NEWFIELD EXPLORATION CO /DE/
Form 10-Q
October 29, 2012

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 September 30, 2012

OR

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

For the Transition Period from to .

Commission File Number: 1-12534

NEWFIELD EXPLORATION COMPANY
(Exact name of Registrant as specified in its charter)

Delaware (State or other jurisdiction of incorporation or organization)	72-1133047 (I.R.S. Employer Identification Number)

4 Waterway Square Place
Suite 100
The Woodlands, Texas 77380
(Address and Zip Code of principal executive offices)

(281) 210-5100
(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 þ No o

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T

(§232.405) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes þ No o

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

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

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

As of October 22, 2012, there were 135,223,639 shares of the registrant's common stock, par value $0.01 per share, outstanding.

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NEWFIELD EXPLORATION COMPANY

CONSOLIDATED BALANCE SHEET
(In millions, except share data)
(Unaudited)

	September 30, 2012	December 31, 2011
ASSETS		
Current assets:		
Cash and cash equivalents	$125	$76
Accounts receivable	427	407
Inventories	125	90
Derivative assets	88	129
Other current assets	94	73
Total current assets	859	775
Property and equipment, at cost, based on the full cost method of accounting for oil and gas properties ($2,009 and $1,965 were excluded from amortization at September 30, 2012 and December 31, 2011, respectively)	15,617	14,526
Less accumulated depreciation, depletion and amortization	(7,211)	(6,506)
Total property and equipment, net	8,406	8,020
Derivative assets	22	61
Long-term investments	55	52
Deferred taxes	41	28
Other assets	48	55
Total assets	$9,431	$8,991
LIABILITIES AND STOCKHOLDERS' EQUITY		
Current liabilities:		
Accounts payable	$76	$112
Accrued liabilities	747	687
Advances from joint owners	27	45
Asset retirement obligations	6	10
Derivative liabilities	19	50
Deferred taxes	24	28
Total current liabilities	899	932
Other liabilities	42	44
Derivative liabilities	16	3
Long-term debt	3,190	3,006
Asset retirement obligations	143	135
Deferred taxes	973	951
Total long-term liabilities	4,364	4,139
Commitments and contingencies (Note 11)	—	—
Stockholders' equity:		
Preferred stock ($0.01 par value, 5,000,000 shares authorized; no shares issued)	—	—

Common stock ($0.01 par value, 200,000,000 shares authorized at September 30, 2012 and December 31, 2011; 136,501,207 and 136,379,381 shares issued at September 30, 2012 and December 31, 2011, respectively)	1	1
Additional paid-in capital	1,512	1,495
Treasury stock (at cost, 1,282,212 and 1,694,623 shares at September 30, 2012 and December 31, 2011, respectively)	(39)	(50)
Accumulated other comprehensive loss	(8)	(10)
Retained earnings	2,702	2,484
Total stockholders' equity	4,168	3,920
Total liabilities and stockholders' equity	$9,431	$8,991

The accompanying notes to consolidated financial statements are an integral part of this statement.

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NEWFIELD EXPLORATION COMPANY

CONSOLIDATED STATEMENT OF NET INCOME
(In millions, except per share data)
(Unaudited)

	Three Months Ended September 30, 2012	Three Months Ended September 30, 2011	Nine Months Ended September 30, 2012	Nine Months Ended September 30, 2011
Oil and gas revenues	$ 615	$ 628	$ 1,921	$ 1,794
Operating expenses:				
Lease operating	128	115	384	333
Production and other taxes	79	95	250	245
Depreciation, depletion and amortization	237	189	702	528
General and administrative	59	51	165	132
Other	6	—	6	—
Total operating expenses	509	450	1,507	1,238
Income from operations	106	178	414	556
Other income (expenses):				
Interest expense	(53)	(43)	(153)	(124)
Capitalized interest	17	24	53	61
Commodity derivative income (expense)	(98)	262	61	249
Other	(16)	3	(18)	2
Total other income (expenses)	(150)	246	(57)	188
Income (loss) before income taxes	(44)	424	357	744
Income tax provision (benefit):				
Current	38	9	134	39
Deferred	(49)	146	5	234
Total income tax provision (benefit)	(11)	155	139	273
Net income (loss)	$ (33)	$ 269	$ 218	$ 471
Earnings (loss) per share:				
Basic	$ (0.24)	$ 2.00	$ 1.62	$ 3.52
Diluted	$ (0.24)	$ 1.99	$ 1.61	$ 3.49
Weighted-average number of shares outstanding for basic earnings (loss) per share	135	134	134	134
Weighted-average number of shares outstanding for diluted earnings (loss) per share	135	135	135	135

The accompanying notes to consolidated financial statements are an integral part of this statement.

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NEWFIELD EXPLORATION COMPANY

CONSOLIDATED STATEMENT OF COMPREHENSIVE INCOME
(In millions)
(Unaudited)

	Three Months Ended September 30, 2012	Three Months Ended September 30, 2011	Nine Months Ended September 30, 2012	Nine Months Ended September 30, 2011
Net income (loss)	$ (33)	$ 269	$ 218	$ 471
Other comprehensive income (loss):				
Unrealized gain (loss) on investments, net of tax	—	(2)	2	2
Other comprehensive income (loss), net of tax	—	(2)	2	2
Comprehensive income (loss)	$ (33)	$ 267	$ 220	$ 473

The accompanying notes to consolidated financial statements are an integral part of this statement.

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NEWFIELD EXPLORATION COMPANY

CONSOLIDATED STATEMENT OF CASH FLOWS
(In millions)
(Unaudited)

	Nine Months Ended September 30, 2012	2011
Cash flows from operating activities:		
Net income	$218	$471
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation, depletion and amortization	702	528
Deferred tax provision	5	234
Stock-based compensation	27	20
Commodity derivative income	(61)	(249)
Cash receipts on derivative settlements, net	123	156
Other non-cash charges	11	2
Changes in operating assets and liabilities:		
(Increase) decrease in accounts receivable	(43)	34
Increase in inventories	(21)	(24)
Increase in other current assets	(21)	(17)
(Increase) decrease in other assets	7	(6)
Increase (decrease) in accounts payable and accrued liabilities	(116)	24
Increase (decrease) in advances from joint owners	(19)	5
Decrease in other liabilities	(8)	(5)
Net cash provided by operating activities	804	1,173
Cash flows from investing activities:		
Additions to oil and gas properties	(1,279)	(1,723)
Acquisitions of oil and gas properties	(9)	(299)
Proceeds from sales of oil and gas properties	382	202
Additions to furniture, fixtures and equipment	(15)	(23)
Redemptions of investments	—	1
Net cash used in investing activities	(921)	(1,842)
Cash flows from financing activities:		
Proceeds from borrowings under credit arrangements	2,347	3,148
Repayments of borrowings under credit arrangements	(2,288)	(3,217)
Proceeds from issuance of senior notes	1,000	750
Debt issue costs	(10)	(16)
Repayment of senior subordinated notes	(875)	—
Proceeds from issuances of common stock	1	12
Purchases of treasury stock, net	(9)	(16)
Net cash provided by financing activities	166	661
Increase (decrease) in cash and cash equivalents	49	(8)
Cash and cash equivalents, beginning of period	76	39
Cash and cash equivalents, end of period	$125	$31

The accompanying notes to consolidated financial statements are an integral part of this statement.

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NEWFIELD EXPLORATION COMPANY

CONSOLIDATED STATEMENT OF STOCKHOLDERS' EQUITY
(In millions)
(Unaudited)

	Common Stock		Treasury Stock		Additional Paid-in	Retained	Accumulated Other Comprehensive Income	Total Stockholders'
	Shares	Amount	Shares	Amount	Capital	Earnings	(Loss)	Equity
Balance, December 31, 2011	136.4	$ 1	(1.7)	$ (50)	$ 1,495	$ 2,484	$ (10)	$ 3,920
Issuances of common stock	0.1	—			1			1
Stock-based compensation					36			36
Treasury stock, net			0.4	11	(20)			(9)
Net income						218		218
Other comprehensive income, net of tax							2	2
Balance, September 30, 2012	136.5	$ 1	(1.3)	$ (39)	$ 1,512	$ 2,702	$ (8)	$ 4,168

The accompanying notes to consolidated financial statements are an integral part of this statement.

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NEWFIELD EXPLORATION COMPANY
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

1. Organization and Summary of Significant Accounting Policies:

Organization and Principles of Consolidation

We are an independent energy company engaged in the exploration, development and production of crude oil, natural gas and natural gas liquids. Our principal domestic areas of operation include the Mid-Continent, the Rocky Mountains and onshore Texas. Internationally, we focus on offshore oil developments in Malaysia and China.

Our financial statements include the accounts of Newfield Exploration Company, a Delaware corporation, and its subsidiaries. We proportionately consolidate our interests in oil and natural gas exploration and production ventures and partnerships in accordance with industry practice. All significant intercompany balances and transactions have been eliminated. Unless otherwise specified or the context otherwise requires, all references in these notes to "Newfield," "we," "us" or "our" are to Newfield Exploration Company and its subsidiaries.

These unaudited consolidated financial statements reflect, in the opinion of our management, all adjustments, consisting only of normal and recurring adjustments, necessary to fairly state our financial position as of and results of operations for the periods presented. These financial statements have been prepared in accordance with the instructions to Form 10-Q and, therefore, do not include all disclosures required for financial statements prepared in conformity with accounting principles generally accepted in the United States of America. Interim period results are not necessarily indicative of results of operations or cash flows for a full year.

These financial statements and notes should be read in conjunction with our audited consolidated financial statements and the notes thereto included in our Annual Report on Form 10-K for the year ended December 31, 2011.

Dependence on Oil and Natural Gas Prices

As an independent oil and natural gas producer, our revenue, profitability and future rate of growth are substantially dependent on prevailing prices for oil and natural gas. Historically, the energy markets have been very volatile, and there can be no assurance that oil and natural gas prices will not be subject to wide fluctuations in the future. A substantial or extended decline in oil or natural gas prices could have a material adverse effect on our financial position, results of operations, cash flows and access to capital and on the quantities of oil and natural gas reserves that we can economically produce.

Use of Estimates

The preparation of financial statements in accordance with accounting principles generally accepted in the United States of America requires our management to make estimates and assumptions that affect the reported amounts of assets and liabilities, disclosure of contingent assets and liabilities at the date of the financial statements, the reported amounts of revenues and expenses during the reporting period and the reported amounts of proved oil and natural gas reserves. Actual results could differ significantly from these estimates. Our most significant financial estimates are associated with our estimated proved oil and natural gas reserves and the fair value of our derivative positions.

Investments

Investments consist primarily of debt and equity securities, as well as auction rate securities, a majority of which are classified as "available-for-sale" and stated at fair value. Accordingly, unrealized gains and losses and the related deferred income tax effects are excluded from earnings and reported as a separate component within the consolidated statement of comprehensive income. Realized gains or losses are computed based on specific identification of the securities sold. We regularly assess our investments for impairment and consider any impairment to be other than temporary if we intend to sell the security, it is more likely than not that we will be required to sell the security, or we do not expect to recover our cost of the security. We realized interest income and net gains on our investment securities of approximately $1 million and $0.3 million for the three-month periods ended September 30, 2012 and 2011, respectively, and approximately $2 million and $1 million for the nine-month periods ended September 30, 2012 and 2011, respectively.

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Inventories

Inventories primarily consist of tubular goods and well equipment held for use in our oil and gas operations and oil produced in our operations offshore Malaysia and China but not sold. Inventories are carried at the lower of cost or market. Substantially all of the crude oil from our operations offshore Malaysia and China is produced into FPSOs and sold periodically as barge quantities are accumulated. The product inventory consisted of approximately 740,000 barrels and 239,000 barrels of crude oil valued at cost of $49 million and $19 million at September 30, 2012 and December 31, 2011, respectively. Cost for purposes of the carrying value of oil inventory is the sum of production costs and depletion expense.

Oil and Gas Properties

We use the full cost method of accounting for our oil and gas producing activities. Under this method, all costs incurred in the acquisition, exploration and development of oil and gas properties, including salaries, benefits and other internal costs directly attributable to these activities, are capitalized into cost centers that are established on a country-by-country basis. We capitalized $29 million and $30 million of internal costs during the three-month periods ended September 30, 2012 and 2011, respectively, and $87 million and $81 million during the nine-month periods ended September 30, 2012 and 2011, respectively. Interest expense related to unproved properties is capitalized into oil and gas properties.

Proceeds from the sale of oil and gas properties are applied to reduce the costs in the applicable cost center unless the reduction would significantly alter the relationship between capitalized costs and proved reserves, in which case a gain or loss is recognized.

Capitalized costs and estimated future development costs are amortized using a unit-of-production method based on proved reserves associated with the applicable cost center. For each cost center, the net capitalized costs of oil and gas properties are limited to the lower of the unamortized cost or the cost center ceiling. A particular cost center ceiling is equal to the sum of:

- the present value (10% per annum discount rate) of estimated future net revenues from proved reserves using oil and natural gas reserve estimation requirements, which require use of the unweighted-average first-day-of-the-month commodity prices for the prior 12 months, adjusted for market differentials applicable to our reserves (including the effects of hedging contracts that are designated for hedge accounting, if any); plus

- the cost of properties not included in the costs being amortized, if any; less

- related income tax effects.

If net capitalized costs of oil and gas properties exceed the cost center ceiling, we are subject to a ceiling test writedown to the extent of such excess. If required, a ceiling test writedown reduces earnings and stockholders' equity in the period of occurrence and, holding other factors constant, results in lower depreciation, depletion and amortization expense in future periods.

The risk that we will be required to writedown the carrying value of our properties increases when oil and natural gas prices decrease significantly for a prolonged period of time or if we have substantial downward revisions in our estimated proved reserves. At September 30, 2012, the ceiling value of our reserves was calculated based upon the unweighted-average first-day-of-the-month commodity prices for the prior 12 months of $2.83 per MMBtu for natural gas and $95.05 per barrel for oil, adjusted for market differentials. Using these prices, the cost center ceilings with respect to our properties in the U.S., Malaysia and China exceeded the net capitalized costs of the respective properties. As such, no ceiling test writedowns were required at September 30, 2012.

Accounting for Asset Retirement Obligations

If a reasonable estimate of the fair value of an obligation to perform site reclamation, dismantle facilities or plug and abandon wells can be made, we record a liability (an asset retirement obligation or ARO) on our consolidated balance sheet and capitalize the present value of the asset retirement cost in oil and gas properties in the period in which the ARO is incurred. Settlements include payments made to satisfy the AROs, as well as transfer of the ARO to purchasers of our divested properties.

In general, the amount of an ARO and the costs capitalized will equal the estimated future cost to satisfy the abandonment obligation assuming the normal operation of the asset, using current prices that are escalated by an assumed inflation factor up to the estimated settlement date, which is then discounted back to the date that the abandonment obligation was incurred using an assumed cost of funds for our company. After recording these amounts, the ARO is accreted to its future estimated value using the same assumed cost of funds, and the additional capitalized costs are depreciated on a unit-of-production basis within the related full cost pool. Both the accretion and the depreciation are included in depreciation, depletion and amortization expense on our consolidated statement of net income.

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The change in our ARO for the nine months ended September 30, 2012 is set forth below (in millions):

Balance at January 1, 2012	$	145
Accretion expense		8
Additions		8
Revisions		12
Settlements		(24)
Balance at September 30, 2012		149
Less: Current portion of ARO at September 30, 2012		(6)
Total long-term ARO at September 30, 2012	$	143

Income Taxes

We use the liability method of accounting for income taxes. Under this method, deferred tax assets and liabilities are determined by applying tax regulations existing at the end of a reporting period to the cumulative temporary differences between the tax bases of assets and liabilities and their reported amounts in our financial statements. A valuation allowance is established to reduce deferred tax assets if it is more likely than not that the related tax benefits will not be realized.

Derivative Financial Instruments

We account for our derivative activities by applying authoritative accounting and reporting guidance, which requires that every derivative instrument be recorded on the consolidated balance sheet as either an asset or a liability measured at its fair value and that changes in the derivative's fair value be recognized currently in earnings unless specific hedge accounting criteria are met. All of the derivative instruments that we utilize are to manage the price risk attributable to our expected oil and gas production. We have elected not to designate price-risk management activities as accounting hedges under the accounting guidance and, accordingly, account for them using the mark-to-market accounting method. Under this method, the changes in contract values are reported currently in earnings. We periodically utilize derivatives to manage our exposure to variable interest rates.

The related cash flow impact of our derivative activities are reflected as cash flows from operating activities. See Note 4, "Derivative Financial Instruments," for a more detailed discussion of our derivative activities.

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NEWFIELD EXPLORATION COMPANY
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

New Accounting Requirements

In May 2011, the FASB issued additional guidance regarding fair value measurement and disclosure requirements. The most significant change requires us, for Level 3 fair value measurements, to disclose quantitative information about unobservable inputs used, a description of the valuation processes used and a qualitative discussion about the sensitivity of the measurements. The guidance is effective for interim and annual periods beginning on or after December 15, 2011. Adopting the additional fair value measurement and disclosure requirements did not have a material impact on our financial position or results of operations.

In December 2011, the FASB issued guidance regarding the disclosure of offsetting assets and liabilities. The guidance will require disclosure of gross information and net information about instruments and transactions eligible for offset arrangement. The guidance is effective for interim and annual periods beginning on or after January 1, 2013. We do not expect adoption of the additional disclosures regarding offsetting assets and liabilities to have a material impact on our financial position or results of operations.

2. Earnings Per Share:

Basic earnings per share (EPS) is calculated by dividing net income (the numerator) by the weighted-average number of shares of common stock (excluding unvested restricted stock and restricted stock units) outstanding during the period (the denominator). Diluted earnings per share incorporates the dilutive impact of outstanding stock options and unvested restricted stock and restricted stock units (using the treasury stock method). Under the treasury stock method, the amount the employee must pay for exercising stock options, the amount of unrecognized compensation expense related to unvested stock-based compensation grants and the amount of excess tax benefits that would be recorded when the award becomes deductible are assumed to be used to repurchase shares. Please see Note 10, "Stock-Based Compensation."

The following is the calculation of basic and diluted weighted-average shares outstanding and EPS for the indicated periods:

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2012	2011	2012	2011
	(In millions, except per share data)			
Income (numerator):				
Net income (loss) — basic and diluted	$ (33)	$ 269	$ 218	$ 471
Weighted-average shares (denominator):				
Weighted-average shares — basic	135	134	134	134
Dilution effect of stock options and unvested restricted stock and restricted stock units outstanding at end of period(1)(2)	—	1	1	1
Weighted-average shares — diluted	135	135	135	135

Earnings (loss) per share:										
Basic	$	(0.24	)	$	2.00	$	1.62	$	3.52	
Diluted	$	(0.24	)	$	1.99	$	1.61	$	3.49	

(1) The effect of stock options and unvested restricted stock and restricted stock units outstanding has not been included in the calculation of shares outstanding for diluted EPS for the three months ended September 30, 2012 as their effect would have been anti-dilutive. Had we recognized net income for that period, incremental shares attributable to the assumed exercise of outstanding options and the assumed vesting of unvested restricted stock and restricted stock units would have increased diluted weighted-average shares outstanding by 0.6 million shares for the three months ended September 30, 2012.

(2) The calculation of shares outstanding for diluted EPS for the nine months ended September 30, 2012 excludes the effect of 3 million unvested restricted stock or restricted stock units and stock options, and the calculation of shares outstanding for diluted EPS for the three and nine months ended September 30, 2011 excludes the effect of 1 million unvested restricted stock or restricted stock units and stock options because including the effect would be anti-dilutive.

3. Oil and Gas Assets:

Property and Equipment

Property and equipment consisted of the following at:

	September 30, 2012	December 31, 2011
	(In millions)	
Oil and gas properties:		
Subject to amortization	$13,456	$12,423
Not subject to amortization	2,009	1,965
Gross oil and gas properties	15,465	14,388
Accumulated depreciation, depletion and amortization	(7,131)	(6,436)
Net oil and gas properties	8,334	7,952
Other property and equipment	152	138
Accumulated depreciation and amortization	(80)	(70)
Net other property and equipment	72	68
Total property and equipment, net	$8,406	$8,020

The following is a summary of our oil and gas properties not subject to amortization as of September 30, 2012. We believe that our evaluation activities related to substantially all of our conventional properties not subject to amortization will be completed within four years. Because of the size of our unconventional resource plays, the entire evaluation will take significantly longer than four years. At September 30, 2012, approximately 77% of oil and gas properties not subject to amortization were associated with our unconventional resource plays.

	Costs Incurred In				
	2012	2011	2010	2009 and prior	Total
			(In millions)		
Acquisition costs	$105	$296	$299	$411	$1,111
Exploration costs	390	44	22	34	490
Development costs	48	62	25	36	171
Fee mineral interests	—	—	—	23	23
Capitalized interest	53	78	55	28	214
Total oil and gas properties not subject to amortization	$596	$480	$401	$532	$2,009

Non-Strategic Asset Sales

During the nine months ended September 30, 2012 and the year ended December 31, 2011, we received payment for sales of non-strategic assets of approximately $382 million and $406 million, respectively. The cash flows and results of operations for the assets included in a sale are included in our consolidated financial statements up to the date of sale. On October 5, 2012, we closed the sale of our remaining Gulf of Mexico assets. See Note 14, “Subsequent Events.”

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4. Derivative Financial Instruments:

Commodity Derivative Instruments

We utilize swap, floor, collar and three-way collar derivative contracts to hedge against the variability in cash flows associated with the forecasted sale of our future oil and gas production. While the use of these derivative instruments limits the downside risk of adverse price movements, their use also may limit future income from favorable price movements.

With respect to a swap contract, the counterparty is required to make a payment to us if the settlement price for any settlement period is less than the swap price, and we are required to make a payment to the counterparty if the settlement price for any settlement period is greater than the swap price. For a floor contract, the counterparty is required to make a payment to us if the settlement price for any settlement period is below the floor price. We are not required to make any payment in connection with the settlement of a floor contract. For a collar contract, the counterparty is required to make a payment to us if the settlement price for any settlement period is below the floor price while we are required to make payment to the counterparty if the settlement price for any settlement period is above the ceiling price. Neither party is required to make a payment to the other party if the settlement price for any settlement period is equal to or greater than the floor price and equal to or less than the ceiling price. A three-way collar contract consists of a standard collar contract plus a put sold by us with a price below the floor price of the collar. This additional put requires us to make a payment to the counterparty if the settlement price for any settlement period is below the put price. Combining the collar contract with the additional put results in us being entitled to a net payment equal to the difference between the floor price of the standard collar and the additional put price if the settlement price is equal to or less than the additional put price. If the settlement price is greater than the additional put price, the result is the same as it would have been with a standard collar contract only. This strategy enables us to increase the floor and the ceiling price of the collar beyond the range of a traditional no cost collar while defraying the associated cost with the sale of the additional put.

All of our derivative contracts are carried at their fair value on our consolidated balance sheet under the captions “Derivative assets” and “Derivative liabilities.” Substantially all of our oil and gas derivative contracts are settled based upon reported prices on the NYMEX. The estimated fair value of these contracts is based upon various factors, including closing exchange prices on the NYMEX, over-the-counter quotations, volatility and, in the case of collars and floors, the time value of options. The calculation of the fair value of collars and floors requires the use of an option-pricing model. Please see Note 7, “Fair Value Measurements.” We recognize all realized and unrealized gains and losses related to these contracts on a mark-to-market basis in our consolidated statement of net income under the caption “Commodity derivative income (expense).” Settlements of derivative contracts are included in operating cash flows on our consolidated statement of cash flows.

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NEWFIELD EXPLORATION COMPANY
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

At September 30, 2012, we had outstanding contracts with respect to our future production that were not designated for hedge accounting as set forth in the tables below.

Natural Gas

		NYMEX Contract Price Per MMBtu							
					Collars				Estimated Fair Value
		Swaps	Additional Put		Floors		Ceilings		
Period and Type of Contract	Volume in MMMBtus	(Weighted Average)	Range	Weighted Average	Range	Weighted Average	Range	Weighted Average	Asset (Liability) (In millions)
October 2012 – December 2012									
Price swap contracts	11,340	$3.19	¾	¾	¾	¾	¾	¾	$ 1
Price swap contracts	(A)	2.72	¾	¾	¾	¾	¾	¾	(9)
3-Way collar contracts	15,070	—	$3.50-$4.50	$4.19	$5.00-$6.00	$5.51	$5.20-$7.55	$6.41	19
January 2013 – December 2013									
Price swap contracts	54,750	4.08	¾	¾	¾	¾	¾	¾	13
Price swap contracts	(A)	3.45	¾	¾	¾	¾	¾	¾	(15)
3-Way collar contracts	39,530	—	3.50-4.50	4.04	5.00-6.00	5.44	6.00-7.55	6.48	42
January 2014 – December 2014									
Price swap contracts	54,750	3.85	¾	¾	¾	¾	¾	¾	(17)
Collar contracts	14,600	¾	¾	¾	3.75	3.75	4.54-4.57	4.55	(1)

$ 33

(A) During the first quarter of 2012, natural gas spot market prices were below the puts we sold on our three-way collars for April through December 2012 and the full-year 2013, exposing us further to the softening natural gas spot market. As a result, during the first quarter of 2012 we entered into additional fixed-price swap contracts in the over-the-counter market that effectively prevented any further erosion in the value of our natural gas three-way collars. The new swap contracts added during the first quarter of 2012 were for the same volumes as our October through December 2012 and the full-year 2013 three-way collar contracts. The economics from the combination of these additional fixed-price swap contracts and our natural gas three-way collar contracts will result in effective average fixed prices of $4.04 and $4.85 per MMBtu for the fourth quarter of 2012 and the full-year 2013, respectively, as long as natural gas spot prices for the respective time periods settle below the puts we sold on our three-way collar contracts.

NEWFIELD EXPLORATION COMPANY
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

Oil

		NYMEX Contract Price Per Bbl						Estimated Fair Value
				Collars				
		Additional Put		Floors		Ceilings		
Period and Type of Contract	Volume in MBbls	Range	Weighted Average	Range	Weighted Average	Range	Weighted Average	Asset (Liability) (In millions)
October 2012 – December 2012								
3-Way collar contracts	3,220	$55.00-$90.00	$66.86	$75.00-$100.00	$82.96	$91.90-$137.80	$108.30	$ 1
January 2013 – December 2013								
3-Way collar contracts	12,115	80.00	80.00	95.00	95.00	106.50-130.40	118.05	30
January 2014 – December 2014								
3-Way collar contracts	5,110	80.00	80.00	95.00	95.00	117.50-120.75	119.16	14
								$ 45

Basis Contracts

At September 30, 2012, we had natural gas basis contracts that were not designated for hedge accounting to lock in the differential between the NYMEX Henry Hub posted prices and those of our physical pricing points in the Rocky Mountains and Mid-Continent, as set forth in the table below.

	Rocky Mountains		Mid-Continent		Estimated
	Volume in	Weighted-	Volume in	Weighted-	Fair Value

	MMMbtus	Average Differential	MMMbtus	Average Differential	Asset (Liability) (In millions)
October 2012 – December 2012	1,230	$ (0.91)	4,600	$ (0.55)	$ (3)

Additional Disclosures about Derivative Instruments and Hedging Activities

We had derivative financial instruments recorded in our consolidated balance sheet as assets (liabilities) at their respective estimated fair value, as set forth below.

Type of Contract	Balance Sheet Location	September 30, 2012	December 31, 2011
		(In millions)	
Derivatives not designated as hedging instruments:			
Natural gas contracts	Derivative assets – current	$ 65	$ 133
Oil contracts	Derivative assets – current	24	1
Basis contracts	Derivative assets – current	(1)	(5)
Natural gas contracts	Derivative assets – noncurrent	1	61
Oil contracts	Derivative assets – noncurrent	21	—
Natural gas contracts	Derivative liabilities – current	(17)	—
Oil contracts	Derivative liabilities – current	—	(45)
Basis contracts	Derivative liabilities – current	(2)	(5)
Natural gas contracts	Derivative liabilities – noncurrent	(16)	—
Oil contracts	Derivative liabilities – noncurrent	—	(3)
Total		$ 75	$ 137

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The amount of gain (loss) recognized in income related to our derivative financial instruments was as follows:

Type of Contract	Location of Gain (Loss) Recognized in Income	Three Months Ended September 30, 2012	Three Months Ended September 30, 2011	Nine Months Ended September 30, 2012	Nine Months Ended September 30, 2011
		(In millions)			
Derivatives not designated as hedging instruments:					
Realized gain on natural gas contracts	Commodity derivative income (expense)	$ 37	$ 68	$ 135	$ 198
Realized gain (loss) on oil contracts	Commodity derivative income (expense)	3	(5)	(4)	(37)
Realized loss on basis contracts	Commodity derivative income (expense)	(3)	(2)	(8)	(5)
Total realized gain		37	61	123	156
Unrealized gain (loss) on natural gas contracts	Commodity derivative income (expense)	(79)	5	(162)	(68)
Unrealized gain (loss) on oil contracts	Commodity derivative income (expense)	(59)	197	92	162
Unrealized gain (loss) on basis contracts	Commodity derivative income (expense)	3	(1)	8	(1)
Total unrealized gain (loss)		(135)	201	(62)	93
Total		$ (98)	$ 262	$ 61	$ 249

The use of derivative transactions involves the risk that the counterparties will be unable to meet the financial terms of such transactions. Our derivative contracts are with multiple counterparties to minimize our exposure to any individual counterparty, and we have netting arrangements with all of our counterparties that provide for offsetting payables against receivables from separate derivative instruments with that counterparty. At September 30, 2012, six of our 14 counterparties accounted for approximately 85% of our estimated future hedged production with no single counterparty accounting for more than 25% of that production.

The counterparties to the majority of our derivative instruments also are lenders under our credit facility. Our credit facility, senior notes, senior subordinated notes and substantially all of our derivative instruments contain provisions that provide for cross defaults and acceleration of those debt and derivative instruments in certain situations.

5. Accounts Receivable:

As of the indicated dates, our accounts receivable consisted of the following:

	September 30, 2012	December 31, 2011
	(In millions)	

Revenue	$298	$301
Joint interest	124	96
Other	6	11
Reserve for doubtful accounts	(1)	(1)
Total accounts receivable	$427	$407

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6. Accrued Liabilities:

As of the indicated dates, our accrued liabilities consisted of the following:

	September 30, 2012	December 31, 2011
	(In millions)	
Revenue payable	$86	$94
Accrued capital costs	332	231
Accrued lease operating expenses	84	86
Employee incentive expense	46	61
Accrued interest on debt	46	52
Taxes payable	116	122
Other	37	41
Total accrued liabilities	$747	$687

7. Fair Value Measurements:

Fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date (exit price). The authoritative guidance requires disclosure of the framework for measuring fair value and requires that fair value measurements be classified and disclosed in one of the following categories:

Level 1: Unadjusted quoted prices in active markets that are accessible at the measurement date for identical, unrestricted assets or liabilities. We consider active markets as those in which transactions for the assets or liabilities occur with sufficient frequency and volume to provide pricing information on an ongoing basis.

Level 2: Quoted prices in markets that are not active, or inputs that are observable, either directly or indirectly, for substantially the full term of the asset or liability. This category includes those derivative instruments that we value using observable market data. Substantially all of these inputs are observable in the marketplace throughout the full term of the derivative instrument, can be derived from observable data or supported by observable levels at which transactions are executed in the marketplace. Instruments in this category include non-exchange traded derivatives such as over-the-counter commodity price swaps and certain investments.

Level 3: Measured based on prices or valuation models that require inputs that are both significant to the fair value measurement and less observable from objective sources (i.e., supported by little or no market activity). Our valuation models for derivative contracts are primarily industry-standard models (i.e., Black-Scholes) that consider various inputs including: (a) quoted forward prices for commodities, (b) time value, (c) volatility factors, (d) counterparty credit risk and (e) current market and contractual prices for the underlying instruments, as well as other relevant economic measures. Our valuation methodology for investments is a discounted cash flow model that considers various inputs including: (a) the coupon rate specified under the debt instruments, (b) the current credit ratings of the underlying issuers, (c) collateral characteristics and (d) risk-adjusted discount rates. Level 3 instruments primarily include derivative instruments, such as basis swaps, commodity options including, price collars, floors and three-way collars, and other financial investments. Although we utilize third-party broker quotes to assess the reasonableness of our prices and valuation techniques for derivative instruments, we do not have sufficient corroborating market evidence to support classifying these assets and liabilities as Level 2.

Financial assets and liabilities are classified based on the lowest level of input that is significant to the fair value measurement. Our assessment of the significance of a particular input to the fair value measurement requires judgment and may affect the valuation of the fair value of assets and liabilities and their placement within the fair value hierarchy levels.

Fair Value of Investments and Derivative Instruments

The following table summarizes the valuation of our investments and financial instrument assets (liabilities) by pricing levels:

	Fair Value Measurement Classification			
	Quoted Prices in Active Markets for Identical Assets or Liabilities (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Total
	(In millions)			
As of December 31, 2011:				
Investments available-for-sale:				
Equity securities	$ 10	$ —	$ —	$ 10
Auction rate securities	—	—	32	32
Oil and gas derivative swap contracts	—	66	(10)	56
Oil and gas derivative option contracts	—	—	81	81
Total	$ 10	$ 66	$ 103	$ 179
As of September 30, 2012:				
Money market fund investments	$ 13	$ —	$ —	$ 13
Investments available-for-sale:				
Equity securities	12	—	—	12
Auction rate securities	—	—	34	34
Oil and gas derivative swap contracts	—	(27)	(3)	(30)
Oil and gas derivative option contracts	—	—	105	105
Total	$ 25	$ (27)	$ 136	$ 134

The determination of the fair values above incorporates various factors, which include not only the impact of our non-performance risk on our liabilities but also the credit standing of the counterparties involved and the impact of credit enhancements (such as cash deposits, letters of credit and priority interests), if any. We utilize credit default swap values to assess the impact of non-performance risk when evaluating both our liabilities to and receivables from counterparties.

As of September 30, 2012, we held $34 million of auction rate securities maturing beginning in 2033 that are classified as a Level 3 fair value measurement. This amount reflects a decrease in the fair value of these investments of $11 million ($7 million net of tax) recorded under the caption “Accumulated other comprehensive loss” on our consolidated balance sheet. As of December 31, 2011, we held $32 million of auction rate securities, which reflected a decrease in the fair value of $13 million ($8 million net of tax). The debt instruments underlying our auction rate securities are mostly investment grade (rated BBB or better) and are guaranteed by the United States government or backed by private loan collateral. We do not believe the decrease in the fair value of these securities is permanent because we currently intend to hold these investments until the auction succeeds, the issuer calls the securities or the securities mature. Our current available borrowing capacity under our credit arrangements provides us the liquidity to continue to hold these securities.

NEWFIELD EXPLORATION COMPANY
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

The following table sets forth a reconciliation of changes in the fair value of financial assets and liabilities classified as Level 3 in the fair value hierarchy for the indicated periods:

	Investments	Derivatives	Total
		(In millions)	
Balance at January 1, 2011	$30	$48	$78
Total realized or unrealized gains (losses):			
Included in earnings	—	163	163
Included in other comprehensive income	3	—	3
Purchases, issuances and settlements:			
Settlements	(1)	(42)	(43)
Transfers in and out of Level 3	—	—	—
Balance at September 30, 2011	$32	$169	$201
Change in unrealized gains or losses included in earnings relating to investments and derivatives still held at September 30, 2011	$—	$150	$150
Balance at January 1, 2012	$32	$71	$103
Total realized or unrealized gains (losses):			
Included in earnings	—	100	100
Included in other comprehensive income	2	—	2
Purchases, issuances and settlements:			
Settlements	—	(69)	(69)
Transfers in and out of Level 3	—	—	—
Balance at September 30, 2012	$34	$102	$136
Change in unrealized gains or losses included in earnings relating to investments and derivatives still held at September 30, 2012	$—	$67	$67

Qualitative Disclosures about Unobservable Inputs for Level 3 Fair Value Measurements

Commodity Derivatives. Our valuation models for derivative contracts are primarily industry-standard models that consider various factors, including certain significant unobservable inputs such as (a) quoted forward prices for commodities, (b) volatility factors and (c) counterparty credit risk. The calculation of the fair value of our option contracts requires the use of an option-pricing model. The estimated future prices are compared to the prices fixed by the hedge agreements and the resulting estimated future cash inflows or outflows over the lives of the hedges are discounted to calculate the fair value of the derivative contracts. These pricing and discounting variables are sensitive to market volatility as well as changes in future price forecasts, regional price differences and interest rates. Significant increases (decreases) in the quoted forward prices for commodities generally leads to corresponding decreases (increases) in the fair value measurement of our oil and gas derivative contracts. Significant changes in the volatility factors utilized in our option-pricing model can cause significant changes in the fair value measurement of our oil and gas derivative contracts.

The determination of the fair values of derivative instruments incorporates various factors that include not only the impact of our non-performance risk on our liabilities but also the credit standing of the counterparties involved and the impact of credit enhancements (such as cash deposits, letters of credit and priority interests). Historically, we have not experienced significant changes in the fair value of our derivative contracts resulting from changes in counterparty credit risk as the counterparties for all of our hedging transactions have an “investment grade” credit rating.

Auction Rate Securities. We utilize a discounted cash flow model in the determination of the valuation of our auction rate securities classified as Level 3. This model considers various inputs including (a) the coupon rate specified under the debt instrument, (b) the current credit rating of the underlying issuers, (c) collateral characteristics and (d) risk-adjusted discount rates. The most significant unobservable factor in the determination of the investments fair value, however, is market liquidity for these instruments. A significant change in the liquidity of the market for auction rate securities would lead to a corresponding change in the fair value measurement of these investments.

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NEWFIELD EXPLORATION COMPANY
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

Quantitative Disclosures about Unobservable Inputs

Instrument Type	Estimated Fair Value Asset (Liability) (In millions)	Quantitative Information about Level 3 Fair Value Measurements				
		Valuation Technique	Unobservable Input	Range		
Basis contracts	$ (3)	Discounted cash flow	NYMEX Natural gas price forward curve	$ 2.93	-	$ 3.62
			Physical pricing point forward curves	$ 2.72	-	$ 3.50
			Credit risk	0.02 %	-	0.08 %
Oil 3-way collar contracts	$ 45	Option model	NYMEX Oil price forward curve	$ 90.77	-	$ 94.12
			Oil price volatility curves	22.32 %	-	39.69 %
			Credit risk	0.01 %	-	4.00 %
Natural gas collars and 3-way collar contracts	$ 60	Option model	NYMEX Natural gas price forward curve	$ 2.93	-	$ 4.44
			Natural gas price volatility curves	23.12 %	-	44.24 %
			Credit risk	0.01 %	-	4.08 %

The underlying inputs in the determination of the valuation of our auction rate securities are developed by a third party and, therefore, not included in the quantitative analysis above.

Fair Value of Debt

The estimated fair value of our notes, based on quoted prices in active markets (Level 1) as of the indicated dates, was as follows:

	September 30, 2012	December 31, 2011
	(In millions)	
5¾% Senior Notes due 2022	$840	$808
5 % Senior Notes due 2024	1,117	—
6 % Senior Subordinated Notes due 2014	—	329
6 % Senior Subordinated Notes due 2016	—	568
7 % Senior Subordinated Notes due 2018	635	635
6 % Senior Subordinated Notes due 2020	770	745

Amounts outstanding under our credit arrangements at September 30, 2012 and December 31, 2011 are stated at cost, which approximates fair value. Please see Note 8, “Debt.”

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NEWFIELD EXPLORATION COMPANY
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8. Debt:

Debt consisted of the following at:

	September 30, 2012	December 31, 2011
	(In millions)	
Senior unsecured debt:		
Revolving credit facility LIBOR based loans	$145	$85
Money market lines of credit(1)	—	1
Total credit arrangements	145	86
5¾% Senior Notes due 2022	750	750
5 % Senior Notes due 2024	1,000	—
Total senior unsecured debt	1,895	836
6 % Senior Subordinated Notes due 2014	—	325
6 % Senior Subordinated Notes due 2016	—	550
7 % Senior Subordinated Notes due 2018	600	600
6 % Senior Subordinated Notes due 2020	695	695
Total long-term debt	$3,190	$3,006

(1) Because capacity under our credit facility was available to repay borrowings under our money market lines of credit as of the indicated dates, amounts outstanding under these obligations, if any, are classified as long-term.

Credit Arrangements

We have a revolving credit facility that matures in June 2016. The terms of the credit facility provide for loan commitments of $1.25 billion from a syndicate of 13 financial institutions, led by JPMorgan Chase Bank, N.A., as agent. In September 2011, we entered into the first amendment to the credit facility, which allows us to issue senior notes or other debt instruments that are secured equally and ratably with the credit facility. As of September 30, 2012, the largest individual loan commitment by any lender was 13% of total commitments.

Loans under the credit facility bear interest, at our option, equal to (a) a rate per annum equal to the higher of the prime rate announced from time to time by JPMorgan Chase Bank, N.A. or the weighted average of the rates on overnight federal funds transactions with members of the Federal Reserve System during the last preceding business day plus 50 basis points, plus a margin that is based on a grid of our debt rating (75 basis points per annum at September 30, 2012) or (b) the London Interbank Offered Rate, plus a margin that is based on a grid of our debt rating (175 basis points per annum at September 30, 2012).

Under our credit facility, we pay commitment fees on available but undrawn amounts based on a grid of our debt rating (30 basis points per annum at September 30, 2012). We incurred aggregate commitment fees under our current credit facility of approximately $0.9 million and $2.5 million for the three and nine months ended September 30, 2012, respectively, which are recorded in “Interest expense” on our consolidated statement of net income. For the three and nine months ended September 30, 2011, we incurred commitment fees under our current and previous credit facility of approximately $0.3 million and $1.2 million, respectively.

Our credit facility has restrictive covenants that include the maintenance of a ratio of total debt to book capitalization not to exceed 0.6 to 1.0 and maintenance of a ratio of earnings before gain or loss on the disposition of assets, interest expense, income taxes and noncash items (such as depreciation, depletion and amortization expense, unrealized gains and losses on commodity derivatives, ceiling test writedowns, and goodwill impairments) to interest expense of at least 3.0 to 1.0. At September 30, 2012, we were in compliance with all of our debt covenants.

As of September 30, 2012, we had $15 million of undrawn letters of credit outstanding under our credit facility. Letters of credit are subject to a fronting fee of 20 basis points and annual fees based on a grid of our debt rating (175 basis points at September 30, 2012). Additionally, as of September 30, 2012, we had $5 million of other undrawn letters of credit outstanding.

Subject to compliance with the restrictive covenants in our credit facility, we also have a total of $195 million of borrowing capacity under money market lines of credit with various financial institutions, the availability of which is at the discretion of the financial institutions.

The credit facility includes events of default relating to customary matters, including, among other things, nonpayment of principal, interest or other amounts; violation of covenants; inaccuracy of representations and warranties in any material respect; a change of control; or certain other material adverse changes in our business. Our senior notes and senior subordinated notes also contain standard events of default. If any of the foregoing defaults were to occur, our lenders under the credit facility could terminate future lending commitments and our lenders under both the credit facility and our notes could declare the outstanding borrowings due and payable. In addition, our credit facility, senior notes, senior subordinated notes and substantially all of our hedging arrangements contain provisions that provide for cross defaults and acceleration of those debt and hedging instruments in certain situations.

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Senior and Senior Subordinated Notes

In September 2011, we issued $750 million of 5¾% Senior Notes due 2022 and received proceeds of $742 million (net of discount and offering costs). These notes were issued at 99.956% of par to yield 5¾%. We used the net proceeds to repay a portion of our then outstanding borrowings under our credit facility and money market lines of credit.

In April 2012, we redeemed our $325 million aggregate principal of 6 % Senior Subordinated Notes due 2014 at 101.1042% of the principal amount plus accrued interest, which included the payment of an early redemption premium of $4 million. This premium was recorded under the caption "Other income (expenses) – Other" on our consolidated statement of net income. The repayment of the outstanding principal balance of $325 million was funded through the use of our revolving credit facility. In addition, unamortized offering costs of approximately $0.6 million were written off.

In June 2012, we issued $1 billion of 5 % Senior Notes due 2024 and received proceeds of $990 million (net of offering costs of approximately $10 million). These notes were issued at par to yield 5 %. We used a portion of the net proceeds to repay borrowings outstanding under our credit facility and money market lines of credit, as well as in July 2012, redeem our $550 million aggregate principal amount of 6 % Senior Subordinated Notes due 2016. In connection with the redemption, we paid a premium of $14 million. The premium was recorded under the caption "Other income (expenses) – Other" on our consolidated statement of income. In addition, unamortized offering costs of approximately $2 million were written off in July 2012 as a result of the repayment.

9. Income Taxes:

The provision (benefit) for income taxes for the indicated periods was different than the amount computed using the federal statutory rate (35%) for the following reasons:

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2012	2011	2012	2011
	(In millions)			
Amount computed using the statutory rate	$(15)	$148	$125	$260
Increase (decrease) in taxes resulting from:				
State and local income taxes, net of federal effect	(1)	4	3	9
Net effect of different tax rates in non-U.S. jurisdictions	5	—	11	1
Other	—	3	—	3
Total provision (benefit) for income taxes	$(11)	$155	$139	$273

As of September 30, 2012, we did not have a liability for uncertain tax positions and as such we had not accrued related interest or penalties. The tax years 2009-2011 remain open to examination for federal income tax purposes and by the other major taxing jurisdictions to which we are subject.

10. Stock-Based Compensation:

All stock-based compensation equity awards to employees and non-employee directors are granted currently under the 2011 Omnibus Stock Plan. The fair value of grants is determined utilizing the Black-Scholes option-pricing model for stock options and a lattice-based model for our performance and market-based restricted stock and restricted stock units. In February 2011, we also granted cash-settled restricted stock units to employees. These awards were not issued under any of our plans as they will be settled in cash upon vesting and are accounted for as liability awards.

As of the indicated dates, our stock-based compensation consisted of the following:

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2012	2011	2012	2011
	(In millions)			
Total stock-based compensation	$13	$9	$37	$28
Capitalized in oil and gas properties	(3)	(3)	(10)	(8)
Net stock-based compensation expense	$10	$6	$27	$20

As of September 30, 2012, we had approximately $94 million of total unrecognized stock-based compensation expense related to unvested stock-based compensation awards. This compensation expense is expected to be recognized on a straight-line basis over the applicable remaining vesting periods. The full amount is expected to be recognized within five years.

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Stock Options. The following table provides information about stock option activity for the nine months ended September 30, 2012:

	Number of Shares Underlying Options (In millions)	Weighted-Average Exercise Price per Share	Weighted-Average Grant Date Fair Value per Share	Weighted-Average Remaining Contractual Life (In years)	Aggregate Intrinsic Value(1) (In millions)
Outstanding at December 31, 2011	1.1	$36.31		4.0	$7
Granted	—	—	$—		
Exercised/Forfeited	(0.1)	20.30			1
Outstanding at September 30, 2012	1.0	$37.52		3.5	$2
Exercisable at September 30, 2012	0.9	$36.61		3.3	$2

(1) The intrinsic value of a stock option is the amount by which the market value of our common stock at the indicated date, or at the time of exercise, exceeds the exercise price of the option.

On September 30, 2012, the last reported sales price of our common stock on the New York Stock Exchange was $31.32 per share.

Restricted Stock. The following table provides information about restricted stock and restricted stock unit activity for the nine months ended September 30, 2012:

	Service-Based Shares	Performance/ Market-Based Shares	Total Shares	Weighted-Average Grant Date Fair Value per Share
	(In millions, except per share data)			
Non-vested shares outstanding at December 31, 2011	2.2	0.3	2.5	$ 49.52
Granted	1.4	0.2	1.6	36.12
Forfeited	(0.2)	—	(0.2)	47.73
Vested	(0.9)	(0.1)	(1.0)	41.80
Non-vested shares outstanding at September 30, 2012	2.5	0.4	2.9	$ 44.37

Cash-Settled Restricted Stock Units. During the first quarter of 2011, we granted cash-settled restricted stock units to employees that vest over three years. The value of the awards, and the associated stock-based compensation expense, is based on the Company’s stock price. In February 2012, the first tranche of the 2011 grants vested, which required settlement of approximately 44,000 cash-settled restricted units for approximately $1.7 million. As of

September 30, 2012, approximately 77,000 cash-settled restricted units were outstanding.

Employee Stock Purchase Plan. Pursuant to our employee stock purchase plan, for each six-month period beginning on January 1 or July 1 during the term of the plan, each eligible employee has the opportunity to purchase our common stock for a purchase price equal to 85% of the lesser of the fair market value of our common stock on the first day of the period or the last day of the period.

During the first six months of 2012, options to purchase approximately 87,000 shares of our common stock were issued under our employee stock purchase plan. The weighted-average fair value of each option was $11.61 per share. The fair value of the options granted was determined using the Black-Scholes option valuation method assuming no dividends, a risk-free weighted-average interest rate of 0.06%, an expected life of six months and weighted-average volatility of 55%.

On July 1, 2012, options to purchase approximately 83,000 shares of our common stock were issued under our employee stock purchase plan. The weighted-average fair value of each option was $7.93 per share. The fair value of the options granted was determined using the Black-Scholes option valuation method assuming no dividends, a risk-free weighted-average interest rate of 0.15%, an expected life of six months and weighted-average volatility of 44%.

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11. Commitments and Contingencies:

We have been named as a defendant in a number of lawsuits and are involved in various other disputes, all arising in the ordinary course of our business, such as (a) claims from royalty owners for disputed royalty payments, (b) commercial disputes, (c) personal injury claims and (d) property damage claims. Although the outcome of these lawsuits and disputes cannot be predicted with certainty, we do not expect these matters to have a material adverse effect on our financial position, cash flows or results of operations.

12. Segment Information:

While we only have operations in the oil and gas exploration and production industry, we are organizationally structured along geographic operating segments. Our current operating segments are the United States, Malaysia, and China. The accounting policies of each of our operating segments are the same as those described in Note 1, “Organization and Summary of Significant Accounting Policies.”

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The following tables provide the geographic operating segment information for the three and nine months ended September 30, 2012 and 2011. Income tax allocations have been determined based on statutory rates in the applicable geographic segment.

Three Months Ended
September 30, 2012:

	Domestic	Malaysia	China	Total
		(In millions)		
Oil and gas revenues	$ 371	$ 228	$ 16	$ 615
Operating expenses:				
Lease operating	99	27	2	128
Production and other taxes	17	59	3	79
Depreciation, depletion and amortization	172	61	4	237
General and administrative	57	2	—	59
Other	6	—	—	6
Allocated income tax	7	30	2	
Net income from oil and gas properties	$ 13	$ 49	$ 5	
Total operating expenses				509
Income from operations				106
Interest expense, net of interest income, capitalized interest and other				(52)
Commodity derivative expense				(98)
Loss before income taxes				$ (44)
Total assets	$ 8,235	$ 878	$ 318	$ 9,431
Additions to long-lived assets	$ 362	$ 61	$ 30	$ 453

Three Months Ended
September 30, 2011:

	Domestic	Malaysia	China	Total
		(In millions)		
Oil and gas revenues	$ 444	$ 159	$ 25	$ 628
Operating expenses:				
Lease operating	93	21	1	115
Production and other taxes	19	71	5	95
Depreciation, depletion and amortization	154	29	6	189
General and administrative	49	1	1	51
Allocated income tax	48	14	3	
Net income from oil and gas properties	$ 81	$ 23	$ 9	

Total operating expenses				450
Income from operations				178
Interest expense, net of interest income, capitalized interest and other				(16)
Commodity derivative income				262
Income before income taxes				$ 424
Total assets	$ 7,879	$ 789	$ 235	$ 8,903
Additions to long-lived assets	$ 597	$ 81	$ 13	$ 691

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Nine Months Ended September 30, 2012:

	Domestic	Malaysia	China	Total
		(In millions)		
Oil and gas revenues	$1,124	$724	$73	$1,921
Operating expenses:				
Lease operating	305	73	6	384
Production and other taxes	53	182	15	250
Depreciation, depletion and amortization	510	175	17	702
General and administrative	161	4	—	165
Other	6	—	—	6
Allocated income tax	33	110	9	
Net income from oil and gas properties	$56	$180	$26	
Total operating expenses				1,507
Income from operations				414
Interest expense, net of interest income, capitalized interest and other				(118)
Commodity derivative income				61
Income before income taxes				$357
Total assets	$8,235	$878	$318	$9,431
Additions to long-lived assets	$1,246	$130	$50	$1,426

Nine Months Ended September 30, 2011:

	Domestic	Malaysia	China	Total
		(In millions)		
Oil and gas revenues	$1,313	$416	$65	$1,794
Operating expenses:				
Lease operating	260	69	4	333
Production and other taxes	56	173	16	245
Depreciation, depletion and amortization	440	73	15	528
General and administrative	128	3	1	132
Allocated income tax	159	37	7	