ADAMS RESOURCES & ENERGY, INC.
Form 10-Q
May 08, 2015

SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D. C. 20549
FORM 10-Q

x Quarterly report pursuant to Section 13 or 15 (d) of the Securities Exchange Act of 1934

For the quarterly period ended March 31, 2015
Commission File Number 1-7908

ADAMS RESOURCES & ENERGY, INC.
(Exact name of Registrant as specified in its charter)

Delaware	74-1753147
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)

17 South Briar Hollow Lane Suite 100, Houston, Texas 77027
(Address of principal executive office & Zip Code)

Registrant's telephone number, including area code (713) 881-3600

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

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

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

Large accelerated filer o Accelerated filer x Non-accelerated filer o Smaller Reporting Company o

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

A total of 4,217,596 shares of Common Stock were outstanding at May 1, 2015.

PART 1 – FINANCIAL INFORMATION

Item 1. Financial Statements

ADAMS RESOURCES & ENERGY, INC. AND SUBSIDIARIES
UNAUDITED CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS
(In thousands, except per share data)

	Three Months Ended March 31,	
	2015	2014
REVENUES:		
Marketing	$537,748	$927,204
Transportation	16,465	17,649
Oil and natural gas	1,360	4,336
	555,573	949,189
COSTS AND EXPENSES:		
Marketing	526,133	915,565
Transportation	13,441	14,661
Oil and gas operations	1,663	2,191
General and administrative	3,331	2,254
Depreciation, depletion and amortization	6,088	6,106
	550,656	940,777
Operating earnings	4,917	8,412
Other income (expense):		
Interest income	78	42
Interest expense	(4)	-
Earnings from continuing operations before income taxes	4,991	8,454
Income tax (provision)	(1,894)	(3,091)
Net earnings	$3,097	$5,363
EARNINGS (LOSS) PER SHARE:		
Basic and diluted net earnings per common share	$.73	$1.27
DIVIDENDS PER COMMON SHARE	$.22	$.22

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

ADAMS RESOURCES & ENERGY, INC. AND SUBSIDIARIES
UNAUDITED CONDENSED CONSOLIDATED BALANCE SHEETS
(In thousands)

	March 31, 2015	December 31, 2014
ASSETS		
Current assets:		
Cash and cash equivalents	$88,132	$80,184
Accounts receivable, net of allowance for doubtful accounts of $171 and $179, respectively	118,941	144,434
Inventory	14,284	13,481
Fair value contracts	806	936
Income tax receivable	-	970
Prepayments	10,598	10,940
Total current assets	232,761	250,945
Property and Equipment		
Marketing	65,984	65,865
Transportation	63,491	63,239
Oil and gas (successful efforts method)	89,499	88,661
Other	186	186
	219,160	217,951
Less – Accumulated depreciation, depletion and amortization	(137,525)	(133,080)
	81,635	84,871
Other Assets:		
Cash deposits and other	5,128	4,998
	$319,524	$340,814
LIABILITIES AND SHAREHOLDERS' EQUITY		
Current Liabilities:		
Accounts payable	$135,238	$160,743
Accounts payable – related party	11	51
Fair value contracts	852	943
Accrued and other liabilities	9,306	6,208
Current deferred income taxes	647	658
Total current liabilities	146,054	168,603
Other Liabilities:		
Asset retirement obligations	2,497	2,464
Deferred taxes and other liabilities	11,306	12,250
	159,857	183,317
Commitments and Contingencies (Note 5)		
Shareholders' Equity:		

Preferred stock - $1.00 par value, 960,000 shares		
authorized, none outstanding	-	-
Common stock - $.10 par value, 7,500,000 shares		
authorized, 4,217,596 shares outstanding	422	422
Contributed capital	11,693	11,693
Retained earnings	147,552	145,382
Total shareholders' equity	159,667	157,497
	$319,524	$340,814

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

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ADAMS RESOURCES & ENERGY, INC. AND SUBSIDIARIES
UNAUDITED CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
(In thousands)

	Three Months Ended March 31,	
	2015	2014
CASH PROVIDED BY OPERATIONS:		
Net earnings	$3,097	$5,363
Adjustments to reconcile net earnings to net cash from operating activities -		
Depreciation, depletion and amortization	6,088	6,106
Property sales (gains)	(512)	(55)
Dry hole costs incurred	34	655
Impairment of oil and gas properties	208	93
Deferred income taxes	(949)	(551)
Net change in fair value contracts	39	316
Decrease (increase) in accounts receivable	25,501	16,533
Decrease (increase) in inventories	(803)	(11,921)
Decrease (increase) in income tax receivable	970	(1,739)
Decrease (increase) in prepayments	342	7,295
Increase (decrease) in accounts payable	(25,385)	11,720
Increase (decrease) in accrued liabilities	3,509	1,758
Other changes, net	(8)	(162)
Net cash provided by operating activities	12,131	35,411
INVESTING ACTIVITIES:		
Property and equipment additions	(3,665)	(7,770)
Insurance and state collateral (deposits) refunds	(103)	(122)
Proceeds from property sales	512	55
Net cash (used in) investing activities	(3,256)	(7,837)
FINANCING ACTIVITIES		
Dividend payments	(927)	(928)
Net cash (used in) financing activities	(927)	(928)
Increase (decrease) in cash and cash equivalents	7,948	26,646
Cash and cash equivalents at beginning of period	80,184	60,733
Cash and cash equivalents at end of period	$88,132	$87,379

The accompanying notes are an integral part of these financial statements

ADAMS RESOURCES & ENERGY, INC. AND SUBSIDIARIES
NOTES TO UNAUDITED CONDENSED
CONSOLIDATED FINANCIAL STATEMENTS

Note 1 - Basis of Presentation

The accompanying unaudited condensed consolidated financial statements, in the opinion of the Company's management, include all adjustments (consisting of normal recurring accruals) necessary for the fair presentation of its financial position at March 31, 2015, its results of operations for the three months ended March 31, 2015 and 2014 and its cash flows for the three months ended March 31, 2015 and 2014. Certain information and note disclosures normally included in annual financial statements prepared in accordance with generally accepted accounting principles (GAAP") have been condensed or omitted pursuant to Securities and Exchange Commission rules and regulations. The impact on the accompanying financial statements of events occurring after March 31, 2015, was evaluated through the date of issuance of these financial statements.

Although the Company believes the disclosures made are adequate to make the information presented not misleading, it is suggested that these unaudited condensed consolidated financial statements be read in conjunction with the financial statements, and the notes thereto, included in the Company's latest annual report on Form 10-K. The interim statement of operations is not necessarily indicative of results to be expected for a full year.

Note 2 - Summary of Significant Accounting Policies

Nature of Operations and Principles of Consolidation

The Company is engaged in the business of crude oil marketing, tank truck transportation of liquid chemicals and oil and gas exploration and production. Its primary area of operation is within a 1,000 mile radius of Houston, Texas. The accompanying unaudited condensed consolidated financial statements include the accounts of Adams Resources & Energy, Inc., a Delaware corporation, and its wholly owned subsidiaries (the Company") after elimination of all intercompany accounts and transactions.

Cash and Cash Equivalents

Cash and cash equivalents include any Treasury bill, commercial paper, money market fund or federal funds with maturity of 90 days or less. Depending on cash availability and market conditions, investments in corporate and municipal bonds, which are classified as investments in marketable securities, may also be made from time to time. Cash and cash equivalents are maintained with major financial institutions and such deposits may exceed the amount of federally backed insurance provided. While the Company regularly monitors the financial stability of such institutions, cash and cash equivalents ultimately remain at risk subject to the financial viability of such institutions.

Inventory

Inventory consists of crude oil held in storage tanks and at third-party pipelines as part of the Company's crude oil marketing operations. Crude oil inventory is carried at the lower of average cost or market.

Prepayments

The components of prepayments and other are as follows (in thousands):

	March 31, 2015	December 31, 2014
Cash collateral deposits for commodity purchases	$8,270	$7,872
Insurance premiums	1,547	2,316
Rents, license and other	781	752
	$10,598	$10,940

Property and Equipment

Expenditures for major renewals and betterments are capitalized, and expenditures for maintenance and repairs are expensed as incurred. Interest costs incurred in connection with major capital expenditures are capitalized and amortized over the lives of the related assets. When properties are retired or sold, the related cost and accumulated depreciation, depletion and amortization is removed from the accounts and any gain or loss is reflected in earnings.

Oil and gas exploration and development expenditures are accounted for in accordance with the successful efforts method of accounting. Direct costs of acquiring developed or undeveloped leasehold acreage, including lease bonus, brokerage and other fees, are capitalized. Exploratory drilling costs are initially capitalized until the properties are evaluated and determined to be either productive or nonproductive. Such evaluations are made on a quarterly basis. If an exploratory well is determined to be nonproductive, the costs of drilling the well are charged to expense. Costs incurred to drill and complete development wells, including dry holes, are capitalized. As of March 31, 2015, the Company had no unevaluated or suspended exploratory drilling costs.

Depreciation, depletion and amortization of the cost of proved oil and gas properties are calculated using the unit-of-production method. The reserve base used to calculate depreciation, depletion and amortization for leasehold acquisition costs and the cost to acquire proved properties is the sum of proved developed reserves and proved undeveloped reserves. For lease and well equipment, development costs and successful exploration drilling costs, the reserve base includes only proved developed reserves. All other property and equipment is depreciated using the straight-line method over the estimated average useful lives of three to twenty years.

The Company reviews its long-lived assets for impairment whenever there is evidence that the carrying value of such assets may not be recoverable. Any impairment recognized is permanent and may not be restored. Producing oil and gas properties are reviewed on a field-by-field basis. For properties requiring impairment, the fair value is estimated based on an internal discounted cash flow model. Cash flows are developed based on estimated future production and prices are then discounted using a market based rate of return consistent with that used by the Company in evaluating cash flows for other assets of a similar nature. For the three-month periods ended March 31, 2015 and 2014 there were $203,000 and zero, respectively, of impairment provisions on producing oil and gas properties.

On a quarterly basis, management evaluates the carrying value of non-producing oil and gas leasehold properties and may deem them impaired based on remaining lease term, area drilling activity and the Company's plans for the property. This fair value measure depends highly on management's assessment of the likelihood of continued exploration efforts in a given area and, as such, data inputs are categorized as unobservable" or Level 3" inputs. Importantly, this fair value measure only applies to the write-down of capitalized costs and will never result in an increase to reported earnings. Accordingly, impairment provisions on non-producing properties totaling $5,000 and $93,000 were recorded for the three-month periods ended March 31, 2015 and 2014, respectively. Capitalized costs for non-producing oil and gas leasehold interests currently represent approximately four percent of total oil and gas property costs and are categorized as follows (in thousands):

	March 31, 2015	December 31, 2014
South Texas Project acreage	$358	$357
Napoleonville, Louisiana acreage	48	48
North Dakota and other acreage areas	606	554
Total Non-producing Leasehold Costs	$1,012	$959

The South Texas and Napoleonville acreage areas have active or scheduled drilling operations underway and holding the underlying acreage is essential to the ongoing exploration effort. The other acreage areas" category consists of smaller onshore interests dispersed over a wide geographical area. Since the Company is generally not the operator of its oil and gas property interest, it does not maintain the underlying detail acreage data and the Company is dependent on the operator when determining which specific acreage will ultimately be drilled. However, the capitalized cost detail on a property-by-property basis is reviewed by management, and deemed impaired if development is not anticipated prior to lease expiration. Onshore leasehold periods are normally three years and may contain renewal options. Capitalized cost activity on the North Dakota and other acreage areas" was as follows (in thousands):

	Leasehold Costs	
	March 31, 2015	December 31, 2014
Net book value January 1	$554	$411
Property additions	54	580
Impairments	(2)	(437)
Net book value end of period	$606	$554

Cash Deposits and Other Assets

The Company has established certain deposits to support participation in its liability insurance program and remittance of state crude oil severance taxes and other state collateral deposits. Insurance collateral deposits are invested at the discretion of the Company's insurance carrier and such investments primarily consist of intermediate term federal government bonds and bonds backed by federal agencies. Components of cash deposits and other assets are as follows (in thousands):

	March 31,	December 31,

	2015	2014
Insurance collateral deposits	$4,627	$4,536
State collateral deposits	167	155
Materials and supplies	334	307
	$5,128	$4,998

Revenue Recognition

Certain commodity purchase and sale contracts utilized by the Company's marketing business qualify as derivative instruments with certain specifically identified contracts also designated as trading activity. From the time of contract origination, such trading activity contracts are marked-to-market and recorded on a net revenue basis in the accompanying financial statements.

Most crude oil purchase contracts and sale contracts qualify and are designated as non-trading activities and the Company considers such contracts as normal purchases and sales activity. For normal purchases and sales, the Company's customers are invoiced monthly based upon contractually agreed upon terms with revenue recognized in the month in which the physical product is delivered to the customer. Such sales are recorded gross in the financial statements because the Company takes title, has risk of loss for the products, is the primary obligor for the purchase, establishes the sale price independently with a third party and maintains credit risk associated with the sale of the product.

Certain crude oil contracts may be with a single counterparty to provide for similar quantities of crude oil to be bought and sold at different locations. These contracts are entered into for a variety of reasons, including effecting the transportation of the commodity, to minimize credit exposure, and/or to meet the competitive demands of the customer. Such buy/sell arrangements are reflected on a net revenue basis in the accompanying unaudited condensed consolidated financial statements. Reporting such crude oil contracts on a gross revenue basis would increase the Company's reported revenues by $130,222,000 and $434,693,000 for the three months ended March 31, 2015 and 2014, respectively.

Transportation segment customers are invoiced, and the related revenue is recognized, as the service is provided. Oil and gas revenue from the Company's interests in producing wells is recognized as title and physical possession of the oil and gas passes to the purchaser.

Sales of long-lived assets

Gains and losses from the sale or disposal of long-lived assets that do not meet the criteria for presentation as a discontinued operation are presented in the accompanying financial statements as a component of operating earnings.

Concentration of Credit Risk

The Company's largest customers consist of large multinational integrated oil companies and independent refiners of crude oil. In addition, the Company transacts business with independent oil producers, major chemical concerns, crude oil trading companies and a variety of commercial energy users. Within this group of customers the Company generally derives approximately 50 percent of its revenues from three or four large crude oil refining concerns. While the Company has ongoing established relationships with certain domestic refiners of crude oil, alternative markets are readily available since the Company supplies less than one percent of U.S. domestic refiner demand. As a fungible commodity delivered to major Gulf Coast supply points, the Company's crude oil sales can be readily delivered to alternative end markets. Management believes that a loss of any of those customers where the Company currently derives more than 10 percent of its revenues would not have a material adverse effect on the Company's operations.

Accounts receivable associated with crude oil activities comprise approximately 95 percent of the Company's total receivables and industry practice requires payment for such sales to occur within 20 days of the end of the month following a transaction. The Company's customer makeup, credit policies and the relatively short duration of receivables mitigate the uncertainty typically associated with receivables management.

Letter of Credit Facility

The Company maintains a Credit and Security Agreement with Wells Fargo Bank to provide a $60 million stand-by letter of credit facility that is used to support the Company's crude oil purchases. This facility is collateralized by the eligible accounts receivable within the segment. Stand-by letters of credit issued totaled $7 million and $15.3 million as of March 31, 2015 and December 31, 2014, respectively. The issued stand-by letters of credit are cancelled as the underlying purchase obligations are satisfied by cash payment when due. The letter of credit facility places certain restrictions on the Company's Gulfmark Energy, Inc. subsidiary. Such restrictions include the maintenance of a combined 1.1 to 1.0 current ratio and the maintenance of positive net earnings excluding inventory valuation changes, as defined, among other restrictions. The Company is currently in compliance with all such financial covenants.

Statement of Cash Flows

Interest paid totaled $4,000 and zero during the three-month periods ended March 31, 2015 and 2014, respectively, while taxes paid during these same periods totaled $1,081,000 and $5,007,000, respectively. Non-cash investing activities for property and equipment were $566,000 and $1,137,000 as of March 31, 2015 and December 31, 2014, respectively and $634,000 and $1,507,000 as of March 31, 2014 and December 31, 2013, respectively. There were no significant non-cash financing activities in any of the periods reported.

Earnings Per Share

Earnings per share are based on the weighted average number of shares of common stock and potentially dilutive common stock shares outstanding during the period presented herein. The weighted average number of shares outstanding was 4,217,596 for 2015 and 2014. There were no potentially dilutive securities during those periods.

Share-Based Payments

During the periods presented herein, the Company had neither stock-based employee compensation plans nor any other share-based payment arrangements.

Use of Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates. Examples of significant estimates used in the accompanying consolidated financial statements include oil and gas reserve volumes forming the foundation for calculating depreciation, depletion and amortization and for estimating cash flows when assessing impairment triggers and when estimating values associated with oil and gas properties. Other examples include revenue accruals, the provision for bad debts, insurance related accruals, income tax permanent and timing differences, contingencies and valuation of fair value contracts.

Income Taxes

Income taxes are accounted for using the asset and liability method. Under this approach, deferred tax assets and liabilities are recognized based on anticipated future tax consequences attributable to differences between financial statement carrying amounts of assets and liabilities and their respective tax basis.

Use of Derivative Instruments

The Company's marketing segment is involved in the purchase and sale of crude oil. The Company seeks to profit by procuring the commodity as it is produced and then delivering the material to the end users or the intermediate use marketplace. As typical for the industry, such transactions are made pursuant to the terms of forward month commodity purchase and/or sale contracts. Some of these contracts meet the definition of a derivative instrument, and therefore, the Company accounts for such contracts at fair value, unless the normal purchase and sale exception is applicable. Such underlying contracts are standard for the industry and are the governing document for the Company's crude oil wholesale distribution businesses. None of the Company's derivative instruments have been designated as hedging instruments. The accounting methodology utilized by the Company for its commodity contracts is further discussed below under the caption Fair Value Measurements".

The estimated fair value of forward month commodity contracts (derivatives) is reflected in the accompanying Unaudited Condensed Consolidated Balance Sheet as of March 31, 2015 as follows (in thousands):

	Balance Sheet Location and Amount			
	Current Assets	Other Assets	Current Liabilities	Other Liabilities
Asset Derivatives				
- Fair Value Forward Hydrocarbon Commodity				
Contracts at Gross Valuation	$871	$-	$-	$-
Liability Derivatives				
- Fair Value Forward Hydrocarbon Commodity				
Contracts at Gross Valuation	-	-	917	-
Less Counterparty Offsets	(65)	-	(65)	-
As Reported Fair Value Contracts	$806	$-	$852	$-

As of March 31, 2015, five commodity purchase and sale contracts comprise the Company's derivative valuations. These contracts encompass approximately 161 barrels per day of crude oil during April 2015 through September 2015 plus 129 barrels per day of crude oil from October 2015 through December 31, 2015 plus 65 barrels per day of diesel fuel from April 2015 through March 2016.

Forward month commodity contracts (derivatives) are reflected in the accompanying Unaudited Condensed Consolidated Balance Sheet as of December 31, 2014 as follows (in thousands):

	Balance Sheet Location and Amount			
	Current Assets	Other Assets	Current Liabilities	Other Liabilities
Asset Derivatives				
- Fair Value Forward Hydrocarbon Commodity				
Contracts at Gross Valuation	$1,332	$-	$-	$-
Liability Derivatives				
- Fair Value Forward Hydrocarbon Commodity				
Contracts at Gross Valuation	-	-	1,339	-
Less Counterparty Offsets	(396)	-	(396)	-

As Reported Fair Value Contracts	$936	$-	$943	$-

As of December 31, 2014, one 100,000 barrel crude oil commodity put option and one commodity purchase and sale contract comprised the Company's derivative valuations. The purchase and sale contract encompasses approximately 175 barrels per day of crude oil in each of January and February 2015.

The Company only enters into commodity contracts with credit worthy counterparties or obtains collateral support for such activities. As of March 31, 2015 and December 31, 2014, the Company was not holding nor has it posted any collateral to support its forward month fair value derivative activity. The Company is not subject to any credit-risk related trigger events. The Company has no other financial investment arrangements that would serve to offset its derivative contracts.

Forward month commodity contracts (derivatives) are reflected in the accompanying Unaudited Condensed Consolidated Statement of Operations for the three months ended March 31, 2015 and 2014 as follows (in thousands):

	Earnings (Loss) Three Months Ended March 31,	
	2015	2014
Revenues – Marketing	$(39)	$398

Fair Value Measurements

The carrying amount reported in the consolidated balance sheet for cash and cash equivalents, accounts receivable and accounts payable approximates fair value because of the immediate or short-term maturity of these financial instruments. Marketable securities are recorded at fair value based on market quotations from actively traded liquid markets.

Fair value contracts consist of derivative financial instruments and are recorded as either an asset or liability measured at its fair value. Changes in fair value are recognized immediately in earnings unless the derivatives qualify for, and the Company elects, cash flow hedge accounting. The Company had no contracts designated for hedge accounting during any current reporting periods.

Fair value estimates are based on assumptions that market participants would use when pricing an asset or liability and the Company uses a fair value hierarchy of three levels that prioritizes the information used to develop those assumptions. Currently, for all items presented herein, the Company utilizes a market approach to valuing its contracts. On a contract by contract, forward month by forward month basis, the Company obtains observable market data for valuing its contracts. The fair value hierarchy gives the highest priority to quoted prices in active markets and the lowest priority to unobservable data. The fair value hierarchy is summarized as follows:

Level 1 – quoted prices in active markets for identical assets or liabilities that may be accessed at the measurement date. Active markets are those in which transactions for the asset or liability occur in sufficient frequency and volume to provide pricing information on an ongoing basis. For Level 1 valuation of marketable securities, the Company utilizes market quotations provided by its primary financial institution and for the valuation of derivative financial instruments the Company utilizes the New York Mercantile Exchange (NYMEX") for such valuations.

Level 2 – (a) quoted prices for similar assets or liabilities in active markets, (b) quoted prices for identical assets or liabilities but in markets that are not actively traded or in which little information is released to the public, (c) observable inputs other than quoted prices and (d) inputs derived from observable market data. Source data for Level 2 inputs include information provided by the NYMEX, published price data and indices, third party price survey data and broker provided forward price statistics.

Level 3 – unobservable market data inputs for assets or liabilities.

As of March 31, 2015, the Company's fair value assets and liabilities are summarized and categorized as follows (in thousands):

	Market Data Inputs				
	Gross Level 1	Gross Level 2	Gross Level 3	Counterparty	
	Quoted Prices	Observable	Unobservable	Offsets	Total
Derivatives					
- Current assets	$-	$871	$ -	$ (65)	$806
- Current liabilities	-	(917)	-	65	(852)
Net Value	$-	$(46)	$ -	$ -	$(46)

As of December 31, 2014, the Company's fair value assets and liabilities are summarized and categorized as follows (in thousands):

	Market Data Inputs			
Gross Level 1	Gross Level 2	Gross Level 3	Counterparty	
Quoted Prices				