SANDRIDGE ENERGY INC
Form 10-Q
November 07, 2011
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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, 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 October 31, 2011, was 412,099,692.

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SANDRIDGE ENERGY, INC.

FORM 10-Q

Quarter Ended September 30, 2011

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PART I. FINANCIAL INFORMATION

PART II. OTHER INFORMATION

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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, the Company s liquidity and capital resources, the timing and success of specific projects, outcomes and effects of litigation, claims and disputes, elements of the Company s business strategy and other statements concerning the Company s 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 plan, goal, should, intend or other words that convey the uncertainty of future events or outcomes. We have based these forward-looking statements on the Company s current expectations and assumptions about future events. These statements are based on certain assumptions and analyses made by the Company in light of its experience and perception of historical trends, current conditions and expected future developments as well as other factors the Company believes are appropriate under the circumstances. However, whether actual results and developments will conform with the Company s 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 the Company s 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 the 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. The Company undertakes no obligation to publicly update or revise any forward-looking statements.

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PART I. Financial Information

ITEM 1. ***Financial Statements***

SANDRIDGE ENERGY, INC. AND SUBSIDIARIES

CONDENSED CONSOLIDATED BALANCE SHEETS

(In thousands, except per share data)

	September 30, 2011 (Unaudited)	December 31, 2010
ASSETS		
Current assets		
Cash and cash equivalents	$ 325,437	$ 5,863
Accounts receivable, net	174,396	146,118
Derivative contracts	96,457	5,028
Inventories	11,672	3,945
Other current assets	20,032	14,636
Total current assets	627,994	175,590
Oil and natural gas properties, using full cost method of accounting		
Proved	8,697,142	8,159,924
Unproved	681,886	547,953
Less: accumulated depreciation, depletion and impairment	(4,707,089)	(4,483,736)
	4,671,939	4,224,141
Other property, plant and equipment, net	531,875	509,724
Restricted deposits	27,892	27,886
Derivative contracts	213,901	
Goodwill	235,396	234,356
Other assets	109,716	59,751
Total assets	$ 6,418,713	$ 5,231,448
LIABILITIES AND EQUITY		
Current liabilities		
Current maturities of long-term debt	$ 1,035	$ 7,293
Accounts payable and accrued expenses	413,830	376,922
Billings and estimated contract loss in excess of costs incurred	42,269	31,474
Derivative contracts	9,020	103,409
Asset retirement obligation	25,360	25,360
Total current liabilities	491,514	544,458
Long-term debt	2,812,775	2,901,793
Derivative contracts	6,867	124,173
Asset retirement obligation	97,223	94,517
Other long-term obligations	24,430	19,024

Total liabilities	3,432,809	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 September 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 September 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 September 30, 2011 and December 31, 2010; aggregate liquidation preference of $300,000	3	3
Common stock, $0.001 par value, 800,000 shares authorized; 412,986 issued and 412,400 outstanding at September 30, 2011 and 406,830 issued and 406,360 outstanding at December 31, 2010	399	398
Additional paid-in capital	4,557,005	4,528,912
Treasury stock, at cost	(4,700)	(3,547)
Accumulated deficit	(2,548,497)	(2,989,576)
Total SandRidge Energy, Inc. stockholders equity	2,004,215	1,536,195
Noncontrolling interest	981,689	11,288
Total equity	2,985,904	1,547,483
Total liabilities and equity	$ 6,418,713	$ 5,231,448

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

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SANDRIDGE ENERGY, INC. AND SUBSIDIARIES

CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS

(In thousands, except per share data)

	Three Months Ended September 30, 2011	Three Months Ended September 30, 2010	Nine Months Ended September 30, 2011	Nine Months Ended September 30, 2010
	(Unaudited)			
Revenues				
Oil and natural gas	$ 318,453	$ 209,998	$ 897,506	$ 529,578
Drilling and services	25,547	5,252	75,118	14,913
Midstream and marketing	15,092	23,281	53,663	73,868
Other	4,661	6,702	15,088	20,308
Total revenues	363,753	245,233	1,041,375	638,667
Expenses				
Production	86,580	66,086	242,371	172,367
Production taxes	10,368	8,904	33,610	19,146
Drilling and services	16,209	4,187	49,308	12,420
Midstream and marketing	14,624	20,779	52,780	66,064
Depreciation and depletion oil and natural gas	86,725	91,237	236,798	197,834
Depreciation and amortization other	13,551	12,441	39,918	36,564
General and administrative	36,272	61,878	108,364	127,419
(Gain) loss on derivative contracts	(596,736)	67,195	(489,096)	(114,378)
(Gain) loss on sale of assets	(422)	(44)	(1,148)	39
Total expenses	(332,829)	332,663	272,905	517,475
Income (loss) from operations	696,582	(87,430)	768,470	121,192
Other income (expense)				
Interest income	51	69	94	236
Interest expense	(59,003)	(63,641)	(180,171)	(189,989)
Loss on extinguishment of debt			(38,232)	
Other (expense) income, net	(672)	1,356	662	2,062
Total other expense	(59,624)	(62,216)	(217,647)	(187,691)
Income (loss) before income taxes	636,958	(149,646)	550,823	(66,499)
Income tax expense (benefit)	954	(457,248)	(6,013)	(457,086)
Net income	636,004	307,602	556,836	390,587
Less: net income attributable to noncontrolling interest	60,895	1,313	74,055	3,547
Net income attributable to SandRidge Energy, Inc.	575,109	306,289	482,781	387,040
Preferred stock dividends	13,881	8,632	41,702	25,894
Income available to SandRidge Energy, Inc. common stockholders	$ 561,228	$ 297,657	$ 441,079	$ 361,146
Earnings per share				
Basic	$ 1.41	$ 0.82	$ 1.11	$ 1.41

Diluted	$	1.16	$	0.73	$	0.97	$	1.24
Weighted average number of common shares outstanding								
Basic		399,270		361,687		398,656		257,028
Diluted		497,700		419,137		496,428		313,283

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

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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)				
Nine months ended September 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 royalty trusts								917,528	917,528
Distributions to noncontrolling interest owners								(21,182)	(21,182)
Stock issuance expense					(231)				(231)
Purchase of treasury stock						(10,626)			(10,626)
Retirement of treasury stock					(10,626)	10,626			
Stock purchases retirement plans, net of distributions			(116)		2,563	(1,153)			1,410
Stock-based compensation					36,336				36,336
Stock-based compensation excess tax benefit					52				52
Issuance of restricted stock awards, net of cancellations			6,156	1	(1)				
Net income							482,781	74,055	556,836
Convertible perpetual preferred stock dividends							(41,702)		(41,702)
Balance, September 30, 2011	7,650	$ 8	412,400	$ 399	$ 4,557,005	$ (4,700)	$ (2,548,497)	$ 981,689	$ 2,985,904

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

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SANDRIDGE ENERGY, INC. AND SUBSIDIARIES

CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS

(In thousands)

	Nine Months Ended September 30, 2011	2010
	(Unaudited)	
CASH FLOWS FROM OPERATING ACTIVITIES		
Net income	$ 556,836	$ 390,587
Adjustments to reconcile net income to net cash provided by operating activities		
Provision for doubtful accounts	1,622	102
Inventory obsolescence	145	200
Depreciation, depletion and amortization	276,716	234,398
Debt issuance costs amortization	8,624	8,044
Discount amortization on long-term debt	1,766	1,595
Loss on extinguishment of debt	38,232	
Deferred income taxes	(6,986)	(456,437)
Unrealized (gain) loss on derivative contracts	(527,166)	135,364
(Gain) loss on sale of assets	(1,148)	39
Investment loss (income)	653	(191)
Stock-based compensation	28,458	24,174
Changes in operating assets and liabilities	(49,796)	1,337
Net cash provided by operating activities	327,956	339,212
CASH FLOWS FROM INVESTING ACTIVITIES		
Capital expenditures for property, plant and equipment	(1,311,383)	(694,187)
Acquisition of assets, net of cash received of $0 and $39,518, respectively	(22,751)	(138,428)
Proceeds from sale of assets	624,767	113,422
Refunds of restricted deposits		5,095
Net cash used in investing activities	(709,367)	(714,098)
CASH FLOWS FROM FINANCING ACTIVITIES		
Proceeds from borrowings	2,033,000	1,595,914
Repayments of borrowings	(2,130,042)	(1,179,083)
Premium on debt redemption	(30,338)	
Debt issuance costs	(19,652)	(11,720)
Proceeds from issuance of royalty trust units	917,528	
Distributions to royalty trust unitholders	(18,431)	
Noncontrolling interest distributions	(2,751)	(3,511)
Noncontrolling interest contributions		306
Stock issuance expense	(231)	(87)
Stock-based compensation excess tax benefit	52	31
Purchase of treasury stock	(12,048)	(5,335)
Dividends paid preferred	(46,243)	(28,525)
Derivative settlements	10,141	1,624
Net cash provided by financing activities	700,985	369,614

NET INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS		319,574		(5,272)
CASH AND CASH EQUIVALENTS, beginning of year		5,863		7,861
CASH AND CASH EQUIVALENTS, end of period	$	325,437	$	2,589
Supplemental Disclosure of Noncash Investing and Financing Activities				
Change in accrued capital expenditures	$	22,010	$	101,406
Convertible perpetual preferred stock dividends payable	$	13,191	$	5,816
Adjustment to oil and natural gas properties for estimated contract loss	$	19,000	$	98,000
Common stock issued in connection with acquisition	$		$	1,246,334

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

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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 and the Mississippian formation in the Mid-Continent. The Company owns and operates other interests in the West Texas Overthrust (WTO), Mid-Continent, 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 unaudited condensed consolidated financial statements should be read in conjunction with the financial statements and notes thereto included in the 2010 Form 10-K.

Reclassifications. Certain amounts in the prior periods presented have been reclassified to conform to the current period presentation. These reclassifications have no effect on the Company s previously reported results of operations.

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 fixed price swap 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 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. 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 the remainder of 2011 and for 2012. 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.

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

SANDRIDGE ENERGY, INC. AND SUBSIDIARIES

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

(Unaudited)

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 by the Company in the first quarter of 2011. The implementation of ASU 2010-06 had no impact on the Company s financial position or results of operations. See Note 4.

Recent Accounting Pronouncements 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 on the Company s financial position or results of operations is expected.

In September 2011, the FASB issued Accounting Standards Update 2011-08, Testing Goodwill for Impairment (ASU 2011-08). ASU 2011-08 allows an entity the option of performing a qualitative assessment to determine whether it is necessary to perform the current two-step annual impairment test. If an entity determines, on the basis of qualitative factors, that the fair value of the reporting unit more-likely-than-not exceeds the carrying amount, the two-step impairment test is not required. ASU 2011-08 does not change how goodwill is calculated or assigned to reporting units, nor does it revise the requirement to test goodwill annually for impairment or amend the requirement to test goodwill for impairment between annual tests if events or circumstances warrant. ASU 2011-08 is effective for annual and interim goodwill impairment tests performed for fiscal years beginning after December 15, 2011, with early adoption permitted. The Company is currently evaluating the impact of this guidance, which it will adopt on January 1, 2012.

3. Acquisitions and Divestitures

Arena Acquisition. On July 16, 2010, the Company acquired all of the outstanding common stock of Arena Resources, Inc. (Arena) for an aggregate purchase price of approximately $1.4 billion. In connection with the acquisition (the Arena Acquisition), the Company incurred approximately $0.6 million and $15.4 million in fees related to the acquisition during the nine-month periods ended September 30, 2011 and 2010, respectively, which have been included in general and administrative expenses in the accompanying unaudited 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 six months of 2011, the Company updated certain estimates used in the purchase price allocation, primarily with respect to deferred taxes and other accruals, resulting in adjustments of $1.0 million to goodwill.

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 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.

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SANDRIDGE ENERGY, INC. AND SUBSIDIARIES

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

(Unaudited)

(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 nine-month periods ended September 30, 2010 as though the Arena Acquisition had been completed as of the beginning of the respective period. The pro forma information is based on the Company s consolidated results of operations for the three and nine-month periods ended September 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 nine-month periods ended September 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.

	Three Months Ended September 30, 2010		Nine Months Ended September 30, 2010	
	Actual	Pro Forma	Actual	Pro Forma
	(in thousands, except per share data)			
Revenues	$ 245,233	$ 253,955	$ 638,667	$ 753,500
Income available to SandRidge Energy, Inc. common stockholders(1)	$ 297,657	$ 285,299	$ 361,146	$ 367,599
Earnings per common share				
Basic	$ 0.82	$ 0.72	$ 1.41	$ 0.93
Diluted	$ 0.73	$ 0.65	$ 1.24	$ 0.87

(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 agreed to sell its Wolfberry assets in the Permian Basin for $151.6 million, net of fees and post-closing adjustments. This asset sale was accounted for as an adjustment to the full cost pool with no gain or loss recognized. The sale was completed in July 2011.

Sale of New Mexico Assets. In April 2011, the Company agreed to sell certain oil and natural gas properties in Lea County and Eddy County, New Mexico, for approximately $199.0 million, net of fees and post-closing adjustments. This asset sale was accounted for as an adjustment to the full cost pool with no gain or loss recognized. The sale was completed in August 2011.

Sale of Working Interest in Mississippian Properties. In September 2011, the Company sold to Atinum MidCon I, LLC (Atinum) 13.2% of its working interest in approximately 860,000 acres the Company has leased in the Mississippian formation in the Mid-Continent. As consideration for the working interest, Atinum paid the Company approximately $270.7 million in cash (including approximately $4.9 million attributable to the Atinum drilling carry described herein and approximately $7.7 million not attributable to the Atinum drilling carry, but to be applied against the Company s future capital expenditures on the properties) and committed to pay 13.2% of SandRidge s share of drilling and completion costs for wells drilled within an area of mutual interest until an additional $250.0 million has been paid (Atinum drilling carry), which is expected to occur over a three-year period. The sale of the working interest was accounted for as an adjustment to the full cost pool with no gain or loss recognized. The amounts received attributable to the Atinum drilling carry will reduce the Company s capital expenditures.

Sale of East Texas Properties. In September 2011, the Company agreed to sell its East Texas natural gas properties in Gregg, Harrison, Rusk and Panola counties for $231.0 million, subject to post closing adjustments. The Company expects the transaction to close in the fourth quarter of 2011.

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SANDRIDGE ENERGY, INC. AND SUBSIDIARIES

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

(Unaudited)

4. Fair Value Measurements

The Company applies the guidance provided under ASC Topic 820 to its financial assets and 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, considers 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 September 30, 2011 or December 31, 2010.

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 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, natural gas and diesel 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, which include 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):

September 30, 2011

	Fair Value Measurements				Assets / Liabilities at Fair Value
	Level 1	Level 2	Level 3	Netting(1)	
Assets					
Restricted deposits	$ 27,892	$	$	$	$ 27,892
Commodity derivative contracts			312,093	(1,735)	310,358
Other assets	5,714				5,714
	$ 33,606	$	$ 312,093	$ (1,735)	$ 343,964
Liabilities					
Commodity derivative contracts	$	$	$ 4,302	$ (1,735)	$ 2,567
Interest rate swaps			13,320		13,320
	$	$	$ 17,622	$ (1,735)	$ 15,887

SANDRIDGE ENERGY, INC. AND SUBSIDIARIES

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

(Unaudited)

December 31, 2010

	Fair Value Measurements				Assets / Liabilities at Fair Value
	Level 1	Level 2	Level 3	Netting(1)	
Assets					
Restricted deposits	$ 27,886	$	$	$	$ 27,886
Commodity derivative contracts			10,576	(5,548)	5,028
Other assets	4,826				4,826
	$ 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

(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 nine-month periods ended September 30, 2011 and 2010 (in thousands):

	$(000,000)	$(000,000)	$(000,000)	$(000,000)	$(000,000)	$(000,000)
	Three Months Ended September 30,					
	2011			2010		
	Commodity Derivative Contracts	Interest Rate Swaps	Total	Commodity Derivative Contracts	Interest Rate Swaps	Total
Balance of Level 3, June 30	$ (293,633)	$ (15,285)	$ (308,918)	$ 67,178	$ (16,548)	$ 50,630
Total realized and unrealized gains (losses)	596,736	(555)	596,181	(67,195)	(5,136)	(72,331)
Purchases	(3,126)		(3,126)	24,929		24,929
Settlements	7,814	2,520	10,334	(77,693)	1,883	(75,810)
Balance of Level 3, September 30	$ 307,791	$ (13,320)	$ 294,471	$ (52,781)	$ (19,801)	$ (72,582)

	$(000,000)	$(000,000)	$(000,000)	$(000,000)	$(000,000)	$(000,000)
	Nine Months Ended September 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	489,096	(3,631)	485,465	114,378	(17,548)	96,830
Purchases	(10,141)		(10,141)	24,929		24,929
Settlements	34,696	7,005	41,701	(238,241)	6,046	(232,195)
Balance of Level 3, September 30	$ 307,791	$ (13,320)	$ 294,471	$ (52,781)	$ (19,801)	$ (72,582)

During the three and nine-month periods ended September 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 which consider the effect of the Company s credit risk. The estimated fair values and the carrying values of the Company s senior notes at September 30, 2011 and December 31, 2010 were as follows (in thousands):

	September 30, 2011		December 31, 2010	
	Fair Value	Carrying Value	Fair Value	Carrying Value
Senior Floating Rate Notes due 2014	$ 338,846	$ 350,000	$ 334,751	$ 350,000
8.625% Senior Notes due 2015			663,181	650,000
9.875% Senior Notes due 2016(1)	385,603	354,093	394,527	352,707
8.0% Senior Notes due 2018	727,500	750,000	762,849	750,000
8.75% Senior Notes due 2020(2)	447,750	443,437	472,968	443,057
7.5% Senior Notes due 2021	837,000	900,000		

(1) Carrying value is net of $11,407 and $12,793 discount at September 30, 2011 and December 31, 2010, respectively.
(2) Carrying value is net of $6,563 and $6,943 discount at September 30, 2011 and December 31, 2010, respectively.

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SANDRIDGE ENERGY, INC. AND SUBSIDIARIES

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

(Unaudited)

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, both of which occurred during 2011.

5. Property, Plant and Equipment

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

	September 30, 2011	December 31, 2010
Oil and natural gas properties		