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

INDEX

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