

FOREST OIL CORP
Form 10-Q
November 10, 2014
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UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

FORM 10-Q
(Mark One)

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

For the quarterly period ended September 30, 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 1-13515

FOREST OIL CORPORATION	
(Exact name of registrant as specified in its charter)	
New York	25-0484900
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)
707 17th Street, Suite 3600	80202
Denver, Colorado	(Zip Code)
(Address of principal executive offices)	

Registrant's telephone number, including area code: (303) 812-1400

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 <input type="checkbox"/>	Accelerated filer <input checked="" type="checkbox"/>
Non-accelerated filer <input type="checkbox"/>	Smaller reporting company <input type="checkbox"/>

(Do not check if a 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

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As of November 6, 2014 there were 119,374,111 shares of the registrant's common stock, par value \$.10 per share, outstanding.

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September 30, 2014

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PART I—FINANCIAL INFORMATION

Item 1. FINANCIAL STATEMENTS

FOREST OIL CORPORATION
CONDENSED CONSOLIDATED BALANCE SHEETS

(Unaudited)

(In Thousands, Except Share Amounts)

	September 30, 2014	December 31, 2013
ASSETS		
Current assets:		
Cash and cash equivalents	\$823	\$66,192
Accounts receivable	38,306	35,654
Derivative instruments	8,033	5,192
Other current assets	6,203	6,756
Total current assets	53,365	113,794
Property and equipment, at cost:		
Oil and natural gas properties, full cost method of accounting:		
Proved, net of accumulated depletion of \$8,722,987 and \$8,460,589	663,853	753,079
Unproved	46,840	53,645
Net oil and natural gas properties	710,693	806,724
Other property and equipment, net of accumulated depreciation and amortization of \$45,892 and \$50,058	6,199	11,845
Net property and equipment	716,892	818,569
Deferred income taxes	3,203	2,230
Goodwill	134,434	134,434
Derivative instruments	1,134	400
Other assets	18,457	48,525
	\$927,485	\$1,117,952
LIABILITIES AND SHAREHOLDERS' EQUITY (DEFICIT)		
Current liabilities:		
Accounts payable and accrued liabilities	\$157,672	\$141,107
Accrued interest	13,244	6,654
Derivative instruments	563	4,542
Deferred income taxes	3,203	2,230
Other current liabilities	4,976	12,201
Total current liabilities	179,658	166,734
Long-term debt	813,155	800,179
Asset retirement obligations	20,487	22,629
Derivative instruments	601	—
Other liabilities	61,620	73,941
Total liabilities	1,075,521	1,063,483
Shareholders' equity (deficit):		
Preferred stock, none issued and outstanding		—
Common stock, 119,374,111 and 119,399,983 shares issued and outstanding	11,937	11,940
Capital surplus	2,560,353	2,554,997
Accumulated deficit	(2,711,639)	(2,502,070)

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Accumulated other comprehensive loss	(8,687) (10,398)
Total shareholders' equity (deficit)	(148,036) 54,469	
	\$927,485	\$1,117,952	

See accompanying Notes to Condensed Consolidated Financial Statements.

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FOREST OIL CORPORATION
CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS
(Unaudited)
(In Thousands, Except Per Share Amounts)

	Three Months Ended September 30,		Nine Months Ended September 30,		
	2014	2013	2014	2013	
Revenues:					
Oil, natural gas, and natural gas liquids sales	\$62,053	\$118,028	\$186,616	\$352,856	
Interest and other	2	166	1,068	326	
Total revenues	62,055	118,194	187,684	353,182	
Costs, expenses, and other:					
Lease operating expenses	14,449	19,245	43,254	59,616	
Production and property taxes	1,266	4,667	7,231	11,912	
Transportation and processing costs	2,228	2,790	7,122	9,168	
General and administrative	5,951	9,765	22,451	42,893	
Depreciation, depletion, and amortization	20,921	43,973	62,639	136,320	
Ceiling test write-down of oil and natural gas properties	127,445	—	204,621	—	
Interest expense	15,882	29,519	47,631	95,039	
Realized and unrealized (gains) losses on derivative instruments, net	(24,139) 5,533	353	(497)
Other, net	5,010	1,075	4,356	31,488	
Total costs, expenses, and other	169,013	116,567	399,658	385,939	
Earnings (loss) before income taxes	(106,958) 1,627	(211,974) (32,757)
Income tax benefit	(1,113) (587) (2,405) (462)
Net earnings (loss)	\$(105,845) \$2,214	\$(209,569) \$(32,295)
Basic earnings (loss) per common share	\$(.90) \$.02	\$(1.79) \$(.28)
Diluted earnings (loss) per common share	\$(.90) \$.02	\$(1.79) \$(.28)

See accompanying Notes to Condensed Consolidated Financial Statements.

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FOREST OIL CORPORATION
 CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME (LOSS)
 (Unaudited)
 (In Thousands)

	Three Months Ended		Nine Months Ended	
	September 30,		September 30,	
	2014	2013	2014	2013
Net earnings (loss)	\$(105,845	) \$2,214	\$(209,569	) \$(32,295
Other comprehensive income:				
Defined benefit postretirement plans - actuarial losses, net of tax	1,364	343	1,711	1,030
Total other comprehensive income	1,364	343	1,711	1,030
Total comprehensive income (loss)	\$(104,481	) \$2,557	\$(207,858	) \$(31,265

See accompanying Notes to Condensed Consolidated Financial Statements.

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FOREST OIL CORPORATION
 CONDENSED CONSOLIDATED STATEMENT OF SHAREHOLDERS' EQUITY (DEFICIT)
 (Unaudited)
 (In Thousands)

	Common Stock		Capital Surplus	Accumulated Deficit	Accumulated Other Comprehensive Loss	Total Shareholders' Equity (Deficit)
	Shares	Amount				
Balances at December 31, 2013	119,400	\$ 11,940	\$2,554,997	\$(2,502,070)	\$(10,398)	\$ 54,469
Employee stock purchase plan	111	11	146	—	—	157
Restricted stock issued, net of forfeitures	106	12	(12)	—	—	—
Amortization of stock-based compensation	—	—	5,887	—	—	5,887
Other, net	(243)	(26)	(665)	—	—	(691)
Net loss	—	—	—	(209,569)	—	(209,569)
Other comprehensive income	—	—	—	—	1,711	1,711
Balances at September 30, 2014	119,374	\$ 11,937	\$2,560,353	\$(2,711,639)	\$(8,687)	\$(148,036)

See accompanying Notes to Condensed Consolidated Financial Statements.

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FOREST OIL CORPORATION
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
(Unaudited)
(In Thousands)

	Nine Months Ended September 30,	
	2014	2013
Operating activities:		
Net loss	\$(209,569	) \$(32,295
Adjustments to reconcile net loss to net cash provided by operating activities:		
Depreciation, depletion, and amortization	62,639	136,320
Deferred income tax	(1,112) —
Unrealized (gains) losses on derivative instruments, net	(6,952	) 22,076
Ceiling test write-down of oil and natural gas properties	204,621	—
Stock-based compensation expense	3,747	7,276
Loss on debt extinguishment	—	25,223
Gain on asset dispositions, net	(21,391) —
Other, net	1,688	3,710
Changes in operating assets and liabilities:		
Accounts receivable	2,170	2,202
Other current assets	526	5,896
Accounts payable and accrued liabilities	(22,122	) 15,494
Accrued interest and other	27,383	(1,917
Net cash provided by operating activities	41,628	183,985
Investing activities:		
Capital expenditures for property and equipment:		
Exploration, development, and leasehold acquisition costs	(168,637	) (290,923
Other property and equipment	(4,835	) (1,266
Proceeds from sales of assets	27,222	370,437
Net cash (used) provided by investing activities	(146,250	) 78,248
Financing activities:		
Proceeds from bank borrowings	82,000	457,000
Repayments of bank borrowings	(69,000	) (407,000
Redemption of senior notes	—	(321,327
Change in bank overdrafts	27,249	11,117
Other, net	(996	) (958
Net cash provided (used) by financing activities	39,253	(261,168
Net (decrease) increase in cash and cash equivalents	(65,369	) 1,065
Cash and cash equivalents at beginning of period	66,192	1,056
Cash and cash equivalents at end of period	\$823	\$2,121
Cash paid during the period for:		
Interest (net of capitalized amounts)	\$38,337	\$89,753
Income taxes (net of refunded amounts)	(21,311	) (736
Non-cash investing activities:		
Increase (decrease) in accrued capital expenditures	\$902	\$(6,290

See accompanying Notes to Condensed Consolidated Financial Statements.

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FOREST OIL CORPORATION
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(Unaudited)

(1) ORGANIZATION AND BASIS OF PRESENTATION

Organization

Forest Oil Corporation is an independent oil and gas company engaged in the acquisition, exploration, development, and production of oil, natural gas, and natural gas liquids (“NGLs”) primarily in North America. Forest was incorporated in New York in 1924, as the successor to a company formed in 1916, and has been a publicly held company since 1969. Forest holds assets in several exploration and producing areas in the United States and has exploratory and development interests in one other country. Unless the context indicates otherwise, the terms “Forest,” the “Company,” “we,” “our,” and “us,” as used in this Quarterly Report on Form 10-Q, refer to Forest Oil Corporation and its subsidiaries.

Basis of Presentation

The Condensed Consolidated Financial Statements included herein are unaudited and include the accounts of Forest and its consolidated subsidiaries. All intercompany balances and transactions have been eliminated. In the opinion of management, all adjustments, which are of a normal recurring nature, have been made that are necessary for a fair presentation of the financial position of Forest at September 30, 2014, and the results of its operations, its comprehensive income (loss), its cash flows, and changes in its shareholders’ equity (deficit) for the periods presented. Interim results are not necessarily indicative of expected annual results because of various factors including the impact of fluctuations in the prices of oil, natural gas, and NGLs and the impact the prices have on Forest’s revenues and the fair values of its derivative instruments.

In the course of preparing the Condensed Consolidated Financial Statements, management makes various assumptions, judgments, and estimates to determine the reported amounts of assets, liabilities, revenues, and expenses, and in the disclosures of commitments and contingencies. Changes in these assumptions, judgments, and estimates will occur as a result of the passage of time and the occurrence of future events and, accordingly, actual results could differ from amounts previously established.

The more significant areas requiring the use of assumptions, judgments, and estimates relate to volumes of oil, natural gas, and NGL reserves used in calculating depletion, the amount of future net revenues used in computing the ceiling test limitations, and the amount of future capital costs and abandonment obligations used in such calculations, assessing investments in unproved properties and goodwill for impairment, determining the need for and the amount of deferred tax asset valuation allowances, and estimating fair values of financial instruments, including derivative instruments.

For a more complete understanding of Forest’s operations, financial position, and accounting policies, reference is made to the consolidated financial statements of Forest, and related notes thereto, included in Forest’s Annual Report on Form 10-K/A for the year ended December 31, 2013, previously filed with the Securities and Exchange Commission (“SEC”).

Pending Merger

On May 5, 2014, Forest entered into an Agreement and Plan of Merger with Sabine Oil & Gas LLC (“Sabine”), under which Forest and Sabine will combine their businesses in an all-stock transaction. This agreement was amended on

July 9, 2014 primarily to change the structure of the transaction, in which Forest now will be the surviving entity. The revised transaction structure does not change the economic terms of the transaction. Under the terms of the amended merger agreement, the owners of Sabine will contribute their interests in Sabine to Forest in exchange for Forest common and preferred stock. Upon closing of the combination transaction, Forest's shareholders will own common shares that represent an approximate 26.5% economic interest in the combined

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company and approximately 20% of the total voting power, and Sabine's equity holders will own common shares and preferred shares that represent an approximate 73.5% economic interest and approximately 80% of the total voting power in the combined company. The combined entity will change its name to Sabine Oil & Gas Corporation and be headquartered in Houston. Consummation of the transaction is subject to approval by Forest shareholders, regulatory approvals, and other customary closing conditions. In late October 2014, Forest commenced mailing definitive proxy materials and scheduled a special meeting of shareholders for November 20, 2014, to consider and vote on the proposed merger agreement with Sabine. Forest shareholders of record at the close of business on October 3, 2014, the record date, are entitled to notice of, and to vote at, the Forest special meeting.

In connection with entering into the amended merger agreement, Forest also adopted a shareholder rights agreement (the "Rights Agreement"), and on July 10, 2014 declared a dividend of one preferred share purchase right (a "Right") on each outstanding share of Forest's common stock. This dividend was issued on July 21, 2014. Each Right allows its holder to purchase from Forest one one-hundredth of a share of Series A Junior Participating Preferred Stock for \$10, once the Rights become exercisable. This portion of a preferred share will give the shareholder approximately the same dividend and liquidation rights as would one Forest common share. Prior to exercise, the Rights do not give their holders any dividend, voting, or liquidation rights. The Rights will expire on December 31, 2014.

The Rights will not be exercisable until ten days after the public announcement that a person or group has become an "Acquiring Person" by obtaining "beneficial ownership" (as defined in the Rights Agreement) of 5% or more of Forest's outstanding common shares; provided that a stockholder will not become an "Acquiring Person" if such stockholder certifies to Forest that (i) such stockholder, together with all affiliates and associates of such stockholder, does not and will not at any time prior to December 31, 2014 own or have any beneficial interest in any transaction, security, or derivative or synthetic arrangements having the characteristics of a "short" position in or with respect to any Forest indebtedness or that would increase in value as a result of a decline in the value of any Forest indebtedness or decline in Forest's credit rating and (ii) such stockholder will continue to satisfy clause (i) for so long as the Rights would otherwise become exercisable. If a person or group becomes an Acquiring Person, all holders of Rights except the Acquiring Person may, for \$10, purchase common shares of Forest with a market value of \$20, based on the market price of Forest's common shares prior to such acquisition. If Forest is later acquired in a merger or similar transaction after the Distribution Date (as defined in the Rights Agreement), all holders of Rights except the Acquiring Person may, for \$10, purchase shares of the acquiring corporation with a market value of \$20, based on the market price of the acquiring corporation's stock prior to such transaction.

The Rights Agreement is intended to prevent persons from acquiring beneficial ownership of 5% or more of Forest's common stock or, for investors that owned in excess of 5% as of July 10, 2014, from increasing their beneficial ownership, but only to the extent such a person has a "short" equivalent position with respect to Forest's debt. This is to prevent certain hedge funds from rejecting the proposed transaction in order to profit from their short positions in Forest's debt (and similar derivative positions).

Going Concern and Management's Plan

The financial statements included in this Form 10-Q have been prepared on a going concern basis of accounting, which contemplates continuity of operations, realization of assets, and satisfaction of liabilities and commitments in the normal course of business. The accompanying financial statements do not reflect any adjustments that might result if the Company is unable to continue as a going concern. At December 31, 2014, the ratio of Forest's total debt to EBITDA likely will exceed the maximum allowed under the credit facility unless Forest undertakes certain mitigating actions. Absent such actions, a resultant breach of the financial covenant could cause a default under the credit facility, potentially resulting in an acceleration of all amounts outstanding under the credit facility as well as the senior unsecured notes due 2019 and 2020. As of September 30, 2014, Forest had \$13.0 million outstanding under the credit facility and \$800.0 million in principal amount outstanding under the notes.

The Company obtained amendments to the credit facility as recently as September 2013 and March 2014 in order to avoid breaching the debt to EBITDA covenant. Forest believes that it could seek, and the lenders under the credit facility would provide, another amendment, or a waiver, of the covenant. Failing an amendment or waiver,

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Forest believes it could sell assets to avoid breaching the financial covenant. Alternatively, Forest could obtain a new credit facility or other sources of financing, although any such alternative source of financing likely would be at higher cost than the credit facility. Forest has not undertaken any of these actions because of the pending transaction with Sabine which, if completed by year end, will result in a termination of the credit facility before any breach of the debt-to-EBITDA covenant occurs. If the combination transaction with Sabine is not completed by year end, Forest may yet undertake some or all of these actions, though there is no assurance Forest could complete any such actions as each involves factors that are outside its control. However, inasmuch as Forest did not obtain a waiver or amendment to the bank credit facility or pursue alternative sources of financing, it was determined that as of October 1, 2014, the date Forest filed the Form 10-K/A, there existed substantial doubt as to Forest's ability to continue as a going concern through December 31, 2014.

(2) EARNINGS (LOSS) PER SHARE

Basic earnings (loss) per share is computed using the two-class method by dividing net earnings (loss) attributable to common stock by the weighted average number of common shares outstanding during each period. The two-class method of computing earnings (loss) per share is required to be used since Forest has participating securities. The two-class method is an earnings allocation formula that determines earnings (loss) per share for each class of common stock and participating security according to dividends declared (or accumulated) and participation rights in undistributed earnings. Holders of restricted stock issued under Forest's stock incentive plans have the right to receive non-forfeitable cash and certain non-cash dividends, participating on an equal basis with common stock. Holders of phantom stock units issued to directors under Forest's stock incentive plans also have the right to receive non-forfeitable cash and certain non-cash dividends, participating on an equal basis with common stock, while phantom stock units issued to employees do not participate in dividends. Stock options and cash-settled performance units issued under Forest's stock incentive plans do not participate in dividends. Share-settled performance units issued under Forest's stock incentive plans do not participate in dividends in their current form. Holders of these performance units participate in dividends paid during the performance units' vesting period only after the performance units vest and common shares are deliverable under the terms of the performance unit awards. Share-settled performance units may vest with no common shares being deliverable, depending on Forest's shareholder return over the performance units' vesting period in relation to the shareholder returns of specified peers. See Note 3 for more information on Forest's stock-based incentive awards. In summary, restricted stock issued to employees and directors and phantom stock units issued to directors are participating securities, and earnings are allocated to both common stock and these participating securities under the two-class method. However, these participating securities do not have a contractual obligation to share in Forest's losses. Therefore, in periods of net loss, none of the loss is allocated to these participating securities.

Diluted earnings (loss) per share is computed by dividing net earnings (loss) attributable to common stock by the weighted average number of common shares outstanding during each period, increasing the denominator to include the number of additional common shares that would have been outstanding if the dilutive potential common shares (e.g. stock options, unvested restricted stock, unvested share-settled phantom stock units, and unvested share-settled performance units) had been issued. Additionally, the numerator is also adjusted for certain contracts that provide the issuer or holder with a choice between settlement methods. Diluted earnings per share is computed using the more dilutive of the treasury stock method or the two-class method. Under the treasury stock method, the dilutive effect of potential common shares is computed by assuming common shares are issued for these securities at the beginning of the period, with the assumed proceeds from exercise, which include average unamortized stock-based compensation costs, assumed to be used to purchase common shares at the average market price for the period, and the incremental shares (the difference between the number of shares assumed issued and the number of shares assumed purchased) included in the denominator of the diluted earnings per share computation. The number of contingently issuable shares pursuant to the outstanding share-settled performance units is included in the denominator of the computation of diluted earnings per share based on the number of shares, if any, that would be issuable if the end of the reporting

period were the end of the contingency period and if the result would be dilutive. Under the two-class method, the dilutive effect of non-participating potential common shares is determined and undistributed earnings are reallocated between common shares and participating securities. No potential common shares are included in the computation of any diluted per share amount when a net loss exists, as was the case for the

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three and nine months ended September 30, 2014 and the nine months ended September 30, 2013. Unvested restricted stock grants were not included in the calculation of diluted earnings per share for the three months ended September 30, 2013 as their inclusion would have an antidilutive effect.

The following reconciles net earnings (loss) as reported in the Condensed Consolidated Statements of Operations to net earnings (loss) used for computing basic and diluted earnings (loss) per share for the periods presented.

	Three Months Ended		Nine Months Ended	
	September 30, 2014	2013	September 30, 2014	2013
	(In Thousands)			
Net earnings (loss)	\$(105,845)	\$2,214	\$(209,569)	\$(32,295)
Less: net earnings attributable to participating securities	—	(67)	—	—
Net earnings (loss) for basic and diluted earnings (loss) per share	\$(105,845)	\$2,147	\$(209,569)	\$(32,295)

The following reconciles basic weighted average common shares outstanding to diluted weighted average common shares outstanding for the periods presented.

	Three Months Ended		Nine Months Ended	
	September 30, 2014	2013	September 30, 2014	2013
	(In Thousands)			
Weighted average common shares outstanding during the period for basic earnings (loss) per share	117,378	116,242	117,113	115,979
Dilutive effects of potential common shares	—	—	—	—
Weighted average common shares outstanding during the period, including the effects of dilutive potential common shares, for diluted earnings (loss) per share	117,378	116,242	117,113	115,979

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(3) STOCK-BASED COMPENSATION

Stock-based Compensation Plans

Forest maintains the 2007 Stock Incentive Plan (the “2007 Plan”) under which qualified and non-qualified stock options, restricted stock, performance units, phantom stock units, and other awards may be granted to employees, consultants, and non-employee directors of Forest and its subsidiaries. Forest also maintains the 2001 Stock Incentive Plan (the “2001 Plan,” and together with the 2007 Plan, the “Plans”) under which certain non-qualified stock options remain outstanding, but under which no new awards may be issued.

Compensation Costs

The table below sets forth stock-based compensation for the three and nine months ended September 30, 2014 and 2013, and the remaining unamortized amounts and weighted average amortization period as of September 30, 2014.

	Restricted Stock (In Thousands)	Performance Units	Phantom Stock Units	Total ⁽¹⁾⁽²⁾
Three Months Ended September 30, 2014:				
Total stock-based compensation costs	\$1,419	\$631	\$(174)	\$1,876
Less: stock-based compensation costs capitalized	(491)	) (118)	) 48	(561)
Stock-based compensation costs expensed	\$928	\$513	\$(126)	\$1,315
Nine Months Ended September 30, 2014:				
Total stock-based compensation costs	\$4,595	\$1,231	\$429	\$6,255
Less: stock-based compensation costs capitalized	(1,894)	) (246)	) (224)	(2,364)
Stock-based compensation costs expensed	\$2,701	\$985	\$205	\$3,891
Unamortized stock-based compensation costs ⁽³⁾	\$4,706	\$1,811	\$995	\$7,512
Weighted average amortization period remaining	1.0 years	1.2 years	1.5 years	1.1 years
Three Months Ended September 30, 2013:				
Total stock-based compensation costs	\$1,644	\$301	\$1,762	\$3,707
Less: stock-based compensation costs capitalized	(877)	) (245)	) (828)	(1,950)
Stock-based compensation costs expensed	\$767	\$56	\$934	\$1,757
Nine Months Ended September 30, 2013:				
Total stock-based compensation costs	\$9,089	\$3,034	\$3,537	\$15,660
Less: stock-based compensation costs capitalized	(3,871)	) (959)	) (1,715)	(6,545)
Stock-based compensation costs expensed	\$5,218	\$2,075	\$1,822	\$9,115

Forest also maintains an employee stock purchase plan (which is not included in the table) under which \$.01 million and \$.1 million of compensation cost was recognized for the three and nine months ended September 30, 2014, respectively, and \$.04 million and \$.2 million of compensation cost was recognized for the three and nine months ended September 30, 2013, respectively.

In connection with the divestiture of the South Texas oil and natural gas properties in the first quarter of 2013, Forest incurred \$2.0 million (\$1.0 million net of capitalized amounts) in stock-based compensation costs due to accelerated vesting of involuntarily terminated employees’ awards. See Note 5 for more information regarding this divestiture.

The unamortized stock-based compensation costs for liability-based awards are based on the closing price of Forest’s common stock at the reporting period end.

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Stock Options

The following table summarizes stock option activity in the Plans for the nine months ended September 30, 2014.

	Number of Options	Weighted Average Exercise Price	Aggregate Intrinsic Value (In Thousands) ⁽¹⁾	Number of Options Exercisable
Outstanding at January 1, 2014	631,206	\$17.21	\$—	631,206
Granted	—	—	—	—
Exercised	—	—	—	—
Cancelled	(267,274	) 14.31	—	—
Outstanding at September 30, 2014	363,932	\$19.34	\$—	363,932

(1) The intrinsic value of a stock option is the amount by which the market value of the underlying stock, as of the date outstanding or exercised, exceeds the exercise price of the option.

Restricted Stock, Performance Units, and Phantom Stock Units

The following table summarizes the restricted stock, performance unit, and phantom stock unit activity in the Plans for the nine months ended September 30, 2014.

	Restricted Stock			Performance Units			Phantom Stock Units		
	Number of Shares ⁽¹⁾	Weighted Average Grant Date Fair Value	Vest Date Fair Value (In Thousands)	Number of Units ⁽²⁾	Weighted Average Grant Date Fair Value	Vest Date Fair Value (In Thousands)	Number of Units ⁽³⁾	Weighted Average Grant Date Fair Value	Vest Date Fair Value (In Thousands)
Unvested at January 1, 2014	2,790,542	\$10.23		1,511,140	\$8.48		1,924,819	\$6.75	
Awarded	407,202	2.22		—	—		67,000	3.51	
Vested	(929,682	) 14.58	\$2,504	(63,840	) 18.11	\$—	(345,617	) 7.05	\$1,131
Forfeited	(300,804	) 10.26		(170,300	) 9.33		(185,155	) 7.54	
Unvested at September 30, 2014	1,967,258	\$6.52		1,277,000	\$7.89		1,461,047	\$6.43	

(1) Of the unvested restricted stock as of September 30, 2014, (i) 436,056 shares, which were granted in 2013, vest in one-third increments on each of the first three anniversary dates of the grant, (ii) 405,702 shares, which were granted in 2014, vest on the first anniversary of the date of the grant, and (iii) all remaining unvested shares of restricted stock cliff vest on the third anniversary of the date of grant.

(2) Of the unvested performance units as of September 30, 2014, 598,500, which were granted in 2013, are cash-based and the remaining unvested performance units are share-based. For both cash- and share-based performance units, the actual settlement amount is dependent upon Forest's relative total shareholder return in comparison to a specified peer group over a thirty-six month performance period. The cash-based performance units are accounted for as a liability within the Condensed Consolidated Financial Statements.

(3) All of the unvested phantom stock units as of September 30, 2014 must be settled in cash. The phantom stock units have been accounted for as a liability within the Condensed Consolidated Financial Statements. All of the phantom stock units that vested during the nine months ended September 30, 2014 were settled in cash. Of the unvested

phantom stock units as of September 30, 2014, (i) 122,393 were granted in 2011 and 463,654 were granted in 2013 and vest in one-third increments on each of the first three anniversaries of the grant date, (ii) 493,000 were granted in 2013 and 67,000 were granted in 2014 and cliff vest on the third anniversary of the grant date, and (iii) 270,000 were granted in 2012 and 45,000 were granted in 2013 and vest over a four-year period in accordance with the following schedule: (a) 10% on the first anniversary of the grant date; (b) 20% on the second anniversary of the grant date; (c) 30% on the third anniversary of the grant date; and (d) 40% on the fourth anniversary of the grant date.

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(4) DEBT

The components of debt are as follows:

	September 30, 2014			December 31, 2013		
	Principal	Unamortized Premium	Total	Principal	Unamortized Premium	Total
	(In Thousands)					
Credit facility	\$13,000	\$—	\$13,000	\$—	\$—	\$—
7¼% senior notes due 2019	577,914	154	578,068	577,914	178	578,092
7½% senior notes due 2020	222,087	—	222,087	222,087	—	222,087
Total long-term debt	\$813,001	\$154	\$813,155	\$800,001	\$178	\$800,179

Bank Credit Facility

As of September 30, 2014, the Company had a \$500.0 million credit facility (the “Credit Facility”) with a syndicate of banks led by JPMorgan Chase Bank, N.A. (the “Administrative Agent”), which matures in June 2016. The size of the Credit Facility may be increased by \$300.0 million, to a total of \$800.0 million, upon agreement between the applicable lenders and Forest.

On March 31, 2014, the Company entered into the Second Amendment to the Credit Facility (the “Second Amendment”), which was effective as of that date. The Second Amendment amended, among other things, the permitted ratio of total debt to EBITDA and the definition of total debt used in the ratio calculation, and reduced the aggregate lender commitments from \$1.5 billion to \$500.0 million and the borrowing base, which governs Forest’s availability under the Credit Facility, from \$400.0 million to \$300.0 million, where it remained as of September 30, 2014.

The determination of the Credit Facility borrowing base is made by the lenders in their sole discretion, on a semi-annual basis, taking into consideration the estimated value of Forest’s oil and natural gas properties based on pricing models determined by the lenders at such time, in accordance with the lenders’ customary practices for oil and natural gas loans. The available borrowing amount under the Credit Facility could increase or decrease based on such redetermination. In addition to the scheduled semi-annual redeterminations, Forest and the lenders each have discretion at any time, but not more often than once during a calendar year, to have the borrowing base redetermined. The borrowing base is also subject to automatic adjustments if certain events occur, such as if Forest or any of its Restricted Subsidiaries (as defined in the Credit Facility) issue senior unsecured notes, in which case the borrowing base will immediately be reduced by an amount equal to 25% of the stated principal amount of such issued senior notes, excluding any senior unsecured notes that Forest or any of its Restricted Subsidiaries may issue to refinance senior notes that were outstanding on June 30, 2011. The borrowing base is also subject to automatic adjustment if Forest or any of its Restricted Subsidiaries sell oil and natural gas properties having a fair market value, including any economic loss of unwinding any related hedging agreement, in excess of 10% of the borrowing base then in effect. In this case, the borrowing base will be reduced by an amount equal to either (i) the percentage of the borrowing base attributable to the sold properties, as determined by the Administrative Agent, or (ii) if none of the borrowing base is attributable to the sold properties, a value agreed upon by Forest and the required lenders. The lenders reaffirmed the \$300.0 million borrowing base on October 22, 2014 and the next scheduled semi-annual redetermination of the borrowing base will occur on or about May 1, 2015. A lowering of the borrowing base could require Forest to repay indebtedness in excess of the borrowing base in order to cover the deficiency.

The Credit Facility is collateralized by Forest’s assets. Under the Credit Facility, Forest is required to mortgage and grant a security interest in 75% of the present value of the estimated proved oil and natural gas properties and related

assets. If Forest's corporate credit ratings issued by Moody's and Standard & Poor's meet pre-established levels, the security requirements would cease to apply and, at Forest's request, the banks would release their liens and security interest on Forest's properties.

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The Credit Facility includes terms and covenants that place limitations on certain types of activities, including restrictions or requirements with respect to additional debt, liens, asset sales, hedging activities, investments, dividends, mergers, and acquisitions, and also includes a financial covenant. The Second Amendment to the Credit Facility provides that Forest will not permit its ratio of total debt to EBITDA (as adjusted for non-cash charges) calculated for the preceding four consecutive fiscal quarter period then most recently ended to be greater than (i) 5.75 to 1.00 at the end of the calendar quarters ending March 31, 2014, June 30, 2014 and September 30, 2014, (ii) 5.50 to 1.00 at the end of the calendar quarter ending December 31, 2014, (iii) 5.25 to 1.00 at the end of the calendar quarter ending March 31, 2015, (iv) 5.00 to 1.00 at the end of the calendar quarter ending June 30, 2015, (v) 4.75 to 1.00 at the end of the calendar quarter ending September 30, 2015, and (vi) 4.50 to 1.00 at the end of any calendar quarter ending after September 30, 2015. The Second Amendment also amends the definition of total debt such that, among other things, during any period of four fiscal quarters ending on or before September 30, 2015, any cash proceeds from the sale of any property permitted pursuant to the terms and provisions of the loan documents that are reported on Forest's consolidated balance sheet on such date are subtracted from total debt. Depending on Forest's overall level of indebtedness, this covenant may limit Forest's ability to borrow funds as needed under the Credit Facility. Forest's ratio of total debt to EBITDA for the four consecutive fiscal quarter period ended September 30, 2014, as calculated in accordance with the Credit Facility, was 5.50.

Based on Forest's current projections, the ratio of total debt to EBITDA likely will exceed the maximum allowed under the Credit Facility at the end of the calendar quarter ending December 31, 2014, if Forest does not obtain a waiver or an additional amendment to the Credit Facility. Forest believes that it will be able to obtain such a waiver or an amendment prior to the ratio exceeding the maximum amount currently allowed. If Forest fails to obtain a waiver or an amendment, the Credit Facility could be terminated. Forest believes it can obtain alternative sources of debt financing sufficient for its needs, including securing liens against its properties or selling additional properties. However, any such alternative source of financing likely would be at a higher cost than the Credit Facility.

At September 30, 2014, there were outstanding borrowings of \$13.0 million under the Credit Facility and Forest had used the Credit Facility for \$2.0 million in letters of credit.

(5) PROPERTY AND EQUIPMENT

Full Cost Method of Accounting

The Company uses the full cost method of accounting for oil and natural gas properties. Separate cost centers are maintained for each country in which the Company has operations. During the periods presented, the Company's primary oil and natural gas operations were conducted in the United States. All costs incurred in the acquisition, exploration, and development of properties (including costs of surrendered and abandoned leaseholds, delay lease rentals, dry holes, and overhead related to exploration and development activities) and the fair value of estimated future costs of site restoration, dismantlement, and abandonment activities are capitalized. During the three months ended September 30, 2014 and 2013, Forest capitalized \$4.0 million and \$6.6 million, respectively, of general and administrative costs (including stock-based compensation). During the nine months ended September 30, 2014 and 2013, Forest capitalized \$13.4 million and \$27.0 million, respectively, of general and administrative costs (including stock-based compensation). During the three and nine months ended September 30, 2013, Forest capitalized \$0.9 million and \$2.0 million of interest costs attributed to significant unproved acreage positions under development. No interest costs were capitalized during the three and nine months ended September 30, 2014.

Investments in unproved properties, including capitalized interest costs, are not depleted pending determination of the existence of proved reserves. Unproved properties are assessed at least annually to ascertain whether impairment has occurred. Unproved properties whose costs are individually significant are assessed individually by considering

factors such as the primary lease terms of the properties, the holding period of the properties, geographic and geologic data obtained relating to the properties, market acreage prices, and estimated discounted future net cash flows from the properties. Estimated discounted future net cash flows are based on

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discounted future net revenues associated with probable and possible reserves, risk adjusted as appropriate. Where it is not practicable to individually assess the amount of impairment of properties for which costs are not individually significant, such properties are grouped for purposes of assessing impairment. The amount of impairment assessed is added to the costs to be amortized, or is reported as a period expense, as appropriate.

The Company performs a ceiling test each quarter on a country-by-country basis under the full cost method of accounting. The ceiling test is a limitation on capitalized costs prescribed by SEC Regulation S-X Rule 4-10. The ceiling test is not a fair value based measurement. Rather, it is a standardized mathematical calculation. The ceiling test provides that capitalized costs less related accumulated depletion and deferred income taxes for each cost center may not exceed the sum of (1) the present value of future net revenue from estimated production of proved oil and natural gas reserves using current prices, excluding the future cash outflows associated with settling asset retirement obligations that have been accrued on the balance sheet, at a discount factor of 10%; plus (2) the cost of properties not being amortized, if any; plus (3) the lower of cost or estimated fair value of unproved properties included in the costs being amortized, if any; less (4) income tax effects related to differences in the book and tax basis of oil and natural gas properties. Should the net capitalized costs for a cost center exceed the sum of the components noted above, a ceiling test write-down would be recognized to the extent of the excess capitalized costs.

As a result of this limitation on capitalized costs, Forest has recognized ceiling test write-downs of its United States cost center for the three and nine months ended September 30, 2014 of \$127.4 million and \$204.6 million, respectively. The ceiling test write-downs were primarily a result of (i) a reduction in the estimated reserves attributable to Forest's proved undeveloped locations in the Eagle Ford, (ii) a reduction in the total number of proved undeveloped locations in the Eagle Ford in the second quarter of 2014 to properly align the number of future drilling locations with expected development pace as of June 30, 2014 (relative to the SEC five year limitation on the age of proved undeveloped locations), and (iii) the decision to reclassify a majority of the remaining proved undeveloped locations in the Eagle Ford to probable locations as of September 30, 2014 as a result of the recent decline in current and future NYMEX oil strip prices well below the average last-twelve-month NYMEX oil price used to calculate proved oil and gas reserves as of September 30, 2014 pursuant to SEC guidelines. The decline in current oil prices and oil price futures sufficiently lowered the expected risk-adjusted rate of return on the Eagle Ford undeveloped locations to a level where Forest would prioritize the drilling on its East Texas acreage in place of the Eagle Ford in future periods. Additional ceiling test write-downs may be required in future periods if, among other things, the unweighted arithmetic average of the first-day-of-the-month oil, natural gas, or NGL prices used in the calculation of the present value of future net revenues from estimated production of proved oil and natural gas reserves declines compared to prices used as of September 30, 2014, unproved properties are impaired, estimated proved reserve volumes are revised downward, or costs incurred in exploration, development, or acquisition activities exceed the discounted future net cash flows from the additional reserves, if any, attributable to the cost center.

Gain or loss is not recognized on the sale of oil and natural gas properties unless the sale significantly alters the relationship between capitalized costs and estimated proved oil and natural gas reserves attributable to a cost center. A significant alteration would not ordinarily be expected to occur for sales involving less than 25% of the reserve quantities of a given cost center.

Depletion of proved oil and natural gas properties is computed on the units-of-production method, whereby capitalized costs, as adjusted for future development costs and asset retirement obligations, are amortized over the total estimated proved reserves. The Company uses its quarter-end reserves estimates to calculate depletion for the current quarter.

Acquisitions

On October 1, 2014, Forest entered into, and closed on, an agreement to purchase approximately 7,700 net acres comprised of both undeveloped and producing properties, including three horizontal Cotton Valley wells, located in Rusk County in East Texas, for a purchase price of \$20.0 million.

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Divestitures

Texas Panhandle

In October 2013, Forest entered into an agreement to sell all of its oil and natural gas properties located in the Texas Panhandle for \$1.0 billion in cash. This divestiture closed on November 25, 2013 and Forest has received total proceeds of \$985.3 million, with the purchase price having been adjusted to, among other things, reflect an economic effective date of October 1, 2013. The total proceeds received include \$20.2 million that Forest received in May 2014 from the final settlement of the escrow account that had been established for this transaction. Forest used a portion of the Panhandle divestiture proceeds to repay the balance outstanding at the time of the closing on its credit facility and to redeem \$422.1 million principal amount of its 7¼% senior notes due 2019 and \$277.9 million principal amount of 7½% senior notes due 2020 in November 2013.

In connection with the Panhandle divestiture, Forest incurred exit costs consisting of \$4.7 million of one-time employee termination benefits and \$8.1 million of other associated costs. No further significant exit costs are expected to be incurred for this divestiture. A reconciliation of the beginning and ending liability balances for these exit costs for the nine months ended September 30, 2014 is set forth in the table below.

	One-Time Employee Termination Benefits	Other Associated Costs ⁽¹⁾	Total
	(In Thousands)		
Liability balance as of December 31, 2013	\$ 1,095	\$ 5,840	\$ 6,935
Costs incurred ⁽²⁾	687	116	803
Costs paid	(1,782)	(5,840)	(7,622)
Liability balance as of September 30, 2014 ⁽³⁾	\$—	\$ 116	\$ 116

(1) Other associated costs consist of financial advisor fees and retention bonuses paid to certain employees.

Of the \$.8 million costs incurred during the nine months ended September 30, 2014, (i) \$.7 million was recognized as an expense in “General and administrative” expense, \$.5 million during the quarter ended March 31, 2014 and \$.1 million during the quarter ended June 30, 2014, and (ii) \$.1 million was recognized as an expense in “Other, net”

(2) during the quarter ended June 30, 2014. During the year ended December 31, 2013, \$12.0 million of costs were incurred, with (i) \$5.0 million recognized as an expense in “General and administrative” expense, (ii) \$5.8 million recognized as an expense in “Other, net”, and (iii) \$1.1 million capitalized in “Oil and natural gas properties” pursuant to the full cost method of accounting.

(3) The September 30, 2014 estimated liability balance is included in “Accounts payable and accrued liabilities” in the Condensed Consolidated Balance Sheet, and Forest expects it will be paid in the fourth quarter of 2014.

The proved reserves associated with the Panhandle divestiture represented more than 25% of Forest’s total proved reserves at the time the divestiture closed. Forest concluded that accounting for the divestiture as an adjustment of capitalized costs would significantly alter the relationship between capitalized costs and proved reserves. Therefore, a gain was recognized on the divestiture. The net gain recognized on the divestiture for the year ended December 31, 2013 was \$193.0 million. A net gain of \$18.2 million was recognized on the divestiture for the nine months ended September 30, 2014, as customary post-closing purchase price adjustments were made and additional proceeds were received. These gains are included in “Other, net” in the Condensed Consolidated Statements of Operations.

South Texas

In January 2013, Forest entered into an agreement to sell all of its oil and natural gas properties located in South Texas, excluding its Eagle Ford oil properties, for \$325.0 million in cash. This transaction closed on February 15, 2013, and Forest has received total proceeds of \$320.9 million, after customary purchase price adjustments. Forest used the proceeds from this divestiture to redeem the remaining \$300.0 million of its 8½% senior notes due 2014. In connection with this divestiture, Forest incurred one-time employee termination benefit costs of \$7.5 million (\$5.7 million net of capitalization), which are included in “General and administrative” expense in the

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Condensed Consolidated Statement of Operations for the nine months ended September 30, 2013 and were paid in full during 2013.

South Africa

In December 2012, Forest entered into an agreement with a third-party to sell its South African subsidiary which holds a production right related to Block 2A in South Africa. Following approval of the sale by the government of South Africa, the sale closed and Forest received a payment of \$1.0 million during the three months ended June 30, 2014. This sale completes Forest's exit from South Africa, though certain regulatory matters are delaying transfer of physical possession of the subsidiary's shares to the purchaser. As a result of this closing, Forest recorded a net gain of \$3.2 million in other income within the "Other, net" line item in the Condensed Consolidated Statement of Operations. Forest may receive future payments depending on the purchaser's success in obtaining natural gas sales contracts and commencing development operations.

Acquisition and Development Agreement

In April 2013, Forest entered into an Acquisition and Development Agreement ("ADA") with a third-party for the future development of Forest's Eagle Ford acreage in Gonzales County, Texas. Under the terms of the ADA, the third-party will pay a \$90.0 million drilling carry in the form of future drilling and completion services and related development capital in exchange for a 50% working interest in Forest's Eagle Ford acreage position. Upon completion of the phased contribution of the drilling carry, Forest and the third-party will participate in future drilling on a 50/50 basis. The ADA applies to wells spud on or subsequent to November 28, 2012, none of which had been placed on production prior to April 1, 2013, and Forest retained all of its interests in wells that were spud prior to November 28, 2012 and production from those wells. Forest is the operator of the drilling program. As of September 30, 2014, Forest had realized \$74.7 million of the drilling carry.

Asset Retirement Obligations

Forest records the fair value of a liability for an asset retirement obligation in the period in which it is incurred with a corresponding increase in the carrying amount of the related long-lived asset. Subsequent to initial measurement, the asset retirement obligation is required to be accreted each period to its present value. Capitalized costs are depleted as a component of the full cost pool using the units-of-production method. Forest's asset retirement obligations consist of costs related to the plugging of wells, the removal of facilities and equipment, and site restoration on oil and natural gas properties.

(6) INCOME TAXES

The significant differences between Forest's blended federal and state statutory income tax rate of 36% and its effective income tax rates of 1.0% and 1.1% for the three and nine months ended September 30, 2014, respectively, and (36.1)% and 1.4% for the three and nine months ended September 30, 2013, respectively, were primarily due to changes in the valuation allowance on Forest's deferred tax assets. The deferred income tax benefit of \$1.1 million recognized during the three months ended September 30, 2014 was due to a change in the valuation allowance related to postretirement benefit plans.

In assessing the need for a valuation allowance, Forest considers whether it is more likely than not that some portion or all of the deferred tax assets will be realized. In making this assessment, Forest considers the scheduled reversal of deferred tax liabilities, available taxes in carryback periods, tax planning strategies, and projected future taxable income. If the ultimate realization of deferred tax assets is dependent upon future book income, assessing the need for, or the sufficiency of, a valuation allowance requires the evaluation of all available evidence, both negative and

positive, as to whether it is more likely than not that a deferred tax asset will be realized.

Negative evidence considered by Forest included a three-year cumulative book loss driven primarily by the ceiling test write-downs. Positive evidence considered by Forest included forecasted book income in future periods

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based on expected future oil, natural gas, and NGL production and expected commodity prices based on NYMEX oil and natural gas futures. Based upon the evaluation of what was determined to be relevant evidence, Forest has recorded a valuation allowance against its deferred tax assets.

As of December 31, 2013, Forest had a non-current income tax receivable of \$20.7 million, which was included in "Other assets." During the nine months ended September 30, 2014, Forest received refunds totaling \$22.3 million, including \$1.0 million of interest income, with \$.7 million recorded as credits to current income tax expense.

(7) FAIR VALUE MEASUREMENTS

Forest's assets and liabilities measured at fair value on a recurring basis at September 30, 2014 and December 31, 2013 are set forth in the table below.

	September 30, 2014 Using Significant Observable Inputs (Level 2) ⁽¹⁾ (In Thousands)	December 31, 2013 Other
Assets:		
Derivative instruments ⁽²⁾ :		
Commodity	\$9,167	\$5,592
Liabilities:		
Derivative instruments ⁽²⁾ :		
Commodity	\$1,164	\$4,542

The authoritative accounting guidance regarding fair value measurements for assets and liabilities measured at fair value establishes a three-tier fair value hierarchy, which prioritizes the inputs used to measure fair value. These tiers consist of: Level 1, defined as unadjusted quoted prices in active markets for identical assets or liabilities; Level 2, defined as inputs other than quoted prices in active markets that are either directly or indirectly observable; and Level 3, defined as unobservable inputs for use when relevant observable inputs are not available.

(1) There were no transfers between levels of the fair value hierarchy during the three and nine months ended September 30, 2014. Forest's policy is to recognize transfers between levels of the fair value hierarchy as of the beginning of the reporting period in which the event or change in circumstances caused the transfer. Forest's currently outstanding derivative assets and liabilities include commodity derivatives (see Note 8 for more information on these instruments). Forest utilizes present value techniques and option-pricing models for valuing its derivatives. Inputs to these valuation techniques include published forward prices, volatilities, and credit risk considerations, including the incorporation of published interest rates and credit spreads. All of the significant inputs are observable, either directly or indirectly; therefore, Forest's derivative instruments are included within the Level 2 fair value hierarchy.

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The fair values and carrying amounts of Forest's financial instruments are summarized below as of the dates indicated.

	September 30, 2014		Fair Value Measurements	
	Carrying Amount	Total Fair Value ⁽¹⁾	Using Quoted Prices in Active Markets for Identical Liabilities (Level 1)	Using Significant Other Observable Inputs (Level 2)
	(In Thousands)			
Assets:				
Derivative instruments	\$9,167	\$9,167	\$—	\$9,167
Liabilities:				
Derivative instruments	1,164	1,164	—	1,164
Credit facility	13,000	13,000	—	13,000
7¼% senior notes due 2019	578,068	540,407	540,407	—
7½% senior notes due 2020	222,087	214,036	214,036	—

Forest used various assumptions and methods in estimating the fair values of its financial instruments. The fair values of the senior notes were estimated based on quoted market prices. The carrying amount of the Credit Facility approximated fair value due to the short original maturities of the borrowings and because the borrowings bear interest at variable market rates. The methods used to determine the fair values of the derivative instruments are discussed above. See also Note 8 for more information on the derivative instruments.

	December 31, 2013		Fair Value Measurements	
	Carrying Amount	Total Fair Value ⁽¹⁾	Using Quoted Prices in Active Markets for Identical Liabilities (Level 1)	Using Significant Other Observable Inputs (Level 2)
	(In Thousands)			
Assets:				
Derivative instruments	\$5,592	\$5,592	\$—	\$5,592
Liabilities:				
Derivative instruments	4,542	4,542	—	4,542
7¼% senior notes due 2019	578,092	568,147	568,147	—
7½% senior notes due 2020	222,087	224,030	224,030	—

Forest used various assumptions and methods in estimating the fair values of its financial instruments. The fair values of the senior notes were estimated based on quoted market prices. The methods used to determine the fair values of the derivative instruments are discussed above. See also Note 8 for more information on the derivative instruments.

(8) DERIVATIVE INSTRUMENTS

Commodity Derivatives

Forest periodically enters into commodity derivative instruments in order to moderate the effects of wide fluctuations in commodity prices on Forest's cash flow and to manage its exposure to commodity price risk. Forest's commodity derivative instruments generally serve as effective economic hedges of commodity price exposure;

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however, Forest has elected not to designate its derivatives as hedging instruments for accounting purposes. As such, Forest recognizes all changes in fair value of its derivative instruments as unrealized gains or losses on derivative instruments in the line item "Realized and unrealized losses (gains) on derivative instruments, net" in the Condensed Consolidated Statement of Operations.

The table below sets forth Forest's outstanding commodity swaps as of September 30, 2014.

Commodity Swaps

Remaining Swap Term	Natural Gas (NYMEX HH)		Oil (NYMEX WTI)	
	Bbtu Per Day	Weighted Average Hedged Price per MMBtu	Barrels Per Day	Weighted Average Hedged Price per Bbl
October 2014 - December 2014	70	\$4.38	3,500	\$95.34
Calendar 2015	50	4.21	1,000	89.25

The table below sets forth Forest's outstanding commodity collars as of September 30, 2014.

Commodity Collars

Collar Term	Natural Gas (NYMEX HH)	
	Bbtu Per Day	Hedged Floor and Ceiling Price per MMBtu
January 2015 - March 2015	20	\$ 4.50/5.31
Calendar 2015	10	4.10/4.30

In connection with several of its natural gas and oil swaps, Forest granted option instruments (swaptions and puts) to the swap counterparties in exchange for Forest receiving premium hedged prices on the natural gas and oil swaps. Under the terms of the swaption agreements, the counterparties have the option to enter into future swaps with Forest. The swaptions may not be exercised until their expiration dates. Under the terms of the put agreements, the counterparties have the option to put specified quantities of oil to Forest at specified prices. The puts may be exercised monthly by the counterparties. The table below sets forth the outstanding options as of September 30, 2014.

Commodity Options

Underlying Term	Option Expiration	Natural Gas (NYMEX HH)		Oil (NYMEX WTI)	
		Underlying Bbtu Per Day	Underlying Hedged Price per MMBtu	Underlying Barrels Per Day	Underlying Hedged Price per Bbl
Natural Gas Swaptions:					
Calendar 2016	December 2014	10	\$ 4.18	—	\$—
Oil Swaptions:					
Calendar 2015	December 2014	—	—	3,000	100.00
Calendar 2015	December 2014	—	—	1,000	106.00
Calendar 2015	December 2014	—	—	1,000	99.00
Calendar 2016	December 2015	—	—	1,000	98.00
Oil Put Options:					
Monthly Calendar 2014	Monthly Calendar 2014	—	—	2,000	70.00

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Fair Value and Gains and Losses

The table below summarizes the location and fair value amounts of Forest's derivative instruments reported in the Condensed Consolidated Balance Sheets as of the dates indicated. These derivative instruments are not designated as hedging instruments for accounting purposes. For financial reporting purposes, Forest does not offset asset and liability fair value amounts recognized for derivative instruments with the same counterparty under its master netting arrangements. See "Credit Risk" below for more information regarding Forest's master netting arrangements and gross and net presentation of derivative instruments. See also Note 7 for more information on the fair values of Forest's derivative instruments.

	September 30, 2014	December 31, 2013
	(In Thousands)	
Current assets:		
Derivative instruments:		
Commodity	\$8,033	\$5,192
Long-term assets:		
Derivative instruments:		
Commodity	\$1,134	\$400
Current liabilities:		
Derivative instruments:		
Commodity	\$563	\$4,542
Long-term liabilities:		
Derivative instruments:		
Commodity	\$601	\$—

The table below summarizes the amount of derivative instrument gains and losses reported in the Condensed Consolidated Statements of Operations as realized and unrealized losses (gains) on derivative instruments, net, for the periods indicated. Realized gains and losses represent cash settlements on derivative instruments and unrealized gains and losses represent changes in the fair value of derivative instruments. These derivative instruments are not designated as hedging instruments for accounting purposes.

	Three Months Ended September 30, 2014		September 30, 2013		Nine Months Ended September 30, 2014		September 30, 2013	
	(In Thousands)							
Commodity derivatives:								
Realized (gains) losses	\$(1,451	)	\$(1,145	)	\$7,305	\$	(9,688)
Unrealized (gains) losses	(22,688	)	6,678	)	(6,952	)	9,016)
Interest rate derivatives:								
Realized gains	—	—	—	—	—	—	(12,885)
Unrealized losses	—	—	—	—	—	—	13,060)
Realized and unrealized (gains) losses on derivative instruments, net	\$(24,139	)	\$5,533	)	\$353	\$	(497)

Due to the volatility of oil and natural gas prices, the estimated fair values of Forest's commodity derivative instruments are subject to large fluctuations from period to period. Forest has experienced the effects of these commodity price fluctuations and expects that volatility in commodity prices will continue.

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Credit Risk

Forest executes with each of its derivative counterparties an International Swap and Derivatives Association, Inc. (“ISDA”) Master Agreement, which is a standard industry form contract containing general terms and conditions applicable to many types of derivative transactions. Additionally, Forest executes, with each of its derivative counterparties, a Schedule, which modifies the terms and conditions of the ISDA Master Agreement according to the parties’ requirements and the specific types of derivatives to be transacted. As of September 30, 2014, all but one of Forest’s derivative counterparties are lenders, or affiliates of lenders, under the Credit Facility. The terms of the Credit Facility provide that any security granted by Forest thereunder shall also extend to and be available to those lenders that are counterparties to derivative transactions. None of these counterparties requires collateral beyond that already pledged under the Credit Facility. The remaining counterparty, a purchaser of Forest’s natural gas production, generally owes money to Forest and therefore does not require collateral under the ISDA Master Agreement and Schedule it has executed with Forest.

The ISDA Master Agreements and Schedules contain cross-default provisions whereby a default under the Credit Facility will also cause a default under the derivative agreements. Such events of default include non-payment, breach of warranty, non-performance of the financial covenant, default on other indebtedness, certain pension plan events, certain adverse judgments, change of control events, and a failure of the liens securing the Credit Facility. In addition, bankruptcy and insolvency events with respect to Forest or certain of its U.S. subsidiaries will result in an automatic acceleration of the indebtedness under the Credit Facility. None of these events of default is specifically credit-related, but some could arise if there were a general deterioration of Forest’s credit. The ISDA Master Agreements and Schedules contain a further credit-related termination event that would occur if Forest were to merge with another entity and the creditworthiness of the resulting entity was materially weaker than that of Forest.

The majority of Forest’s derivative counterparties are financial institutions that are engaged in similar activities and have similar economic characteristics that, in general, could cause their ability to meet contractual obligations to be similarly affected by changes in economic or other conditions. Forest does not require the posting of collateral for its benefit under its derivative agreements. However, the ISDA Master Agreements and Schedules generally contain netting provisions whereby if on any date amounts would otherwise be payable by each party to the other, then on such date, the party that owes the larger amount will pay the excess of that amount over the smaller amount owed by the other party, thus satisfying each party’s obligations. These provisions generally apply to all derivative transactions, or all derivative transactions of the same type (e.g., commodity, interest rate, etc.), with the particular counterparty. If all counterparties failed, Forest would be exposed to a risk of loss equal to this net amount owed to Forest, the fair value of which was \$8.6 million at September 30, 2014. If Forest suffered an event of default, each counterparty could demand immediate payment, subject to notification periods, of the net obligations due to it under the derivative agreements. At September 30, 2014, Forest owed a net derivative liability to its counterparties, the fair value of which was \$.6 million. In the absence of netting provisions, at September 30, 2014, Forest would be exposed to a risk of loss of \$9.2 million under its derivative agreements, and Forest’s derivative counterparties would be exposed to a risk of loss of \$1.2 million.

For financial reporting purposes, Forest has elected not to offset asset and liability fair value amounts recognized for derivative instruments with the same counterparty under its master netting arrangements, although such derivative instruments are subject to enforceable master netting arrangements. The following tables disclose information regarding the potential effect of netting arrangements on Forest’s Condensed Consolidated Balance Sheets as of the dates indicated.

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	Derivative Assets	
	September 30, 2014	December 31, 2013
	(In Thousands)	
Gross amounts of recognized assets	\$9,167	\$5,592
Gross amounts offset in the balance sheet	—	—
Net amounts of assets presented in the balance sheet	9,167	5,592
Gross amounts not offset in the balance sheet:		
Derivative instruments	(553	) (1,049
Cash collateral received	—	—
Net amount	\$8,614	\$4,543
	Derivative Liabilities	
	September 30, 2014	December 31, 2013
	(In Thousands)	
Gross amounts of recognized liabilities	\$1,164	\$4,542
Gross amounts offset in the balance sheet	—	—
Net amounts of liabilities presented in the balance sheet	1,164	4,542
Gross amounts not offset in the balance sheet:		
Derivative instruments	(553	) (1,049
Cash collateral pledged	—	—
Net amount	\$611	\$3,493

On July 21, 2010, the Dodd-Frank Wall Street Reform and Consumer Protection Act (the “Dodd-Frank Act”) was enacted, which included derivatives reform as part of a broader financial regulatory reform. Congress delegated many of the details of the Dodd-Frank Act to federal regulatory agencies. Forest currently expects that the Dodd-Frank Act and related rules will have little impact on its existing derivative transactions under its outstanding ISDA Master Agreements and Schedules. However, the legislation could have a substantial impact on Forest’s counterparties and increase the cost of Forest’s derivative agreements in the future.

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(9) COSTS, EXPENSES, AND OTHER

The table below sets forth the components of “Other, net” in the Condensed Consolidated Statements of Operations for the periods indicated.

	Three Months Ended		Nine Months Ended	
	September 30, 2014	2013	September 30, 2014	2013
	(In Thousands)			
Accretion of asset retirement obligations	\$348	\$546	\$1,242	\$2,339
Write-off of debt issuance costs	—	—	3,323	—
Loss on debt extinguishment	—	—	—	25,223
Gain on asset dispositions, net	—	—	(21,391)) —
Merger-related costs	2,170	—	12,372	—
Rig stacking/lease termination	2,035	2,076	10,294	6,372
Other, net	457	(1,547)	) (1,484)	) (2,446)
	\$5,010	\$1,075	\$4,356	\$31,488

Accretion of Asset Retirement Obligations

Accretion of asset retirement obligations is the expense recognized to increase the carrying amount of the liability associated with Forest’s asset retirement obligations as a result of the passage of time. Forest’s asset retirement obligations consist of costs related to the plugging of wells, the removal of facilities and equipment, and site restoration on oil and natural gas properties.

Write-off of Debt Issuance Costs

On March 31, 2014 Forest entered into the Second Amendment to the Credit Facility, which was effective as of that date. The Second Amendment reduced aggregate lender commitments from \$1.5 billion to \$500.0 million, necessitating a proportionate write-off of \$3.3 million in unamortized debt issuance costs associated with the Credit Facility prior to the Second Amendment.

Loss on Debt Extinguishment

In March 2013, Forest redeemed \$300.0 million in principal amount of 8½% senior notes at 107.11% of par, recognizing a loss of \$25.2 million upon redemption due to the \$21.3 million call premium and write-off of \$3.9 million of unamortized debt issuance costs and discount.

Gain on Asset Dispositions, Net

In October 2013, Forest entered into an agreement to sell all of its oil and natural gas properties located in the Texas Panhandle for \$1.0 billion in cash. This divestiture closed in November 2013 and Forest has received total proceeds of \$985.3 million, after customary purchase price adjustments. A net gain of \$18.2 million was recognized on the divestiture during the nine months ended September 30, 2014, as customary post-closing purchase price adjustments were made and additional proceeds were received, including \$20.2 million received in May 2014. Also included in the gain on asset dispositions line item is a \$3.2 million gain recognized on the closing of the sale of Forest’s South African subsidiary in June 2014. See Note 5 for more information on these divestitures.

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Merger-Related Costs

In connection with the pending merger with Sabine, Forest has incurred expenses that are comprised primarily of legal and financial advisor costs. See Note 1 for more information on the pending merger.

Rig Stacking/Lease Termination

Rig stacking comprises the expenses incurred to operate and maintain drilling rigs, which Forest has historically leased under operating leases, that were not being utilized on capital projects. Rig stacking expenses for the three and nine months ended September 30, 2014 were \$1.1 million and \$5.5 million, respectively. Rig stacking expenses for the three and nine months ended September 30, 2013 were \$2.1 million and \$6.4 million, respectively.

During the nine months ended September 30, 2014, Forest terminated the operating leases on nine drilling rigs. In connection with these lease terminations and the current activities underway to return the remaining six rigs to the lessors due to the completion of their lease terms, Forest recognized losses of \$.9 million and \$4.8 million during the three and nine months ended September 30, 2014, respectively.

(10) COMPREHENSIVE INCOME (LOSS)

Comprehensive income (loss) is a term used to refer to net earnings (loss) plus other comprehensive income (loss). Other comprehensive income (loss) is comprised of revenues, expenses, gains, and losses that, under generally accepted accounting principles, are reported as separate components of shareholders' equity instead of net earnings (loss). Forest's other comprehensive income during the three and nine months ended September 30, 2014 consists of actuarial losses reclassified from accumulated other comprehensive loss and included in net periodic benefit cost, which is included in the line item "General and administrative" in the Condensed Consolidated Statements of Operations.

The components of other comprehensive income, both before-tax and net-of-tax, for the three and nine months ended September 30, 2014 are as follows:

	Before-Tax (In Thousands)	Tax (Expense) / Benefit	Net-of-Tax
Three Months Ended September 30, 2014:			
Defined benefit postretirement plans			
Actuarial losses reclassified from accumulated other comprehensive loss and included in net periodic benefit cost	\$2,476	\$(1,112)	) \$1,364
Other comprehensive income	\$2,476	\$(1,112)	) \$1,364
Nine Months Ended September 30, 2014:			
Defined benefit postretirement plans			
Actuarial losses reclassified from accumulated other comprehensive loss and included in net periodic benefit cost	\$2,823	\$(1,112)) \$1,711
Other comprehensive income	\$2,823	\$(1,112)) \$1,711

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The change in the accumulated balance of other comprehensive loss during the nine months ended September 30, 2014 is as follows:

	Accumulated Other Comprehensive Loss ⁽¹⁾ (In Thousands)
Defined benefit postretirement plans	
Balance at December 31, 2013	\$(10,398)
Amounts reclassified from accumulated other comprehensive loss	1,711
Other comprehensive income	1,711
Balance at September 30, 2014	\$(8,687)

(1) All amounts are net of tax.

(11) RECENTLY ISSUED ACCOUNTING STANDARDS

In May 2014, the Financial Accounting Standards Board issued Accounting Standards Update No. 2014-09, “Revenue from Contracts with Customers (Topic 606)” (“ASU 2014-09”). ASU 2014-09 is the result of a joint project with the International Accounting Standards Board intended to clarify the principles for recognizing revenue and to develop a common revenue standard for U.S. generally accepted accounting principles and International Financial Reporting Standards. The guidance is expected to enhance comparability of revenue recognition practices across entities, industries, jurisdictions, and capital markets. The core principle of the guidance is that an entity should recognize revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. Additionally, the guidance requires improved disclosures to help users of financial statements better understand the nature, amount, timing, and uncertainty of revenue that is recognized. Entities must adopt ASU 2014-09 using either a full retrospective approach or a modified retrospective approach with a cumulative effect of adoption recognized in the opening balance of retained earnings at the date of adoption. ASU 2014-09 is effective for annual reporting periods beginning after December 15, 2016, including interim periods within that reporting period. Early adoption is not permitted. Forest has not yet determined the effect that adoption of ASU 2014-09 will have on its financial statements, nor has Forest determined which transition method it will use upon adoption.

In April 2014, the Financial Accounting Standards Board issued Accounting Standards Update No. 2014-08, “Presentation of Financial Statements (Topic 205) and Property, Plant, and Equipment (Topic 360)—Reporting Discontinued Operations and Disclosures of Disposals of Components of an Entity” (“ASU 2014-08”). ASU 2014-08 changes the requirements for reporting discontinued operations and requires expanded disclosures for discontinued operations and individually significant components of an entity that either have been disposed of or are classified as held for sale, but do not qualify for discontinued operations reporting. Only those disposals of components of an entity that represent a strategic shift that has (or will have) a major effect on an entity’s operations and financial results will be reported as discontinued operations in the financial statements. ASU 2014-08 is effective for annual periods, and interim periods within those years, beginning on or after December 15, 2014 and is applied prospectively. Early adoption is permitted, but only for disposals or classifications as held for sale that have not been reported in financial statements previously issued or available for issuance. Forest adopted ASU 2014-08 during the quarter ended March 31, 2014 and there was no impact to its consolidated financial statements.

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Item 2. MANAGEMENT’S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

OVERVIEW

All expectations, forecasts, assumptions, and beliefs about our future financial results, condition, operations, strategic plans, and performance are forward-looking statements, as described in more detail under the heading “Forward-Looking Statements” below. Our actual results may differ materially because of a number of risks and uncertainties. Historical statements made herein are accurate only as of the date of filing of this Quarterly Report on Form 10-Q with the Securities and Exchange Commission (“SEC”), and may be relied upon only as of that date. The following discussion and analysis should be read in conjunction with Forest’s Condensed Consolidated Financial Statements and the Notes thereto, the information included or incorporated by reference under the headings “Forward-Looking Statements” and “Risk Factors” below, and the information included or incorporated by reference in Forest’s 2013 Annual Report on Form 10-K and Forest’s 2013 Amended Annual Report on Form 10-K/A under the headings “Risk Factors” and “Management’s Discussion and Analysis of Financial Condition and Results of Operations.” Unless the context indicates otherwise, all references in this document to “Forest,” “the Company,” “we,” “our,” “ours,” and “us” refer to Forest Oil Corporation and its consolidated subsidiaries.

Forest is an independent oil and gas company engaged in the acquisition, exploration, development, and production of oil, natural gas, and natural gas liquids (“NGLs”) primarily in North America. Forest was incorporated in New York in 1924, as the successor to a company formed in 1916, and has been a publicly held company since 1969. We currently conduct our operations in one reportable geographical segment - the United States. Our core operational areas are in the Eagle Ford in South Texas and the Ark-La-Tex region in Texas, Louisiana, and Arkansas.

Recent Events

On October 1, 2014, we entered into, and closed on, an agreement to purchase approximately 7,700 net acres comprised of both undeveloped and producing properties, including three horizontal Cotton Valley wells, located in Rusk County in East Texas, for a purchase price of \$20 million.

On May 5, 2014, we entered into an Agreement and Plan of Merger with Sabine Oil & Gas LLC (“Sabine”), under which Forest and Sabine will combine their businesses in an all-stock transaction. This agreement was amended on July 9, 2014 primarily to change the structure of the transaction, in which Forest now will be the surviving legal entity. The revised transaction structure does not change the economic terms of the transaction. Under the terms of the amended merger agreement, the owners of Sabine will contribute their interests in Sabine to Forest, in exchange for Forest common and preferred stock. Upon closing of the combination transaction, Forest’s shareholders will own common shares that represent an approximate 26.5% economic interest in the combined company and approximately 20% of the total voting power, and Sabine’s equity holders will own common shares and preferred shares that represent an approximate 73.5% economic interest and approximately 80% of the total voting power in the combined company. The combined entity will change its name to Sabine Oil & Gas Corporation and be headquartered in Houston. Consummation of the transaction is subject to approval by Forest shareholders, regulatory approvals, and other customary closing conditions. In late October 2014, Forest commenced mailing definitive proxy materials and scheduled a special meeting of shareholders for November 20, 2014, to consider and vote on the proposed merger agreement with Sabine. Forest shareholders of record at the close of business on October 3, 2014, the record date, are entitled to notice of, and to vote at, the Forest special meeting.

In October 2013, we entered into an agreement to sell all of our oil and natural gas properties located in the Texas Panhandle for \$1 billion in cash. This transaction closed in November 2013 and we received total proceeds of \$985

million, including \$20 million received in May 2014, after customary purchase price adjustments and escrow account settlements. In January 2013, we entered into an agreement to sell all of our oil and natural gas properties located in South Texas, excluding our Eagle Ford oil properties, for \$325 million in cash. This transaction closed in February 2013 and we received total proceeds of \$321 million, after customary purchase price adjustments. We used

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the proceeds from these property divestitures to reduce our debt. These property divestitures affect the comparability of the results of our operations between the three and nine months ended September 30, 2014 and the three and nine months ended September 30, 2013 presented herein.

RESULTS OF OPERATIONS

For the three and nine months ended September 30, 2014, we recognized net losses of \$106 million and \$210 million, respectively, compared to net earnings of \$2 million and a net loss of \$32 million for the three and nine months ended September 30, 2013, respectively. Adjusted EBITDA, which is a measure used by management, securities analysts, and investors that consists of net earnings (loss) before interest expense, income taxes, depreciation, depletion, and amortization, as well as other items including ceiling test write-downs and unrealized gains and losses on derivative instruments, was \$39 million and \$105 million for the three and nine months ended September 30, 2014, respectively, compared to \$85 million and \$268 million for the three and nine months ended September 30, 2013, respectively. The decreases in EBITDA in the 2014 periods as compared to the 2013 periods were primarily due to the property divestitures referenced above under "Recent Events." Adjusted EBITDA is a performance measure not calculated in accordance with generally accepted accounting principles ("GAAP"). See "Reconciliation of Non-GAAP Measure" at the end of this Item 2 for a reconciliation of Adjusted EBITDA to our reported net earnings (loss), the most directly comparable financial measure calculated and presented in accordance with GAAP.

Management's analysis of the individual components of the changes in our quarterly and year-to-date results follows.

Oil, Natural Gas, and Natural Gas Liquids Volumes, Revenues, and Prices

Oil, natural gas, and natural gas liquids sales volumes, revenues, and per unit price realizations for the three and nine months ended September 30, 2014 and 2013 are set forth in the table below.

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2014	2013	2014	2013
Sales volumes:				
Oil (MBbls)	330	621	948	1,781
Natural gas (MMcf)	6,666	11,568	19,320	37,306
NGLs (MBbls)	224	655	584	2,047
Totals (MMcfe)	9,990	19,224	28,512	60,274
Revenues (in thousands):				
Oil	\$30,141	\$63,926	\$88,580	\$174,204
Natural gas	25,516	34,966	80,232	118,785
NGLs	6,396	19,136	17,804	59,867
Totals	\$62,053	\$118,028	\$186,616	\$352,856
Per unit price realizations:				
Oil (\$/Bbl)	\$91.34	\$102.94	\$93.44	\$97.81
Natural gas (\$/Mcf)	3.83	3.02	4.15	3.18
NGLs (\$/Bbl)	28.55	29.22	30.49	29.25
Totals (\$/Mcf)	\$6.21	\$6.14	\$6.55	\$5.85

We sold a substantial amount of oil and natural gas properties in 2013, which significantly impacts the comparability of our reported results between each of the respective periods in 2013 and 2014. Accordingly, the tables below distinguish oil, natural gas, and NGL sales revenues and volumes, as well as per unit price realizations, between those oil and natural gas properties that we divested in 2013, i.e., South Texas and Texas Panhandle

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properties (the “Divested properties”) and those oil and natural gas properties that we continued to own as of September 30, 2014 (the “Retained properties”).

Three Months Ended September 30, 2014 and 2013

	Oil, Natural Gas, and NGL Revenues		\$ Change	Oil, Natural Gas, and NGL Sales Volumes		Volume Change	Per Unit Price Realizations		\$ Change (1)	Change In Revenues Attributable to Change In:		
	Three Months Ended September 30,			Three Months Ended September 30,			Three Months Ended September 30,			Volumes (2)	Prices (3)	Total
	2014	2013		2014	2013		2014	2013				
	(In Thousands)			MBbls			\$/Bbl			(In Thousands)		
Oil Retained properties	\$30,141	\$37,363	\$(7,222)	330	358	(28)	\$91.34	\$104.37	\$(13.03)	\$(2,922)	\$(4,300)	\$(7,222)
Oil Divested properties	—	26,563	(26,563)	—	263	(263)	—	101.00	(101.00)	(26,563)	—	(26,563)
	\$30,141	\$63,926	\$(33,785)	330	621	(291)	\$91.34	\$102.94	\$(11.60)	\$(29,956)	\$(3,829)	\$(33,785)
Natural gas Retained properties	\$25,516	\$23,308	\$2,208	6,666	7,202	(536)	\$3.83	\$3.24	\$0.59	\$(1,735)	\$3,943	\$2,208
Natural gas Divested properties	—	11,658	(11,658)	—	4,366	(4,366)	—	2.67	(2.67)	(11,658)	—	(11,658)
	\$25,516	\$34,966	\$(9,450)	6,666	11,568	(4,902)	\$3.83	\$3.02	\$0.81	\$(14,817)	\$5,367	\$(9,450)
NGLs Retained properties	\$6,396	\$5,804	\$592	224	198	26	\$28.55	\$29.31	\$(0.76)	\$762	\$(170)	\$592
NGLs Divested properties	—	13,332	(13,332)	—	457	(457)	—	29.17	(29.17)	(13,332)	—	(13,332)
	\$6,396	\$19,136	\$(12,740)	224	655	(431)	\$28.55	\$29.22	\$(0.66)	\$(12,592)	\$(148)	\$(12,740)
Total Retained properties	\$62,053	\$66,475	\$(4,422)	9,990	10,538	(548)	\$6.21	\$6.31	\$(0.10)	\$(3,457)	\$(965)	\$(4,422)
Total Divested properties	—	51,553	(51,553)	—	8,686	(8,686)	—	5.94	(5.94)	(51,553)	—	(51,553)
	\$62,053	\$118,028	\$(55,975)	9,990	19,224	(9,234)	\$6.21	\$6.14	\$0.07	\$(56,693)	\$718	\$(55,975)

(1) Certain amounts may not recalculate due to rounding.

(2) The change in revenues attributable to the change in volumes is calculated as the product of (i) the per unit price realization for the three months ended September 30, 2013 and (ii) the change in volumes between the three months ended September 30, 2013 and the three months ended September 30, 2014. Certain amounts may not recalculate or foot due to rounding.

(3) The change in revenues attributable to the change in prices is calculated as the product of (i) the volumes for the three months ended September 30, 2014 and (ii) the change in the per unit price realization between

the three months ended September 30, 2013 and the three months ended September 30, 2014. Certain amounts may not recalculate or foot due to rounding.

Equivalent sales volumes were 10.0 Bcfe for the three months ended September 30, 2014 as compared to 19.2 Bcfe for the three months ended September 30, 2013. The 9.2 Bcfe, or 48%, decrease in equivalent sales volumes for the three months ended September 30, 2014 compared to the three months ended September 30, 2013 was primarily due to the divestitures of producing oil and natural gas properties in the Texas Panhandle, which accounted for 8.7 Bcfe of the decrease. Equivalent sales volumes attributable to properties we continued to own as

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of September 30, 2014 decreased 5% to 10.0 Bcfe for the three months ended September 30, 2014 from 10.5 Bcfe for the three months ended September 30, 2013. The 5% decrease in these equivalent sales volumes was due to a 7% decrease in natural gas production and an 8% decrease in oil production, partially offset by a 13% increase in NGL production. The increase in NGL production was due to our drilling program in East Texas, where we incurred approximately \$53 million in direct exploration, development, and leasehold acquisition capital expenditures during the three months ended September 30, 2014. The decrease in oil production was a result of the reduced pace of drilling in the Eagle Ford starting in the first quarter of 2014 and from the natural decline in oil production from existing wells. Natural gas production declined 7% due to the natural decline in production from existing wells, which exceeded the incremental natural gas production we added during the three months ended September 30, 2014 from drilling liquids-rich East Texas wells.

Revenues from oil, natural gas, and NGLs were \$62 million in the third quarter of 2014 as compared to \$118 million in the third quarter of 2013. The \$56 million, or 47%, decrease in revenues in the third quarter of 2014 compared to the third quarter of 2013 was primarily due to the divestitures of producing oil and natural gas properties in the Texas Panhandle, which accounted for \$52 million of the decrease. Revenues from the properties we continued to own as of September 30, 2014 decreased by \$4 million primarily due to decreased oil per unit price realizations and oil and natural gas production, partially offset by increased natural gas per unit price realizations between the two periods.

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Nine Months Ended September 30, 2014 and 2013

	Oil, Natural Gas, and NGL Revenues			Oil, Natural Gas, and NGL Sales Volumes			Per Unit Price Realizations		Change In Revenues Attributable to Change In:			
	Nine Months Ended		\$ Change	Nine Months Ended		Volume Change	Nine Months Ended		\$ Change (1)	Volumes (2)	Prices (3)	Total
September 30, 2014	September 30, 2013	September 30, 2014		September 30, 2013	September 30, 2014		September 30, 2013					
	(In Thousands)			MBbls			\$/Bbl		(In Thousands)			
Oil												
Retained properties	\$88,580	\$93,133	\$(4,553)	948	905	43	\$93.44	\$102.91	\$(9.47)	\$4,425	\$(8,978)	\$(4,553)
Divested properties	—	81,071	(81,071)	—	876	(876)	—	92.55	(92.55)	(81,071)	—	(81,071)
	\$88,580	\$174,204	\$(85,624)	948	1,781	(833)	\$93.44	\$97.81	\$(4.37)	\$(81,478)	\$(4,146)	\$(85,624)
Natural gas												
Retained properties	\$80,232	\$74,194	\$6,038	19,320	22,014	(2,694)	\$4.15	\$3.37	\$.78	\$(9,080)	\$15,118	\$6,038
Divested properties	—	44,591	(44,591)	—	15,292	(15,292)	—	2.92	(2.92)	(44,591)	—	(44,591)
	\$80,232	\$118,785	\$(38,553)	19,320	37,306	(17,986)	\$4.15	\$3.18	\$.97	\$(57,269)	\$18,716	\$(38,553)
NGLs												
Retained properties	\$17,804	\$16,469	\$1,335	584	552	32	\$30.49	\$29.84	\$.65	\$955	\$380	\$1,335
Divested properties	—	43,398	(43,398)	—	1,495	(1,495)	—	29.03	(29.03)	(43,398)	—	(43,398)
	\$17,804	\$59,867	\$(42,063)	584	2,047	(1,463)	\$30.49	\$29.25	\$1.24	\$(42,787)	\$724	\$(42,063)
Total												
Retained properties	\$186,616	\$183,796	\$2,820	28,512	30,756	(2,244)	\$6.55	\$5.98	\$.57	\$(13,410)	\$16,230	\$2,820
Divested properties	—	169,060	(169,060)	—	29,518	(29,518)	—	5.73	(5.73)	(169,060)	—	(169,060)
	\$186,616	\$352,856	\$(166,240)	28,512	60,274	(31,762)	\$6.55	\$5.85	\$.69	\$(185,941)	\$19,701	\$(166,240)

(1) Certain amounts may not recalculate due to rounding.

The change in revenues attributable to the change in volumes is calculated as the product of (i) the per unit price realization for the nine months ended September 30, 2013 and (ii) the change in volumes between the nine months ended September 30, 2013 and the nine months ended September 30, 2014. Certain amounts may not recalculate or foot due to rounding.

(2) The change in revenues attributable to the change in prices is calculated as the product of (i) the volumes for the nine months ended September 30, 2014 and (ii) the change in the per unit price realization between the nine months ended September 30, 2013 and the nine months ended September 30, 2014. Certain amounts may not recalculate or foot due to rounding.

Equivalent sales volumes were 28.5 Bcfe for the nine months ended September 30, 2014 compared to 60.3 Bcfe for the nine months ended September 30, 2013. The 31.8 Bcfe, or 53%, decrease in equivalent sales volumes for the nine

months ended September 30, 2014 compared to the nine months ended September 30, 2013 was primarily due to the divestitures of producing oil and natural gas properties in South Texas and the Texas Panhandle, which accounted for 29.5 Bcfe of the decrease. Equivalent sales volumes attributable to properties we continued to own as of September 30, 2014 decreased 7% to 28.5 Bcfe for the nine months ended September 30, 2014 from 30.8 Bcfe for the nine months ended September 30, 2013. The 7% decrease in these equivalent sales volumes was due to a 12% decrease in natural gas production partially offset by a 5% increase in oil production and a 6% increase in NGL production. The increase in NGL production was due to our drilling program in East Texas, where we incurred

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approximately \$111 million in direct exploration, development, and leasehold acquisition capital expenditures in the nine months ended September 30, 2014. The increase in oil production was a result of our development efforts, primarily through the first half of 2014, in the Eagle Ford, where we incurred approximately \$57 million in direct exploration, development, and leasehold acquisition capital expenditures in the nine months ended September 30, 2014. Natural gas production declined 12% due to the natural decline in production from existing wells, which exceeded the incremental natural gas production we added during the nine months ended September 30, 2014 from drilling liquids-rich East Texas wells.

Revenues from oil, natural gas, and NGLs were \$187 million in the first nine months of 2014 compared to \$353 million in the first nine months of 2013. The \$166 million, or 47%, decrease in the first nine months of 2014 compared to the first nine months of 2013 was primarily due to the divestitures of producing oil and natural gas properties in South Texas and the Texas Panhandle, which accounted for \$169 million of the decrease. Revenues from the properties we continued to own as of September 30, 2014 increased by \$3 million, due to increased natural gas and NGL per unit price realizations and oil and NGL production, partially offset by decreased natural gas production and oil per unit price realizations between the two periods.

The revenues and per unit price realizations reflected in the tables above exclude the effects of commodity derivative instruments because we have elected not to designate our derivative instruments as cash flow hedges. See “Realized and Unrealized Gains and Losses on Derivative Instruments” below for more information on gains and losses relating to our commodity derivative instruments.

Production Expense

The table below sets forth the detail of production expense for the periods indicated.

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2014	2013	2014	2013
	(In Thousands, Except Per Mcfe Data)			
Production expense:				
Lease operating expenses	\$14,449	\$19,245	\$43,254	\$59,616
Production and property taxes	1,266	4,667	7,231	11,912
Transportation and processing costs	2,228	2,790	7,122	9,168
Production expense	\$17,943	\$26,702	\$57,607	\$80,696
Production expense per Mcfe:				
Lease operating expenses	\$1.45	\$1.00	\$1.52	\$.99
Production and property taxes	.13	.24	.25	.20
Transportation and processing costs	.22	.15	.25	.15
Production expense per Mcfe	\$1.80	\$1.39	\$2.02	\$1.34

We sold a substantial amount of oil and natural gas properties in 2013, which significantly impacts the comparability of our reported results between each of the respective periods in 2013 and 2014. Accordingly, the tables below distinguish lease operating expenses, production and property taxes, and transportation and processing costs, as well as per unit production expense, between those oil and natural gas properties we sold in 2013, i.e., the South Texas and Texas Panhandle properties (the “Divested properties”) and those oil and natural gas properties that we continued to own as of September 30, 2014 (the “Retained properties”).

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Three Months Ended September 30, 2014 and 2013

	Production Expense Three Months Ended			Production Expense per Mcfe Three Months Ended		
	September 30, 2014	2013	\$ Change	September 30, 2014	2013	\$ Change
Lease operating expenses	(In Thousands)			\$/Mcfe		
Retained properties	\$14,449	\$12,648	\$1,801	\$1.45	\$1.20	\$.25
Divested properties	—	6,597	(6,597)	—	.76	(.76)
	\$14,449	\$19,245	\$(4,796)	\$1.45	\$1.00	\$.45
Production and property taxes						
Retained properties	\$1,266	\$2,701	\$(1,435)	\$.13	\$.26	\$(.13)
Divested properties	—	1,966	(1,966)	—	.23	(.23)
	\$1,266	\$4,667	\$(3,401)	\$.13	\$.24	\$(.11)
Transportation and processing costs						
Retained properties	\$2,228	\$2,703	\$(475)	\$.22	\$.26	\$(.04)
Divested properties	—	87	(87)	—	.01	(.01)
	\$2,228	\$2,790	\$(562)	\$.22	\$.15	\$.07
Total						
Retained properties	\$17,943	\$18,052	\$(109)	\$1.80	\$1.71	\$.09
Divested properties	—	8,650	(8,650)	—	1.00	(1.00)
	\$17,943	\$26,702	\$(8,759)	\$1.80	\$1.39	\$.41

Nine Months Ended September 30, 2014 and 2013

	Production Expense Nine Months Ended			Production Expense per Mcfe Nine Months Ended		
	September 30, 2014	2013	\$ Change	September 30, 2014	2013	\$ Change
Lease operating expenses	(In Thousands)			\$/Mcfe		
Retained properties	\$43,254	\$35,769	\$7,485	\$1.52	\$1.16	\$.36
Divested properties	—	23,847	(23,847)	—	.81	(.81)
	\$43,254	\$59,616	\$(16,362)	\$1.52	\$.99	\$.53
Production and property taxes						
Retained properties	\$7,231	\$7,366	\$(135)	\$.25	\$.24	\$.01
Divested properties	—	4,546	(4,546)	—	.15	(.15)
	\$7,231	\$11,912	\$(4,681)	\$.25	\$.20	\$.05
Transportation and processing costs						
Retained properties	\$7,122	\$8,736	\$(1,614)	\$.25	\$.28	\$(.03)
Divested properties	—	432	(432)	—	.01	(.01)
	\$7,122	\$9,168	\$(2,046)	\$.25	\$.15	\$.10
Total						
Retained properties	\$57,607	\$51,871	\$5,736	\$2.02	\$1.69	\$.33
Divested properties	—	28,825	(28,825)	—	.98	(.98)
	\$57,607	\$80,696	\$(23,089)	\$2.02	\$1.34	\$.68

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Lease Operating Expenses

Lease operating expenses in the third quarter of 2014 were \$14 million, or \$1.45 per Mcfe, compared to \$19 million, or \$1.00 per Mcfe, in the third quarter of 2013. Lease operating expenses in the first nine months of 2014 were \$43 million, or \$1.52 per Mcfe, compared to \$60 million, or \$.99 per Mcfe, in the first nine months of 2013. Lease operating expenses decreased \$5 million in the third quarter of 2014 compared to the third quarter of 2013 and \$16 million in the first nine months of 2014 as compared to the first nine months of 2013. The decreases in lease operating expenses were primarily the result of oil and natural gas property divestitures, as reflected in the tables above, offset by increases in the lease operating expenses associated with properties we continued to own as of September 30, 2014, which increased by \$2 million and \$7 million during the third quarter of 2014 and the first nine months of 2014, respectively, as compared to the comparable prior year periods. The \$2 million increase in the third quarter of 2014 was primarily due to chemical treatment costs related to our oil production increasing by approximately \$1 million as well as increases in other miscellaneous lease operating costs. The \$7 million increase in the first nine months of 2014 was primarily due to increases in chemical treatment and saltwater disposal costs related to our oil production of approximately \$3 million and \$1 million, respectively, and an increase in workover expense of approximately \$1 million.

Production and Property Taxes

Production and property taxes, consisting primarily of severance taxes paid on the value of the oil, natural gas, and NGLs sold, were 2.0% and 4.0% of oil, natural gas, and NGL revenues for the three months ended September 30, 2014 and 2013, respectively, and 3.9% and 3.4% of oil, natural gas, and NGL revenues for the nine months ended September 30, 2014 and 2013, respectively. Excluding the Divested properties, production and property taxes were 4.1% and 4.0% of oil, natural gas, and NGL revenues for the three and nine months ended September 30, 2013, respectively. The reduced rate of 2.0% for the third quarter of 2014 was caused by approximately \$1 million of severance tax incentive refund credits recorded during the third quarter of 2014 due to the third quarter 2014 approval of reduced severance tax rates with retrospective application on several wells in East Texas. Additionally, the rate is lower in the third quarter of 2014 due to ad valorem taxes being lower by approximately \$.3 million as compared to the third quarter of 2013. Normal fluctuations occur in the production and property taxes as a percentage of oil and natural gas revenues between periods based upon changes in tax rates and changes in the assessed values of oil and natural gas properties and equipment for purposes of ad valorem taxes.

Transportation and Processing Costs

Transportation and processing costs in the third quarter of 2014 were \$2 million, or \$.22 per Mcfe, compared to \$3 million, or \$.15 per Mcfe, in the third quarter of 2013. Transportation and processing costs in the first nine months of 2014 were \$7 million, or \$.25 per Mcfe, compared to \$9 million, or \$.15 per Mcfe, in the first nine months of 2013. The divested South Texas and Texas Panhandle properties had minimal transportation and processing costs associated with them, and as a result these divestitures had a lesser impact in reducing transportation and processing costs. Beginning in June 2014, all oil sales in the Eagle Ford are at the wellhead, which decreased transportation and processing costs on the Retained properties by approximately \$.4 million and \$.6 million in the three and nine months ended September 30, 2014, respectively, as compared to the comparable 2013 periods.

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General and Administrative Expense

The table below sets forth the components of general and administrative expense for the periods indicated.

	Three Months Ended		Nine Months Ended	
	September 30,		September 30,	
	2014	2013	2014	2013
	(In Thousands)			
Stock-based compensation costs	\$1,889	\$3,734	\$6,316	\$15,839
Stock-based compensation costs capitalized	(561	) (1,950	) (2,364	) (6,545
	1,328	1,784	3,952	9,294
Salary and benefit costs	4,385	8,455	17,287	40,724
Other general and administrative costs	3,675	4,202	12,255	13,352
General and administrative costs capitalized	(3,437	) (4,676	) (11,043	) (20,477
	4,623	7,981	18,499	33,599
General and administrative expense	\$5,951	\$9,765	\$22,451	\$42,893

General and administrative expense was \$6 million in the third quarter of 2014 compared to \$10 million in the third quarter of 2013, and was \$22 million in the first nine months of 2014 compared to \$43 million in the first nine months of 2013. The primary factors causing the decreases in general and administrative expense between the comparative quarterly and year-to-date periods are the South Texas and Texas Panhandle oil and natural gas property divestitures that occurred in February 2013 and November 2013, respectively, each of which included a reduction in employee headcount; as well as a general reduction in headcount throughout 2014 not directly related to the property divestitures in 2013.

Salary and benefit costs decreased \$4 million, or 48%, in the third quarter of 2014 as compared to the third quarter of 2013, and \$23 million, or 58%, in the nine months ended September 30, 2014 as compared to the nine months ended September 30, 2013. The nine months ended September 30, 2013 included \$8 million of employee-related South Texas asset divestiture costs comprised of severance paid to involuntarily terminated employees and retention bonuses paid to certain employees due to the South Texas asset divestiture. This compares to \$.7 million of employee-related Panhandle asset divestiture costs included in the nine months ended September 30, 2014.

Stock-based compensation costs, net of costs capitalized, decreased \$.5 million and \$5 million during the three and nine months ended September 30, 2014 as compared to the three and nine months ended September 30, 2013. The decreases were primarily due to a reduction in employee headcount and a decrease in the Company's stock price.

The percentage of general and administrative costs capitalized under the full cost method of accounting ranged from 37% to 40% in the periods presented.

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Depreciation, Depletion, and Amortization

The table below sets forth the components of depreciation, depletion, and amortization expense for the periods indicated.

	Three Months Ended September 30,				Nine Months Ended September 30,			
	2014		2013		2014		2013	
	In Thousands	\$/Mcfe	In Thousands	\$/Mcfe	In Thousands	\$/Mcfe	In Thousands	\$/Mcfe
Depletion	\$20,287	\$2.03	\$42,633	\$2.22	\$59,947	\$2.10	\$131,842	\$2.19
Depreciation	634	.06	1,340	.07	2,692	.09	4,478	.07
Depreciation, depletion, and amortization	\$20,921	\$2.09	\$43,973	\$2.29	\$62,639	\$2.20	\$136,320	\$2.26

Depreciation, depletion, and amortization expense (“DD&A”) in the third quarter of 2014 was \$21 million, or