CHESAPEAKE UTILITIES CORP
Form 10-Q
November 09, 2018
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UNITED STATES
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: September 30, 2018
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: 001-11590

CHESAPEAKE UTILITIES CORPORATION
(Exact name of registrant as specified in its charter)

Delaware	51-0064146
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)

909 Silver Lake Boulevard, Dover, Delaware 19904
(Address of principal executive offices, including Zip Code)
(302) 734-6799
(Registrant’s telephone number, including area code)
Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15 (d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes x No ¨

Indicate by check mark whether the registrant has submitted electronically every Interactive Data File required to be submitted 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 such files). Yes x No ¨
Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, a smaller reporting company, or an emerging growth company. See definitions of “large accelerated filer,” “accelerated filer,” “smaller reporting company,” and "emerging growth company" in Rule 12b-2 of the Exchange Act.
Large accelerated filer x Accelerated filer ¨

Non-accelerated filer	¨	Smaller reporting company	¨
		Emerging growth company	¨

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If an emerging growth company, indicate by check mark if the registrant has elected not to use the extended transition period for complying with any new or revised financial accounting standards provided pursuant to Section 13(a) of the Exchange Act.
¨

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

Common Stock, par value $0.4867 — 16,378,545 shares outstanding as of October 31, 2018.

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GLOSSARY OF DEFINITIONS

ARM: ARM Energy Management, LLC, a natural gas supply and supply management company servicing commercial and industrial customers in Western Pennsylvania, which sold certain natural gas marketing assets to PESCO in August 2017

ASC: Accounting Standards Codification issued by the FASB

Aspire Energy: Aspire Energy of Ohio, LLC, a wholly-owned subsidiary of Chesapeake Utilities

ASU: Accounting Standards Update issued by the FASB

AutoGas: Alliance AutoGas, a national consortium of companies, of which Sharp is a member, providing an industry-leading complete program for fleets interested in shifting from gasoline to clean-burning propane

CDD: Cooling degree-day, which is a measure of the variation in weather based on the extent to which the daily average temperature (from 10:00 am to 10:00 am) is above 65 degrees Fahrenheit

Central Gas: Central Gas Company of Okeechobee, Incorporated, a propane distribution provider in Southeast Florida, which sold certain assets to Flo-gas in December 2017

CGC: Consumer Gas Cooperative, an Ohio natural gas cooperative

CGS: Community Gas Systems

Chesapeake or Chesapeake Utilities: Chesapeake Utilities Corporation, and its direct and indirect subsidiaries, as appropriate in the context of the disclosure

Chesapeake Pension Plan: A defined benefit pension plan sponsored by Chesapeake Utilities

Chesapeake Postretirement Plan: An unfunded postretirement health care and life insurance plan sponsored by Chesapeake Utilities

Chesapeake SERP: An unfunded supplemental executive retirement pension plan sponsored by Chesapeake Utilities

Chipola: Chipola Propane Gas Company, Inc., a propane distribution service provider in Northwest Florida, which sold certain assets to Flo-gas in August 2017

CHP: Combined heat and power plant

Columbia Gas: Columbia Gas of Ohio, an unaffiliated local distribution company based in Ohio

Company: Chesapeake Utilities Corporation, and its direct and indirect subsidiaries, as appropriate in the context of the disclosure

CP: Certificate of Public Convenience and Necessity

Credit Agreement: The Credit Agreement dated October 8, 2015, among Chesapeake Utilities and the Lenders related to the Revolver

Deferred Compensation Plan: A non-qualified, deferred compensation arrangement under which certain of our executives and members of the Board of Directors are able to defer payment of all or a part of certain specified types of compensation, including executive salaries and cash bonuses, executive performance shares, and directors' retainers

Degree-Day: A degree-day is the measure of the variation in the weather based on the extent to which the average daily temperature (from 10:00 am to 10:00 am) falls above or below 65 degrees Fahrenheit

Delaware Division: Chesapeake Utilities' natural gas distribution operation serving customers in Delaware

Del-Mar Energy Pathway Project - A project for the construction of pipeline looping in Kent County, Delaware, and additional mainline extension in Sussex County, Delaware. The project also upgrades an existing pressure control facility, which includes a portion of mainline extension in Sussex County, Delaware, as well as in Somerset County, Maryland.

Delmarva Peninsula: A peninsula on the east coast of the United States of America occupied by Delaware and portions of Maryland and Virginia

DNREC: Delaware Department of Natural Resources and Environmental Control
Dt(s): Dekatherm(s), which is a natural gas unit of measurement that includes a standard measure for heating value
Dts/d: Dekatherms per day
Eastern Shore: Eastern Shore Natural Gas Company, a wholly-owned natural gas transmission subsidiary of Chesapeake Utilities
EGWIC: Eastern Gas & Water Investment Company, LLC, an affiliate of ESG
Eight Flags: Eight Flags Energy, LLC, a subsidiary of Chesapeake OnSight Services, LLC, which owns and operates a CHP plant on Amelia Island, Florida, that supplies electricity to FPU and industrial steam to Rayonier
EPA: United States Environmental Protection Agency
ESG: Eastern Shore Gas Company and its affiliates
FASB: Financial Accounting Standards Board
FDEP: Florida Department of Environmental Protection
FERC: Federal Energy Regulatory Commission, an independent agency of the United States government that regulates the interstate transmission of electricity, natural gas, and oil
FGT: Florida Gas Transmission Company
Flo-gas: Flo-gas Corporation, a wholly-owned subsidiary of FPU
FPL: Florida Power & Light Company, an unaffiliated electric company that supplies electricity to FPU
FPU: Florida Public Utilities Company, a wholly-owned subsidiary of Chesapeake Utilities
FPU Medical Plan: A separate unfunded postretirement medical plan for FPU sponsored by Chesapeake Utilities
FPU Pension Plan: A separate defined benefit pension plan for FPU sponsored by Chesapeake Utilities
GAAP: Accounting principles generally accepted in the United States of America
GRIP: The Gas Reliability Infrastructure Program, a natural gas pipeline replacement program in Florida pursuant to which we collect a surcharge from certain of our customers to recover capital and other program-related costs associated with the replacement of qualifying distribution mains and services
Gulf Power: Gulf Power Company, an unaffiliated electric company that supplies electricity to FPU
Gulfstream: Gulfstream Natural Gas System, LLC, an unaffiliated pipeline network that supplies natural gas to FPU
HDD: Heating degree-day, which is a measure of the variation in weather based on the extent to which the daily average temperature (from 10:00 am to 10:00 am) is below 65 degrees Fahrenheit
Lenders: PNC, Bank of America N.A., Citizens Bank N.A., Royal Bank of Canada, and Wells Fargo Bank, National Association, which are collectively the lenders that entered into the Credit Agreement with Chesapeake Utilities
MDE: Maryland Department of Environment
MetLife: MetLife Investment Advisors, an institutional debt investment management firm, with which we entered into the MetLife Shelf Agreement
MetLife Shelf Agreement: An agreement entered into by Chesapeake Utilities and MetLife in March 2017 pursuant to which Chesapeake Utilities may request that MetLife purchase, through March 2, 2020, up to $150.0 million of unsecured senior debt at a fixed interest rate and with a maturity date not to exceed 20 years from the date of issuance
MetLife Shelf Notes: Unsecured senior promissory notes issuable under the MetLife Shelf Agreement
MGP: Manufactured gas plant, which is a site where coal was previously used to manufacture gaseous fuel for industrial, commercial and residential use

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MTM: Fair value (mark-to-market) accounting required for derivatives in accordance with ASC 815, Derivatives and Hedging
NOPR: Notice of Proposed Rulemaking
NYL: New York Life Investors LLC, an institutional debt investment management firm, with which we entered into the NYL Shelf Agreement
NYL Shelf Agreement: An agreement entered into by Chesapeake Utilities and NYL in March 2017 pursuant to which Chesapeake Utilities may request that NYL purchase, through March 2, 2020, up to $100.0 million of unsecured senior debt at a fixed interest rate and with a maturity date not to exceed 20 years from the date of issuance
NYL Shelf Notes: Unsecured senior promissory notes issuable under the NYL Shelf Agreement
OPT Service: Off Peak ≤ 30 or ≤ 90 Firm Transportation Service, a tariff associated with Eastern Shore's firm transportation service that allows Eastern Shore to not schedule service for up to 30 or 90 days during the peak months of November through April each year
OTC: Over-the-counter
Peninsula Pipeline: Peninsula Pipeline Company, Inc., Chesapeake Utilities' wholly-owned Florida intrastate pipeline subsidiary
PESCO: Peninsula Energy Services Company, Inc., Chesapeake Utilities' wholly-owned natural gas marketing subsidiary
PNC: PNC Bank, National Association, the administrative agent and primary lender for our Revolver
Prudential: PGIM, Inc., formerly known as Prudential Investment Management Inc., an institutional investment management firm, with which we have entered into the Prudential Shelf Agreement
Prudential Shelf Agreement: An agreement entered into by Chesapeake Utilities and Prudential in October 2015 pursuant to which Chesapeake Utilities could request that Prudential purchase, through October 7, 2018, up to $150.0 million of Prudential Shelf Notes at a fixed interest rate and with a maturity date not to exceed 20 years from the date of issuance, as subsequently amended in September 2018, pursuant to which we may request that Prudential purchase up to $150.0 million of our unsecured debt over a three-year period, expiring in August 2021
Prudential Shelf Notes: Unsecured senior promissory notes issuable under the Prudential Shelf Agreement
PSC: Public Service Commission, which is the state agency that regulates the rates and services provided by Chesapeake Utilities’ natural gas and electric distribution operations in Delaware, Maryland and Florida and Peninsula Pipeline in Florida
Rayonier: Rayonier Performance Fibers, LLC, the company that owns the property on which Eight Flags' CHP plant is located, and a customer of the steam generated by the CHP plant
Retirement Savings Plan: A qualified 401(k) retirement savings plan sponsored by Chesapeake Utilities
Revolver: Our unsecured revolving credit facility with the Lenders
ROU: Right of use
Sandpiper: Sandpiper Energy, Inc., Chesapeake Utilities' wholly-owned subsidiary, which provides a tariff-based distribution service to customers in Worcester County, Maryland
Sanford Group: FPU and other responsible parties involved with the Sanford MGP site
SEC: U.S. Securities and Exchange Commission
Senior Notes: Our unsecured long-term debt issued primarily to insurance companies on various dates
Sharp: Sharp Energy, Inc., Chesapeake Utilities' wholly-owned propane distribution subsidiary
SICP: Chesapeake Utilities' 2013 Stock and Incentive Compensation Plan
TCJA: The Tax Cuts and Jobs Act of 2017, which is legislation passed by Congress and signed into law by the President on December 22, 2017, and which, among other things, reduced the corporate income tax rate from 35 percent to 21 percent, effective January 1, 2018

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TETLP: Texas Eastern Transmission, LP, an interstate pipeline interconnected with Eastern Shore's pipeline
Xeron: Xeron, Inc., an inactive subsidiary of Chesapeake Utilities, which previously engaged in propane and crude oil trading

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PART I—FINANCIAL INFORMATION
Item 1. Financial Statements
Chesapeake Utilities Corporation and Subsidiaries
Condensed Consolidated Statements of Income (Unaudited)

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2018	2017	2018	2017
(in thousands, except shares and per share data)				
Operating Revenues				
Regulated Energy	$72,770	$ 69,703	$252,667	$238,353
Unregulated Energy and other	67,509	57,233	263,632	198,827
Total Operating Revenues	140,279	126,936	516,299	437,180
Operating Expenses				
Regulated Energy cost of sales	21,501	22,794	89,741	87,206
Unregulated Energy and other cost of sales	55,660	44,066	204,880	145,325
Operations	32,821	29,274	101,804	91,778
Maintenance	3,208	2,737	10,419	9,370
Gain from a settlement	—	—	(130)	(130)
Depreciation and amortization	10,633	9,362	30,176	27,267
Other taxes	4,420	4,071	13,719	12,572
Total Operating Expenses	128,243	112,304	450,609	373,388
Operating Income	12,036	14,632	65,690	63,792
Other expense, net	(11)	(154)	(204)	(1,855)
Interest charges	4,430	3,321	11,976	9,133
Income Before Income Taxes	7,595	11,157	53,510	52,804
Income taxes	2,057	4,324	14,731	20,781
Net Income	$5,538	$ 6,833	$38,779	$32,023
Weighted Average Common Shares Outstanding:				
Basic	16,378,545	16,344,442	16,366,608	16,334,210
Diluted	16,428,439	16,389,635	16,416,255	16,378,633
Earnings Per Share of Common Stock:				
Basic	$0.34	$ 0.42	$2.37	$1.96
Diluted	$0.34	$ 0.42	$2.36	$1.96
Cash Dividends Declared Per Share of Common Stock	$0.3700	$ 0.3250	$1.0650	$0.9550

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

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Chesapeake Utilities Corporation and Subsidiaries
Condensed Consolidated Statements of Comprehensive Income (Unaudited)

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2018	2017	2018	2017
(in thousands)				
Net Income	$5,538	$6,833	$38,779	$32,023
Other Comprehensive Income (Loss), net of tax:				
Employee Benefits, net of tax:				
Amortization of prior service cost, net of tax of $(5), $(8), $(16) and $(23), respectively	(14)	(11)	(42)	(35)
Net gain, net of tax of $38, $69, $118 and $212, respectively	100	102	317	297
Cash Flow Hedges, net of tax:				
Unrealized gain (loss) on commodity contract cash flow hedges, net of tax of $257, $(15), $(70) and $(376), respectively	644	(104)	(83)	(643)
Total Other Comprehensive Income (Loss), net of tax	730	(13)	192	(381)
Comprehensive Income	$6,268	$6,820	$38,971	$31,642

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

Chesapeake Utilities Corporation and Subsidiaries
Condensed Consolidated Balance Sheets (Unaudited)

Assets	September 30, 2018	December 31, 2017
(in thousands, except shares and per share data)		
Property, Plant and Equipment		
Regulated Energy	$ 1,242,840	$ 1,073,736
Unregulated Energy	220,721	210,682
Other businesses and eliminations	34,975	27,699
Total property, plant and equipment	1,498,536	1,312,117
Less: Accumulated depreciation and amortization	(295,449)	(270,599)
Plus: Construction work in progress	60,243	84,509
Net property, plant and equipment	1,263,330	1,126,027
Current Assets		
Cash and cash equivalents	6,215	5,614
Trade and other receivables (less allowance for uncollectible accounts of $987 and $936, respectively)	52,660	77,223
Accrued revenue	12,352	22,279
Propane inventory, at average cost	7,444	8,324
Other inventory, at average cost	4,786	12,022
Regulatory assets	6,891	10,930
Storage gas prepayments	6,989	5,250
Income taxes receivable	8,725	14,778
Prepaid expenses	9,775	13,621
Derivative assets, at fair value	10,568	1,286
Other current assets	2,557	7,260
Total current assets	128,962	178,587
Deferred Charges and Other Assets		
Goodwill	19,604	19,604
Other intangible assets, net	4,073	4,686
Investments, at fair value	7,951	6,756
Regulatory assets	76,343	75,575
Other assets	5,293	3,699
Total deferred charges and other assets	113,264	110,320
Total Assets	$ 1,505,556	$ 1,414,934

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

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Chesapeake Utilities Corporation and Subsidiaries
Condensed Consolidated Balance Sheets (Unaudited)

Capitalization and Liabilities	September 30, 2018	December 31, 2017
(in thousands, except shares and per share data)		
Capitalization		
Stockholders' equity		
Preferred stock, par value $0.01 per share (authorized 2,000,000 shares), no shares issued and outstanding	$ —	$ —
Common stock, par value $0.4867 per share (authorized 50,000,000 shares)	7,971	7,955
Additional paid-in capital	255,509	253,470
Retained earnings	249,805	229,141
Accumulated other comprehensive loss	(4,987)	(4,272)
Deferred compensation obligation	3,818	3,395
Treasury stock	(3,818)	(3,395)
Total stockholders' equity	508,298	486,294
Long-term debt, net of current maturities	241,597	197,395
Total capitalization	749,895	683,689
Current Liabilities		
Current portion of long-term debt	9,613	9,421
Short-term borrowing	268,293	250,969
Accounts payable	60,228	74,688
Customer deposits and refunds	34,887	34,751
Accrued interest	3,969	1,742
Dividends payable	6,060	5,312
Accrued compensation	10,396	13,112
Regulatory liabilities	9,099	6,485
Derivative liabilities, at fair value	9,774	6,247
Other accrued liabilities	14,819	10,273
Total current liabilities	427,138	413,000
Deferred Credits and Other Liabilities		
Deferred income taxes	146,814	135,850
Regulatory liabilities	141,840	140,978
Environmental liabilities	7,941	8,263
Other pension and benefit costs	28,839	29,699
Deferred investment tax credits and other liabilities	3,089	3,455
Total deferred credits and other liabilities	328,523	318,245
Environmental and other commitments and contingencies (Notes 5 and 6)		
Total Capitalization and Liabilities	$ 1,505,556	$ 1,414,934

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

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Chesapeake Utilities Corporation and Subsidiaries
Condensed Consolidated Statements of Cash Flows (Unaudited)

	Nine Months Ended September 30,	
(in thousands)	2018	2017
Operating Activities		
Net income	$38,779	$32,023
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	30,176	27,267
Depreciation and accretion included in other costs	6,464	5,989
Deferred income taxes	11,047	29,520
Realized loss (gain) on commodity contracts/sale of assets/investments	4,015	(2,817)
Unrealized gain on investments/commodity contracts	(427)	(695)
Employee benefits and compensation	456	1,212
Share-based compensation	2,535	1,608
Other, net	(35)	(39)
Changes in assets and liabilities:		
Accounts receivable and accrued revenue	32,988	12,912
Propane inventory, storage gas and other inventory	6,379	(8,256)
Regulatory assets/liabilities, net	3,899	927
Prepaid expenses and other current assets	(1,533)	(2,860)
Accounts payable and other accrued liabilities	(9,590)	4,515
Income taxes receivable	6,053	(3,810)
Customer deposits and refunds	136	3,255
Accrued compensation	(2,804)	(2,030)
Other assets and liabilities, net	(542)	(349)
Net cash provided by operating activities	127,996	98,372
Investing Activities		
Property, plant and equipment expenditures	(171,410)	(130,137)
Proceeds from sales of assets	565	601
Acquisitions, net of cash acquired	—	(11,707)
Environmental expenditures	(322)	(210)
Net cash used in investing activities	(171,167)	(141,453)
Financing Activities		
Common stock dividends	(16,171)	(14,780)
(Purchase) issuance of stock under the Dividend Reinvestment Plan	(518)	254
Stock issuance	—	(10)
Tax withholding payments related to net settled stock compensation	(1,210)	(692)
Change in cash overdrafts due to outstanding checks	712	(3,013)
Net borrowing (repayment) under line of credit agreements and short-term borrowing under the Revolver	16,612	(3,760)
Proceeds from long-term debt and long-term borrowing under the Revolver	74,901	69,800
Repayment of long-term debt, long-term borrowing under the Revolver and capital lease obligation	(30,554)	(5,510)
Net cash provided in financing activities	43,772	42,289
Net Increase (Decrease) in Cash and Cash Equivalents	601	(792)
Cash and Cash Equivalents—Beginning of Period	5,614	4,178

Cash and Cash Equivalents—End of Period	$6,215	$3,386

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

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Chesapeake Utilities Corporation and Subsidiaries
Condensed Consolidated Statements of Stockholders' Equity (Unaudited)

	Common Stock [1]							
(in thousands, except shares and per share data)	Number of Shares[2]	Par Value	Additional Paid-In Capital	Retained Earnings	Accumulated Other Comprehensive Loss	Deferred Compensation	Treasury Stock	Total
Balance at December 31, 2016	16,303,499	$7,935	$250,967	$192,062	$ (4,878)	$ 2,416	$(2,416)	$446,086
Net income	—	—	—	58,124	—	—	—	58,124
Other comprehensive income	—	—	—	—	606	—	—	606
Dividend declared ($1.28 per share)	—	—	—	(21,045)	—	—	—	(21,045)
Dividend reinvestment plan	10,771	5	730	—	—	—	—	735
Stock issuance	—	—	(10)	—	—	—	—	(10)
Share-based compensation and tax benefit [3][4]	30,172	15	1,783	—	—	—	—	1,798
Treasury stock activities	—	—	—	—	—	979	(979)	—
Balance at December 31, 2017	16,344,442	7,955	253,470	229,141	(4,272)	3,395	(3,395)	486,294
Net income	—	—	—	38,779	—	—	—	38,779
Cumulative effect of the adoption of ASU 2014-09	—	—	—	(1,498)	—	—	—	(1,498)
Reclassification upon the adoption of ASU 2018-02	—	—	—	907	(907)	—	—	—
Other comprehensive income	—	—	—	—	192	—	—	192
Dividend declared ($1.065 per share)	—	—	—	(17,524)	—	—	—	(17,524)
Dividend reinvestment plan	—	—	(2)	—	—	—	—	(2)
Share-based compensation and tax benefit [3] [4]	34,103	16	2,041	—	—	—	—	2,057
Treasury stock activities	—	—	—	—	—	423	(423)	—
Balance at September 30, 2018	16,378,545	$7,971	$255,509	$249,805	$ (4,987)	$ 3,818	$(3,818)	$508,298

(1) 2,000,000 shares of preferred stock at $0.01 par value have been authorized. None has been issued or is outstanding; accordingly, no information has been included in the statements of stockholders' equity.

(2) Includes 96,622 and 90,961 shares at September 30, 2018 and December 31, 2017, respectively, held in a Rabbi Trust related to our Deferred Compensation Plan.

(3) Includes amounts for shares issued for directors' compensation.

(4) The shares issued under the SICP are net of shares withheld for employee taxes. For the nine months ended September 30, 2018, and for the year ended December 31, 2017, we withheld 16,918 and 10,269 shares, respectively, for taxes.

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

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NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

1. Summary of Accounting Policies

Basis of Presentation

References in this document to the “Company,” “Chesapeake Utilities,” “we,” “us” and “our” are intended to mean Chesapeake Utilities Corporation, its divisions and/or its subsidiaries, as appropriate in the context of the disclosure.

The accompanying unaudited condensed consolidated financial statements have been prepared in compliance with the rules and regulations of the SEC and GAAP. In accordance with these rules and regulations, certain information and disclosures normally required for audited financial statements have been condensed or omitted. These financial statements should be read in conjunction with the consolidated financial statements and notes thereto, included in our latest Annual Report on Form 10-K for the year ended December 31, 2017. In the opinion of management, these financial statements reflect normal recurring adjustments that are necessary for a fair presentation of our results of operations, financial position and cash flows for the interim periods presented.

Due to the seasonality of our business, results for interim periods are not necessarily indicative of results for the entire fiscal year. Revenue and earnings are typically greater during the first and fourth quarters, when consumption of energy is highest due to colder temperatures.

ARM, Chipola and Central Gas Asset Acquisitions

In August 2017, PESCO acquired certain natural gas marketing assets of ARM. The acquired assets complemented PESCO’s existing asset portfolio and expanded our regional footprint and retail demand in a market where we had existing pipeline capacity and wholesale liquidity. We accounted for the purchase of these assets as a business combination and initially recorded goodwill of $6.8 million within our Unregulated Energy segment. In connection with the acquisition, we initially recorded a contingent consideration liability of $2.5 million, based on our preliminary analysis projecting that the acquired business would achieve at least a certain gross margin target in 2018. During the second quarter of 2018, we identified certain known information as of the acquisition date that was not considered in our original analysis and would have resulted in no contingent consideration liability being initially recorded. Therefore, we reversed the originally-recorded contingent liability and reduced goodwill by $2.5 million. We similarly revised the condensed consolidated balance sheet as of December 31, 2017. These revisions are considered immaterial to our condensed consolidated financial statements. The need for a contingent consideration liability will be re-evaluated in the final reporting period in 2018. However, our current assessment is that no contingent consideration will be paid.

In August 2017, Flo-gas acquired certain operating assets of Chipola, which provided propane distribution service to approximately 800 residential and commercial customers in Bay, Calhoun, Gadsden, Jackson, Liberty, and Washington Counties, Florida.

In December 2017, Flo-gas acquired certain operating assets of Central Gas, which provides propane distribution service to approximately 325 residential and commercial customers in Glades, Highlands, Martin, Okeechobee, and St. Lucie Counties, Florida.

The revenue and net income from these acquisitions, which were included in our condensed consolidated statements of income for the three and nine months ended September 30, 2018, were not material. The acquisition accounting amounts recorded in conjunction with the ARM and Chipola acquisitions are now final although the amounts associated with the Central Gas acquisition are preliminary and subject to adjustment based on additional valuations performed during the measurement period.

FASB Statements and Other Authoritative Pronouncements

Recently Adopted Accounting Standards

Revenue from Contracts with Customers (ASC 606) - On January 1, 2018, we adopted ASU 2014-09, Revenue from Contracts with Customers, and all the related amendments using the modified retrospective method. We recognized the cumulative effect of initially applying the new revenue standard to all of our contracts as an adjustment to the beginning balance of retained earnings. The comparative information has not been restated and continues to be reported under the accounting standards in effect for those periods. The impact of adoption of the new revenue standard was immaterial to our net income.

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This standard requires entities to recognize revenue when control of the promised goods or services is transferred to customers at an amount that reflects the consideration that the entity expects to receive in exchange for those goods or services. The guidance also requires a number of disclosures regarding the nature, amount, timing, and uncertainty of revenue and the related cash flows. See Note 3, Revenue Recognition, for additional information.

The following highlights the impact of the adoption of ASC 606 on our condensed consolidated income statements for the three and nine months ended September 30, 2018 and condensed consolidated balance sheet as of September 30, 2018:

Income statement	Three Months Ended September 30, 2018			Nine Months Ended September 30, 2018		
	As Reported	Without Adoption of ASC 606	Effect of Change Higher (Lower)	As Reported	Without Adoption of ASC 606	Effect of Change Higher (Lower)
(in thousands)						
Regulated Energy operating revenues	$72,770	$72,879	$(109)	$252,667	$253,659	$(992)
Regulated Energy cost of sales	21,501	21,512	(11)	89,741	90,454	(713)
Depreciation and amortization	10,633	10,629	4	30,176	30,150	26
Income before income taxes	7,595	7,697	(102)	53,510	53,815	(305)
Income taxes	2,057	2,086	(29)	14,731	14,819	(88)
Net income	5,538	5,611	(73)	38,779	38,996	(217)

Balance sheet	As of September 30, 2018		
	As Reported	Without Adoption of ASC 606	Effect of Change Higher (Lower)
(in thousands)			
Assets			
Accrued revenues	$12,352	$13,658	$(1,306)
Other assets	$5,293	$5,702	$(409)
Capitalization			
Retained earnings	$249,805	$251,520	$(1,715)

The primary impact of the adoption of ASC 606 on our income statement was the delayed recognition of approximately $305,000 in revenue in the first nine months of 2018 to future years and a cumulative adjustment that decreased retained earnings and other assets by $1.7 million at September 30, 2018, associated with a long-term firm transmission contract with an industrial customer.

Compensation-Retirement Benefits (ASC 715) - In March 2017, the FASB issued ASU 2017-07, Improving the Presentation of Net Periodic Pension Cost and Net Periodic Post Retirement Benefit Cost. Under this guidance, employers are required to report the service cost component in the same line item or items as other compensation costs arising from services rendered by the pertinent employees during the period. The other components of net benefit costs are required to be presented in the income statement separately from the service cost component and should not be included operating expenses. The update allows for capitalization of the service cost component when applicable. We adopted ASU 2017-07 on January 1, 2018 and applied the changes in the presentation of the service cost and other components of net benefit costs, retrospectively. Aside from changes in presentation, implementation of this standard did not have a material impact on our financial position or results of operations.

Statement of Cash Flows (ASC 230) - In August 2016, the FASB issued ASU 2016-15, Classification of Certain Cash Receipts and Cash Payments, which clarifies how certain transactions are classified in the statement of cash flows. We adopted ASU 2016-15 on January 1, 2018. Implementation of this new standard did not have a material impact on our condensed consolidated statement of cash flows.

Compensation - Stock Compensation (ASC 718) - In May 2017, the FASB issued ASU 2017-09, Scope of Modification Accounting, to clarify when to account for a change in the terms or conditions of a share-based payment award as a modification. Under this guidance, modification accounting is required only if the fair value, the vesting conditions or the award classification (equity or liability) change because of a change in the terms or conditions of the award. We adopted

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ASU 2017-09, prospectively, on January 1, 2018. Implementation of this new standard did not have a material impact on our financial position or results of operations.

Income Statement - Reporting Comprehensive Income (ASC 220) - In February 2018, the FASB issued ASU 2018-02, Reclassification of Certain Tax Effects from Accumulated Other Comprehensive Income, which allows a reclassification from accumulated other comprehensive income to retained earnings for stranded tax effects resulting from the TCJA. We adopted ASU 2018-02 on January 1, 2018, and reclassified stranded tax effects from accumulated other comprehensive loss related to our employee benefit plans and commodity contract cash flows hedges. Implementation of this new standard did not have a material impact on our financial position and results of operations. See Note 8, Stockholders' Equity, for additional information.

Derivatives and Hedging (ASC 815) - In August 2017, the FASB issued ASU 2017-12, Targeted Improvements to Accounting for Hedging Activities, to better align an entity’s risk management activities and financial reporting for hedging relationships through changes to both the designation and measurement guidance for qualifying hedging relationships and the presentation of hedge results. ASU 2017-12 expands the risks that can be designated as hedged risks in cash flow hedges to include cash flow variability from contractually specified components of forecasted purchases or sales of non-financial assets. ASU 2017-12 requires the entire change in fair value of a hedging instrument that is included in the assessment of hedge effectiveness to be presented in the same income statement line that is used to present the earnings effects of the hedged item for fair value hedges and in other comprehensive income for cash flow hedges. ASU 2017-12 requires a tabular presentation of the income statement effect of fair value and cash flow hedges and eliminates the requirement to disclose the ineffective portion of the change in fair value of hedging instruments. ASU 2017-12 will be effective for our annual and interim financial statements beginning January 1, 2019, although early adoption is permitted. We adopted ASU 2017-12 effective July 1, 2018, with no material impact on our financial statements. See Note 12, Derivative Instruments, for additional information with respect to the disclosures required by ASU 2017-12.

Recent Accounting Standards Yet to be Adopted

Leases (ASC 842) - In February 2016, the FASB issued ASU 2016-02, Leases, which requires lessees to recognize leases on the balance sheet and disclose key information about leasing arrangements. The standard establishes a ROU model that requires a lessee to recognize a ROU asset and lease liability for all leases with a term greater than 12 months. The update also expands the required quantitative and qualitative disclosures surrounding leases. ASC 842 was subsequently amended by ASU No. 2018-01, Land Easement Practical Expedient for Transition to Topic 842; ASU No. 2018-10, Codification Improvements to Topic 842, Leases; and ASU No. 2018-11, Targeted Improvements. ASU 2016-02 will be effective for our annual and interim financial statements, beginning January 1, 2019, although early adoption is permitted. We expect to adopt ASU 2016-02 effective January 1, 2019 and use the modified retrospective transition approach to all existing leases.

The new standard permits companies to elect several practical expedients. We expect to elect: (1) the ‘package of practical expedients,’ pursuant to which we do not need to reassess our prior conclusions about lease identification, lease classification and initial direct costs and (2) the ‘use-of-hindsight’ practical expedient, which allows us to use hindsight in assessing impairment of our existing land easements. We also intend to aggregate all non-lease components with the lease components to which they relate.

The most significant effect of ASC 842 will be recognition of ROU assets and lease liabilities on our balance sheet for our operating leases and providing significant new disclosures about our leasing activities. We currently expect that upon adoption, we will recognize lease liabilities ranging from $4.0 million to $5.0 million, with corresponding ROU of the same amount based on the present value of the remaining minimum rental payments for existing operating leases.

Intangibles-Goodwill (ASC 350) - In January 2017, the FASB issued ASU 2017-04, Simplifying the Test for Goodwill Impairment, which simplifies how an entity is required to test goodwill for impairment by eliminating Step 2 from the goodwill impairment test. ASU 2017-04 will be effective for our annual and interim financial statements beginning January 1, 2020, although early adoption is permitted. The amendments included in this ASU are to be applied prospectively. We believe that implementation of this new standard will not have a material impact on our

financial position or results of operations.
Compensation - Stock Compensation (ASC 718) - In June 2018, the FASB issued ASU 2018-07, Improvements to Nonemployee Share-Based Payment Accounting, which expands the scope of Topic 718 to include share-based payment transactions for acquiring goods and services from nonemployees. ASU 2018-07 will be effective for our annual and interim financial statements beginning January 1, 2019, although early adoption is permitted. We believe that implementation of this new standard will not have a material impact on our financial position or results of operations.

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Fair Value Measurement (ASC 820) - In August 2018, the FASB issued ASU 2018-13, Disclosure Framework - Changes to the Disclosure Requirements for Fair Value Measurement, which removes, modifies and adds certain disclosure requirements on fair value measurements in ASC 820. ASU 2018-13 will be effective for our annual and interim financial statements beginning January 1, 2020 and, since the changes only impact disclosures, will not have a material impact on our financial position or results of operations.
Compensation - Retirement Benefits - Defined Benefit Plans - General (ASC 715-20) - In August 2018, the FASB issued ASU 2018-14, Disclosure Framework - Changes to the Disclosure Requirements for Defined Benefit Plans, which removes, clarifies and adds certain disclosure requirements in ASC 715-20 related to defined benefit pension and other postretirement plans. ASU 2018-14 will be effective for our annual and interim financial statements, on a retrospective basis, beginning January 1, 2021 and, since the changes only impact disclosures, will not have a material impact on our financial position or results of operations.

2. Calculation of Earnings Per Share

	Three Months Ended		Nine Months Ended	
	September 30,		September 30,	
	2018	2017	2018	2017
(in thousands, except shares and per share data)				
Calculation of Basic Earnings Per Share:				
Net Income	$5,538	$ 6,833	$38,779	$ 32,023
Weighted average shares outstanding	16,378,545	16,344,442	16,366,608	16,334,210
Basic Earnings Per Share	$0.34	$ 0.42	$2.37	$ 1.96
Calculation of Diluted Earnings Per Share:				
Reconciliation of Numerator:				
Net Income	$5,538	$ 6,833	$38,779	$ 32,023
Reconciliation of Denominator:				
Weighted shares outstanding—Basic	16,378,545	16,344,442	16,366,608	16,334,210
Effect of dilutive securities—Share-based compensation	49,894	45,193	49,647	44,423
Adjusted denominator—Diluted	16,428,439	16,389,635	16,416,255	16,378,633
Diluted Earnings Per Share	$0.34	$ 0.42	$2.36	$ 1.96

3. Revenue Recognition

We recognize revenue when our performance obligations under contracts with customers have been satisfied, which generally occurs when our businesses have delivered or transported natural gas, electricity or propane to customers. We exclude sales taxes and other similar taxes from the transaction price. Typically, our customers pay for the goods and/or services we provide in the month following the satisfaction of our performance obligation.

The following table displays our revenue by major source based on product and service type for the three months ended September 30, 2018:

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(in thousands)	Regulated Energy	Unregulated Energy	Other and Eliminations	Total
Energy distribution				
Florida natural gas division	$ 6,282	$ —	$ —	$6,282
Delaware natural gas division	7,010	—	—	7,010
FPU electric distribution	23,830	—	—	