

CONTINENTAL RESOURCES, INC

Form 10-Q

November 08, 2012

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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, 2012

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: 001-32886

CONTINENTAL RESOURCES, INC.

(Exact name of registrant as specified in its charter)

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Oklahoma (State or other jurisdiction of incorporation or organization)	73-0767549 (I.R.S. Employer Identification No.)
20 N. Broadway, Oklahoma City, Oklahoma (Address of principal executive offices)	73102 (Zip Code)
(405) 234-9000	
(Registrant's telephone number, including area code)	

Not Applicable

(Former name, former address and former fiscal year, if changed since last report)

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

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

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

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

185,015,995 shares of our \$0.01 par value common stock were outstanding on October 26, 2012.

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When we refer to us, we, our, Company, or Continental we are describing Continental Resources, Inc. and our subsidiaries.

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Glossary of Crude Oil and Natural Gas Terms

The terms included in this section are used throughout this report.

Bbl One stock tank barrel, of 42 U.S. gallons liquid volume, used herein in reference to crude oil, condensate or natural gas liquids.

Boe Barrels of crude oil equivalent, with six thousand cubic feet of natural gas being equivalent to one barrel of crude oil based on the average equivalent energy content of the two commodities.

completion The process of treating a drilled well followed by the installation of permanent equipment for the production of crude oil and/or natural gas.

conventional play An area believed to be capable of producing crude oil and natural gas occurring in discrete accumulations in structural and stratigraphic traps.

DD&A Depreciation, depletion, amortization and accretion.

developed acreage The number of acres allocated or assignable to productive wells or wells capable of production.

development well A well drilled within the proved area of a crude oil or natural gas reservoir to the depth of a stratigraphic horizon known to be productive.

dry gas Refers to natural gas that remains in a gaseous state in the reservoir and does not produce large quantities of liquid hydrocarbons when brought to the surface. Also may refer to gas that has been processed or treated to remove all natural gas liquids.

dry hole Exploratory or development well that does not produce crude oil and/or natural gas in economically producible quantities.

enhanced recovery The recovery of crude oil and natural gas through the injection of liquids or gases into the reservoir, supplementing its natural energy. Enhanced recovery methods are sometimes applied when production slows due to depletion of the natural pressure.

exploratory well A well drilled to find a new field or to find a new reservoir in a field previously found to be productive of crude oil or natural gas in another reservoir.

field An area consisting of a single reservoir or multiple reservoirs all grouped on, or related to, the same individual geological structural feature or stratigraphic condition. The field name refers to the surface area, although it may refer to both the surface and the underground productive formations.

formation A layer of rock which has distinct characteristics that differs from nearby rock.

horizontal drilling A drilling technique used in certain formations where a well is drilled vertically to a certain depth and then drilled at a right angle within a specified interval.

hydraulic fracturing A process involving the high pressure injection of water, sand and additives into rock formations to stimulate crude oil and natural gas production.

injection well A well into which liquids or gases are injected in order to push additional crude oil or natural gas out of underground reservoirs and into the wellbores of producing wells; typically considered an enhanced recovery process.

MBbl One thousand barrels of crude oil, condensate or natural gas liquids.

MBoe One thousand Boe.

Mcf One thousand cubic feet of natural gas.

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MMBtu One million British thermal units. A British thermal unit represents the amount of energy needed to heat one pound of water by one degree Fahrenheit and can be used to describe the energy content of fuels.

MMcf One million cubic feet of natural gas.

net acres The percentage of total acres an owner has out of a particular number of acres, or a specified tract. An owner who has a 50% interest in 100 acres owns 50 net acres.

NYMEX The New York Mercantile Exchange.

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play A portion of the exploration and production cycle following the identification by geologists and geophysicists of areas with potential crude oil and natural gas reserves.

productive well A well found to be capable of producing hydrocarbons in sufficient quantities such that proceeds from the sale of the production exceed production expenses and taxes.

prospect A potential geological feature or formation which geologists and geophysicists believe may contain hydrocarbons. A prospect can be in various stages of evaluation, ranging from a prospect that has been fully evaluated and is ready to drill to a prospect that will require substantial geological and/or geophysical analysis and interpretation.

proved reserves The quantities of crude oil and natural gas, which, by analysis of geoscience and engineering data, can be estimated with reasonable certainty to be economically producible from a given date forward, from known reservoirs and under existing economic conditions, operating methods, and government regulations prior to the time at which contracts providing the right to operate expire, unless evidence indicates renewal is reasonably certain.

proved developed reserves Proved reserves expected to be recovered through existing wells with existing equipment and operating methods.

proved undeveloped reserves or PUD Proved reserves expected to be recovered from new wells on undrilled acreage or from existing wells where a relatively major expenditure is required for recompletion.

reservoir A porous and permeable underground formation containing a natural accumulation of producible crude oil and/or natural gas that is confined by impermeable rock or water barriers and is separate from other reservoirs.

resource play Refers to an expansive contiguous geographical area with prospective crude oil and/or natural gas reserves that has the potential to be developed uniformly with repeatable commercial success due to advancements in horizontal drilling and multi-stage fracturing technologies.

royalty interest Refers to the ownership of a percentage of the resources or revenues produced from a crude oil or natural gas property. A royalty interest owner does not bear exploration, development, or operating expenses associated with drilling and producing a crude oil or natural gas property.

unconventional play An area believed to be capable of producing crude oil and/or natural gas occurring in accumulations that are regionally extensive, but require recently developed technologies to achieve profitability. These areas tend to have low permeability and may be closely associated with source rock as is the case with oil and gas shale, tight oil and gas sands and coalbed methane.

undeveloped acreage Lease acreage on which wells have not been drilled or completed to a point that would permit the production of economically producible quantities of crude oil and/or natural gas.

unit The joining of all or substantially all interests in a reservoir or field, rather than a single tract, to provide for development and operation without regard to separate property interests. Also, the area covered by a unitization agreement.

working interest The right granted to the lessee of a property to explore for and to produce and own crude oil, natural gas, or other minerals. The working interest owners bear the exploration, development, and operating costs on either a cash, penalty, or carried basis.

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Cautionary Statement for the Purpose of the Safe Harbor Provisions of the Private Securities Litigation Reform Act of 1995

This report includes forward-looking statements within the meaning of Section 27A of the Securities Act of 1933 and Section 21E of the Securities Exchange Act of 1934. All statements other than statements of historical fact, including, but not limited to, statements or information concerning the Company's future operations, performance, financial condition, production and reserves, schedules, plans, timing of development, returns, budgets, costs, business strategy, objectives, and cash flow, included in this report are forward-looking statements. When used in this report, the words could, may, believe, anticipate, intend, estimate, expect, project, budget, plan, continue, potential, and similar expressions are intended to identify forward-looking statements, although not all forward-looking statements contain such identifying words. Forward-looking statements are based on the Company's current expectations and assumptions about future events and currently available information as to the outcome and timing of future events. Although the Company believes that the expectations reflected in the forward-looking statements are reasonable and based on reasonable assumptions, no assurance can be given that such expectations will be correct or achieved or that the assumptions are accurate. When considering forward-looking statements, you should keep in mind the risk factors and other cautionary statements described under *Part II, Item 1A. Risk Factors* included in this report, our Annual Report on Form 10-K for the year ended December 31, 2011, registration statements filed from time to time with the SEC, and other announcements we make from time to time.

Without limiting the generality of the foregoing, certain statements incorporated by reference, if any, or included in this report constitute forward-looking statements.

Forward-looking statements may include statements about:

our business strategy;

our future operations;

our reserves;

our technology;

our financial strategy;

crude oil, natural gas liquids, and natural gas prices and differentials;

the timing and amount of future production of crude oil and natural gas;

the amount, nature and timing of capital expenditures;

estimated revenues, expenses and results of operations;

drilling and completing wells;

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competition;

marketing of crude oil and natural gas;

transportation of crude oil, natural gas liquids, and natural gas to markets;

exploitation or property acquisitions and dispositions;

costs of exploiting and developing our properties and conducting other operations;

our financial position;

general economic conditions;

credit markets;

our liquidity and access to capital;

the impact of governmental policies, laws and regulations, as well as regulatory and legal proceedings involving us and of scheduled or potential regulatory or legal changes;

our future operating results;

plans, objectives, expectations and intentions contained in this report that are not historical, including, without limitation, statements regarding our future growth plans;

our commodity hedging arrangements; and

the ability and willingness of current or potential lenders, hedging contract counterparties, customers, and working interest owners to fulfill their obligations to us or to enter into transactions with us in the future on terms that are acceptable to us.

We caution you these forward-looking statements are subject to all of the risks and uncertainties, most of which are difficult to predict and many of which are beyond our control, incident to the exploration for, and development, production, and sale of, crude oil and natural gas. These risks include, but are not limited to, commodity price volatility, inflation, lack of availability of drilling, completion and production equipment and services, environmental risks, drilling and other operating risks, regulatory changes, the uncertainty inherent in estimating crude oil and natural gas reserves and in projecting future rates of production, cash flows and access to capital, the timing of development expenditures, and the other risks described under *Part II, Item 1A. Risk Factors* in this report, our Annual Report on Form 10-K for the year ended December 31, 2011, registration statements filed from time to time with the SEC, and other announcements we make from time to time.

Readers are cautioned not to place undue reliance on forward-looking statements, which speak only as of the date hereof. Should one or more of the risks or uncertainties described in this report occur, or should underlying assumptions prove incorrect, our actual results and plans could differ materially from those expressed in any forward-looking statements. All forward-looking statements are expressly qualified in their entirety by this cautionary statement. This cautionary statement should also be considered in connection with any subsequent written or oral forward-looking statements that we or persons acting on our behalf may issue.

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Except as otherwise required by applicable law, we disclaim any duty to update any forward-looking statements to reflect events or circumstances after the date of this report.

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Table of Contents**PART I. Financial Information****ITEM 1. Financial Statements****Continental Resources, Inc. and Subsidiaries****Condensed Consolidated Balance Sheets**

	September 30, 2012 (Unaudited)	December 31, 2011
	<i>In thousands, except par values and share data</i>	
Assets		
Current assets:		
Cash and cash equivalents	\$ 259,445	\$ 53,544
Receivables:		
Crude oil and natural gas sales	481,976	366,441
Affiliated parties	10,720	31,108
Joint interest and other, net	360,028	379,991
Derivative assets	6,587	6,669
Inventories	47,296	41,270
Deferred and prepaid taxes	21,917	47,658
Prepaid expenses and other	6,313	9,692
Total current assets	1,194,282	936,373
Net property and equipment, based on successful efforts method of accounting	6,922,283	4,681,733
Net debt issuance costs and other	57,268	24,355
Noncurrent derivative assets	52,517	3,625
Total assets	\$ 8,226,350	\$ 5,646,086
Liabilities and shareholders equity		
Current liabilities:		
Accounts payable trade	\$ 624,370	\$ 642,889
Revenues and royalties payable	271,527	222,027
Payables to affiliated parties	6,060	9,939
Accrued liabilities and other	165,977	117,674
Derivative liabilities	26,039	116,985
Current portion of asset retirement obligations	1,576	2,287
Current portion of long-term debt	1,935	
Total current liabilities	1,097,484	1,111,801
Long-term debt, net of current portion	2,943,741	1,254,301
Other noncurrent liabilities:		
Deferred income tax liabilities	1,196,313	850,282
Asset retirement obligations, net of current portion	55,494	60,338
Noncurrent derivative liabilities	4,602	57,598
Other noncurrent liabilities	3,345	3,640
Total other noncurrent liabilities	1,259,754	971,858
Commitments and contingencies (Note 7)		
Shareholders equity:		

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Preferred stock, \$0.01 par value; 25,000,000 shares authorized; no shares issued and outstanding

Common stock, \$0.01 par value; 500,000,000 shares authorized; 185,057,399 shares issued and outstanding at September 30, 2012; 180,871,688 shares issued and outstanding at December 31, 2011

Additional paid-in capital	1,209,023	1,110,694
Retained earnings	1,714,497	1,195,623
Total shareholders' equity	2,925,371	2,308,126
Total liabilities and shareholders' equity	\$ 8,226,350	\$ 5,646,086

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

Table of Contents**Continental Resources, Inc. and Subsidiaries****Unaudited Condensed Consolidated Statements of Income**

	Three months ended September 30,		Nine months ended September 30,	
	2012	2011	2012	2011
	<i>In thousands, except per share data</i>			
Revenues				
Crude oil and natural gas sales	\$ 617,934	\$ 408,037	\$ 1,664,438	\$ 1,103,165
Crude oil and natural gas sales to affiliates	15,410	15,822	44,557	35,945
Gain (loss) on derivative instruments, net	(158,294)	537,340	144,377	372,490
Crude oil and natural gas service operations	8,679	7,790	30,176	24,071
Total revenues	483,729	968,989	1,883,548	1,535,671
Operating costs and expenses				
Production expenses	53,952	35,666	137,447	95,508
Production and other expenses to affiliates	1,454	793	3,950	2,582
Production taxes and other expenses	61,717	39,262	159,524	100,315
Exploration expenses	4,899	9,814	17,752	21,660
Crude oil and natural gas service operations	7,626	6,198	24,723	19,713
Depreciation, depletion, amortization and accretion	189,374	105,085	499,847	264,236
Property impairments	27,375	26,225	93,153	66,315
General and administrative expenses	31,925	18,140	86,704	51,696
(Gain) loss on sale of assets, net	(115)	188	(67,139)	(15,387)
Total operating costs and expenses	378,207	241,371	955,961	606,638
Income from operations	105,522	727,618	927,587	929,033
Other income (expense):				
Interest expense	(39,205)	(18,981)	(95,174)	(56,737)
Other	710	994	2,280	2,525
	(38,495)	(17,987)	(92,894)	(54,212)
Income before income taxes	67,027	709,631	834,693	874,821
Provision for income taxes	22,931	270,488	315,819	333,685
Net income	\$ 44,096	\$ 439,143	\$ 518,874	\$ 541,136
Basic net income per share	\$ 0.24	\$ 2.45	\$ 2.88	\$ 3.06
Diluted net income per share	\$ 0.24	\$ 2.44	\$ 2.86	\$ 3.05

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

Table of Contents**Continental Resources, Inc. and Subsidiaries****Condensed Consolidated Statements of Shareholders Equity**

	Shares outstanding	Common stock	Additional paid-in capital	Retained earnings	Total shareholders equity
	<i>In thousands, except share data</i>				
Balance at December 31, 2011	180,871,688	\$ 1,809	\$ 1,110,694	\$ 1,195,623	\$ 2,308,126
Net income (unaudited)				518,874	518,874
Common stock issued in exchange for assets (unaudited)	3,916,157	39	82,857		82,896
Stock-based compensation (unaudited)			21,123		21,123
Stock options:					
Exercised (unaudited)	86,500		60		60
Repurchased and canceled (unaudited)	(32,984)		(2,951)		(2,951)
Restricted stock:					
Issued (unaudited)	279,763	3			3
Repurchased and canceled (unaudited)	(37,592)		(2,760)		(2,760)
Forfeited (unaudited)	(26,133)				
Balance at September 30, 2012	185,057,399	\$ 1,851	\$ 1,209,023	\$ 1,714,497	\$ 2,925,371

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

Table of Contents**Continental Resources, Inc. and Subsidiaries****Unaudited Condensed Consolidated Statements of Cash Flows**

	Nine months ended September 30,	
	2012	2011
	<i>In thousands</i>	
Cash flows from operating activities		
Net income	\$ 518,874	\$ 541,136
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation, depletion, amortization and accretion	500,359	266,281
Property impairments	93,153	66,315
Change in fair value of derivatives	(192,752)	(403,471)
Stock-based compensation	20,804	11,742
Provision for deferred income taxes	323,543	324,354
Dry hole costs	319	3,758
Gain on sale of assets, net	(67,139)	(15,387)
Other, net	3,604	2,800
Changes in assets and liabilities:		
Accounts receivable	(112,316)	(177,627)
Inventories	(6,285)	(23,543)
Prepaid expenses and other	(5,080)	(18,937)
Accounts payable trade	(26,918)	21,206
Revenues and royalties payable	49,499	55,893
Accrued liabilities and other	48,240	17,012
Other noncurrent assets and liabilities	(8)	(1,718)
Net cash provided by operating activities	1,147,897	669,814
Cash flows from investing activities		
Exploration and development	(2,584,434)	(1,245,688)
Purchase of producing crude oil and natural gas properties	(62,519)	(2,771)
Purchase of other property and equipment	(45,472)	(37,449)
Proceeds from sale of assets	101,298	22,769
Net cash used in investing activities	(2,591,127)	(1,263,139)
Cash flows from financing activities		
Revolving credit facility borrowings	1,524,000	135,000
Repayment of revolving credit facility	(1,882,000)	(165,000)
Proceeds from issuance of Senior Notes	1,999,000	
Proceeds from issuance of common stock		659,736
Proceeds from other debt	22,000	
Repayment of other debt	(1,101)	
Debt issuance costs	(7,117)	(37)
Equity issuance costs		(368)
Repurchase of equity grants	(5,711)	(1,656)
Exercise of stock options	60	9
Net cash provided by financing activities	1,649,131	627,684
Net change in cash and cash equivalents	205,901	34,359
Cash and cash equivalents at beginning of period	53,544	7,916
Cash and cash equivalents at end of period	\$ 259,445	\$ 42,275

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

Table of Contents**Continental Resources, Inc. and Subsidiaries****Notes to Unaudited Condensed Consolidated Financial Statements****Note 1. Organization and Nature of Business***Description of the Company*

Continental's principal business is crude oil and natural gas exploration, development and production with operations in the North, South, and East regions of the United States. The North region consists of properties north of Kansas and west of the Mississippi river and includes North Dakota Bakken, Montana Bakken, and the Red River units. The South region includes Kansas and all properties south of Kansas and west of the Mississippi river including the South Central Oklahoma Oil Province (SCOOP), Northwest Cana, and Arkoma Woodford plays in Oklahoma. The SCOOP and Northwest Cana plays were previously combined by the Company and referred to as the Anadarko Woodford play. The East region primarily includes properties east of the Mississippi river including the Illinois Basin and the state of Michigan. The Company's operations are geographically concentrated in the North region, with that region comprising approximately 76% of the Company's crude oil and natural gas production for the nine months ended September 30, 2012. The Company has focused its operations on the exploration and development of crude oil since the 1980s. For the nine months ended September 30, 2012, crude oil accounted for approximately 70% of the Company's crude oil and natural gas production and approximately 89% of its crude oil and natural gas revenues.

Note 2. Basis of Presentation and Significant Accounting Policies*Basis of presentation*

The condensed consolidated financial statements include the accounts of Continental and its wholly owned subsidiaries after all significant inter-company accounts and transactions have been eliminated.

This report has been prepared pursuant to the rules and regulations of the Securities and Exchange Commission (the SEC) applicable to interim financial information. Because this is an interim period filing presented using a condensed format, it does not include all disclosures required by accounting principles generally accepted in the United States (U.S. GAAP), although the Company believes the disclosures are adequate to make the information not misleading. You should read this Form 10-Q together with the Company's Annual Report on Form 10-K for the year ended December 31, 2011 (2011 Form 10-K), which includes a summary of the Company's significant accounting policies and other disclosures.

The condensed consolidated financial statements as of September 30, 2012 and for the three and nine month periods ended September 30, 2012 and 2011 are unaudited. The condensed consolidated balance sheet as of December 31, 2011 was derived from the audited balance sheet included in the 2011 Form 10-K. The Company has evaluated events or transactions through the date this report on Form 10-Q was filed with the SEC in conjunction with its preparation of these condensed consolidated financial statements.

The preparation of financial statements in conformity with U.S. GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, the disclosure of contingent 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. The most significant of the estimates and assumptions that affect reported results are the estimates of the Company's crude oil and natural gas reserves, which are used to compute depreciation, depletion, amortization and impairment of proved crude oil and natural gas properties. In the opinion of management, all adjustments (consisting only of normal recurring adjustments) necessary for a fair presentation in accordance with U.S. GAAP have been included in these unaudited interim condensed consolidated financial statements. The results of operations for any interim period are not necessarily indicative of the results of operations that may be expected for any other interim period or for the entire year.

Inventories

Inventories are stated at the lower of cost or market and consist of the following:

In thousands	September 30, 2012	December 31, 2011
Tubular goods and equipment	\$ 18,377	\$ 15,665
Crude oil	28,919	25,605

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Total	\$	47,296	\$	41,270
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Crude oil inventories are valued at the lower of cost or market using the first-in, first-out inventory method. Crude oil inventories consist of the following volumes:

Table of Contents**Continental Resources, Inc. and Subsidiaries****Notes to Unaudited Condensed Consolidated Financial Statements**

<i>MBbl</i>	September 30, 2012	December 31, 2011
Crude oil line fill requirements	396	283
Temporarily stored crude oil	84	152
Total	480	435

Earnings per share

Basic net income per share is computed by dividing net income by the weighted-average number of shares outstanding for the period. Diluted net income per share reflects the potential dilution of non-vested restricted stock awards and stock options, which are calculated using the treasury stock method as if the awards and options were exercised. The following table presents the calculation of basic and diluted weighted average shares outstanding and net income per share for the three and nine months ended September 30, 2012 and 2011:

	Three months ended September 30,		Nine months ended September 30,	
	2012	2011	2012	2011
	<i>In thousands, except per share data</i>			
Income (numerator):				
Net income - basic and diluted	\$ 44,096	\$ 439,143	\$ 518,874	\$ 541,136
Weighted average shares (denominator):				
Weighted average shares - basic	181,909	179,458	180,471	176,899
Non-vested restricted stock	628	696	624	705
Stock options		91	21	97
Weighted average shares - diluted	182,537	180,245	181,116	177,701
Net income per share:				
Basic	\$ 0.24	\$ 2.45	\$ 2.88	\$ 3.06
Diluted	\$ 0.24	\$ 2.44	\$ 2.86	\$ 3.05

Note 3. Supplemental Cash Flow Information

The following table discloses supplemental cash flow information about cash paid for interest and income taxes. Also disclosed is information about investing activities that affects recognized assets and liabilities but does not result in cash receipts or payments.

	Nine months ended September 30,	
	2012	2011
	<i>In thousands</i>	
Supplemental cash flow information:		
Cash paid for interest	\$ 67,638	\$ 69,658
Cash paid for income taxes	759	10,485
Cash received for income tax refunds	(72)	(116)
Non-cash investing activities:		
Increase in accrued capital expenditures	4,521	117,825
Acquisition of assets through issuance of common stock	176,563	
Asset retirement obligations, net	4,910	1,691

Note 4. Derivative Instruments

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The Company is required to recognize all derivative instruments on the balance sheet as either assets or liabilities measured at fair value. The Company has not designated its derivative instruments as hedges for accounting purposes and, as a result, marks its derivative instruments to fair value and recognizes the realized and unrealized changes in fair value in the unaudited condensed consolidated statements of income under the caption Gain (loss) on derivative instruments, net.

The Company has utilized swap and collar derivative contracts to hedge against the variability in cash flows associated with the forecasted sale of future crude oil and natural gas production. While the use of these derivative instruments limits the downside risk of adverse price movements, their use also limits future revenues from upward price movements.

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Continental Resources, Inc. and Subsidiaries

Notes to Unaudited Condensed Consolidated Financial Statements

During the nine months ended September 30, 2012, the Company entered into several new swap derivative contracts covering a portion of its forecasted crude oil and natural gas production for 2012, 2013 and 2014. The new contracts were entered into in the ordinary course of business and the Company may enter into additional similar contracts in the future. None of the new contracts have been designated for hedge accounting.

With respect to a fixed price swap contract, the counterparty is required to make a payment to the Company if the settlement price for any settlement period is less than the swap price, and the Company is required to make a payment to the counterparty if the settlement price for any settlement period is greater than the swap price. For a collar contract, the counterparty is required to make a payment to the Company if the settlement price for any settlement period is below the floor price, the Company is required to make a payment to the counterparty if the settlement price for any settlement period is above the ceiling price, and neither party is required to make a payment to the other party if the settlement price for any settlement period is between the floor price and the ceiling price.