SANDRIDGE ENERGY INC
Form 10-Q
August 08, 2011

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

Form 10-Q

(Mark One)

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

For the quarterly period ended June 30, 2011

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: 001-33784

SANDRIDGE ENERGY, INC.

(Exact name of registrant as specified in its charter)

Delaware	**20-8084793**
(State or other jurisdiction of incorporation or organization)	**(I.R.S. Employer Identification No.)**
123 Robert S. Kerr Avenue Oklahoma City, Oklahoma	**73102**
(Address of principal executive offices)	**(Zip Code)**

Registrant s telephone number, including area code:

(405) 429-5500

Former name, former address and former fiscal year, if changed since last report: Not applicable

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 þ No ¨

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate website, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes þ 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	þ	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 þ

The number of shares outstanding of the registrant s common stock, par value $0.001 per share, as of the close of business on July 29, 2011, was 412,428,752.

SANDRIDGE ENERGY, INC.

FORM 10-Q

Quarter Ended June 30, 2011

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PART I. FINANCIAL INFORMATION

PART II. OTHER INFORMATION

DISCLOSURES REGARDING FORWARD-LOOKING STATEMENTS

This Quarterly Report on Form 10-Q (Quarterly Report) includes forward-looking statements within the meaning of Section 27A of the Securities Act of 1933, as amended (the Securities Act), and Section 21E of the Securities Exchange Act of 1934, as amended (the Exchange Act). These statements express a belief, expectation or intention and generally are accompanied by words that convey projected future events or outcomes. These forward-looking statements may include projections and estimates concerning capital expenditures, our liquidity and capital resources, the timing and success of specific projects, outcomes and effects of litigation, claims and disputes, elements of our business strategy and other statements concerning our operations, economic performance and financial condition. Forward-looking statements are generally accompanied by words such as estimate, project, predict, believe, expect, anticipate, potential, could, may, foresee, plan, other words that convey the uncertainty of future events or outcomes. We have based these forward-looking statements on our current expectations and assumptions about future events. These statements are based on certain assumptions and analyses made by us in light of our experience and our perception of historical trends, current conditions and expected future developments as well as other factors we believe are appropriate under the circumstances. However, whether actual results and developments will conform with our expectations and predictions is subject to a number of risks and uncertainties, including the risk factors discussed in Item 1A of Part II of this Quarterly Report and in Item 1A of our Annual Report on Form 10-K for the fiscal year ended December 31, 2010 (the 2010 Form 10-K). The actual results or developments anticipated may not be realized or, even if substantially realized, they may not have the expected consequences to or effects on our company, business or operations. Such statements are not guarantees of future performance and actual results or developments may differ materially from those projected in such forward-looking statements. We undertake no obligation to publicly update or revise any forward-looking statements.

PART I. Financial Information

ITEM 1. ***Financial Statements***

SANDRIDGE ENERGY, INC. AND SUBSIDIARIES

CONDENSED CONSOLIDATED BALANCE SHEETS

(In thousands, except per share data)

	June 30, 2011 (Unaudited)	December 31, 2010
ASSETS		
Current assets		
Cash and cash equivalents	$ 4,615	$ 5,863
Accounts receivable, net	162,976	146,118
Derivative contracts	2,513	5,028
Inventories	7,571	3,945
Other current assets	12,897	14,636
Total current assets	190,572	175,590
Oil and natural gas properties, using full cost method of accounting		
Proved	8,552,148	8,159,924
Unproved	624,668	547,953
Less: accumulated depreciation, depletion and impairment	(4,625,330)	(4,483,736)
	4,551,486	4,224,141
Other property, plant and equipment, net	519,364	509,724
Restricted deposits	27,902	27,886
Goodwill	235,396	234,356
Other assets	71,954	59,751
Total assets	$ 5,596,674	$ 5,231,448
LIABILITIES AND EQUITY		
Current liabilities		
Current maturities of long-term debt	$ 1,019	$ 7,293
Accounts payable and accrued expenses	423,971	376,922
Billings and estimated contract loss in excess of costs incurred	41,232	31,474
Derivative contracts	149,374	103,409
Asset retirement obligation	25,360	25,360
Total current liabilities	640,956	544,458
Long-term debt	2,892,434	2,901,793
Derivative contracts	162,057	124,173
Asset retirement obligation	93,780	94,517
Other long-term obligations	10,762	19,024
Total liabilities	3,799,989	3,683,965
Commitments and contingencies (Note 15)		
Equity		
SandRidge Energy, Inc. stockholders equity		
Preferred stock, $0.001 par value, 50,000 shares authorized		

8.5% Convertible perpetual preferred stock; 2,650 shares issued and outstanding at June 30, 2011 and December 31, 2010; aggregate liquidation preference of $265,000	3	3
6.0% Convertible perpetual preferred stock; 2,000 shares issued and outstanding at June 30, 2011 and December 31, 2010; aggregate liquidation preference of $200,000	2	2
7.0% Convertible perpetual preferred stock; 3,000 shares issued and outstanding at June 30, 2011 and December 31, 2010; aggregate liquidation preference of $300,000	3	3
Common stock, $0.001 par value, 800,000 shares authorized; 410,498 issued and 409,918 outstanding at June 30, 2011 and 406,830 issued and 406,360 outstanding at December 31, 2010	398	398
Additional paid-in capital	4,550,689	4,528,912
Treasury stock, at cost	(4,525)	(3,547)
Accumulated deficit	(3,109,725)	(2,989,576)
Total SandRidge Energy, Inc. stockholders equity	1,436,845	1,536,195
Noncontrolling interest	359,840	11,288
Total equity	1,796,685	1,547,483
Total liabilities and equity	$ 5,596,674	$ 5,231,448

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

SANDRIDGE ENERGY, INC. AND SUBSIDIARIES

CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS

(In thousands, except per share data)

	Three Months Ended June 30, 2011	Three Months Ended June 30, 2010	Six Months Ended June 30, 2011	Six Months Ended June 30, 2010
	(Unaudited)			
Revenues				
Oil and natural gas	$ 312,111	$ 149,995	$ 579,053	$ 319,580
Drilling and services	28,537	3,901	49,571	9,661
Midstream and marketing	16,313	22,598	38,570	50,587
Other	7,813	5,945	10,427	13,606
Total revenues	364,774	182,439	677,621	393,434
Expenses				
Production	81,834	56,009	155,791	106,281
Production taxes	12,666	5,404	23,242	10,242
Drilling and services	18,058	1,024	33,099	8,233
Midstream and marketing	15,873	19,779	38,156	45,285
Depreciation and depletion oil and natural gas	76,186	54,319	150,072	106,597
Depreciation and amortization other	13,275	11,820	26,368	24,123
General and administrative	37,678	33,865	72,091	65,539
(Gain) loss on derivative contracts	(169,988)	(119,621)	107,640	(181,573)
(Gain) loss on sale of assets	(524)	388	(725)	84
Total expenses	85,058	62,987	605,734	184,811
Income from operations	279,716	119,452	71,887	208,623
Other income (expense)				
Interest income	38	98	43	167
Interest expense	(61,725)	(64,259)	(121,167)	(126,348)
Loss on extinguishment of debt	(2,051)		(38,232)	
Other income (expense), net	138	(530)	1,335	706
Total other expense	(63,600)	(64,691)	(158,021)	(125,475)
Income (loss) before income taxes	216,116	54,761	(86,134)	83,148
Income tax (benefit) expense	(7,054)	150	(6,967)	162
Net income (loss)	223,170	54,611	(79,167)	82,986
Less: net income attributable to noncontrolling interest	13,154	1,096	13,161	2,234
Net income (loss) attributable to SandRidge Energy, Inc.	210,016	53,515	(92,328)	80,752
Preferred stock dividends	13,881	8,631	27,821	17,263
Income available (loss applicable) to SandRidge Energy, Inc. common stockholders	$ 196,135	$ 44,884	$ (120,149)	$ 63,489
Earnings (loss) per share				
Basic	$ 0.49	$ 0.22	$ (0.30)	$ 0.31

Diluted	$ 0.42	$ 0.21	$ (0.30)	$ 0.31
Weighted average number of common shares outstanding				
Basic	398,435	203,839	398,343	203,831
Diluted	495,982	259,566	398,343	226,406

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

SANDRIDGE ENERGY, INC. AND SUBSIDIARIES

CONDENSED CONSOLIDATED STATEMENT OF CHANGES IN EQUITY

(In thousands)

	SandRidge Energy, Inc. Stockholders								
	Convertible Perpetual Preferred Stock		Common Stock		Additional Paid-In Capital	Treasury Stock	Accumulated Deficit	Noncontrolling Interest	Total
	Shares	Amount	Shares	Amount					
	(Unaudited)								
Six months ended June 30, 2011									
Balance, December 31, 2010	7,650	$ 8	406,360	$ 398	$ 4,528,912	$ (3,547)	$ (2,989,576)	$ 11,288	$ 1,547,483
Issuance of units by SandRidge Mississippian Trust I								336,892	336,892
Distributions to noncontrolling interest owners								(1,501)	(1,501)
Stock issuance expense					(231)				(231)
Purchase of treasury stock						(4,984)			(4,984)
Retirement of treasury stock					(4,984)	4,984			
Stock purchases retirement plans, net of distributions			(110)		1,998	(978)			1,020
Stock-based compensation					24,987				24,987
Stock-based compensation excess tax benefit					7				7
Issuance of restricted stock awards, net of cancellations			3,668						
Net (loss) income							(92,328)	13,161	(79,167)
Convertible perpetual preferred stock dividends							(27,821)		(27,821)
Balance, June 30, 2011	7,650	$ 8	409,918	$ 398	$ 4,550,689	$ (4,525)	$ (3,109,725)	$ 359,840	$ 1,796,685

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

SANDRIDGE ENERGY, INC. AND SUBSIDIARIES

CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS

(In thousands)

	Six Months Ended June 30, 2011	Six Months Ended June 30, 2010
	(Unaudited)	
CASH FLOWS FROM OPERATING ACTIVITIES		
Net (loss) income	$ (79,167)	$ 82,986
Adjustments to reconcile net (loss) income to net cash provided by operating activities		
Provision for doubtful accounts	1,596	84
Inventory obsolescence	20	124
Depreciation, depletion and amortization	176,440	130,720
Debt issuance costs amortization	5,748	5,121
Discount amortization on long-term debt	1,162	1,049
Loss on extinguishment of debt	38,232	
Deferred income taxes	(6,986)	
Unrealized loss (gain) on derivative contracts	79,350	(12,776)
(Gain) loss on sale of assets	(725)	84
Investment (income) loss	(67)	261
Stock-based compensation	18,301	14,218
Changes in operating assets and liabilities	27,100	36,588
Net cash provided by operating activities	261,004	258,459
CASH FLOWS FROM INVESTING ACTIVITIES		
Capital expenditures for property, plant and equipment	(871,901)	(427,336)
Proceeds from sale of assets	369,251	6,042
Refunds of restricted deposits		5,095
Net cash used in investing activities	(502,650)	(416,199)
CASH FLOWS FROM FINANCING ACTIVITIES		
Proceeds from borrowings	1,725,000	841,914
Repayments of borrowings	(1,741,795)	(662,869)
Premium on debt redemption	(30,338)	
Debt issuance costs	(19,640)	(11,546)
Proceeds from issuance of units by SandRidge Mississippian Trust I	336,892	
Noncontrolling interest distributions	(1,501)	(1,506)
Noncontrolling interest contributions		157
Stock issuance expense	(231)	(87)
Stock-based compensation excess tax benefit	7	14
Purchase of treasury stock	(6,030)	(2,852)
Dividends paid preferred	(28,980)	(11,263)
Derivative settlements	7,014	
Net cash provided by financing activities	240,398	151,962
NET DECREASE IN CASH AND CASH EQUIVALENTS	(1,248)	(5,778)
CASH AND CASH EQUIVALENTS, beginning of year	5,863	7,861
CASH AND CASH EQUIVALENTS, end of period	$ 4,615	$ 2,083

Supplemental Disclosure of Noncash Investing and Financing Activities				
Change in accrued capital expenditures	$	2,351	$	50,209
Convertible perpetual preferred stock dividends payable	$	16,572	$	14,447
Adjustment to oil and natural gas properties for estimated contract loss	$	19,000	$	

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

SANDRIDGE ENERGY, INC. AND SUBSIDIARIES

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited)

1. Basis of Presentation

Nature of Business. SandRidge Energy, Inc. (including its subsidiaries, the Company or SandRidge) is an independent oil and natural gas company concentrating on development and production activities related to the exploitation of its significant holdings in West Texas and the Mid-Continent area of Oklahoma and Kansas. The Company s primary areas of focus are the Permian Basin in West Texas, the Mississippian formation in the Mid-Continent and the West Texas Overthrust (WTO). The Company owns and operates other interests in the Mid-Continent, Cotton Valley Trend in East Texas, Gulf Coast and Gulf of Mexico. The Company also operates businesses that are complementary to its primary development and production activities, including gas gathering and treating facilities, a gas marketing business, an oil field services business, including a drilling rig business, and tertiary oil recovery operations.

Interim Financial Statements. The accompanying condensed consolidated financial statements as of December 31, 2010 have been derived from the audited financial statements contained in the Company s 2010 Form 10-K. The unaudited interim condensed consolidated financial statements have been prepared by the Company in accordance with the accounting policies stated in the audited consolidated financial statements contained in the 2010 Form 10-K. Certain information and footnote disclosures normally included in financial statements prepared in accordance with accounting principles generally accepted in the United States of America (GAAP) have been condensed or omitted, although the Company believes that the disclosures contained herein are adequate to make the information presented not misleading. In the opinion of management, all adjustments, which consist only of normal recurring adjustments, necessary to state fairly the information in the Company s unaudited condensed consolidated financial statements have been included. These condensed consolidated financial statements should be read in conjunction with the financial statements and notes thereto included in the 2010 Form 10-K.

Risks and Uncertainties. The Company s revenue, profitability and future growth are substantially dependent upon the prevailing and future prices for oil and natural gas, each of which depends on numerous factors beyond the Company s control such as economic conditions, regulatory developments and competition from other energy sources. Oil and natural gas prices historically have been volatile, and may be subject to significant fluctuations in the future. The Company s derivative arrangements serve to mitigate a portion of the effect of this price volatility on the Company s cash flows, and while derivative contracts are in place for the majority of expected oil production for 2011 through 2013, fixed price swap contracts are in place for only a portion of expected natural gas production in 2011 and 2012 and oil production for 2014 and 2015. No fixed price swap contracts are in place for the Company s natural gas production beyond 2012 or oil production beyond 2015. The Company has natural gas collars in place for a portion of expected natural gas production through 2015. See Note 12 for the Company s open oil and natural gas commodity derivative contracts.

The Company has incurred, and will have to continue to incur, capital expenditures to achieve production targets contained in certain gathering and treating arrangements. The Company depends on the availability of borrowings under its senior secured revolving credit facility (the senior credit facility), along with cash flows from operating activities and the proceeds from planned asset sales or other asset monetizations, to fund those capital expenditures. Based on anticipated oil and natural gas prices, availability under the senior credit facility, potential access to the capital markets and anticipated proceeds from sales or other monetizations of assets, the Company expects to be able to fund its planned capital expenditures budget, debt service requirements and working capital needs for 2011. However, a substantial or extended decline in oil or natural gas prices could have a material adverse effect on the Company s financial position, results of operations, cash flows and quantities of oil and natural gas reserves that may be economically produced, which could adversely impact the Company s ability to comply with the financial covenants under its senior credit facility, which in turn would limit further borrowings to fund capital expenditures. See Note 11 for discussion of the financial covenants in the senior credit facility.

SANDRIDGE ENERGY, INC. AND SUBSIDIARIES

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

(Unaudited)

2. Recent Accounting Pronouncements

For a description of the Company s significant accounting policies, refer to Note 1 of the consolidated financial statements included in the 2010 Form 10-K.

Recently Adopted Accounting Pronouncements. In January 2010, the Financial Accounting Standards Board (the FASB) issued Accounting Standards Update 2010-06, Fair Value Measurements and Disclosures: Improving Disclosures about Fair Value Measurements (ASU 2010-06). ASU 2010-06 requires additional disclosures and clarifies existing disclosure requirements about fair value measurement as set forth in Accounting Standards Codification (ASC) Topic 820, Fair Value Measurements and Disclosures. The new disclosure requirements regarding activity in Level 3 fair value measurements, which are effective for fiscal years beginning after December 15, 2010, were implemented in the first quarter of 2011 by the Company. The implementation of ASU 2010-06 had no impact on the Company s financial position or results of operations. See Note 4.

Recent Accounting Pronouncement Not Yet Adopted. In May 2011, the FASB issued Accounting Standards Update 2011-04, Amendments to Achieve Common Fair Value Measurement and Disclosure Requirements in U.S. GAAP and IFRS (ASU 2011-04). ASU 2011-04 clarifies the FASB s intent about the application of existing fair value measurements as set forth in ASC Topic 820 and requires additional disclosure information regarding valuation processes and inputs used. The new disclosure requirements are effective for interim and annual reporting periods beginning after December 15, 2011. As the additional requirements under ASU 2011-04, which will be implemented January 1, 2012, pertain to fair value measurement disclosures, no effect to the Company s financial position or results of operations is expected.

3. Acquisitions and Divestitures

Arena Acquisition. On July 16, 2010, the Company acquired all of the outstanding common stock of Arena Resources, Inc. (Arena). In connection with the acquisition (the Arena Acquisition), the Company issued 4.7771 shares of its common stock and paid $4.50 in cash to Arena stockholders for each outstanding share of Arena unrestricted common stock. This resulted in the issuance of approximately 190.3 million shares of Company common stock and payment of approximately $177.9 million in cash for an aggregate estimated purchase price to stockholders of Arena equal to approximately $1.4 billion. The Company incurred approximately $0.2 million and $3.8 million in fees related to the acquisition during the three-month periods ended June 30, 2011 and 2010, respectively, and $0.6 million and $4.8 million in fees during the six-month periods ended June 30, 2011 and 2010, respectively, which have been included in general and administrative expenses in the accompanying condensed consolidated statements of operations.

In the second quarter of 2011, the Company completed its valuation of assets acquired and liabilities assumed related to the Arena Acquisition. Upon receipt of final confirmatory information for certain accruals in the second quarter of 2011 and completion of the 2010 Arena federal income tax return, the Company increased current assets, the net deferred tax liability and the value assigned to goodwill and reduced current liabilities. The accompanying condensed consolidated balance sheet at December 31, 2010 included certain preliminary allocations of the purchase price for the Arena Acquisition. During the first quarter of 2011, the Company updated certain estimates used in the purchase price allocation, primarily with respect to accruals, resulting in adjustments of $0.8 million to goodwill. Additional adjustments in the second quarter of 2011, primarily with respect to deferred taxes and other accruals, resulted in adjustments of $0.2 million to goodwill.

SANDRIDGE ENERGY, INC. AND SUBSIDIARIES

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

(Unaudited)

The following table summarizes the final valuation of assets acquired and liabilities assumed in connection with the Arena Acquisition (in thousands):

Current assets	$ 83,563
Oil and natural gas properties(1)	1,587,630
Other property, plant and equipment	5,963
Deferred tax assets	48,997
Other long-term assets	16,181
Goodwill(2)	235,396
Total assets acquired	1,977,730
Current liabilities	38,964
Long-term deferred tax liability(2)	503,483
Other long-term liabilities	8,851
Total liabilities assumed	551,298
Net assets acquired	$ 1,426,432

(1) Weighted average commodity prices utilized in the preliminary determination of the fair value of oil and natural gas properties were $105.58 per barrel of oil and $8.56 per Mcf of natural gas, after adjustment for transportation fees and regional price differentials. The prices utilized were based upon forward commodity strip prices, as of July 16, 2010, for the first four years and escalated for inflation at a rate of 2.5% annually beginning with the fifth year through the end of production, which was more than 50 years. Approximately 91.0% of the fair value allocated to oil and natural gas properties is attributed to oil reserves.

(2) The Company received carryover tax basis in Arena s assets and liabilities because the merger was not a taxable transaction under the Internal Revenue Code (IRC). Based upon the final purchase price allocation, a step-up in basis related to the property acquired from Arena resulted in a net deferred tax liability of approximately $454.5 million, which in turn contributed to an excess of the consideration transferred to acquire Arena over the estimated fair value on the acquisition date of the net assets acquired, or goodwill. See Note 6 for further discussion of goodwill and Note 13 for further discussion of the net deferred tax liability.

The following unaudited pro forma results of operations are provided for the three and six-month periods ended June 30, 2010 as though the Arena Acquisition had been completed as of the beginning of each respective period. The pro forma information is based on the Company s consolidated results of operations for the three and six-month periods ended June 30, 2010, Arena s historical results of operations and estimates of the effect of the transaction on the combined results. The pro forma combined results of operations for the three and six-month periods ended June 30, 2010 have been prepared by adjusting the historical results of the Company to include the historical results of Arena, certain reclassifications to conform Arena s presentation to the Company s accounting policies and the impact of the purchase price allocation. These supplemental pro forma results of operations are provided for illustrative purposes only and do not purport to be indicative of the actual results that would have been achieved by the combined company for the periods presented or that may be achieved by the combined company in the future. The pro forma results of operations do not include any cost savings or other synergies that resulted from the acquisition or any estimated costs that have been incurred by the Company to integrate Arena. Future results may vary significantly from the results reflected in this pro forma financial information because of future events and transactions, as well as other factors.

SANDRIDGE ENERGY, INC. AND SUBSIDIARIES

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

(Unaudited)

	Three Months Ended June 30, 2010		Six Months Ended June 30, 2010	
	Actual	Pro Forma	Actual	Pro Forma
	(in thousands, except per share data)			
Revenues	$ 182,439	$ 236,751	$ 393,434	$ 499,544
Income available to SandRidge Energy, Inc. common stockholders(1)	$ 44,884	$ 503,597	$ 63,489	$ 536,985
Earnings per common share				
Basic	$ 0.22	$ 1.28	$ 0.31	$ 1.36
Diluted	$ 0.21	$ 1.14	$ 0.31	$ 1.23

(1) Pro forma columns reflect a $454.5 million reduction in tax expense related to the release of a portion of the Company s valuation allowance on existing deferred tax assets.

Sale of Wolfberry Assets. In January 2011, the Company sold its Wolfberry assets in the Permian Basin for $153.8 million, net of fees and subject to post-closing adjustments. This asset sale was accounted for as an adjustment to the full cost pool with no gain or loss recognized.

Sale of New Mexico Assets. In April 2011, the Company sold certain oil and natural gas properties in Lea County and Eddy County, New Mexico, for approximately $198.5 million, net of fees and subject to post-closing adjustments. This asset sale was accounted for as an adjustment to the full cost pool with no gain or loss recognized.

4. Fair Value Measurements

The Company applies the guidance provided under ASC Topic 820 to its financial assets and liabilities and nonfinancial liabilities that are measured and reported on a fair value basis. Pursuant to this guidance, the Company has classified and disclosed its fair value measurements using the following levels of the fair value hierarchy:

Level 1: Unadjusted quoted prices in active markets that are accessible at the measurement date for identical, unrestricted assets or liabilities.

Level 2: Quoted prices in markets that are not active, or inputs which are observable, either directly or indirectly, for substantially the full term of the asset or liability.

Level 3: Measurement based on prices or valuation models that require inputs that are both significant to the fair value measurement and less observable for objective sources (*i.e.*, supported by little or no market activity).

Assets and liabilities that are measured at fair value are classified based on the lowest level of input that is significant to the fair value measurement. The Company s assessment of the significance of a particular input to the fair value measurement requires judgment, which may affect the valuation of the fair value of assets and liabilities and their placement within the fair value hierarchy levels as described in ASC Topic 820. The determination of the fair values, stated below, takes into account the market for the Company s financial assets and liabilities, the associated credit risk and other factors as required by ASC Topic 820. The Company considers active markets as those in which transactions for the assets or liabilities occur in sufficient frequency and volume to provide pricing information on an ongoing basis. The Company has assets and liabilities it has classified as Level 1 and Level 3, as described below. The Company did not have any assets or liabilities classified as Level 2 at June 30, 2011 or December 31, 2010.

SANDRIDGE ENERGY, INC. AND SUBSIDIARIES

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

(Unaudited)

Level 1 Fair Value Measurements

Restricted deposits. The fair value of restricted deposits invested in mutual funds or municipal bonds is based on quoted market prices. For restricted deposits held in savings accounts, carrying value is deemed to approximate fair value.

Other long-term assets. The fair value of other long-term assets, consisting of assets attributable to the Company s deferred compensation plan, is based on quoted market prices.

Level 3 Fair Value Measurements

Derivative Contracts. The fair values of the Company s oil and natural gas fixed price swaps, natural gas basis swaps, natural gas collars and interest rate swap are based upon quotes obtained from counterparties to the derivative contracts. The Company reviews other readily available market prices for its derivative contracts as there is an active market for these contracts. However, the Company does not have access to the specific valuation models used by its counterparties or other market participants. Included in these models are discount factors that the Company must estimate in its calculation. Additionally, the Company applies a weighted average credit default risk rating factor for its counterparties or gives effect to its credit risk, as applicable, in determining the fair value of its derivative contracts. Based on the inputs for the fair value measurement, the Company has classified its derivative contract assets and liabilities as Level 3.

The following tables summarize the Company s financial assets and liabilities measured at fair value on a recurring basis by the fair value hierarchy (in thousands):

June 30, 2011

	Fair Value Measurements				Assets /
	Level 1	**Level 2**	**Level 3**	**Netting(1)**	**Liabilities at Fair Value**
Assets					
Restricted deposits	$ 27,902	$	$	$	$ 27,902
Other long-term assets	4,908				4,908
Commodity derivative contracts			12,246	(9,733)	2,513
	$ 32,810	$	$ 12,246	$ (9,733)	$ 35,323
Liabilities					
Commodity derivative contracts	$	$	$ 305,879	$ (9,733)	$ 296,146
Interest rate swap			15,285		15,285
	$	$	$ 321,164	$ (9,733)	$ 311,431

December 31, 2010

	Fair Value Measurements				Assets /
	Level 1	**Level 2**	**Level 3**	**Netting(1)**	**Liabilities at Fair Value**

Assets					
Restricted deposits	$ 27,886	$	$	$	$ 27,886
Other long-term assets	4,826				4,826
Commodity derivative contracts			10,576	(5,548)	5,028
	$ 32,712	$	$ 10,576	$ (5,548)	$ 37,740
Liabilities					
Commodity derivative contracts	$	$	$ 216,436	$ (5,548)	$ 210,888
Interest rate swaps			16,694		16,694
	$	$	$ 233,130	$ (5,548)	$ 227,582

SANDRIDGE ENERGY, INC. AND SUBSIDIARIES

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

(Unaudited)

(1) Represents the impact of netting assets and liabilities with counterparties with which the right of offset exists.

The tables below set forth a reconciliation of the Company s financial assets and liabilities measured at fair value on a recurring basis using significant unobservable inputs (Level 3) during the three and six-month periods ended June 30, 2011 and 2010 (in thousands):

	Three Months Ended June 30,					
	2011			2010		
	Commodity Derivative Contracts	Interest Rate Swaps	Total	Commodity Derivative Contracts	Interest Rate Swaps	Total
Balance of Level 3, March 31	$ (478,541)	$ (14,929)	$ (493,470)	$ 65,512	$ (12,147)	$ 53,365
Total realized and unrealized gains (losses)	169,988	(2,798)	167,190	119,621	(6,477)	113,144
Purchases	(3,353)		(3,353)			
Settlements	18,273	2,442	20,715	(117,955)	2,076	(115,879)
Balance of Level 3, June 30	$ (293,633)	$ (15,285)	$ (308,918)	$ 67,178	$ (16,548)	$ 50,630

	Six Months Ended June 30,					
	2011			2010		
	Commodity Derivative Contracts	Interest Rate Swaps	Total	Commodity Derivative Contracts	Interest Rate Swaps	Total
Balance of Level 3, December 31	$ (205,860)	$ (16,694)	$ (222,554)	$ 46,153	$ (8,299)	$ 37,854
Total realized and unrealized (losses) gains	(107,640)	(3,076)	(110,716)	181,573	(12,412)	169,161
Purchases	(7,014)		(7,014)			
Settlements	26,881	4,485	31,366	(160,548)	4,163	(156,385)
Balance of Level 3, June 30	$ (293,633)	$ (15,285)	$ (308,918)	$ 67,178	$ (16,548)	$ 50,630

During the three and six-month periods ended June 30, 2011 and 2010, the Company did not have any transfers between Level 1, Level 2 or Level 3 fair value measurements.

See Note 12 for further discussion of the Company s derivative contracts.

Fair Value of Debt

The Company measures the fair value of its long-term debt based on quoted market prices and also considers the effect of the Company s credit risk. The estimated fair values of the Company s senior notes and the carrying value at June 30, 2011 and December 31, 2010 were as follows (in thousands):

	June 30, 2011	December 31, 2010

	Fair Value	Carrying Value	Fair Value	Carrying Value
Senior Floating Rate Notes due 2014	$ 349,127	$ 350,000	$ 334,751	$ 350,000
8.625% Senior Notes due 2015			663,181	650,000
9.875% Senior Notes due 2016(1)	406,146	353,619	394,527	352,707
8.0% Senior Notes due 2018	763,636	750,000	762,849	750,000
8.75% Senior Notes due 2020(2)	479,767	443,307	472,968	443,057
7.5% Senior Notes due 2021	909,203	900,000		

SANDRIDGE ENERGY, INC. AND SUBSIDIARIES

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

(Unaudited)

(1) Carrying value is net of $11,881 and $12,793 discount at June 30, 2011 and December 31, 2010, respectively.
(2) Carrying value is net of $6,693 and $6,943 discount at June 30, 2011 and December 31, 2010, respectively.

The carrying values of the Company s senior credit facility and remaining fixed rate debt instruments approximate fair value based on current rates applicable to similar instruments. See Note 11 for discussion of the Company s long-term debt, including the purchase and redemption of all outstanding 8.625% Senior Notes due 2015 and the issuance of the 7.5% Senior Notes due 2021, which both occurred during 2011.

5. Property, Plant and Equipment

Property, plant and equipment consists of the following (in thousands):

	June 30, 2011	December 31, 2010
Oil and natural gas properties		
Proved	$ 8,552,148	$ 8,159,924
Unproved	624,668	547,953
Total oil and natural gas properties	9,176,816	8,707,877
Less: accumulated depreciation, depletion and impairment	(4,625,330)	(4,483,736)
Net oil and natural gas properties capitalized costs	4,551,486	4,224,141
Land	14,192	14,418
Non oil and natural gas equipment(1)	674,211	666,233
Buildings and structures	106,711	89,813
Total	795,114	770,464
Less: accumulated depreciation and amortization	(275,750)	(260,740)
Net capitalized costs	519,364	509,724
Total property, plant and equipment, net	$ 5,070,850	$ 4,733,865

(1) Includes capitalized interest of approximately $5.2 million and $4.7 million at June 30, 2011 and December 31, 2010, respectively.

There were no full cost ceiling impairments during the three or six-month periods ended June 30, 2011 or 2010. Cumulative full cost ceiling limitation impairment charges of $3,548.3 million at both June 30, 2011 and December 31, 2010 were included in accumulated depreciation, depletion and impairment for oil and natural gas properties in the table above.

6. Goodwill

At June 30, 2011, the Company had $235.4 million of goodwill, including the effects of the $0.8 million and $0.2 million purchase price adjustments recorded in the first and second quarters of 2011, respectively, as a result of the excess consideration over the fair value of net assets acquired in the Arena Acquisition. Goodwill recorded in the Arena Acquisition is primarily attributable to operational and cost synergies expected to be realized from the acquisition by using the Company s current presence in the Permian Basin, its Fort Stockton, Texas service base and its existing rig ownership to efficiently increase its drilling and oil production from Arena assets

SANDRIDGE ENERGY, INC. AND SUBSIDIARIES

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

(Unaudited)

acquired in the Central Basin Platform, as these assets have a proven production history. See Note 3 for additional discussion of the Arena Acquisition. The Company assigned all of the goodwill related to the Arena Acquisition to its exploration and production segment, which will be the reporting unit for impairment testing purposes. The Company will test goodwill for impairment annually on July 1, beginning in 2011. The Company monitors the existence of potential impairment indicators throughout the year. As of June 30, 2011, no such indicators were noted. Goodwill recognized is not deductible for tax purposes.

7. Other Assets

Other assets consist of the following (in thousands):

	June 30, 2011	December 31, 2010
Debt issuance costs, net of amortization	$ 56,662	$ 50,637
Investments	4,908	4,826
Other	10,384	4,288
Total other assets	$ 71,954	$ 59,751

8. Variable Interest Entities

In accordance with the guidance in ASC Topic 810, Consolidation, including the guidance in Accounting Standards Update 2009-17, Consolidations Improvements to Financial Reporting by Enterprises Involved with Variable Interest Entities (ASU 2009-17), the Company consolidates the activities of variable interest entities (VIEs) of which it is the primary beneficiary. The primary beneficiary of a VIE is that variable interest holder possessing a controlling financial interest through (i) its power to direct the activities of the VIE that most significantly impact the VIE s economic performance and (ii) its obligation to absorb losses or its right to receive benefits from the VIE that could potentially be significant to the VIE. In order to determine whether the Company owns a variable interest in a VIE, the Company performs a qualitative analysis of the entity s design, organizational structure, primary decision makers and related financial agreements.

The Company s significant associated VIEs, including those for which the Company has determined it is the primary beneficiary and those for which it has determined it is not, are described below.

SandRidge Mississippian Trust I. On April 12, 2011, SandRidge Mississippian Trust I (the Mississippian Trust), a newly formed Delaware statutory trust, completed its initial public offering of 17,250,000 common units representing beneficial interests in the Mississippian Trust. Net proceeds to the Mississippian Trust, after certain offering expenses, were approximately $336.9 million. In conjunction with the closing, the Company conveyed certain royalty interests to the Mississippian Trust in exchange for the net proceeds of the Mississippian Trust s initial public offering and 10,750,000 units (3,750,000 common units and 7,000,000 subordinated units) representing approximately 38.4% of the beneficial interest in the Mississippian Trust. The royalty interests conveyed to the Mississippian Trust are in certain oil and natural gas properties leased by the Company in the Mississippian formation in five counties in Northern Oklahoma. The conveyance of the royalty interests to the Mississippian Trust was recorded in April 2011 at the historical cost to the Company, or $309.0 million, and was determined by allocating the historical net book value of the Company s full cost pool based on the fair value of the conveyed royalty interests relative to the fair value of the Company s total full cost pool.

In order to provide support for cash distributions on the Mississippian Trust s common units, SandRidge agreed to subordinate a portion of the Mississippian Trust units it owns (the subordinated units), which

SANDRIDGE ENERGY, INC. AND SUBSIDIARIES

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

(Unaudited)

constitute 25% of the total outstanding Mississippian Trust units. The subordinated units are entitled to receive pro rata distributions from the Mississippian Trust each quarter if and to the extent there is sufficient cash to provide a cash distribution on the common units that is no less than the applicable quarterly subordination threshold. If there is not sufficient cash to fund such a distribution on all common units, the distribution to be made with respect to the subordinated units will be reduced or eliminated for such quarter in order to make a distribution, to the extent possible, of up to the subordination threshold amount on all common units, including common units held by the Company.

SandRidge and one of its wholly owned subsidiaries entered into a development agreement with the Mississippian Trust that obligates the Company to drill, or cause to be drilled, a specified number of wells, which are also subject to the royalty interest, by December 31, 2014. In the event of delays, the Company will have until December 31, 2015 to fulfill its drilling obligation. At the end of the fourth full calendar quarter following satisfaction of the Company s drilling obligation (the subordination period), the Company s subordinated units will automatically convert into common units on a one-for-one basis and the Company s right to receive incentive distributions will terminate. Incentive distributions are equal to 50% of the amount by which the cash available for distribution on all of the Mississippian Trust units for any quarter is 20% or greater than the target distribution for such quarter. One of the Company s wholly owned subsidiaries also granted to the Mississippian Trust a lien in the Company s interests in the properties where the development wells will be drilled, in order to secure the estimated amount of the drilling costs for the wells. As the Company fulfills its drilling obligation, the total amount that may be recovered by the Mississippian Trust will be proportionately reduced and completed development wells will be released from the lien. As of June 30, 2011, the maximum amount recoverable by the Mississippian Trust under the lien was $136.4 million. Additionally, the Company and the Mississippian Trust entered into an administrative services agreement, pursuant to which the Company provides certain administrative services to the Mississippian Trust, and a derivatives agreement, pursuant to which the Company passes to the Mississippian Trust the benefits and obligations of certain of the Company s derivative contracts. The tables below present open oil and natural gas commodity derivative contracts at June 30, 2011, the benefits and obligations of which will be passed to the Mississippian Trust under the derivatives agreement. See Note 12 for further discussion of the derivatives agreement between the Company and the Mississippian Trust and a complete listing of the Company s open commodity derivative contracts at June 30, 2011, including the derivative contracts the effects of which have been conveyed to the Mississippian Trust.

Oil

Period and Type of Contract	Notional (MBbl)	Weighted Avg. Fixed Price
July 2011 December 2011		
Price swap contracts	241	$ 103.60
January 2012 December 2012		
Price swap contracts	454	$ 104.15
January 2013 December 2013		
Price swap contracts	488	$ 102.07
January 2014 December 2014		
Price swap contracts	541	$ 100.94
January 2015 December 2015		
Price swap contracts	468	$ 101.07

SANDRIDGE ENERGY, INC. AND SUBSIDIARIES

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

(Unaudited)

Natural Gas

Period and Type of Contract	Notional (MMcf)(1)	Weighted Avg. Fixed Price	Collar Range
July 2011 December 2011			
Price swap contracts	2,086	$ 4.61	
January 2012 June 2012			
Price swap contracts	2,190	$ 4.90	
July 2012 December 2012			
Collars	402		$ 4.00 - $6.20
January 2013 December 2013			
Collars	858		$ 4.00 - $7.15
January 2014 December 2014			
Collars	937		$ 4.00 - $7.78
January 2015 December 2015			
Collars	1,010		$ 4.00 - $8.55

(1) Assumes ratio of 1:1 for Mcf to MMBtu.

The Mississippian Trust is considered a VIE due to the lack of voting or similar decision-making rights by its equity holders regarding activities that have a significant effect on the success of the Mississippian Trust. The Company s ownership in the Mississippian Trust constitutes a variable interest. The Company has determined it is the primary beneficiary of the Mississippian Trust as it has (a) the power to direct the activities that most significantly impact the economic performance of the Mississippian Trust through (i) its participation in the creation and structure of the Mississippian Trust, (ii) the manner in which it fulfills its drilling obligation to the Mississippian Trust, and (iii) the manner in which it operates the Underlying Properties, and (b) through the end of the subordination period, the obligation to absorb losses and right to receive residual returns, through its ownership of the subordinated units, that could potentially be significant to the Mississippian Trust. As a result, the Company began consolidating the activities of the Mississippian Trust into its results of operations in April 2011. In consolidation, the common units of the Mississippian Trust owned by third parties are reflected as noncontrolling interest. As discussed above, the Company s subordinated Mississippian Trust units will automatically convert to common Mississippian Trust units at the end of the subordination period.

The Mississippian Trust s assets can be used to settle its own obligations and not other obligations of the Company. The Mississippian Trust s creditors have no contractual recourse to the general credit of the Company. Although the Mississippian Trust is included in the Company s consolidated financial statements, the Company s legal interest in the Mississippian Trust s assets is limited to its ownership of the Mississippian Trust units. At June 30, 2011, $350.2 million of noncontrolling interest in the accompanying condensed consolidated balance sheets was attributable to the Mississippian Trust. The Mississippian Trust s assets and liabilities included in the accompanying condensed consolidated balance sheet at June 30, 2011 consisted of the following (in thousands):

Current assets	$ 6,570
Investment in royalty interests, net(1)	304,656
Total assets	$ 311,226
Current liabilities	$ 651
Total liabilities	$ 651

SANDRIDGE ENERGY, INC. AND SUBSIDIARIES

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

(Unaudited)

(1) Included in oil and natural gas properties on the condensed consolidated balance sheet.

Grey Ranch, L.P. Primarily engaged in treating and transportation of natural gas, Grey Ranch Plant, L.P. (GRLP) is a limited partnership that operates the Company s Grey Ranch plant (the Plant) located in Pecos County, Texas. The Company has long-term operating and gathering agreements with GRLP and also owns a 50% interest in GRLP. Income or losses of GRLP are allocated to the partners based on ownership percentage and any operating or cash shortfalls require contributions from the partners. The Company has determined that GRLP qualifies as a VIE under the provisions of ASC Topic 810. Agreements related to the ownership and operation of GRLP provide for GRLP to pay management fees to the Company to operate the Plant and lease payments for the Plant. Under the operating agreements, lease payments are reduced if throughput volumes are below those expected. The Company has determined that it is the primary beneficiary of GRLP as it has both (i) the power to direct the activities of GRLP that most significantly impact its economic performance as operator of the Plant and (ii) the obligation to absorb losses, as a result of the operating and gathering agreements, that could potentially be significant to GRLP.

GRLP s assets can be used to settle its own obligations and not other obligations of the Company. GRLP s creditors have no recourse to the general credit of the Company. Although GRLP is included in the Company s consolidated financial statements, the Company s legal interest in GRLP s assets is limited to its 50% ownership. At June 30, 2011 and December 31, 2010, $9.6 million and $11.3 million, respectively, of noncontrolling interest in the accompanying condensed consolidated balance sheets were related to GRLP. GRLP s assets and liabilities included in the accompanying condensed consolidated balance sheets at June 30, 2011 and December 31, 2010 consisted of the following (in thousands):

	June 30, 2011	December 31, 2010
Current assets	$ 3,719	$ 8,215
Other property, plant and equipment, net	15,560	16,079
Total assets	$ 19,279	$ 24,294
Current liabilities	$ 318	$ 1,751
Total liabilities	$ 318	$ 1,751

Grey Ranch Plant Genpar, LLC. The Company owns a 50% interest in Grey Ranch Plant Genpar, LLC (Genpar), the managing partner and 1% owner of GRLP. Additionally, the Company serves as Genpar s administrative manager. Genpar s ownership interest in GRLP is its only asset.

As managing partner of GRLP, Genpar has the sole right to manage, control and conduct the business of GRLP. However, Genpar is restricted from making certain major decisions, including the decision to remove the Company as operator of the Plant. The rights afforded the Company under the Plant operating agreement and the restrictions on Genpar serve to limit Genpar s ability to make decisions on behalf of GRLP. Therefore, Genpar is considered a VIE. Although both the Company and Genpar s other equity owner share equally in Genpar s economic losses and benefits and also have agreements that may be considered variable interests, the Company determined it was the primary beneficiary due to (i) its ability, as administrative manager, to direct the activities of Genpar that most significantly impact its performance and (ii) its obligation or right, as operator of the Plant, to absorb the losses of or receive benefits from Genpar that could potentially be significant to Genpar. As the primary beneficiary, the Company consolidates Genpar s activity. However, its sole asset, the investment in GRLP, is eliminated in consolidation. Genpar has no liabilities.

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NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

(Unaudited)

Piñon Gathering Company, LLC. The Company has 20-year gas gathering and operations and maintenance agreements with Piñon Gathering Company, LLC (PGC). Under the gas gathering agreement, the Company is required to compensate PGC for any throughput shortfalls below a required minimum volume. By guaranteeing a minimum throughput, the Company absorbs the risk that lower than projected volumes will be gathered by the gathering system. Therefore, PGC is a VIE. While the Company operates the assets of PGC as directed under the operations and management agreement, the member and managers of PGC have the authority to directly control PGC and make substantive decisions regarding PGC s activities including terminating the Company as operator without cause. As the Company does not have the ability to control the activities of PGC that most significantly impact PGC s economic performance, the Company is not the primary beneficiary of PGC. Therefore, the results of PGC s activities are not consolidated into the Company s financial statements.

9. Century Plant Contract

The Company is constructing the Century Plant, a CO_2 treatment plant in Pecos County, Texas (the Century Plant), and associated compression and pipeline facilities pursuant to an agreement with Occidental Petroleum Corporation (Occidental). Under the terms of the agreement, the Company will construct the Century Plant and Occidental will pay the Company a minimum of 100% of the contract price, or $800.0 million, plus any subsequently agreed-upon revisions, through periodic cost reimbursements based upon the percentage of the project completed by the Company. The Company expects to complete the Century Plant in two phases. Upon completion of each phase of the Century Plant, Occidental will take ownership of the related assets and will operate the Century Plant for the purpose of separating and removing CO_2 from delivered natural gas. Phase I is in the commissioning process with completion and transfer of title to Occidental expected in the third quarter of 2011, and Phase II is under construction and expected to be completed in mid 2012. Pursuant to a 30-year treating agreement executed simultaneously with the construction agreement, Occidental will remove CO_2 from the Company s delivered production volumes. The Company will retain all methane gas from the natural gas it delivers to the Century Plant.

The Company accounts for construction of the Century Plant using the completed-contract method, under which contract revenues and costs are recognized when work under both phases of the contract is completed and assets have been transferred to Occidental. In the interim, costs incurred on and billings related to contracts in process are accumulated on the balance sheet. Contract gains or losses will be recorded, as development costs within the Company s oil and natural gas properties as part of the full cost pool, when it is determined that a gain or loss will be incurred. The Company recorded an addition of $124.0 million ($105.0 million in 2010 and $19.0 million in the first quarter of 2011) to its oil and natural gas properties for the estimated loss identified based on projections of the costs to be incurred in excess of contract amounts. Billings and estimated contract loss in excess of costs incurred of $41.2 million and $31.5 million at June 30, 2011 and December 31, 2010, respectively, are reported as current liabilities in the accompanying condensed consolidated balance sheets.

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(Unaudited)

10. Asset Retirement Obligation

A reconciliation of the beginning and ending aggregate carrying amounts of the asset retirement obligation for the period from December 31, 2010 to June 30, 2011 is as follows (in thousands):

Asset retirement obligation, December 31, 2010	$ 119,877
Liability incurred upon acquiring and drilling wells	2,702
Sales of reserves in place	(6,855)
Liability settled in current period	(1,370)
Accretion of discount expense	4,786
Asset retirement obligation, June 30, 2011	119,140
Less: current portion	25,360
Asset retirement obligation, net of current	$ 93,780

11. Long-Term Debt

Long-term debt consists of the following (in thousands):

	June 30, 2011	December 31, 2010
Senior credit facility	$ 80,000	$ 340,000
Other notes payable		
Drilling rig fleet and related oil field services equipment		6,302
Mortgage	16,527	17,020
Senior Floating Rate Notes due 2014	350,000	350,000
8.625% Senior Notes due 2015		650,000
9.875% Senior Notes due 2016, net of $11,881 and $12,793 discount, respectively	353,619	352,707
8.0% Senior Notes due 2018	750,000	750,000
8.75% Senior Notes due 2020, net of $6,693 and $6,943 discount, respectively	443,307	443,057
7.5% Senior Notes due 2021	900,000	
Total debt	2,893,453	2,909,086
Less: current maturities of long-term debt	1,019	7,293
Long-term debt	$ 2,892,434	$ 2,901,793

For the three-month periods ended June 30, 2011 and 2010, interest payments were approximately $56.9 million and $83.3 million, respectively. For the six-month periods ended June 30, 2011 and 2010, interest payments were approximately $110.3 million and $92.3 million, respectively. Interest paid for the three and six-month periods ended June 30, 2011 included $1.5 million and $25.7 million, respectively, of accrued interest paid in connection with the purchase and redemption of the 8.625% Senior Notes due 2015. See discussion of redemption below.

Senior Credit Facility. The senior credit facility is available to be drawn on subject to limitations based on its terms and certain financial covenants, as described below. The senior credit facility matures on April 15, 2014.

On February 23, 2011, the senior credit facility was amended to, among other things, (a) exclude from the calculation of Consolidated Net Income the net income (or loss) of a Royalty Trust, except to the extent of cash

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distributions received by the Company, (b) establish that an investment in a Royalty Trust and dispositions to, and of interests in, Royalty Trusts are permitted, (c) clarify that a Royalty Trust is not a Subsidiary, (d) allow the Company to net against its calculation of Consolidated Funded Indebtedness cash balances exceeding $10.0 million in the event no loans are outstanding under the senior credit facility at that time, and (e) establish that, for any fiscal quarter ending prior to March 31, 2012, if the ratio of the Company s secured indebtedness to EBITDA is less than 1.5:1.0 then compliance with the Company s Consolidated Leverage Ratio covenant is not required. Terms capitalized in the preceding sentence have the meaning given to them in the senior credit facility, as amended.

On April 20, 2011, the senior credit facility was amended. The amendment permits the Company to pay cash dividends on its 7.0% convertible perpetual preferred stock and reaffirms the borrowing base at $790.0 million.

As of June 30, 2011, the senior credit facility contained financial covenants, including maintaining agreed levels for the (i) ratio of total funded debt to EBITDA, which may not exceed 4.5:1.0 at each quarter end, calculated using the last four completed fiscal quarters, unless, for any quarter ending prior to March 31, 2012, the ratio of the Company s secured indebtedness to EBITDA is less than 1.5:1.0, calculated using the last four completed fiscal quarters (in each case through the second quarter of 2011, adjusted for annualized amounts of the post-acquisition results of operations of Arena), (ii) ratio of current assets to current liabilities, which must be at least 1.0:1.0 at each quarter end (in the current ratio calculation (as defined in the senior credit facility), any amounts available to be drawn under the senior credit facility are included in current assets, and unrealized assets and liabilities resulting from mark-to-market adjustments on the Company s derivative contracts are disregarded) and (iii) ratio of the Company s secured indebtedness to EBITDA, which may not exceed 2.0:1.0 at each quarter end, calculated using the last four completed fiscal quarters (in each case through the second quarter of 2011, adjusted for annualized amounts of the post-acquisition results of operations of Arena). As of and during the three and six-month periods ended June 30, 2011, the Company was in compliance with all of the financial covenants under the senior credit facility.

Additionally, the senior credit facility contains various covenants that limit the ability of the Company and certain of its subsidiaries to grant certain liens; make certain loans and investments; make distributions; redeem stock; redeem or prepay debt; merge or consolidate with or into a third party; or engage in certain asset dispositions, including a sale of all or substantially all of the Company s assets. Additionally, the senior credit facility limits the ability of the Company and certain of its subsidiaries to incur additional indebtedness with certain exceptions.

The obligations under the senior credit facility are guaranteed by certain Company subsidiaries and are secured by first priority liens on all shares of capital stock of each of the Company s material present and future subsidiaries; all intercompany debt of the Company; and substantially all of the Company s assets, including proved oil and natural gas reserves representing at least 80% of the discounted present value (as defined in the senior credit facility) of proved oil and natural gas reserves considered by the lenders in determining the borrowing base for the senior credit facility.

At the Company s election, interest under the senior credit facility is determined by reference to (a) the London Interbank Offered Rate (LIBOR) plus an applicable margin between 2.00% and 3.00% per annum or (b) the base rate, which is the highest of (i) the federal funds rate plus 0.5%, (ii) the prime rate published by Bank of America or (iii) the Eurodollar rate (as defined in the senior credit facility) plus 1.00% per annum, plus, in each case under scenario (b), an applicable margin between 1.00% and 2.00% per annum. Interest is payable quarterly for base rate loans and at the applicable maturity date for LIBOR loans, except that if the interest period

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NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

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for a LIBOR loan is six months, interest is paid at the end of each three-month period. The average annual interest rate paid on amounts outstanding under the senior credit facility was 2.51% and 2.65% for the three-month periods ended June 30, 2011 and 2010, respectively, and 2.70% and 2.52% for the six-month periods ended June 30, 2011 and 2010, respectively.

Borrowings under the senior credit facility may not exceed the lower of the borrowing base or the committed amount. On March 15, 2011, the borrowing base was reduced from $850.0 million to $790.0 million as a result of the issuance of the 7.5% Senior Notes due 2021, discussed below. The Company s borrowing base is redetermined in April and October of each year. With respect to each redetermination, the administrative agent and the lenders under the senior credit facility consider several factors, including the Company s proved reserves and projected cash requirements, and make assumptions regarding, among other things, oil and natural gas prices and production. Because the value of the Company s proved reserves is a key factor in determining the amount of the borrowing base, changing commodity prices and the Company s success in developing reserves may affect the borrowing base. At the April 2011 redetermination, the borrowing base remained $790.0 million. The Company at times incurs additional costs related to the senior credit facility as a result of amendments to the credit agreement and changes to the borrowing base. During the first six months of 2011, additional costs of approximately $0.3 million were incurred. These costs have been deferred and are included in other assets in the accompanying condensed consolidated balance sheets.

At June 30, 2011, the Company had $80.0 million outstanding under the senior credit facility and $24.5 million in outstanding letters of credit, which affect the availability under the senior credit facility on a dollar-for-dollar basis.

Other Notes Payable. The Company financed a portion of its drilling rig fleet and related oil field services equipment through the issuance of notes secured by such equipment. In March 2011, the Company paid the outstanding $4.3 million principal balance on these notes.

The debt incurred to purchase the downtown Oklahoma City property that serves as the Company s corporate headquarters is fully secured by a mortgage on one of the buildings located on the property. The note underlying the mortgage bears interest at 6.08% annually and matures on November 15, 2022. Payments of principal and interest in the amount of approximately $0.5 million are due on a quarterly basis through the maturity date.

Senior Floating Rate Notes Due 2014 and 8.625% Senior Notes Due 2015. The Company s Senior Floating Rate Notes due 2014 (the Senior Floating Rate Notes) and 8.625% Senior Notes due 2015 (the 8.625% Senior Notes) were issued in May 2008. The Senior Floating Rate Notes are jointly and severally guaranteed unconditionally on an unsecured basis by certain of the Company s wholly owned subsidiaries and are freely tradable. See Note 20 for condensed financial information of the subsidiary guarantors. As discussed below, on April 1, 2011, the Company redeemed the 8.625% Senior Notes that remained outstanding following the completion of its tender offer in respect of such notes.

The Senior Floating Rate Notes bear interest at LIBOR plus 3.625% (3.93% at June 30, 2011). Interest is payable quarterly with the principal due on April 1, 2014. The average interest rate paid on the outstanding Senior Floating Rate Notes was 3.93% and 3.92% for the three-month periods ended June 30, 2011 and 2010, respectively, and 3.93% and 3.90% for the six-month periods ended June 30, 2011 and 2010, respectively, without consideration of the interest rate swap discussed below. The Company may redeem, at specified redemption prices, some or all of the Senior Floating Rate Notes at any time.

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As of June 30, 2011, the Company had a $350.0 million notional interest rate swap agreement to fix the variable interest rate on the Senior Floating Rate Notes through April 1, 2013. The swap agreement effectively serves to fix the rate on the Senior Floating Rate Notes at an annual rate of 6.69% for the period from April 1, 2011 to April 1, 2013. This swap has not been designated as a hedge.

On March 1, 2011, the Company announced a cash tender offer to purchase any and all of the outstanding $650.0 million aggregate principal amount of its 8.625% Senior Notes for total consideration of $1,046.88 per $1,000 principal amount of such notes tendered by March 14, 2011. Holders tendering after March 14, 2011 were eligible to receive $1,016.88 per $1,000 principal amount of notes tendered. All holders whose notes were purchased received accrued and unpaid interest from the last interest payment date. As of March 31, 2011, the Company had purchased approximately 94.5%, or $614.2 million, of the aggregate principal amount of its 8.625% Senior Notes pursuant to the tender offer, which expired on March 28, 2011. On April 1, 2011, the Company redeemed the remaining outstanding $35.8 million aggregate principal amount of its 8.625% Senior Notes for $1,043.13 per $1,000 principal amount outstanding, plus accrued interest. All holders whose notes were redeemed received accrued and unpaid interest from October 1, 2010. The premium paid to purchase these notes and the unamortized debt issuance costs associated with the notes, totaling $2.0 million and $38.2 million for the three and six-month periods ended June 30, 2011, respectively, were recorded as a loss on extinguishment of debt and are included in the accompanying condensed consolidated statements of operations.

The $9.4 million of debt issuance costs associated with the Senior Floating Rate Notes is included in other assets in the accompanying condensed consolidated balance sheets and is being amortized over the term of the notes.

9.875% Senior Notes Due 2016. The Company s unsecured 9.875% Senior Notes due 2016 (the 9.875% Senior Notes) were issued in May 2009 and bear interest at a fixed rate of 9.875% per annum, payable semi-annually, with the principal due on May 15, 2016. The 9.875% Senior Notes were issued at a discount, which is amortized into interest expense over the term of the notes. The 9.875% Senior Notes are redeemable, in whole or in part, prior to their maturity at specified redemption prices and are jointly and severally guaranteed unconditionally on an unsecured basis by certain of the Company s wholly owned subsidiaries and are freely tradable.

Debt issuance costs of $7.9 million incurred in connection with the offering of the 9.875% Senior Notes are included in other assets in the accompanying condensed consolidated balance sheets and are being amortized over the term of the notes.

8.0% Senior Notes Due 2018. The Company s unsecured 8.0% Senior Notes due 2018 (the 8.0% Senior Notes) were issued in May 2008 and bear interest at a fixed rate of 8.0% per annum, payable semi-annually, with the principal due on June 1, 2018. The notes are redeemable, in whole or in part, prior to their maturity at specified redemption prices and are jointly and severally guaranteed unconditionally on an unsecured basis, by certain of the Company s wholly owned subsidiaries and are freely tradable.

The Company incurred $16.0 million of debt issuance costs in connection with the offering of the 8.0% Senior Notes. These costs are included in other assets in the accompanying condensed consolidated balance sheets and are being amortized over the term of the notes.

8.75% Senior Notes Due 2020. The Company s unsecured 8.75% Senior Notes due 2020 (the 8.75% Senior Notes) were issued in December 2009 and bear interest at a fixed rate of 8.75% per annum, payable semi-annually, with the principal due on January 15, 2020. The 8.75% Senior Notes were issued at a discount which is

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amortized into interest expense over the term of the notes. The 8.75% Senior Notes are redeemable, in whole or in part, prior to their maturity at specified redemption prices and are jointly and severally, guaranteed unconditionally on an unsecured basis by certain of the Company s wholly owned subsidiaries and are freely tradable. See Note 20 for condensed financial information of the subsidiary guarantors.

Debt issuance costs of $9.7 million incurred in connection with the offering of and subsequent registered exchange of the 8.75% Senior Notes are included in other assets in the accompanying condensed consolidated balance sheets and are being amortized over the term of the notes.

7.5% Senior Notes Due 2021. In March 2011, the Company issued $900.0 million of unsecured 7.5% Senior Notes due 2021 (the 7.5% Senior Notes) to qualified institutional buyers eligible under Rule 144A of the Securities Act and to persons outside the United States under Regulation S under the Securities Act. Net proceeds from the offering were approximately $880.7 million after deducting offering expenses, and were used to fund the tender offer for the 8.625% Senior Notes, including any accrued and unpaid interest, the redemption of the 8.625% Senior Notes that remained outstanding following the conclusion of the tender offer, including accrued and unpaid interest (each as described above) and to repay borrowings under the Company s senior credit facility. The 7.5% Senior Notes bear interest at a fixed rate of 7.5% per annum, payable semi-annually, with the principal due on March 15, 2021. Prior to March 15, 2016, the 7.5% Senior Notes are redeemable, in whole or in part, at a specified redemption price plus accrued and unpaid interest. On or after March 15, 2016, the 7.5% Senior Notes are redeemable, in whole or in part, prior to their maturity at other various specified redemption prices. The notes are jointly and severally guaranteed unconditionally on an unsecured basis by certain of the Company s wholly owned subsidiaries.

In conjunction with the issuance of the 7.5% Senior Notes, the Company entered into a Registration Rights Agreement requiring the Company to conduct a registered exchange offer for or register the resale of these notes before March 14, 2012. The Company is required to pay additional interest if it fails to fulfill its obligations under the agreement within the specified time periods.

Debt issuance costs of $19.3 million incurred in connection with the offering of the 7.5% Senior Notes are included in other assets in the accompanying condensed consolidated balance sheets and are being amortized over the term of the notes.

Indentures. The indentures governing the Company s senior notes contain limitations on the incurrence of indebtedness, payment of dividends, investments, asset sales, certain asset purchases, transactions with related parties and consolidations or mergers. As of and for the three and six-month periods ended June 30, 2011, the Company was in compliance with all of the covenants contained in the indentures governing the senior notes.

12. Derivatives

None of the Company s derivative contracts have been designated as hedges. The Company records all derivative contracts, which include commodity derivatives and an interest rate swap, at fair value. Changes in derivative contract fair values are recognized in earnings. Cash settlements and valuation gains and losses are included in (gain) loss on derivative contracts for the commodity derivative contracts and in interest expense for interest rate swaps in the consolidated statement of operations. Commodity derivative contracts are settled on a monthly basis. Settlements on interest rate swaps occur quarterly. Derivative assets and liabilities arising from the Company s derivative contracts with the same counterparty that provide for net settlement are reported on a net basis in the consolidated balance sheet.

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Commodity Derivatives. The Company is exposed to commodity price risk, which impacts the predictability of its cash flows from the sale of oil and natural gas. The Company seeks to manage this risk through the use of commodity derivative contracts. These derivative contracts allow the Company to limit its exposure to a portion of its projected oil and natural gas sales. None of the Company s derivative contracts may be terminated early as a result of a party to the contract having its credit rating downgraded. At June 30, 2011, the Company s commodity derivative contracts consisted of fixed price swaps, collars and basis swaps, which are described below:

Fixed price swaps:	The Company receives a fixed price for the contract and pays a floating market price to the counterparty over a specified period for a contracted volume.
Collars:	Collars contain a fixed floor price (put) and a fixed ceiling price (call). If the market price exceeds the call strike price or falls below the put strike price, the Company receives the fixed price and pays the market price. If the market price is between the call and the put strike price, no payments are due from either party.
Basis swaps:	The Company receives a payment from the counterparty if the settled price differential is greater than the stated terms of the contract and pays the counterparty if the settled price differential is less than the stated terms of the contract, which guarantees the Company a price differential for natural gas from a specified delivery point.

On April 12, 2011, the Company entered into a derivatives agreement with the Mississippian Trust, effective April 1, 2011, that provides the Mississippian Trust with the benefit of certain oil and natural gas derivative contracts previously entered into by the Company with third parties. The underlying commodity derivative contracts cover volumes of oil and natural gas production through December 31, 2015. Under this arrangement, the Company will pay the Mississippian Trust amounts it receives from its counterparties in accordance with the underlying contracts, and the Mississippian Trust will pay the Company any amounts that it is required to pay its counterparties under such contracts. These commodity derivative contracts are included in the open oil and natural gas derivative contracts tables below. See Note 8 for additional discussion of the Mississippian Trust and a listing of the derivative contracts, the benefits and obligations of which will be passed to the Mississippian Trust.

Interest Rate Swaps. The Company is exposed to interest rate risk on its long-term fixed and variable interest rate borrowings. Fixed rate debt, where the interest rate is fixed over the life of the instrument, exposes the Company to (i) changes in market interest rates reflected in the fair value of the debt and (ii) the risk that the Company may need to refinance maturing debt with new debt at a higher rate. Variable rate debt, where the interest rate fluctuates, exposes the Company to short-term changes in market interest rates as the Company s interest obligations on these instruments are periodically redetermined based on prevailing market interest rates, primarily LIBOR and the federal funds rate.

The Company has an interest rate swap agreement to manage the interest rate risk on a portion of its floating rate debt by effectively fixing the variable interest rate on its Senior Floating Rate Notes through April 1, 2013. See Note 11 for further discussion of the Company s interest rate swap.

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Fair Value of Derivatives. In accordance with ASC Topic 815, Derivatives and Hedging, the following table presents the fair value of the Company s derivative contracts at June 30, 2011 and December 31, 2010 on a gross basis without regard to same-counterparty netting (in thousands):

Type of Contract	**Balance Sheet Classification**	**June 30, 2011**	**December 31, 2010**
Derivative assets			
Oil price swaps	Derivative contracts-current	$ 2,674	$
Natural gas price swaps	Derivative contracts-current		