NEWFIELD EXPLORATION CO /DE/
Form 10-Q
May 01, 2006

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 March 31, 2006

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: 1-12534

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

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

363 North Sam Houston Parkway East
Suite 2020
Houston, Texas 77060
(Address and Zip Code of principal executive offices)

(281) 847-6000
(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 ¨

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

Large accelerated filer þ Accelerated filer ¨ Non-accelerated filer ¨

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Act).

Yes ¨ No þ

As of April 27, 2006, there were 128,609,519 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)

	March 31, 2006	December 31, 2005
ASSETS		
Current assets:		
Cash and cash equivalents	$ 41	$ 39
Accounts receivable	329	370
Inventories	31	22
Derivative assets	94	10
Deferred taxes	26	46
Other current assets	47	53
Total current assets	568	540
Oil and gas properties (full cost method, of which $941 at March 31, 2006 and $901 at December 31, 2005 were excluded from amortization)	7,433	7,042
Less—accumulated depreciation, depletion and amortization	(2,760)	(2,632)
	4,673	4,410
Furniture, fixtures and equipment, net	20	20
Derivative assets	8	17
Other assets	22	23
Deferred taxes	10	9
Goodwill	62	62
Total assets	$ 5,363	$ 5,081
LIABILITIES AND STOCKHOLDERS' EQUITY		
Current liabilities:		
Accounts payable	$ 53	$ 41
Accrued liabilities	457	454
Advances from joint owners	39	29
Asset retirement obligation	44	47
Derivative liabilities	126	99
Total current liabilities	719	670
Other liabilities	22	21
Derivative liabilities	236	209
Long-term debt	868	870
Asset retirement obligation	217	213
Deferred taxes	772	720
Total long-term liabilities	2,115	2,033
Commitments and contingencies (Note 5)	—	—

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 March 31, 2006 and December 31, 2005; 130,459,329 and 129,356,162 shares issued and outstanding at March 31, 2006 and December 31, 2005, respectively)		1		1
Additional paid-in capital		1,159		1,186
Treasury stock (at cost; 1,876,310 and 1,815,594 shares at March 31, 2006 and December 31, 2005, respectively)		(31)		(27)
Unearned compensation		—		(34)
Accumulated other comprehensive income (loss):				
Foreign currency translation adjustment		(4)		(4)
Commodity derivatives		(41)		(40)
Retained earnings		1,445		1,296
Total stockholders' equity		2,529		2,378
Total liabilities and stockholders' equity	$	5,363	$	5,081

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

NEWFIELD EXPLORATION COMPANY
CONSOLIDATED STATEMENT OF INCOME
(In millions, except per share data)
(Unaudited)

	Three Months Ended March 31, 2006	Three Months Ended March 31, 2005
Oil and gas revenues	$ 431	$ 413
Operating expenses:		
Lease operating	52	46
Production and other taxes	16	11
Depreciation, depletion and amortization	131	136
General and administrative	30	23
Business interruption insurance benefit	(30)	—
Total operating expenses	199	216
Income from operations	232	197
Other income (expenses):		
Interest expense	(18)	(18)
Capitalized interest	12	12
Commodity derivative income (expense)	6	(109)
Other	1	—
	1	(115)
Income before income taxes	233	82
Income tax provision:		
Current	11	16
Deferred	73	6
	84	22
Net income	$ 149	$ 60
Earnings per share:		
Basic	$ 1.18	$ 0.48
Diluted	$ 1.17	$ 0.47
Weighted average number of shares outstanding for basic earnings per share	126	124
Weighted average number of shares outstanding for diluted earnings per share	128	127

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NEWFIELD EXPLORATION COMPANY
CONSOLIDATED STATEMENT OF CASH FLOWS
(In millions)
(Unaudited)

	Three Months Ended March 31, 2006	Three Months Ended March 31, 2005
Cash flows from operating activities:		
Net income	$ 149	$ 60
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation, depletion and amortization	131	136
Deferred taxes	73	6
Stock-based compensation	7	1
Unrealized commodity derivative (income) expense	(8)	107
Changes in operating assets and liabilities:		
Decrease in accounts receivable	41	3
Increase in inventories	(7)	(8)
Decrease in other current assets	5	11
Decrease in other assets		1
Decrease in accounts payable and accrued liabilities	(45)	(52)
Decrease in commodity derivative liabilities	(16)	(5)
Increase in advances from joint owners	9	1
Increase in other liabilities	1	
Net cash provided by operating activities	340	261
Cash flows from investing activities:		
Additions to oil and gas properties	(337)	(245)
Additions to furniture, fixtures and equipment	(2)	(1)
Net cash used in investing activities	(339)	(246)
Cash flows from financing activities:		
Proceeds from borrowings under credit arrangements	229	258
Repayments of borrowings under credit arrangements	(229)	(315)
Proceeds from issuances of common stock	2	15
Stock-based compensation excess tax benefit	1	
Purchases of treasury stock	(3)	
Net cash used in financing activities		(42)
Effect of exchange rate changes on cash and cash equivalents	1	
Increase (decrease) in cash and cash equivalents	2	(27)
Cash and cash equivalents, beginning of period	39	58
Cash and cash equivalents, end of period	$ 41	$ 31

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

NEWFIELD EXPLORATION COMPANY
CONSOLIDATED STATEMENT OF STOCKHOLDERS' EQUITY
(In millions)
(Unaudited)

	Common Stock		Treasury Stock		Additional Paid-in	Unearned	Retained	Accumulated Other Comprehensive Income	Total Stockholders'
	Shares	Amount	Shares	Amount	Capital	Compensation	Earnings	(Loss)	Equity
Balance, December 31, 2005	129.4	$ 1	(1.8)	$ (27)	$ 1,186	$ (34)	$ 1,296	$ (44)	$ 2,378
Issuance of common and restricted stock	1.1				2				2
Stock-based compensation					4				4
Treasury stock, at cost			(0.1)	(4)					(4)
Tax benefit from stock-based compensation					1				1
Adoption of SFAS No. 123(R)					(34)	34			
Comprehensive income:									
Net income							149		149
Reclassification adjustments for settled hedging positions, net of tax of $9								(16)	(16)
Changes in fair value of outstanding hedging positions, net of tax of ($8)								15	15
Total comprehensive income									148
Balance, March 31, 2006	130.5	$ 1	(1.9)	$ (31)	$ 1,159	$	$ 1,445	$ (45)	$ 2,529

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 oil and gas company engaged in the exploration, development and acquisition of crude oil and natural gas properties. Our company was founded in 1989 and initially focused on the shallow waters of the Gulf of Mexico. Today, we have a diversified asset base. Our domestic areas of operation include the onshore Gulf Coast, the Anadarko and Arkoma Basins of the Mid-Continent, the Uinta Basin of the Rocky Mountains and the Gulf of Mexico. Internationally, we are active offshore Malaysia and China and in the U.K. North Sea.

Our financial statements include the accounts of Newfield Exploration Company, a Delaware corporation, and its subsidiaries. We proportionately consolidate our interests in oil and 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 state fairly 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, 2005.

Common Stock Split

Following the close of trading on May 25, 2005, we completed a two-for-one split of our common stock. The split was effected by a common stock dividend. The stated par value per share of our common stock was not changed from $0.01. The financial statements and notes as of and for the quarter ended March 31, 2005 have been restated to retroactively reflect the stock split.

Dependence on Oil and Gas Prices

As an independent oil and gas producer, our revenue, profitability and future rate of growth are substantially dependent on prevailing prices for natural gas and oil. Historically, the energy markets have been very volatile and it is likely that oil and gas prices will continue to be subject to wide fluctuations in the future. A substantial or extended decline in oil or 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 gas reserves that we can economically produce.

Use of Estimates

The preparation of our consolidated 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 gas reserves. Actual results could differ from these estimates. Our most significant financial estimates are related to our proved oil and gas reserves.

Reclassifications

Certain reclassifications have been made to prior years' reported amounts in order to conform with the current year presentation. These reclassifications did not impact our net income, stockholders' equity or cash flows.

NEWFIELD EXPLORATION COMPANY

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

Insurance Recoveries

During the first quarter of 2006, we recognized a $30 million benefit related to our business interruption insurance coverage as a result of Hurricanes Katrina and Rita.

Inventories

Inventories consist primarily of tubular goods and well equipment held for use in our oil and gas operations and oil produced but not sold. Inventories are carried at the lower of cost or market. Crude oil from our operations offshore Malaysia is produced into a floating production, storage and off-loading vessel and sold periodically as a barge quantity is accumulated. The product inventory consisted of approximately 172,000 barrels of crude oil valued at $4 million at March 31, 2006 and 36,000 barrels of crude oil valued at $1 million at December 31, 2005. Cost for purposes of the carrying value of oil inventory is a sum of production costs and depreciation, depletion and amortization expense.

Foreign Currency

The British pound is the functional currency for our operations in the United Kingdom. Translation adjustments resulting from translating our United Kingdom subsidiaries' British pound financial statements into U.S. dollars are included as accumulated other comprehensive income on our consolidated balance sheet and statement of stockholders' equity. The functional currency for all other foreign operations is the U.S. dollar. Gains and losses incurred on currency transactions in other than a country's functional currency are recorded under the caption "Other" on our consolidated statement of income.

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 asset retirement cost in oil and gas properties in the period in which the retirement obligation is incurred. In general, the amount of an ARO and the costs capitalized will be equal to the estimated future cost to satisfy the abandonment obligation 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 on our consolidated statement of income.

The change in our ARO for the three months ended March 31, 2006 is set forth below (in millions):

Balance as of January 1, 2006	$ 260
Accretion expense	4
Settlements	(3)
	261

Balance as of March 31, 2006	
Less: Current portion	44
Noncurrent ARO	$ 217

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NEWFIELD EXPLORATION COMPANY

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

Stock-Based Compensation

On January 1, 2006, we adopted SFAS No. 123 (revised 2004), "Share-Based Payment," (SFAS No. 123 (R)) to account for stock-based employee compensation. Among other items, SFAS No. 123(R) eliminates the use of APB 25 and the intrinsic value method of accounting and requires companies to recognize the cost of employee services received in exchange for awards of equity instruments based on the grant date fair value of those awards in their financial statements. We elected to use the modified prospective method for adoption, which requires compensation expense to be recorded for all unvested stock options and other equity-based compensation beginning in the first quarter of adoption. For all unvested options outstanding as of January 1, 2006, the previously measured but unrecognized compensation expense, based on the fair value at the original grant date, will be recognized in our financial statements over the remaining vesting period. For equity-based compensation awards granted or modified subsequent to January 1, 2006, compensation expense, based on the fair value on the date of grant, will be recognized in our financial statements over the vesting period. We utilize the Black-Scholes option pricing model to measure the fair value of stock options and a lattice-based model for our performance based restricted shares. Prior to the adoption of SFAS No. 123(R), we followed the intrinsic value method in accordance with APB 25 to account for employee stock-based compensation. Prior period financial statements have not been restated.

It is our policy to use unissued shares of stock when stock options are exercised. At March 31, 2006, we had approximately 2.6 million additional shares available for issuance pursuant to our existing employee and director plans. Of the shares available at March 31, 2006, only 1.2 million could be granted as restricted shares. Grants of restricted stock under the 2004 Omnibus Stock Plan reduce the total number of shares available under that plan by two times the number of shares issued as restricted stock.

The modified prospective method requires us to estimate forfeitures in calculating the expense related to stock-based compensation as opposed to our prior policy of recognizing the forfeitures as they occurred. We recorded a cumulative effect gain of a change in accounting principle of $1 million as a result of the adoption of this standard. Because the amount was immaterial, we included it in general and administrative expense on our consolidated statement of income.

The modified prospective method precludes changes to the grant date fair value of equity awards granted before the required effective date of adoption of SFAS No. 123(R). Any unearned compensation recorded under APB 25 related to these awards should be eliminated against the appropriate equity accounts. As a result, upon adoption we eliminated $34 million of unearned compensation cost and reduced by a like amount additional paid-in capital on our consolidated balance sheet.