

WORLD FUEL SERVICES CORP

Form 10-Q

October 30, 2013

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UNITED STATES
SECURITIES AND EXCHANGE COMMISSION

Washington, DC 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 SEPTEMBER 30, 2013

- o 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 1-9533

WORLD FUEL SERVICES CORPORATION

(Exact name of registrant as specified in its charter)

Florida

(State or other jurisdiction of
incorporation or organization)

59-2459427

(I.R.S. Employer
Identification No.)

9800 N.W. 41st Street, Suite 400

Miami, Florida

(Address of Principal Executive Offices)

33178

(Zip Code)

Registrant's Telephone Number, including area code: **(305) 428-8000**

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

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

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

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

The registrant had a total of 72,261,000 shares of common stock, par value \$0.01 per share, issued and outstanding as of October 24, 2013.

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Part I Financial Information

General

The following unaudited consolidated financial statements and notes thereto of World Fuel Services Corporation and its subsidiaries have been prepared in accordance with the instructions to Quarterly Reports on Form 10-Q and, therefore, omit or condense certain footnotes and other information normally included in financial statements prepared in accordance with accounting principles generally accepted in the United States. In the opinion of management, all adjustments necessary for a fair presentation of the financial information, which are of a normal and recurring nature, have been made for the interim periods reported. Results of operations for the three and nine months ended September 30, 2013 are not necessarily indicative of the results for the entire fiscal year. The unaudited consolidated financial statements and notes thereto included in this Quarterly Report on Form 10-Q for the quarterly period ended September 30, 2013 ("10-Q Report") should be read in conjunction with the audited consolidated financial statements and notes thereto included in our Annual Report on Form 10-K for the fiscal year ended December 31, 2012 ("2012 10-K Report"). World Fuel Services Corporation ("World Fuel" or the "Company") and its subsidiaries are collectively referred to in this 10-Q Report as "we," "our" and "us."

Table of Contents**Item 1. Financial Statements****World Fuel Services Corporation and Subsidiaries****Consolidated Balance Sheets**

(Unaudited - In thousands, except per share data)

	September 30, 2013	As of December 31, 2012
Assets:		
Current assets:		
Cash and cash equivalents	\$ 333,223	\$ 172,740
Accounts receivable, net	2,514,683	2,193,866
Inventories	614,293	572,313
Prepaid expenses	111,853	158,909
Other current assets	201,737	183,549
Total current assets	3,775,789	3,281,377
Property and equipment, net	153,013	112,525
Goodwill	477,258	470,506
Identifiable intangible and other non-current assets	250,340	243,343
Total assets	\$ 4,656,400	\$ 4,107,751
Liabilities:		
Current liabilities:		
Short-term debt	\$ 28,642	\$ 26,065
Accounts payable	2,154,129	1,814,794
Accrued expenses and other current liabilities	302,875	308,439
Total current liabilities	2,485,646	2,149,298
Long-term debt	430,003	354,253
Non-current income tax liabilities, net	63,651	50,879
Other long-term liabilities	14,844	11,697
Total liabilities	2,994,144	2,566,127
Commitments and contingencies		
Equity:		
World Fuel shareholders' equity:		
Preferred stock, \$1.00 par value; 100 shares authorized, none issued		
Common stock, \$0.01 par value; 100,000 shares authorized, 72,277 and 72,147 issued and outstanding as of September 30, 2013 and December 31, 2012, respectively	723	721
Capital in excess of par value	506,005	517,589
Retained earnings	1,158,082	1,014,882
Accumulated other comprehensive loss	(25,078)	(16,018)
Total World Fuel shareholders' equity	1,639,732	1,517,174
Noncontrolling interest equity	22,524	24,450
Total equity	1,662,256	1,541,624
Total liabilities and equity	\$ 4,656,400	\$ 4,107,751

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

Table of Contents**World Fuel Services Corporation and Subsidiaries****Consolidated Statements of Income and Comprehensive Income**

(Unaudited - In thousands, except per share data)

	For the Three Months ended September 30,		For the Nine Months ended September 30,	
	2013	2012	2013	2012
Revenue	\$ 10,493,661	\$ 9,911,673	\$ 31,157,294	\$ 29,009,525
Cost of revenue	10,307,320	9,730,921	30,600,116	28,499,415
Gross profit	186,341	180,752	557,178	510,110
Operating expenses:				
Compensation and employee benefits	72,184	65,843	214,358	176,553
Provision for bad debt	1,863	3,631	5,675	4,413
General and administrative	48,091	40,230	137,265	126,482
	122,138	109,704	357,298	307,448
Income from operations	64,203	71,048	199,880	202,662
Non-operating expenses, net:				
Interest expense and other financing costs, net	(4,580)	(4,305)	(12,818)	(14,403)
Other (expense) income, net	(1,135)	838	(1,207)	1,316
	(5,715)	(3,467)	(14,025)	(13,087)
Income before income taxes	58,488	67,581	185,855	189,575
Provision for income taxes	8,191	14,683	32,090	33,249
Net income including noncontrolling interest	50,297	52,898	153,765	156,326
Net (loss) income attributable to noncontrolling interest	(1,175)	1,404	2,552	9,817
Net income attributable to World Fuel	\$ 51,472	\$ 51,494	\$ 151,213	\$ 146,509
Basic earnings per common share	\$ 0.72	\$ 0.72	\$ 2.12	\$ 2.06
Basic weighted average common shares	71,371	71,216	71,387	71,128
Diluted earnings per common share	\$ 0.72	\$ 0.72	\$ 2.10	\$ 2.04
Diluted weighted average common shares	71,877	71,816	71,970	71,791
Comprehensive income:				
Net income including noncontrolling interest	\$ 50,297	\$ 52,898	\$ 153,765	\$ 156,326
Other comprehensive income (loss):				
Foreign currency translation adjustments	121	(739)	(8,975)	(8,818)
Cash flow hedges, net of income taxes of \$2 and \$25 for the three and nine months ended September 30, 2013, respectively, and \$27 for the three and nine months ended September 30, 2012	(10)	87	(85)	87
	111	(652)	(9,060)	(8,731)
Comprehensive income including noncontrolling interest	50,408	52,246	144,705	147,595
Comprehensive (loss) income attributable to noncontrolling interest	(1,175)	1,404	2,552	9,817
Comprehensive income attributable to World Fuel	\$ 51,583	\$ 50,842	\$ 142,153	\$ 137,778

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

Table of Contents**World Fuel Services Corporation and Subsidiaries****Consolidated Statements of Shareholders' Equity**

(Unaudited - In thousands)

	Common Stock Shares	Common Stock Amount	Capital in Excess of Par Value	Retained Earnings	Accumulated Other Comprehensive Loss	Total World Fuel Shareholders Equity	Noncontrolling Interest Equity	Total Equity
Balance as of December 31, 2012	72,147	\$ 721	\$ 517,589	\$ 1,014,882	\$ (16,018)	\$ 1,517,174	\$ 24,450	\$ 1,541,624
Net income				151,213		151,213	2,552	153,765
Cash dividends declared				(8,013)		(8,013)		(8,013)
Investment by noncontrolling interest							10,019	10,019
Distribution of noncontrolling interest							(14,497)	(14,497)
Amortization of share-based payment awards			12,371			12,371		12,371
Issuance of common stock related to share-based payment awards, including income tax benefit of \$2,692	681	7	2,685			2,692		2,692
Purchases of common stock tendered by employees to satisfy the required withholding taxes related to share-based payment awards	(15)		(6,645)			(6,645)		(6,645)
Purchases of common stock	(536)	(5)	(19,995)			(20,000)		(20,000)
Other comprehensive loss					(9,060)	(9,060)		(9,060)
Balance as of September 30, 2013	72,277	\$ 723	\$ 506,005	\$ 1,158,082	\$ (25,078)	\$ 1,639,732	\$ 22,524	\$ 1,662,256

	Common Stock Shares	Common Stock Amount	Capital in Excess of Par Value	Retained Earnings	Accumulated Other Comprehensive Loss	Total World Fuel Shareholders Equity	Noncontrolling Interest Equity	Total Equity
Balance as of December 31, 2011	71,154	\$ 712	\$ 502,551	\$ 836,222	\$ (6,524)	\$ 1,332,961	\$ 13,757	\$ 1,346,718
Net income				146,509		146,509	9,817	156,326
Cash dividends declared				(8,019)		(8,019)		(8,019)
Distribution of noncontrolling interest							(1,322)	(1,322)
Amortization of share-based payment awards			9,800			9,800		9,800
Issuance of common stock related to share-based payment awards, including income tax benefit of \$1,519	967	9	4,239			4,248		4,248
Purchases of common stock tendered by employees to satisfy the required withholding taxes related to share-based payment awards	(34)		(4,730)			(4,730)		(4,730)
Other comprehensive loss					(8,731)	(8,731)		(8,731)

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Balance as of September 30, 2012	72,087	\$	721	\$	511,860	\$	974,712	\$	(15,255)	\$	1,472,038	\$	22,252	\$	1,494,290
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The accompanying notes are an integral part of these unaudited consolidated financial statements.

Table of Contents**World Fuel Services Corporation and Subsidiaries****Consolidated Statements of Cash Flows**

(Unaudited - In thousands)

	For the Nine Months ended September 30,	
	2013	2012
Cash flows from operating activities:		
Net income including noncontrolling interest	\$ 153,765	\$ 156,326
Adjustments to reconcile net income including noncontrolling interest to net cash provided by operating activities:		
Depreciation and amortization	32,812	26,800
Provision for bad debt	5,675	4,413
Share-based payment award compensation costs	12,578	10,341
Deferred income tax (benefit) provision	(113)	4,724
Extinguishment of liabilities	(4,918)	(9,956)
Foreign currency losses (gains), net	2,427	(3,644)
Other	2,142	1,391
Changes in assets and liabilities, net of acquisitions:		
Accounts receivable, net	(294,271)	(173,120)
Inventories	(40,192)	(110,578)
Prepaid expenses	40,532	(126,750)
Other current assets	(28,563)	(18,465)
Cash collateral with financial counterparties	19,793	6,941
Other non-current assets	(7,455)	2,360
Accounts payable	316,003	247,514
Accrued expenses and other current liabilities	837	30,664
Non-current income tax, net and other long-term liabilities	2,695	(690)
Total adjustments	59,982	(108,055)
Net cash provided by operating activities	213,747	48,271
Cash flows from investing activities:		
Acquisitions and other investments, net of cash acquired	(40,412)	(71,337)
Capital expenditures	(50,286)	(18,737)
Purchase of short-term investments	(21,588)	
Proceeds from the sale of short-term investments	21,588	
Issuance of notes receivable	(469)	(787)
Repayment of notes receivable		401
Net cash used in investing activities	(91,167)	(90,460)
Cash flows from financing activities:		
Borrowings under senior revolving credit facility and senior term loans	3,433,500	2,901,000
Repayments under senior revolving credit facility and senior term loans	(3,349,000)	(2,901,250)
Borrowings of other debt	3,393	
Repayments of other debt	(12,713)	(8,306)
Dividends paid on common stock	(8,020)	(8,019)
Payment of earn-out liability		(4,304)
Investment by noncontrolling interest	10,019	
Distribution of noncontrolling interest	(14,497)	(1,401)
Purchases of common stock	(20,000)	
Federal and state tax benefits resulting from tax deductions in excess of the compensation cost recognized for share-based payment awards	2,692	1,519
Purchases of common stock tendered by employees to satisfy the required withholding taxes related to share-based payment awards	(6,645)	(4,730)
Net cash provided by (used in) financing activities	38,729	(25,491)

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Effect of exchange rate changes on cash and cash equivalents	(826)	1,666
Net increase (decrease) in cash and cash equivalents	160,483	(66,014)
Cash and cash equivalents, as of beginning of period	172,740	205,415
Cash and cash equivalents, as of end of period	\$ 333,223	\$ 139,401

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

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Supplemental Schedule of Noncash Investing and Financing Activities:

Cash dividends declared, but not yet paid, were \$2.7 million as of September 30, 2013 and 2012, and were paid in October 2013 and 2012, respectively.

As of September 30, 2013, we had accrued capital expenditures totaling \$2.8 million, which were recorded in accounts payable.

During the nine months ended September 30, 2012, we granted equity awards to certain employees of which \$2.7 million was previously recorded in accrued expenses and other current liabilities.

In connection with our acquisitions for the periods presented, the following table presents the assets acquired, net of cash and liabilities assumed:

	For the Nine Months ended September 30,			
	2013		2012	
Assets acquired, net of cash	\$	54,998	\$	140,725
Liabilities assumed	\$	30,286	\$	69,859

In connection with our acquisitions during the nine months ended September 30, 2013, we issued \$3.0 million of promissory notes and recorded amounts payable to sellers related to purchase price adjustments of \$2.0 million. In connection with our acquisitions during the nine months ended September 30, 2012, we issued \$7.2 million of promissory notes.

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

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World Fuel Services Corporation and Subsidiaries

Notes to the Consolidated Financial Statements

(Unaudited)

1. Significant Accounting Policies

Except as updated below, the significant accounting policies we use for quarterly financial reporting are the same as those disclosed in Note 1 of the Notes to the Consolidated Financial Statements included in our 2012 10-K Report.

Basis of Consolidation

The accompanying consolidated financial statements and related notes include the accounts of our wholly-owned and majority-owned subsidiaries and joint ventures where we exercise operational control or have a primary benefit of its profits. All significant intercompany accounts, transactions and profits are eliminated upon consolidation.

Reclassifications

Certain amounts in prior periods have been reclassified to conform to the current period's presentation.

Goodwill

During the first nine months of 2013, we recorded goodwill of \$9.6 million in our land segment in connection with two acquisitions completed during the period, which were not material individually or in the aggregate. In addition, based on our ongoing fair value assessment of certain of our 2012 acquisitions, we recorded a \$2.0 million reduction in goodwill within our land segment principally due to a \$3.3 million increase in identifiable intangible assets, partially offset by a \$0.9 million decrease in other acquired assets and a \$0.4 million increase in assumed liabilities. Additionally, we reclassified \$6.5 million in goodwill from our land segment to our aviation segment. We had additional goodwill reductions of \$0.5 million and \$0.3 million as a result of foreign currency translation adjustments of our non-U.S. dollar functional currency subsidiaries in our marine and aviation segments, respectively.

Recent Accounting Pronouncements

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Presentation of an Unrecognized Tax Benefit When a Net Loss Carryforward, a Similar Tax Loss, or a Tax Credit Carryforward Exists. In July 2013, the Financial Accounting Standards Board (FASB) issued an accounting standards update (ASU) on the presentation of an unrecognized tax benefit when a net operating loss carryforward exists. Under this guidance, an unrecognized tax benefit, or a portion of an unrecognized tax benefit, should be presented in the financial statements as a reduction to a deferred tax asset for a net operating loss carryforward. This update is effective for fiscal years, and interim periods within those years, beginning after December 15, 2013. We are currently evaluating whether the adoption of this new guidance will have a significant impact on our consolidated financial statements and disclosures.

Inclusion of the Fed Funds Effective Swap Rate (or Overnight Index Swap Rate) as a Benchmark Interest Rate for Hedge Accounting Purposes. In July 2013, the FASB issued an ASU which includes amendments permitting the Fed Funds Effective Swap Rate to be used as a U.S. benchmark interest rate for hedge accounting purposes, in addition to U.S. Government and London Interbank Offered Rate. The amendments also remove the restriction on using different benchmark rates for similar hedges. This update is effective prospectively for qualifying new or redesignated hedging relationships entered into on or after July 17, 2013. The adoption of this ASU did not have a significant impact on our consolidated financial statements and disclosures.

Foreign Currency Matters Parent's Accounting for the Cumulative Translation Adjustment upon Derecognition of Certain Foreign Subsidiaries. In March 2013, the FASB issued an ASU aimed at resolving the diversity in practice of accounting for the release of the cumulative translation adjustment into net income when a parent either sells a part or all of its investment in a foreign entity or no longer holds a controlling financial interest in a subsidiary or group of assets that is a nonprofit activity or a business within a foreign entity. In addition, the amendments in this ASU resolve the diversity in practice for the treatment of business combinations achieved in stages (sometimes also referred to as step acquisitions) involving a foreign entity. This update is effective for fiscal years, and interim periods within those years, beginning after December 15, 2013. We do not believe the adoption of this new guidance will have a significant impact on our consolidated financial statements and disclosures.

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Disclosure Obligations Resulting from Joint and Several Liability Arrangements. In February 2013, the FASB issued an ASU clarifying the guidance for the recognition, measurement and disclosure of obligations resulting from joint and several liability arrangements for which the total amount of the obligation within the scope of this ASU is fixed at the reporting date, except for obligations addressed within existing guidance in U.S. GAAP. This update is effective for fiscal years, and interim periods within those years, beginning after December 15, 2013 and will be applied retrospectively. We do not believe the adoption of this new guidance will have a significant impact on our consolidated financial statements and disclosures.

Disclosure Relating to Amounts Reclassified Out of Accumulated Other Comprehensive Income. In February 2013, the FASB issued an ASU amending the information that companies will be required to present relating to reclassifications out of accumulated other comprehensive income. The amendments require presentation, either on the face of the financial statements or in the notes, of amounts reclassified out of accumulated other comprehensive income by component and by net income line item. This update is effective for fiscal years, and interim periods within those years, beginning after December 15, 2012. The adoption of this ASU resulted in additional derivative disclosures included in Note 2 - Derivatives and did not have a significant impact on our consolidated financial statements.

Disclosure About Offsetting Assets and Liabilities. In December 2011, the FASB issued an ASU which requires companies to disclose information about financial instruments that have been offset and related arrangements to enable users of its financial statements to understand the effect of those arrangements on its financial position. Companies will be required to provide both net (offset amounts) and gross information in the notes to the financial statements for relevant assets and liabilities that are offset. In January 2013, the FASB issued an ASU clarifying that the requirement to disclose information about financial instruments that have been offset and related arrangements applies only to derivatives, repurchase agreements and reverse purchase agreements, and securities borrowing and lending transactions that are either offset in accordance with specific criteria contained in the FASB Accounting Standards Codification or subject to a master netting arrangement or similar agreement. This update became effective at the beginning of our 2013 fiscal year. The adoption of this ASU did not have a significant impact on our consolidated financial statements and disclosures.

Consolidated Statement of Cash Flows for the Six Months ended June 30, 2013

We identified an incorrect cash flow presentation of \$17.7 million related to an acquisition payment that was classified as an operating activity versus an investing activity in the consolidated statement of cash flows for the six months ended June 30, 2013. We assessed the materiality of this incorrect presentation and concluded it was not material. As prior period financial information is presented in future SEC filings, we will modify the presentation of the consolidated statement of cash flows to include this revision.

2. Derivatives

We enter into financial derivative contracts in order to mitigate the risk of market price fluctuations in aviation, marine and land fuel, to offer our customers fuel pricing alternatives to meet their needs and to mitigate the risk of fluctuations in foreign currency exchange rates. We also enter into proprietary derivative transactions, primarily intended to capitalize on arbitrage opportunities related to basis or time spreads related to fuel products we sell. We have applied the normal purchase and normal sales exception (NPNS), as provided by accounting guidance for derivative instruments and hedging activities, to certain of our physical forward sales and purchase contracts. While these contracts are considered derivative instruments under the guidance for derivative instruments and hedging activities, they are not recorded at fair value, but rather are recorded in our consolidated financial statements when physical settlement of the contracts occurs. If it is determined that a transaction designated as NPNS no longer meets the scope of the exception, the fair value of the related contract is recorded as an asset or liability on the

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consolidated balance sheet and the difference between the fair value and the contract amount is immediately recognized through earnings.

The following describes our derivative classifications:

Cash Flow Hedges. Includes certain of our foreign currency forward contracts we enter into in order to mitigate the risk of currency exchange rate fluctuations.

Fair Value Hedges. Includes derivatives we enter into in order to hedge price risk associated with our inventory and certain firm commitments relating to fixed price purchase and sale contracts.

Non-designated Derivatives. Includes derivatives we primarily enter into in order to mitigate the risk of market price fluctuations in aviation, marine and land fuel in the form of swaps or futures as well as certain fixed price purchase and sale contracts and proprietary trading. In addition, non-designated derivatives are also entered into to hedge the risk of currency rate fluctuations.

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As of September 30, 2013, our derivative instruments, at their respective fair value positions were as follows (in thousands, except weighted average fixed price and weighted average mark-to-market amount):

Hedge Strategy	Settlement Period	Derivative Instrument	Notional	Unit	Weighted Average Fixed Price	Weighted Average Mark-to-Market Amount	Fair Value Amount
Cash Flow Hedge	2013	Foreign currency contracts (long)	333	EUR	\$ 1.24	\$ 0.11	\$ 38
Fair Value Hedge	2013	Commodity contracts for inventory hedging (long)	322	BBL	\$ 112.71	\$ (0.78)	\$ (252)
	2013	Commodity contracts for inventory hedging (short)	2,293	BBL	118.61	2.56	5,879
	2014	Commodity contracts for inventory hedging (short)	12	BBL	115.93	6.50	78
							\$ 5,705
Non-Designated	2013	Commodity contracts (long)	20,078	BBL	\$ 72.44	\$ 0.15	\$ 2,967
	2013	Commodity contracts (short)	16,540	BBL	89.59	0.23	3,848
	2014	Commodity contracts (long)	11,275	BBL	82.69	0.02	218
	2014	Commodity contracts (short)	8,445	BBL			