

Energy Industry Issues and Potential Impact

Federal Issues

(Federal legislation and regulation impacts where and how we drill and produce energy.)



It has been decades since independent oil and gas producers like Newfield have faced so many challenges in our nation's capitol. Whether its proposals to increase oil and gas taxes, increase regulation on drilling or restrict access on public lands – independent producers seem to have been targeted by some policymakers that seem intent on discouraging oil and gas activity.

It seems ironic that only six months ago not only were many U.S. lawmakers vocally pushing for increased domestic drilling, but polling of U.S. voters found that more than 60% favored increased domestic oil and gas drilling.

We're not sure if voter attitudes have changed since the November elections, but most certainly those calling the shots on oil and gas policy have. Unfortunately, leaders in Congress and the administration that are formulating energy policy represent mainly



urban areas with no oil and gas constituencies, resulting in little understanding of our industry.

Independent producers like Newfield are today more active in Washington attempting to educate lawmakers on the fundamentals of our industry and the consequences of higher taxes and increased regulation.

“It has never been more important for our industry and our employees to ramp up our efforts to educate federal lawmakers on the consequences of punitive taxes and regulation,” said Newfield President and CEO Lee K. Boothby. “The results of higher taxes and increased regulation would be less energy security, less investment, fewer wells drilled, fewer jobs and higher energy prices.”

Newfield activities in Washington are focused primarily on

- Defeating proposals to increase oil and gas taxes on producers.
- Preventing federal regulation that restricts hydraulic fracturing.
- Protecting oil and gas operations in any climate change bill that emerges, and ensuring that the benefits of the increased use of natural gas are considered by lawmakers who are addressing climate change initiatives.
- Impact the various proposals and agency actions to restrict access to public lands for oil and gas activities.

Increased Taxes



(The current administration is pointing the way towards new energy taxes.)

Included in President Obama's 2010 proposed budget is the repeal of a number of oil and gas tax provisions that, if passed, would increase taxes on our industry by a whopping \$31 billion.

Why the proposed increases?

“We don’t believe it makes sense to significantly subsidize the production and use of sources of energy (like oil and gas) that are dramatically going to add to our climate change imperative,” said U.S. Treasury Secretary Tim Geithner on March 4, 2009, in testimony before the U.S. Senate Finance Committee.

The bottom line is that if only one of the proposals is adopted – repealing the expensing of Intangible Drilling Costs – the first year annual impact to Newfield is estimated at more than \$200 million. This is a deduction that has been on the books for nearly 100 years.

“If passed, the result would be a commensurate reduction in our drilling budgets,” said Boothby. “We would simply drill fewer wells – which reduces domestic supply and ultimately raises commodity prices.”

Other proposals in the President’s budget include:

- Repeal percentage depletion for oil and natural gas.
- Repeal the marginal well tax credit.
- Repeal the enhanced oil recovery credit.
- Repeal the manufacturing tax deduction.
- Place an excise tax on Gulf of Mexico production.

Independent producers, including Newfield, are working hard to educate lawmakers on the consequences of dramatic increases in oil and gas taxes.

Increased Regulation of Hydraulic Fracturing

There are currently proposals in the U.S. House of Representatives and Senate that would impose new federal guidelines on hydraulic fracturing (HF). More than 95% of Newfield wells are fracture stimulated, and more than 90% of new domestic oil and gas wells are hydraulically fractured.

The HF process has been safely and effectively regulated by state regulators for decades, but the proposals in Congress would subject HF to regulation under the Safe Drinking Water Act, forcing producers to obtain HF permits from the EPA.





(Hydraulic fracturing operations like this in the Woodford Shale could be impacted by new federal legislation.)

“Based on the timing issues we now have when requesting permits from the EPA, which have historically taken six months, there is reason to worry that our growth and flexibility to operate will be hindered with the addition of permit requirements for every frac operation,” said Paul Weddle Newfield Rocky Mountain completions engineer. “This also will impact well economics if we end up with a six-month delay between drilling and completion of wells.”

At issue is whether hydraulic fracturing has the potential to contaminate potable water zones. State regulators and industry experts strongly disagree.

For example, the Interstate Oil and Gas Compact Commission (IOGCC), composed of state regulators from oil and gas producing states, has passed a resolution opposing federal regulation of HF. Erica Carr, a spokesperson for the IOGCC, said a survey of its 30 member states revealed that none of the state agencies had responded to instances of contamination related to hydraulic fracturing. Also, the Groundwater Protection Council recently released a study that opposed federal regulation of HF.

And even the EPA has concluded in numerous past studies that regulation of hydraulic fracturing is safe and should be left to state regulators.

Studies commissioned by Energy in Depth, an industry coalition, indicate that federal regulation of HF could result in a drop of 183,000 BOPD and 245 BCF of natural gas every year.

The Energy in Depth Website (www.energyinddepth.org) has excellent information on this and other energy issues.



Newfield will continue to work with lawmakers and industry colleagues to oppose federal regulation of hydraulic fracturing.

Climate Change – Challenge or Opportunity?

Leaders in Congress and President Obama campaigned last Fall on the promise to address the perceived climate change crisis by forcing reductions in man-made greenhouse gas. The preferred method is to impose a major “cap and trade” system aimed at reducing carbon dioxide emissions (mainly from fossil fuels).



(The issue of climate change is a stormy one at the federal level.)

Regardless of how we personally view climate change, current congressional and administration leaders pushed hard on a “cap and trade” bill that was recently passed by the House in June. The controversial bill, H.R. 2454 (“Waxman-Markey bill”), was passed by a narrow margin, and sets a goal of reducing greenhouse gases 17% by 2020, 42% by 2030 and 83% by 2050 (all cuts are from 2005 levels). Under “cap and trade,” the federal government would limit the total volume of CO₂ that U.S. companies can emit each year and would issue credits that companies would be required to have for each ton of CO₂ emitted. Once issued, the credits would be tradable and could be bought and sold, establishing a market price reflecting the targeted CO₂ reduction, with a tougher standard and fewer available permits leading to higher prices.

In that regard, the Congressional Budget Office estimates the cost of “cap and trade” to each American household would be about \$1,600 per year. Which begs the question of whether a costly “cap and trade” bill is politically viable in the midst of today’s economic downturn. Many congressional observers say “no,” that although the bill narrowly passed through the House, passage by the Senate is less likely.

Why should independent producers and Newfield be concerned with the Waxman-Markey bill?

“Generally, the bill has the long-term goal of reducing the use of fossil fuels, two of which we produce – oil and natural gas,” said Mike Pontiff, Newfield HS&E. “We need to ensure that the point of regulation on oil and gas facilities do not disadvantage domestic production to the advantage of foreign production.”

Any attempt to limit greenhouse gas will result in the use of more natural gas. It's the only resource we have that's abundant, economic and available without significant new investment in infrastructure. Natural gas emits on average 50% less CO₂ than coal. Newfield is participating in a newly formed coalition: America's Natural Gas Alliance (ANGA). Its purpose is to promote demand of natural gas. Natural gas is a natural bridge fuel to the future. It is domestic and abundant, and should be looked at for increased power generation and as a vehicle fuel. ANGA is chaired by Newfield Chairman of the Board David Trice.

State Legislatures End Sessions

Lawmakers in states where Newfield has operations were generally supportive of industry activities. State legislators in Oklahoma, Utah, North Dakota, Wyoming and Montana, not only killed legislation that could have impacted our operations negatively, but also passed measures that could have long term positive impact on independent producers.

State legislatures in these areas have now adjourned for the year. It is noteworthy that legislative action at the state level generally moves at a much more rapid pace than at the federal level. So, companies often work with oil and gas trade associations to influence the state legislative process. On issues directly impacting Newfield operations, however, we tend to take a pro-active role in lobbying policymakers.

Following are the highlights of the past five months of legislative activities.

Taxes

-In Oklahoma, the current menu of gross production tax incentives was extended for another three years, or until June 30, 2012. Newfield's primary focus was the horizontal well incentive, which provides for a gross production tax exemption for 48 months or “payout,” whichever occurs first (worth about \$350K per horizontal well). Newfield participated heavily in the effort to pass the extension, beginning with a presentation by Newfield's Sam Langford to legislators in January on the positive impacts of the horizontal incentive on development of the Woodford Shale. Newfield representatives like Don Miller, Steve Armstrong and I also worked to enhance the value of the horizontal incentive in numerous meetings with legislators, tax officials and industry counterparts, but fell short due to budget constraints and Oklahoma Tax Commission



revenue impact estimates. We will continue to work on changes during the interim that will make Oklahoma's horizontal incentive more competitive with surrounding states.

-The North Dakota Legislature passed a new "horizontal tax holiday" that is essentially a back-up incentive for when the current horizontal incentive is suspended. The new incentive, very generally, applies when the average price of WTI is between \$55 and \$70. A well drilled during the "activated" period would pay a 7% tax rate (as opposed to the usual 11.5% rate) for the first 18 months, 75,000 barrels of production, or the first \$4.5 million in gross revenues, or whichever comes first. The state estimated the provision could aid producers by approximately \$62 million. The bill was signed by the Governor.

-In Montana, a proposal by Governor Schweitzer to impose a \$1 per barrel surtax on oil, and an \$.08 per Mcf on gas, was defeated after intense lobbying by the oil and gas industry and support from industry friendly legislators. Newfield worked against the bill, which would have cost us about \$600,000 annually.

-In Utah, a proposal was considered by the Utah Tax Review Commission prior to the legislative session that would have eliminated severance tax incentives on marginal production. The Commission voted to not recommend the proposal, which would have cost Newfield an estimated \$10 million annually. Newfield's Keith Specht gave effective testimony to the Commission highlighting the negative consequences of the proposal to operations at Monument Butte.

Other Significant State Issues

-After many years of frustration, a comprehensive tort reform bill was passed and signed by the Oklahoma Governor that includes steps to discourage royalty class action suits against oil and gas producers.

-In Utah, Oklahoma, Wyoming, Montana and North Dakota, resolutions were passed by the state legislatures encouraging their respective federal delegations to oppose proposals to regulate hydraulic fracturing by the EPA under the Safe Drinking Water Act. Newfield was instrumental in instigating the resolution in Utah, working with the Utah Petroleum Association.

-In Oklahoma and Utah, legislation was passed that incentivizes the use of natural gas in vehicles and provides for incentives to build re-fueling infrastructure for natural gas vehicles.

-In North Dakota, a bill passed that requires an operator to hold all proceeds from sales of oil or gas separately from other funds until they are paid to owners.



-Several states passed legislation that will clarify the law in regards to carbon sequestration activities such as storage and using CO2 in enhanced oil recovery techniques.

-A number of proposals in each of our states that would have restricted the rights of operators to the benefit of landowners were stopped by industry lobbying.

In the coming months, we will continue efforts to educate Newfield employees and seek your help on state and federal legislative activities through various means of communication. In the meantime, if I can answer any questions or if you have suggestions; please do not hesitate to call.

– Bruce Stallsworth, manager of
Government Relations