from continuing operations	142,668	259,889	311,954	442,572
Income (loss) from discontinued operations, net of taxes	(13,256)	142,755	(27,289)	320,671
NET INCOME	$ 129,412	402,644	284,665	763,243
PER COMMON SHARE BASIC				
Income from continuing operations	$ 0.80	1.38	1.73	2.33
Income (loss) from discontinued operations	(0.08)	0.75	(0.15)	1.69
Net income	$ 0.72	2.13	1.58	4.02
PER COMMON SHARE DILUTED				
Income from continuing operations	$ 0.79	1.37	1.72	2.32
Income (loss) from discontinued operations	(0.07)	0.75	(0.15)	1.68
Net income	$ 0.72	2.12	1.57	4.00
Average common shares outstanding				
Basic	178,500,440	189,002,146	180,003,605	189,753,673
Diluted	180,045,020	189,944,793	181,327,914	190,702,248

* Reclassified to conform to current presentation See Note D.
See Notes to Consolidated Financial Statements, page 7.

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Murphy Oil Corporation and Consolidated Subsidiaries

CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME (unaudited)

(Thousands of dollars)

	Three Months Ended June 30,		Six Months Ended June 30,	
	2014	2013	2014	2013
Net income	$ 129,412	402,644	284,665	763,243
Other comprehensive income (loss), net of tax				
Net gain (loss) from foreign currency translation	133,559	(117,254)	(3,045)	(235,008)
Retirement and postretirement benefit plans	1,026	4,532	2,491	7,270
Deferred loss on interest rate hedges reclassified to interest expense	483	484	966	970
Other comprehensive income (loss)	135,068	(112,238)	412	(226,768)
COMPREHENSIVE INCOME	$ 264,480	290,406	285,077	536,475

See Notes to Consolidated Financial Statements, page 7.

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Murphy Oil Corporation and Consolidated Subsidiaries

CONSOLIDATED STATEMENTS OF CASH FLOWS (unaudited)

(Thousands of dollars)

	Six Months Ended June 30, 2014	Six Months Ended June 30, 2013[1]
OPERATING ACTIVITIES		
Net income	$ 284,665	763,243
Adjustments to reconcile net income to net cash provided by operating activities		
Loss (income) from discontinued operations	27,289	(320,671)
Depreciation, depletion and amortization	855,242	744,526
Impairment of assets	0	21,587
Amortization of deferred major repair costs	4,313	4,415
Dry hole costs	127,827	81,305
Amortization of undeveloped leases	37,764	32,052
Accretion of asset retirement obligations	24,392	23,857
Deferred and noncurrent income tax charges	18,122	72,745
Pretax loss from disposition of assets	4,997	224
Net (increase) decrease in noncash operating working capital	48,449	(131,812)
Other operating activities, net	22,106	(22,487)
Net cash provided by continuing operations	1,455,166	1,268,984
Net cash provided by discontinued operations	4,517	400,026
Net cash provided by operating activities	1,459,683	1,669,010
INVESTING ACTIVITIES		
Property additions and dry hole costs[2]	(1,840,544)	(1,853,902)
Proceeds from sales of assets	3,089	130
Purchase of investment securities[3]	(372,861)	(373,196)
Proceeds from maturity of investment securities[3]	320,331	358,915
Investing activities of discontinued operations		
Sales proceeds	0	282,202
Property additions and other	(9,092)	(122,807)
Other net	(13,007)	1,718
Net cash required by investing activities	(1,912,084)	(1,706,940)
FINANCING ACTIVITIES		
Borrowings of long-term debt[2]	850,000	461,978
Purchase of treasury stock	(375,000)	(250,000)
Proceeds from exercise of stock options and employee stock purchase plans	0	2,628
Withholding tax on stock-based incentive awards	(6,784)	(8,966)
Cash dividends paid	(112,126)	(119,376)
Other net	(1,224)	(2,724)
Net cash provided by financing activities	354,866	83,540
Effect of exchange rate changes on cash and cash equivalents	8,466	(18,500)

Net increase (decrease) in cash and cash equivalents	(89,069)	27,110
Cash and cash equivalents at January 1	750,155	947,316
Cash and cash equivalents at June 30	$ 661,086	974,426

[1] Reclassified to conform to current presentation See Note D.

[2] Excludes non-cash asset and long-term obligation of $356,170 in 2013 associated with lease commencement for production equipment at the Kakap field offshore Malaysia.

[3] Investments 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)

	Six Months Ended June 30, 2014	2013
Cumulative Preferred Stock par $100, authorized 400,000 shares, none issued	0	0
Common Stock par $1.00, authorized 450,000,000 shares, issued 195,017,103 at June 30, 2014 and 194,770,571 shares at June 30, 2013		
Balance at beginning of period	$ 194,920	194,616
Exercise of stock options	97	155
Balance at end of period	195,017	194,771
Capital in Excess of Par Value		
Balance at beginning of period	902,633	873,934
Exercise of stock options, including income tax benefits	(11,232)	1,928
Restricted stock transactions and other	(27,970)	(24,485)
Stock-based compensation	22,884	30,327
Other	(23)	(87)
Balance at end of period	886,292	881,617
Retained Earnings		
Balance at beginning of period	8,058,792	7,717,389
Net income for the period	284,665	763,243
Cash dividends	(112,126)	(119,376)
Balance at end of period	8,231,331	8,361,256
Accumulated Other Comprehensive Income		
Balance at beginning of period	172,119	408,901
Foreign currency translation loss, net of income taxes	(3,045)	(235,008)
Retirement and postretirement benefit plans, net of income taxes	2,491	7,270
Deferred loss on interest rate hedges reclassified to interest expense, net of income taxes	966	970
Balance at end of period	172,531	182,133
Treasury Stock		
Balance at beginning of period	(732,734)	(252,805)
Purchase of treasury shares	(375,000)	(250,000)
Sale of stock under employee stock purchase plans	275	655
Awarded restricted stock, net of forfeitures	21,185	16,545
Balance at end of period	(1,086,274)	(485,605)
Total Stockholders Equity	$ 8,398,897	9,134,172

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 Interim Financial Statements

The consolidated financial statements of the Company presented herein have not been audited by independent auditors, except for the Consolidated Balance Sheet at December 31, 2013. 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 June 30, 2014, and the results of operations, cash flows and changes in stockholders equity for the three-month and six-month periods ended June 30, 2014 and 2013, 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 2013 Form 10-K report, as certain notes and other pertinent information have been abbreviated or omitted in this report. Financial results for the three-month and six-month periods ended June 30, 2014 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.

At June 30, 2014, the Company had total capitalized exploratory well costs pending the determination of proved reserves of $396.4 million. The following table reflects the net changes in capitalized exploratory well costs during the six-month periods ended June 30, 2014 and 2013.

(Thousands of dollars)	2014	2013
Beginning balance at January 1	$ 393,030	445,697
Additions pending the determination of proved reserves	3,376	27,129
Reclassifications to proved properties based on the determination of proved reserves	0	(28,398)
Balance at June 30	$ 396,406	444,428

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.

	June 30,					
	2014			2013		
(Thousands of dollars)	Amount	No. of Wells	No. of Projects	Amount	No. of Wells	No. of Projects
Aging of capitalized well costs:						
Zero to one year	$ 32,192	2	1	$ 49,994	3	1
One to two years	50,333	3	1	37,898	5	1
Two to three years	37,969	5	0	73,863	7	3
Three years or more	275,912	22	7	282,673	26	5
	$ 396,406	32	9	$ 444,428	41	10

Of the $364.2 million of exploratory well costs capitalized more than one year at June 30, 2014, $214.2 million is in Malaysia, $116.3 million is in the U.S. and $33.7 million is in Brunei. In all three geographical areas, either further appraisal or development drilling is planned and/or development studies/plans are in various stages of completion.

See also Note E for discussion regarding a capital lease of production equipment at the Kakap field.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Contd.)

Note C Inventories

Inventories are carried at the lower of cost or market. For the Company s U.K. refining and marketing operations reported as discontinued operations, the cost of crude oil and finished products is predominantly determined on the last-in, first-out (LIFO) method. At June 30, 2014 and December 31, 2013, the carrying value of inventories under the LIFO method was $161.2 million and $268.6 million, respectively, less than such inventories would have been valued using the first-in, first-out (FIFO) method. These inventories are included in assets held for sale on the Consolidated Balance Sheet.

Note D Discontinued Operations

The Company has previously announced its intention to sell its U.K. refining and marketing operations. The Company has accounted for this U.K. downstream business as discontinued operations for all periods presented, including a reclassification of 2013 operating results and cash flows for this business to discontinued operations. The U.K. downstream operations were previously reported as a separate segment within the Company s former refining and marketing business. On July 31, 2014, Murphy signed an agreement to sell the Milford Haven, Wales, refinery and terminal assets. Pending regulatory approval and subject to other material conditions, this transaction is scheduled to be completed by October 31, 2014. Additionally, a separate transaction for sale of the U.K. retail marketing business is at an advanced stage.

On August 30, 2013, Murphy Oil Corporation (the Company) distributed 100% of the outstanding common stock of Murphy USA Inc. (MUSA) to its shareholders in a generally tax-free spin-off for U.S. federal income tax purposes. Prior to the separation, MUSA held all of the Company s U.S. downstream operations, including retail gasoline stations and other marketing assets, plus two ethanol production facilities. The shares of MUSA common stock are traded on the New York Stock Exchange under the ticker symbol MUSA. The Company has no continuing involvement with MUSA operations. Accordingly, the operating results and the cash flows for these former U.S. downstream operations have been reported as discontinued operations in the 2013 consolidated financial statements. The U.S. downstream operations were previously reported as a separate segment within the Company s former refining and marketing business.

The Company also sold its oil and gas assets in the United Kingdom during 2013. After-tax gains on sale of the assets were $68.8 million in the three months ended June 30, 2013 and $216.2 million in the six months ended June 30, 2013. The Company has accounted for these U.K. upstream operations as discontinued operations in its consolidated financial statements for all periods presented.

The results of operations associated with these discontinued operations for the three-month and six-month periods ended June 30, 2014 and 2013 were as follows:

	Three Months Ended June 30,		Six Months Ended June 30,	
(Thousands of dollars)	2014	2013	2014	2013
Revenues	$ 811,134	5,964,045	2,243,520	11,479,583
Income before income taxes, including pretax gain on disposals of $55,640 and $130,568 during the three-month and six-month periods in 2013	$ (16,938)	184,418	(34,233)	317,339
Income tax expense (benefit)	(3,682)	41,663	(6,944)	(3,332)
Income (loss) from discontinued operations	$ (13,256)	142,755	(27,289)	320,671

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Contd.)

Note D Discontinued Operations (Contd.)

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 June 30, 2014 and December 31, 2013:

(Millions of dollars)	June 30, 2014	December 31, 2013
Current assets		
Cash	$ 242,438	301,302
Accounts receivable	165,972	302,059
Inventories	126,656	254,240
Other	82,128	86,131
Total current assets held for sale	$ 617,194	943,732
Non-current assets		
Property, plant and equipment, net	$ 279,555	360,347
Other	22,596	21,057
Total non-current assets held for sale	$ 302,151	381,404
Current liabilities		
Accounts payable	$ 255,470	637,432
Other	465	1,708
Total current liabilities associated with assets held for sale	$ 255,935	639,140
Non-current liabilities		
Deferred income taxes payable	$ 75,896	68,096
Deferred credits and other liabilities	18,031	27,448
Total non-current liabilities associated with assets held for sale	$ 93,927	95,544

Note E Financing Arrangements and Debt

The Company has a $2.0 billion committed credit facility that expires in June 2017. Borrowings under the facility bear interest at 1.25% above LIBOR based on the Company s current credit rating as of June 30, 2014. In addition, facility fees of 0.25% are charged on the full $2.0 billion commitment. 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 2015.

During June 2013, the Company and its partners entered into 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 June 2028. Current maturities and long-term debt on the Consolidated Balance Sheet include $35.1 million and $341.7 million associated with this lease at June 30, 2014.

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Contd.)

Note F Cash Flow Disclosures

Additional disclosures regarding cash flow activities are provided below.

(Thousands of dollars)	Six Months Ended June 30, 2014	2013
Net (increase) decrease in operating working capital other than cash and cash equivalents:		
Increase in accounts receivable	$ (53,133)	(367,478)
Decrease (increase) in inventories	5,574	(11,154)
Increase in prepaid expenses	(41,191)	(112,303)
Decrease in deferred income tax assets	1,895	75,616
Increase in accounts payable and accrued liabilities	55,729	127,301
Increase in current income tax liabilities	79,575	156,206
Total	$ 48,449	(131,812)
Supplementary disclosures (including discontinued operations):		
Cash income taxes paid	$ 234,071	196,923
Interest paid, net of amounts capitalized	41,922	25,010

Note G 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.

Effective with the spin-off of Murphy s former U.S. retail marketing operation, Murphy USA Inc. (MUSA) on August 30, 2013, significant modifications were made to the U.S. defined benefit pension plan. Certain Murphy employees benefits under the U.S. plan were frozen at that time. No further benefit service will accrue for the affected employees; however, the plan will recognize future eligible earnings after the spin-off date. In addition, all previously unvested benefits became fully vested at the spin-off date. For those affected active employees of the Company, additional U.S. retirement plan benefits will accrue in future periods under a cash balance formula. Employees hired after August 30, 2013 will only accrue plan benefits under the cash balance formula. Upon the spin-off of MUSA, Murphy retained all vested pension defined benefit and other postretirement benefit obligations associated with current and former employees of this separated business. No additional benefit will accrue for any employees of MUSA under the Company s retirement plan after the spin-off date.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Contd.)

Note G Employee and Retiree Benefit Plans ***(Contd.)***

The table that follows provides the components of net periodic benefit expense for the three-month and six-month periods ended June 30, 2014 and 2013.

	Three Months Ended June 30,			
	Pension Benefits		Other Postretirement Benefits	
(Thousands of dollars)	2014	2013	2014	2013
Service cost	$ 6,284	7,094	672	1,230
Interest cost	8,253	7,700	1,277	1,279
Expected return on plan assets	(8,528)	(7,569)	0	0
Amortization of prior service cost	228	303	(20)	(44)
Amortization of transitional asset	212	121	2	2
Recognized actuarial loss	1,733	4,759	59	473
Net periodic benefit expense	$ 8,182	12,408	1,990	2,940

	Six Months Ended June 30,			
	Pension Benefits		Other Postretirement Benefits	
(Thousands of dollars)	2014	2013	2014	2013
Service cost	$ 12,840	14,697	1,344	2,397
Interest cost	16,468	14,131	2,555	2,513
Expected return on plan assets	(17,008)	(13,269)	0	0
Amortization of prior service cost	453	579	(41)	(86)
Amortization of transitional asset	420	241	3	4
Recognized actuarial loss	3,466	8,291	118	930
Net periodic benefit expense	$ 16,639	24,670	3,979	5,758

During the six-month period ended June 30, 2014, the Company made contributions of $36.2 million to its defined benefit pension and postretirement benefit plans. Remaining funding in 2014 for the Company s defined benefit pension and postretirement plans is anticipated to be $15.6 million.

Note H Incentive Plans

The costs resulting from all share-based payment transactions are recognized as an expense in the Consolidated Statements of Income 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, 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.

On February 4, 2014, the Committee granted stock options for 772,900 shares at an exercise price of $55.82 per share. The Black-Scholes valuation for these awards was $12.84 per option. The Committee also granted 464,300 performance-based restricted stock units (RSU) and 233,400 time-based RSU on that date. The fair value of the performance-based RSU, using a Monte Carlo valuation model, ranged from $33.90 to $51.30 per unit. The fair value

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Contd.)

Note H Incentive Plans *(Contd.)*

of time-based RSU was estimated based on the fair market value of the Company s stock on the date of grant, which was $55.82 per share. Additionally, on February 4, 2014, the Committee granted 183,200 SAR and 170,900 units of cash-settled RSU (RSU-C) to certain employees. 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. On February 5, 2014, the Committee granted 43,848 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 fair value of these awards was estimated at $55.20 per unit.

Beginning January 1, 2014, all stock option exercises are non-cash transactions for the Company. The employee will receive net shares, after applicable withholding taxes, upon each exercise. Cash received from options exercised under all share-based payment arrangements for the six-month period ended June 30, 2013 was $2.6 million. The actual income tax benefit realized for the tax deductions from option exercises of the share-based payment arrangements totaled $3.1 million and $3.0 million for the six-month periods ended June 30, 2014 and 2013, respectively.

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

	Six Months Ended June 30,	
(Thousands of dollars)	2014	2013
Compensation charged against income before tax benefit	$ 32,142	35,142
Related income tax benefit recognized in income	9,978	7,246

Note I Earnings per Share

Net income was used as the numerator in computing both basic and diluted income per Common share for the three-month and six-month periods ended June 30, 2014 and 2013. The following table reconciles the weighted-average shares outstanding used for these computations.

	Three Months Ended June 30,		Six Months Ended June 30,	
(Weighted-average shares)	2014	2013	2014	2013
Basic method	178,500,440	189,002,146	180,003,605	189,753,673
Dilutive stock options and restricted stock units	1,544,580	942,647	1,324,309	948,575
Diluted method	180,045,020	189,944,793	181,327,914	190,702,248

The following table reflects certain options to purchase shares of common stock that were outstanding during the 2014 and 2013 periods but were not included in the computation of diluted EPS above because the incremental shares from assumed conversion were antidilutive.

	Three Months Ended June 30,		Six Months Ended June 30,	
	2014	2013	2014	2013

Antidilutive stock options excluded from diluted shares		1,161,442		1,731,425		1,810,012		1,414,286
Weighted average price of these options	$	60.02	$	63.52	$	58.90	$	64.39

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Contd.)

Note J Income Taxes

The Company s effective income tax rate generally exceeds the statutory U.S. tax rate of 35%. The effective tax rate is calculated as the amount of income tax expense divided by income before income tax expense. For the three-month and six-month periods in 2014 and 2013, the Company s effective income tax rates were as follows:

	2014	2013
Three months ended June 30	53.2%	42.8%
Six months ended June 30	51.2%	45.6%

The effective tax rates for the periods presented exceeded 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.

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 June 30, 2014, the earliest years remaining open for audit and/or settlement in our major taxing jurisdictions are as follows: United States 2010; Canada 2008; United Kingdom 2011; and Malaysia 2006.

Note K Financial Instruments and Risk Management

Murphy utilizes 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. 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 unrealized gains and losses on these derivative contracts in its Consolidated Statements of Income. Certain interest rate derivative contracts were accounted for as hedges and the loss associated with settlement of these contracts was deferred in Accumulated Other Comprehensive Income. This loss is being reclassified to Interest Expense in the Consolidated Statements of Income 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 it will produce and sell in 2014. The Company has entered into a series of West Texas Intermediate (WTI) crude oil fixed-price swap financial contracts covering a portion of its Eagle Ford Shale production from July 2014 through December 2014. Under these contracts, which mature monthly, the Company will pay the average monthly price in effect and will receive the fixed contract prices. WTI open contracts at June 30, 2014 were as follows:

Dates	Volumes (barrels per day)	Swap Prices
July September 2014	26,000	$ 94.89 per barrel
October December 2014	16,000	$ 92.33 per barrel

The fair value of these open commodity derivative contracts was a net liability of $36.9 million at June 30, 2014.

Foreign Currency Exchange Risks

The Company is subject to foreign currency exchange risk associated with operations in countries outside the United States. Short-term derivative instruments were outstanding at June 30, 2013 to manage the risk of certain future income taxes that are payable in Malaysian ringgits. The equivalent U.S. dollars of Malaysian ringgit derivative contracts open at June 30, 2013 were approximately $153.4 million. There were no open ringgit contracts at June 30, 2014. Short-term derivative instrument contracts totaling $33.0 million and $48.0 million U.S. dollars were also outstanding at June 30, 2014 and 2013, respectively, to manage the risk of certain U.S. dollar accounts receivable associated with sale of crude oil production in Canada. The impact from marking to market these foreign currency derivative contracts increased income before taxes by $0.7 million for the six-month period ended June 30, 2014 and reduced income before taxes by $5.6 million for the six-month period ended June 30, 2013.

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Contd.)

Note K Financial Instruments and Risk Management *(Contd.)*

At June 30, 2014 and December 31, 2013, the fair value of derivative instruments not designated as hedging instruments are presented in the following table.

(Thousands of dollars)	June 30, 2014 Asset (Liability) Derivatives		December 31, 2013 Asset (Liability) Derivatives	
Type of Derivative Contract	Balance Sheet Location	Fair Value	Balance Sheet Location	Fair Value
Commodity	Accounts payable	$ (36,926)	Accounts receivable	$ 1,970
Foreign exchange	Accounts receivable	650	Accounts payable	(1,038)

For the three-month and six-month periods ended June 30, 2014 and 2013, the gains and losses recognized in the Consolidated Statements of Income for derivative instruments not designated as hedging instruments are presented in the following table.

		Gain (Loss)			
(Thousands of dollars)	Statement of Income	Three Months Ended June 30,		Six Months Ended June 30,	
Type of Derivative Contract	Location	2014	2013	2014	2013
Commodity	Crude oil and product purchases	$ (36,041)	0	(54,455)	0
Commodity	Discontinued operations	0	2,834	0	(1,376)
Foreign exchange	Interest and other income	1,464	(1,328)	4,900	(4,146)
		$ (34,577)	1,506	(49,555)	(5,522)

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 a loss on these contracts to match the payment of interest on these notes through 2022. During each of the six-month periods ended June 30, 2014 and 2013, $1.5 million of the deferred loss on the interest rate swaps was charged to income as a component of Interest Expense. The remaining loss deferred on these matured contracts at June 30, 2014 was $23.4 million, which is recorded, net of income taxes of $8.2 million, in Accumulated Other Comprehensive Income in the Consolidated Balance Sheet. The Company expects to charge approximately $1.5 million of this deferred loss to income in the form of interest expense during the remaining six months of 2014.

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 June 30, 2014 and December 31, 2013 are presented in the following table.

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Contd.)

Note K Financial Instruments and Risk Management ***(Contd.)***