PIONEER NATURAL RESOURCES CO
Form 10-Q
November 05, 2012
Table of Contents

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

FORM 10-Q

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

For the quarterly period ended September 30, 2012

or

¨ 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: 1-13245

PIONEER NATURAL RESOURCES COMPANY
(Exact name of Registrant as specified in its charter)

Delaware (State or other jurisdiction of incorporation or organization)	75-2702753 (I.R.S. Employer Identification No.)
5205 N. O'Connor Blvd., Suite 200, Irving, Texas (Address of principal executive offices)	75039 (Zip Code)

(972) 444-9001
(Registrant's telephone number, including area code)
Not applicable
(Former name, former address and former fiscal year, if changed since last report)

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 ý No ¨

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§ 232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes ý 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	ý	Accelerated filer	¨
Non-accelerated filer	o (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 ý

Number of shares of Common Stock outstanding as of October 31, 2012 123,232,483

Table of Contents

PIONEER NATURAL RESOURCES COMPANY
TABLE OF CONTENTS

		Page
Cautionary Statement Concerning Forward-Looking Statements		3
Definitions of Certain Terms and Conventions Used Herein		4
PART I. FINANCIAL INFORMATION		
Item 1.	Financial Statements	
	Consolidated Balance Sheets as of September 30, 2012 and December 31, 2011	5
	Consolidated Statements of Operations for the three and nine months ended September 30, 2012 and 2011	7
	Consolidated Statements of Comprehensive Income for the three and nine months ended September 30, 2012	8
	Consolidated Statement of Equity for the nine months ended September 30, 2012	9
	Consolidated Statements of Cash Flows for the nine months ended September 30, 2012 and 2011	10
	Notes to Consolidated Financial Statements	11
Item 2.	Management's Discussion and Analysis of Financial Condition and Results of Operations	31
Item 3.	Quantitative and Qualitative Disclosures About Market Risk	44
Item 4.	Controls and Procedures	48
PART II. OTHER INFORMATION		
Item 1.	Legal Proceedings	49
Item 1A.	Risk Factors	49
Item 2.	Unregistered Sales of Equity Securities and Use of Proceeds	49
Item 4.	Mine Safety Disclosures	49
Item 6.	Exhibits	50
Signatures		51
Exhibit Index		52

Table of Contents

PIONEER NATURAL RESOURCES COMPANY

Cautionary Statement Concerning Forward-Looking Statements

The information in this Quarterly Report on Form 10-Q (the "Report") contains forward-looking statements that involve risks and uncertainties. When used in this document, the words "believes," "plans," "expects," "anticipates," "forecasts," "intends," "continue," "may," "will," "could," "should," "future," "potential," "estimate" or the negative of such terms and similar expressions as they relate to Pioneer Natural Resources Company ("Pioneer" or the "Company") are intended to identify forward-looking statements. The forward-looking statements are based on the Company's current expectations, assumptions, estimates and projections about the Company and the industry in which the Company operates. Although the Company believes that the expectations and assumptions reflected in the forward-looking statements are reasonable, they involve risks and uncertainties that are difficult to predict and, in many cases, beyond the Company's control.

These risks and uncertainties include, among other things, volatility of commodity prices, product supply and demand, competition, the ability to obtain environmental and other permits and the timing thereof, other government regulation or action, the ability to obtain approvals from third parties and negotiate agreements (including joint venture agreements) with third parties on mutually acceptable terms, litigation, the costs and results of drilling and operations, availability of equipment, services, resources and personnel required to complete the Company's operating activities, access to and availability of transportation, processing and refining facilities, Pioneer's ability to replace reserves, implement its business plans (including its plan to complete certain asset divestments) or complete its development activities as scheduled, access to and cost of capital, the financial strength of counterparties to Pioneer's credit facility and derivative contracts and the purchasers of Pioneer's oil, NGL and gas production, uncertainties about estimates of reserves and the ability to add proved reserves in the future, the assumptions underlying production forecasts, quality of technical data, environmental and weather risks, including the possible impacts of climate change, the risks associated with the ownership and operation of an industrial sand mining business and acts of war or terrorism. These and other risks are described in the Company's Annual Report on Form 10-K, this and other Quarterly Reports on Form 10-Q and other filings with the United States Securities and Exchange Commission (the "SEC"). In addition, the Company may be subject to currently unforeseen risks that may have a materially adverse effect on it. Accordingly, no assurances can be given that the actual events and results will not be materially different than the anticipated results described in the forward-looking statements. See "Part I, Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations," "Part 1, Item 3. Quantitative and Qualitative Disclosures About Market Risk" and "Part II, Item 1A. Risk Factors" in this Report and "Part I, Item 1. Business — Competition, Markets and Regulations," "Part I, Item 1A. Risk Factors," "Part II, Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations" and "Part II, Item 7A. Quantitative and Qualitative Disclosures About Market Risk" in the Company's Annual Report on Form 10-K for the year ended December 31, 2011 for a description of various factors that could materially affect the ability of Pioneer to achieve the anticipated results described in the forward-looking statements. Readers are cautioned not to place undue reliance on forward-looking statements, which speak only as of the date hereof. The Company undertakes no duty to publicly update these statements except as required by law.

Table of Contents

PIONEER NATURAL RESOURCES COMPANY

Definitions of Certain Terms and Conventions Used Herein

Within this Report, the following terms and conventions have specific meanings:

- "BBL" means a standard barrel containing 42 United States gallons.
- "BOE" means a barrel of oil equivalent and is a standard convention used to express oil and gas volumes on a comparable oil equivalent basis. Gas equivalents are determined under the relative energy content method by using the ratio of six thousand cubic feet of gas to one BBL of oil or natural gas liquid.
- "BOEPD" means BOE per day.
- "BTU" means British thermal unit, which is a measure of the amount of energy required to raise the temperature of one pound of water one degree Fahrenheit.
- "Conway" means the daily average natural gas liquids components as priced in Oil Price Information Service ("OPIS") in the table "U.S. and Canada LP – Gas Weekly Averages" at Conway, Kansas.
- "DD&A" means depletion, depreciation and amortization.
- "GAAP" means accounting principles that are generally accepted in the United States of America.
- "LIBOR" means London Interbank Offered Rate, which is a market rate of interest.
- "MCF" means one thousand cubic feet and is a measure of gas volume.
- "MMBTU" means one million BTUs.
- "MMBTUPD" means MMBTU per day.
- "Mont Belvieu" means the daily average natural gas liquids components as priced in OPIS in the table "U.S. and Canada LP – Gas Weekly Averages" at Mont Belvieu, Texas.
- "NGL" means natural gas liquid.
- "NYMEX" means the New York Mercantile Exchange.
- "Pioneer" or the "Company" means Pioneer Natural Resources Company and its subsidiaries.
- "Pioneer Southwest" means Pioneer Southwest Energy Partners L.P. and its subsidiaries.
- "Proved reserves" mean the quantities of oil and gas, which, by analysis of geoscience and engineering data, can be estimated with reasonable certainty to be economically producible – from a given date forward, from known reservoirs, and under existing economic conditions, operating methods, and government regulations – prior to the time at which contracts providing the right to operate expire, unless evidence indicates that renewal is reasonably certain, regardless of whether deterministic or probabilistic methods are used for the estimation. The project to extract the hydrocarbons must have commenced or the operator must be reasonably certain that it will commence the project within a reasonable time.

(i) The area of the reservoir considered as proved includes: (A) The area identified by drilling and limited by fluid contacts, if any, and (B) Adjacent undrilled portions of the reservoir that can, with reasonable certainty, be judged to be continuous with it and to contain economically producible oil or gas on the basis of available geoscience and engineering data.

(ii) In the absence of data on fluid contacts, proved quantities in a reservoir are limited by the lowest known hydrocarbons ("LKH") as seen in a well penetration unless geoscience, engineering, or performance data and reliable technology establishes a lower contact with reasonable certainty.

(iii) Where direct observation from well penetrations has defined a highest known oil ("HKO") elevation and the potential exists for an associated gas cap, proved oil reserves may be assigned in the structurally higher portions of the reservoir only if geoscience, engineering or performance data and reliable technology establish the higher contact with reasonable certainty.

(iv) Reserves which can be produced economically through application of improved recovery techniques (including, but not limited to, fluid injection) are included in the proved classification when: (A) Successful testing by a pilot project in an area of the reservoir with properties no more favorable than in the reservoir as a whole, the operation of an installed program in the reservoir or an analogous reservoir, or other evidence using reliable technology establishes the reasonable certainty of the engineering analysis on which the project or program was based; and (B) The project has been approved for development by all necessary parties and entities, including governmental entities.

(v) Existing economic conditions include prices and costs at which economic producibility from a reservoir is to be determined. The price shall be the average during the 12-month period prior to the ending date of the period covered by the report, determined as an unweighted arithmetic average of the first-day-of-the-month price for each month within such period, unless prices are defined by contractual arrangements, excluding escalations based upon future conditions.

- "U.S." means United States.
- With respect to information on the working interest in wells, drilling locations and acreage, "net" wells, drilling locations and acres are determined by multiplying "gross" wells, drilling locations and acres by the Company's working interest in such wells, drilling locations or acres. Unless otherwise specified, wells, drilling locations and acreage statistics quoted herein represent gross wells, drilling locations or acres.
- Unless otherwise indicated, all currency amounts are expressed in U.S. dollars.

Table of Contents

PART I. FINANCIAL INFORMATION
Item 1. Financial Statements
PIONEER NATURAL RESOURCES COMPANY
CONSOLIDATED BALANCE SHEETS
(in thousands)

	September 30, 2012 (Unaudited)	December 31, 2011
ASSETS		
Current assets:		
Cash and cash equivalents	$333,886	$537,484
Accounts receivable:		
Trade, net of allowance for doubtful accounts of $832 and $806 as of September 30, 2012 and December 31, 2011, respectively	298,320	275,991
Due from affiliates	2,250	7,822
Income taxes receivable	10,126	3
Inventories	277,419	241,609
Prepaid expenses	21,657	14,263
Discontinued operations held for sale	400,392	73,349
Other current assets:		
Derivatives	225,900	238,835
Other	9,934	12,936
Total current assets	1,579,884	1,402,292
Property, plant and equipment, at cost:		
Oil and gas properties, using the successful efforts method of accounting:		
Proved properties	13,250,249	12,013,805
Unproved properties	203,285	235,527
Accumulated depletion, depreciation and amortization	(4,107,432)	(3,648,465)
Total property, plant and equipment	9,346,102	8,600,867
Goodwill	293,449	298,142
Other property and equipment, net	1,186,131	573,075
Other assets:		
Investment in unconsolidated affiliate	194,003	169,532
Derivatives	101,023	243,240
Other, net of allowance for doubtful accounts of $644 and $340 as of September 30, 2012 and December 31, 2011, respectively	113,409	160,008
	$12,814,001	$11,447,156

The financial information included as of September 30, 2012 has been prepared by management without audit by independent registered public accountants.
The accompanying notes are an integral part of these consolidated financial statements.

Table of Contents

PIONEER NATURAL RESOURCES COMPANY
CONSOLIDATED BALANCE SHEETS (continued)
(in thousands, except share data)

	September 30, 2012 (Unaudited)	December 31, 2011
LIABILITIES AND EQUITY		
Current liabilities:		
Accounts payable:		
Trade	$736,381	$647,455
Due to affiliates	68,255	68,756
Interest payable	40,960	57,240
Income taxes payable	222	9,788
Deferred income taxes	63,927	57,713
Discontinued operations held for sale	5,919	75,901
Other current liabilities:		
Derivatives	14,815	74,415
Deferred revenue	10,575	42,069
Other	50,794	36,174
Total current liabilities	991,848	1,069,511
Long-term debt	3,562,070	2,528,905
Derivatives	27,938	33,561
Deferred income taxes	2,209,472	1,942,446
Other liabilities	222,564	221,595
Equity:		
Common stock, $.01 par value; 500,000,000 shares authorized; 134,782,883 and 133,121,092 shares issued at September 30, 2012 and December 31, 2011, respectively	1,348	1,331
Additional paid-in capital	3,641,248	3,613,808
Treasury stock at cost: 11,551,195 and 11,264,936 at September 30, 2012 and December 31, 2011, respectively	(504,140)	(458,281)
Retained earnings	2,485,935	2,335,066
Accumulated other comprehensive loss - net deferred hedge losses, net of tax	—	(3,130)
Total equity attributable to common stockholders	5,624,391	5,488,794
Noncontrolling interests in consolidating subsidiaries	175,718	162,344
Total equity	5,800,109	5,651,138
Commitments and contingencies		
	$12,814,001	$11,447,156

The financial information included as of September 30, 2012 has been prepared by management without audit by independent registered public accountants.
The accompanying notes are an integral part of these consolidated financial statements.

Table of Contents

PIONEER NATURAL RESOURCES COMPANY
CONSOLIDATED STATEMENTS OF OPERATIONS
(in thousands, except per share data)
(Unaudited)

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2012	2011	2012	2011
Revenues and other income:				
Oil and gas	$695,422	$574,114	$2,014,920	$1,595,563
Interest and other	18,733	7,311	53,224	49,378
Derivative gains (losses), net	(123,994)	401,072	243,568	386,118
Gain (loss) on disposition of assets, net	13,237	1,048	57,973	(1,439)
	603,398	983,545	2,369,685	2,029,620
Costs and expenses:				
Oil and gas production	176,711	112,661	449,861	305,098
Production and ad valorem taxes	49,036	37,713	137,797	105,982
Depletion, depreciation and amortization	204,264	138,413	557,064	387,320
Exploration and abandonments	26,652	14,021	108,914	42,809
General and administrative	62,567	49,618	180,591	137,868
Accretion of discount on asset retirement obligations	2,369	1,993	6,994	5,930
Interest	54,441	45,560	150,307	135,782
Hurricane activity, net	—	(1,487)	—	(1,418)
Other	31,923	17,057	86,028	46,971
	607,963	415,549	1,677,556	1,166,342
Income (loss) from continuing operations before income taxes	(4,565)	567,996	692,129	863,278
Income tax provision	(8,386)	(182,728)	(248,535)	(278,732)
Income (loss) from continuing operations	(12,951)	385,268	443,594	584,546
Income (loss) from discontinued operations, net of tax	34,650	330	(240,474)	410,556
Net income	21,699	385,598	203,120	995,102
Net income attributable to noncontrolling interests	(2,475)	(34,134)	(39,669)	(49,467)
Net income attributable to common stockholders	$19,224	$351,464	$163,451	$945,635
Basic earnings per share:				
Income (loss) from continuing operations attributable to common stockholders	$(0.13)	$2.96	$3.27	$4.53
Income (loss) from discontinued operations attributable to common stockholders	0.28	—	(1.96)	3.47
Net income attributable to common stockholders	$0.15	$2.96	$1.31	$8.00
Diluted earnings per share:				
Income (loss) from continuing operations attributable to common stockholders	$(0.13)	$2.95	$3.19	$4.44
Income (loss) from discontinued operations attributable to common stockholders	0.28	—	(1.91)	3.41
Net income attributable to common stockholders	$0.15	$2.95	$1.28	$7.85
Weighted average shares outstanding:				
Basic	123,111	116,281	122,874	116,122
Diluted	123,111	117,075	126,111	118,350
Dividends declared per share	$0.04	$0.04	$0.08	$0.08

Amounts attributable to common stockholders:				
Income (loss) from continuing operations	$(15,426)	$351,134	$403,925	$535,079
Income (loss) from discontinued operations, net of tax	34,650	330	(240,474)	410,556
Net income	$19,224	$351,464	$163,451	$945,635

The financial information included herein has been prepared by management without audit by independent registered public accountants.

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

Table of Contents

PIONEER NATURAL RESOURCES COMPANY
CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME
(in thousands)
(Unaudited)

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2012	2011	2012	2011
Net income	$21,699	$385,598	$203,120	$995,102
Other comprehensive activity:				
Net hedge (gains) losses included in continuing operations	—	(8,224)	4,855	(24,418)
Income tax (benefit) provision	—	1,838	(1,725)	6,724
Other comprehensive activity	—	(6,386)	3,130	(17,694)
Comprehensive income	21,699	379,212	206,250	977,408
Comprehensive income attributable to the noncontrolling interests	(2,475)	(30,670)	(39,669)	(39,192)
Comprehensive income attributable to common stockholders	$19,224	$348,542	$166,581	$938,216

The financial information included herein has been prepared by management
without audit by independent registered public accountants.
The accompanying notes are an integral part of these consolidated financial statements.

Table of Contents

PIONEER NATURAL RESOURCES COMPANY
CONSOLIDATED STATEMENT OF EQUITY
(in thousands, except dividends per share)
(Unaudited)

	Equity Attributable To Common Stockholders							
	Shares Outstanding	Common Stock	Additional Paid-in Capital	Treasury Stock	Retained Earnings	Accumulated Other Comprehensive Loss	Noncontrolling Interests	Total Equity
Balance as of December 31, 2011	121,856	$1,331	$3,613,808	$(458,281)	$2,335,066	$ (3,130)	$ 162,344	$5,651,138
Dividends declared ($0.08 per share)	—	—	—	—	(9,999)	—	—	(9,999)
Exercise of long-term incentive plan stock options and employee stock purchases	190	—	(969)	10,624	(2,583)	—	—	7,072
Treasury stock purchases	(477)	—	—	(56,488)	—	—	(189)	(56,677)
Conversion of 2.875% senior convertible notes	—	—	(5)	5	—	—	—	—
Tax benefit related to stock-based compensation	—	—	31,330	—	—	—	—	31,330
Deferred tax provision attributable to 2008 Pioneer Southwest initial public offering	—	—	(49,072)	—	—	—	—	(49,072)
Compensation costs:								
Vested compensation awards, net	1,663	17	(17)	—	—	—	—	—
Compensation costs included in net income	—	—	46,173	—	—	—	864	47,037
Cash distributions to noncontrolling interests	—	—	—	—	—	—	(26,970)	(26,970)
Net income	—	—	—	—	163,451	—	39,669	203,120
Other comprehensive activity:								
Deferred hedging activity, net of tax:								

Net hedge losses included in continuing operations	—	—	—	—	—	3,130	—	3,130
Balance as of September 30, 2012	123,232	$1,348	$3,641,248	$(504,140)	$2,485,935	$ —	$ 175,718	$5,800,109

The financial information included herein has been prepared by management without audit by independent registered public accountants.
The accompanying notes are an integral part of these consolidated financial statements.

9

Table of Contents

PIONEER NATURAL RESOURCES COMPANY
CONSOLIDATED STATEMENTS OF CASH FLOWS
(in thousands)
(Unaudited)

	Nine Months Ended September 30, 2012	2011
Cash flows from operating activities:		
Net income	$203,120	$995,102
Adjustments to reconcile net income to net cash provided by operating activities:		
Depletion, depreciation and amortization	557,064	387,320
Exploration expenses, including dry holes	52,574	5,228
Deferred income taxes	241,608	270,657
(Gain) loss on disposition of assets, net	(57,973)	1,439
Accretion of discount on asset retirement obligations	6,994	5,930
Discontinued operations	293,646	(371,767)
Interest expense	26,812	23,412
Derivative related activity	93,088	(269,746)
Amortization of stock-based compensation	46,899	31,525
Amortization of deferred revenue	(31,494)	(33,620)
Other noncash items	(20,998)	3,480
Change in operating assets and liabilities, net of effects from acquisitions and dispositions:		
Accounts receivable, net	(7,946)	(35,252)
Income taxes receivable	(8,632)	28,588
Inventories	(6,347)	(115,961)
Prepaid expenses	(6,772)	(7,558)
Other current assets	7,898	8,520
Accounts payable	23,554	83,632
Interest payable	(16,302)	(25,053)
Income taxes payable	(9,566)	(1,807)
Other current liabilities	(29,757)	45,969
Net cash provided by operating activities	1,357,470	1,030,038
Cash flows from investing activities:		
Proceeds from disposition of assets, net of cash sold	92,473	819,638
Payments for acquisition, net of cash acquired	(296,959)	—
Investment in unconsolidated subsidiary	—	(89,620)
Additions to oil and gas properties	(2,072,800)	(1,319,131)
Additions to other assets and other property and equipment, net	(238,803)	(265,740)
Net cash used in investing activities	(2,516,089)	(854,853)
Cash flows from financing activities:		
Borrowings under long-term debt	1,608,618	102,616
Principal payments on long-term debt	(596,000)	(135,883)
Distributions to noncontrolling interests	(26,970)	(19,944)
Payments of other liabilities	(894)	(503)
Exercise of long-term incentive plan stock options and employee stock purchases	7,072	3,690
Purchases of treasury stock	(56,677)	(40,326)
Excess tax benefits from share-based payment arrangements	31,330	28,123
Payment of financing fees	(6,430)	(8,741)

Dividends paid	(5,028)	(4,812)
Net cash provided by (used in) financing activities	955,021	(75,780)
Net increase (decrease) in cash and cash equivalents	(203,598)	99,405
Cash and cash equivalents, beginning of period	537,484	111,160
Cash and cash equivalents, end of period	$333,886	$210,565

The financial information included herein has been prepared by management without audit by independent registered public accountants.

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

Table of Contents
PIONEER NATURAL RESOURCES COMPANY
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
September 30, 2012
(Unaudited)

NOTE A. Organization and Nature of Operations

Pioneer Natural Resources Company ("Pioneer" or the "Company") is a Delaware corporation whose common stock is listed and traded on the New York Stock Exchange. The Company is a large independent oil and gas exploration and production company with operations in the United States.

NOTE B. Basis of Presentation

Presentation. In the opinion of management, the consolidated financial statements of the Company as of September 30, 2012 and for the three and nine months ended September 30, 2012 and 2011 include all adjustments and accruals, consisting only of normal recurring accrual adjustments, which are necessary for a fair presentation of the results for the interim periods. These interim results are not necessarily indicative of results for a full year.

Certain information and footnote disclosures normally included in financial statements prepared in accordance with generally accepted accounting principles in the United States ("GAAP") have been condensed or omitted in this Report pursuant to the rules and regulations of the United States Securities and Exchange Commission (the "SEC"). These consolidated financial statements should be read together with the consolidated financial statements and notes thereto included in the Company's Annual Report on Form 10-K for the year ended December 31, 2011.

Certain reclassifications have been made to the 2011 financial statement and footnote amounts in order to conform to the 2012 presentation.

On May 6, 2008, the Company recognized a noncash gain on the sale of common units of Pioneer Southwest Energy Partners L.P. ("Pioneer Southwest," a majority-owned and consolidated subsidiary) as a component of additional paid-in capital in stockholders' equity. In accordance with the Financial Accounting Standards Board ("FASB") Accounting Standards Codification (“ASC”) Topic 740 Income Taxes, deferred income taxes of $49.1 million should be recognized for the future tax effects arising from the noncash gain on the sale of the Pioneer Southwest common units, with a corresponding decrease to additional paid-in capital. The Company recorded the deferred income taxes associated with this transaction in June 2012. The effect of this adjustment is immaterial to the accompanying financial statements.

Revision for deferred income taxes. The accompanying consolidated balance sheet as of December 31, 2011 has been revised for a change in the classification of deferred income taxes associated with the Company's unrealized current derivative net gains as of December 31, 2011. The noncash revisions resulted in a $77.0 million decrease in current deferred tax assets, a $57.7 million increase in current deferred tax liabilities and a $134.7 million decrease in noncurrent deferred tax liabilities from the amounts previously reported at December 31, 2011. These revisions were made to appropriately reflect the impact on deferred income taxes based on the expected settlement periods related to derivatives, which remained subject to market risk as of December 31, 2011. See "- Derivatives and hedging," below and Notes E and H for more information about derivative fair values and market risk.

Derivatives and hedging. All derivatives are recorded in the accompanying consolidated balance sheets at their estimated fair values. See Note E for information about the fair value of the Company's derivatives. Effective February 1, 2009, the Company discontinued hedge accounting on all of its then-existing derivative hedge contracts. Changes in the fair value of effective cash flow hedges prior to the Company's discontinuance of hedge accounting were recorded as a component of accumulated other comprehensive income or loss ("AOCI - Hedging"), in the equity section of the Company's consolidated balance sheets, and were transferred to earnings during the same periods in which the hedged transactions were recognized in the Company's earnings. During the six months ended June 30, 2012, the remaining hedge gains or losses that were previously deferred in AOCI - Hedging were transferred to earnings. Since discontinuing hedge accounting, the Company has recognized all changes in the fair values of its derivative contracts as gains or losses in the earnings of the periods in which they occur.

The Company classifies the fair value amounts of derivative assets and liabilities executed under master netting arrangements as net current or noncurrent derivative assets or net current or noncurrent derivative liabilities, whichever the case may be, by commodity and counterparty. Net derivative asset values are determined, in part, by utilization of the derivative counterparties' credit-adjusted risk-free rate curves and net derivative liabilities are determined, in part, by utilization of the Company's and Pioneer Southwest's credit-adjusted risk-free rate curves. The credit-adjusted risk-free rate curves for the Company and its counterparties are generally based on their independent market-quoted credit default swap rate curves plus the United States Treasury Bill yield

curve as of the valuation date. Pioneer Southwest's credit-adjusted risk-free rate curve is based on independent market-quoted forward London Interbank Offered Rate ("LIBOR") curves plus 162.5 basis points, representing Pioneer Southwest's borrowing rate.
Goodwill. Goodwill is assessed for impairment whenever events or circumstances indicate that impairment of the carrying value of goodwill is likely, but no less often than annually. If the carrying value of goodwill is determined to be impaired, it is reduced for the impaired value with a corresponding charge to pretax earnings in the period in which it is determined to be impaired. During the third quarter of 2012, the Company performed a qualitative assessment of goodwill in accordance with FASB Accounting Standards Update ("ASU") No. 2011-08, Intangibles - Goodwill and Other (Topic 350) ("ASU 2011-08"), which permits an entity to first assess qualitative factors to determine whether it is more likely than not that the fair value of a reporting unit is less than its carrying amount as a basis for determining whether it is necessary to perform the two-step goodwill impairment test, and determined that it was not likely that the Company's goodwill was impaired. During the third quarter of 2012, the Company classified its Barnett Shale field assets and liabilities as discontinued operations held for sale. Associated therewith, the Company reclassified $4.7 million of goodwill attributable to the Barnett Shale assets to discontinued operations held for sale on the accompanying consolidated balance sheet at September 30, 2012. See Note C for more information about the Company's plan to sell its Barnett Shale net assets.

Impairment of assets. The Company reviews its long-lived assets for impairment, including oil and gas properties, whenever events or circumstances indicate that their carrying values may not be fully recoverable. If the carrying value of long-lived assets is determined to be impaired, it is reduced to its estimated fair value with a corresponding charge to pretax earnings in the period in which it is determined to be impaired. See Note O for additional information about the Company's recent impairments and its risk of future impairments.

NOTE C. Acquisitions and Divestitures

Premier Silica Business Combination

On April 2, 2012, a wholly-owned subsidiary of Pioneer acquired 100 percent of the share capital of Industrial Sands Holding Company and its wholly-owned subsidiary, Oglebay Norton Industrial Sands, LLC (the "Sand Acquisition"). During April 2012, the Company changed the name of Oglebay Norton Industrial Sands, LLC to Premier Silica LLC ("Premier Silica"). Premier Silica's core business is the operation of mines and processing facilities that produce, process and sell sand, primarily to upstream oil and gas companies for proppant used in the fracture stimulation of oil and gas wells in the United States. Premier Silica's business is supportive to the Company's vertical integration strategy of controlling major cost components of the Company's drilling and production activities in the areas where the Company has a significant inventory of drilling locations and a significant number of producing wells. The aggregate purchase price of Premier Silica was $297.0 million, including closing adjustments, and was funded from available cash and borrowings under the Company's credit facility.

The Sand Acquisition was accounted for as a business combination which, among other things, requires that assets acquired and liabilities assumed be measured at their acquisition date fair values. The Company's assessment of the fair values of Premier Silica's assets and liabilities is preliminary, and may be adjusted as a result of normal closing adjustments. The fair value of the tangible assets acquired totaled $472.7 million and were primarily comprised of proved sand reserves, probable sand reserves and mine processing facilities and equipment of $458.2 million. The fair value of liabilities assumed totaled $175.8 million and were primarily comprised of deferred income taxes of $151.0 million.

The Company recognized $246 thousand and $2.4 million of acquisition-related costs associated with the Sand Acquisition that were expensed in the three and nine months ended September 30, 2012, respectively. These costs are included in other expense in the accompanying consolidated statements of operations for the three and nine months ended September 30, 2012.

Divestitures Recorded as Discontinued Operations

Barnett Shale. During the third quarter of 2012, the Company committed to a plan to divest of its net assets in the Barnett Shale field in North Texas. The plan is expected to result in the sale of the Barnett Shale net assets during the first quarter of 2013. The Company has classified its (i) Barnett Shale assets and liabilities as discontinued operations held for sale in the accompanying consolidated balance sheet as of September 30, 2012 and (ii) Barnett Shale results of operations as income from discontinued operations, net of tax, in the accompanying consolidated statements of operations (representing a recasting of the Barnett Shale results of operations for the three and nine months ended September 30, 2011 and six months ended June 30, 2012, which were originally classified as continuing operations).

South Africa. During December 2011, the Company committed to a plan to exit South Africa and initiated a process to divest its net assets in South Africa ("Pioneer South Africa"). During the first quarter of 2012, the Company agreed to sell its net assets in Pioneer South Africa to an unaffiliated third party, effective January 1, 2012, for $60.0 million of cash proceeds before normal closing and other adjustments, and the buyer's assumption of certain liabilities of the Company's South Africa subsidiaries. In August 2012, the Company completed the sale of Pioneer South Africa for net cash proceeds of $15.9 million, including normal closing adjustments for cash revenues and costs and expenses from the effective date through the date of the sale, resulting in a pretax gain of $28.6 million. The Company classified (i) Pioneer South Africa's assets and liabilities as discontinued operations held for sale in the accompanying consolidated balance sheet as of December 31, 2011 and (ii) Pioneer South Africa's results of operations as income from discontinued operations, net of tax, in the accompanying consolidated statements of operations (representing a recasting of Pioneer South Africa results of operations for the three and nine months ended September 30, 2011, which were originally classified as continuing operations).

Tunisia. In February 2011, the Company sold 100 percent of the Company's share holdings in Pioneer Natural Resources Tunisia Ltd. and Pioneer Natural Resources Anaguid Ltd. (referred to in the aggregate as "Pioneer Tunisia") to an unaffiliated third party for cash proceeds of $802.5 million, including normal closing adjustments and excluding cash and cash equivalents sold, resulting in a pretax gain of $645.2 million. Accordingly, the Company has classified the results of operations of Pioneer Tunisia, prior to its sale, as discontinued operations, net of tax, in the accompanying consolidated statement of operations for the three and nine months ended September 30, 2011.

Table of Contents
PIONEER NATURAL RESOURCES COMPANY
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
September 30, 2012
(Unaudited)

The following table represents the components of the Company's discontinued operations for the three and nine months ended September 30, 2012 and 2011 (principally related to the divestitures of the Company's net assets in the Barnett Shale field and Pioneer South Africa and, for the nine months ended September 30, 2011, the divestiture of Pioneer Tunisia):

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2012	2011	2012	2011
	(in thousands)			
Revenues and other income:				
Oil and gas	$30,466	$36,395	$111,426	$118,137
Interest and other	—	224	20	5,195
Gain (loss) on disposition of assets, net	28,179	(58)	28,157	645,241
	58,645	36,561	139,603	768,573
Costs and expenses:				
Oil and gas production	11,573	6,944	35,718	19,023
Production and ad valorem taxes	744	829	2,273	1,720
Depletion, depreciation and amortization (a)	3,134	18,043	32,673	54,717
Impairment of oil and gas properties (a) (b)	—	—	444,880	—
Exploration and abandonments	372	6,005	8,660	19,021
General and administrative	721	471	1,853	9,868
Accretion of discount on asset retirement obligations (a)	344	813	1,898	2,270
Interest	—	—	(75)	773
Other	(26)	245	1,313	4,457
	16,862	33,350	529,193	111,849
Income (loss) from discontinued operations before income taxes	41,783	3,211	(389,590)	656,724
Current tax provision	(4,231)	(9,338)	(8,317)	(35,872)
Deferred tax (provision) benefit (a)	(2,902)	6,457	157,433	(210,296)
Income (loss) from discontinued operations	$34,650	$330	$(240,474)	$410,556

(a) Represents significant noncash components of discontinued operations.
(b) Represents the pretax noncash impairment of Barnett Shale field oil and gas properties that was recorded during the three months ended June 30, 2012. See Note O for additional information about Barnett Shale field impairment.

As of September 30, 2012 and December 31, 2011, the carrying values of Barnett Shale field and Pioneer South Africa assets and liabilities, respectively, were included in discontinued operations held for sale in the accompanying consolidated balance sheet and were comprised of the following:

	September 30, 2012	December 31, 2011
	(in thousands)	
Composition of assets included in discontinued operations held for sale:		
Current assets (excluding cash and cash equivalents)	$13,127	$10,465
Property, plant and equipment	351,736	53,025
Goodwill	4,693	—
Deferred tax assets	28,647	9,816
Other assets, net	2,189	43
Total assets	$400,392	$73,349
Composition of liabilities included in discontinued operations held for sale:		
Current liabilities	$160	$11,689
Deferred revenue	—	34,320
Other liabilities	5,759	29,892
Total liabilities	$5,919	$75,901

Divestitures Recorded in Continuing Operations

The Company's net gain on disposition of assets of $13.2 million for the three months ended September 30, 2012 is primarily associated with the sale of the Company's interest in the Cosmopolitan Unit in the Cook Inlet of Alaska to unaffiliated third parties for cash proceeds of $10.1 million, which, together with certain Company obligations assumed by the purchasers, resulted in a pretax gain of $12.6 million. Additionally, the Company's net gain on disposition of assets for the nine months ended September 30, 2012 of $58.0 million includes the first quarter sale of a portion of its interest in an unproved oil and gas property in the Eagle Ford Shale field to unaffiliated third parties for cash proceeds of $54.7 million, which resulted in a pretax gain of $42.6 million.

During the three and nine months ended September 30, 2011, the Company's net gains and losses on disposition of assets were primarily associated with the sales of excess materials and supplies inventories.

NOTE D. Exploratory Costs

The Company capitalizes exploratory well and project costs until a determination is made that the well or project has either found proved reserves, is impaired or is sold. The Company's capitalized exploratory well and project costs are presented in proved properties in the accompanying consolidated balance sheets. If the exploratory well or project is determined to be impaired, the impaired costs are charged to exploration and abandonments expense.

PIONEER NATURAL RESOURCES COMPANY
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
September 30, 2012
(Unaudited)

The following table reflects the Company's capitalized exploratory well and project activity during the three and nine months ended September 30, 2012:

	Three Months Ended September 30, 2012	Nine Months Ended September 30, 2012
	(in thousands)	
Beginning capitalized exploratory costs	$ 193,727	$ 107,596
Additions to exploratory costs pending the determination of proved reserves	235,500	616,332
Reclassification due to determination of proved reserves	(224,784)	(491,199)
Exploratory well costs charged to exploration expense	(1,563)	(29,849)
Ending capitalized exploratory costs	$ 202,880	$ 202,880

The following table provides an aging, as of September 30, 2012 and December 31, 2011, of capitalized exploratory costs and the number of projects for which exploratory costs have been capitalized for a period greater than one year based on the date drilling was completed:

	September 30, 2012	December 31, 2011
	(in thousands, except project counts)	
Capitalized exploratory costs that have been suspended:		
One year or less	$ 181,022	$ 107,596
More than one year	21,858	—
	$ 202,880	$ 107,596
Number of projects with exploratory costs that have been suspended for a period greater than one year	1	—

As of September 30, 2012, the Company had one project with exploratory costs that had been suspended for a period of one year or more, which is described below. As of December 31, 2011, the Company had no exploratory projects for which exploratory costs had been capitalized for a period greater than one year from the date drilling was completed.

Alaska - Oooguruk. As of September 30, 2012, the Company has $21.9 million of suspended well costs recorded for the K-13 well in the Alaska Oooguruk field. Drilling on the K-13 well was completed during September 2011. During well completion operations, sub-surface damages were sustained. The Company currently expects to recomplete the well in mid-2013.

NOTE E. Fair Value Measurements

Fair value is defined as the price that would be received to sell an asset or the price paid to transfer a liability in an orderly transaction between market participants at the measurement date. Fair value measurements are based upon inputs that market participants use in pricing an asset or liability, which are characterized according to a hierarchy that prioritizes those inputs based on the degree to which they are observable. Observable inputs represent market data obtained from independent sources, whereas unobservable inputs reflect a company's own market assumptions, which are used if observable inputs are not reasonably available without undue cost and effort. The three input levels of the fair value hierarchy are as follows:

- Level 1 – quoted prices for identical assets or liabilities in active markets.
- Level 2 – quoted prices for similar assets or liabilities in active markets, quoted prices for identical or similar assets or liabilities in markets that are not active, inputs other than quoted prices that are observable for the asset or liability (e.g., interest rates) and inputs derived principally from or corroborated by observable market data by correlation or other means.

- Level 3 – unobservable inputs for the asset or liability.

Table of Contents
PIONEER NATURAL RESOURCES COMPANY
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
September 30, 2012
(Unaudited)

Assets and liabilities measured at fair value on a recurring basis. The fair value input hierarchy level to which an asset or liability measurement in its entirety falls is determined based on the lowest level input that is significant to the measurement in its entirety.

The following table presents the Company's assets and liabilities that are measured at fair value as of September 30, 2012:

	Fair Value Measurement at the End of the Reporting Period Using			
	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Fair Value at September 30, 2012
	(in thousands)			
Recurring fair value measurements				
Assets:				
Trading securities	$ 162	$ 157	$ —	$ 319
Commodity derivatives	—	326,923	—	326,923
Deferred compensation plan assets	47,402	—	—	47,402
Total assets	47,564	327,080	—	374,644
Liabilities:				
Commodity derivatives	—	(31,219)	$ —	(31,219)
Interest rate derivatives	—	(11,534)	—	(11,534)
Total liabilities	—	(42,753)	—	(42,753)
Total recurring fair value measurements	$ 47,564	$ 284,327	$ —	$ 331,891

Trading securities and deferred compensation plan assets. The Company's trading securities are comprised of securities that are both actively traded and not actively traded on major exchanges. The Company's deferred compensation plan assets represent investments in equity and mutual fund securities that are actively traded on major exchanges. These investments are measured based on observable prices on major exchanges. As of September 30, 2012, substantially all of the significant inputs to these asset exchange values represented Level 1 independent active exchange market price inputs. Inputs for certain trading securities that are not actively traded on major exchanges were classified as Level 2 inputs.

Interest rate derivatives. The Company's interest rate derivative liabilities as of September 30, 2012 represent interest rate swap contracts. The Company utilizes discounted cash flow models for valuing its interest rate derivatives. The net derivative values attributable to the Company's interest rate derivative contracts as of September 30, 2012 are based on (i) the contracted notional amounts, (ii) LIBOR rate yield curves provided by counterparties and corroborated with forward active market-quoted LIBOR yield curves and (iii) the applicable credit-adjusted risk-free rate yield curve. The Company's interest rate derivative liability measurements represent Level 2 inputs in the hierarchy priority.

Commodity derivatives. The Company's commodity derivatives represent oil, natural gas liquids ("NGL") and gas swap contracts, collar contracts and collar contracts with short puts. The Company's oil, NGL and gas swap, collar and collar contracts with short puts asset and liability measurements represent Level 2 inputs in the hierarchy priority. The Company utilizes discounted cash flow and option-pricing models for valuing its commodity derivatives.

The asset and liability values attributable to the Company's commodity derivatives were determined based on inputs which include (i) the contracted notional volumes, (ii) independent active market price quotes, (iii) the applicable estimated credit-adjusted risk-free rate yield curve and (iv) the implied rate of volatility inherent in the collar and collar contracts with short puts, which is based on active and independent market-quoted volatility factors.

Financial instruments not carried at fair value. Carrying values and fair values of financial instruments that are not carried at fair value in the consolidated balance sheet as of September 30, 2012 and December 31, 2011 are as follows:

	September 30, 2012		December 31, 2011	
	Carrying Value	Fair Value	Carrying Value	Fair Value
	(in thousands)			
Long-term debt	$ 3,562,070	$ 4,449,088	$ 2,528,905	$ 3,105,585

Long term debt includes the Company's credit facility, the Pioneer Southwest credit facility and the Company's senior notes. The fair value of debt is determined utilizing inputs that are Level 2 measurements in the fair value hierarchy.

Credit facilities. The fair values of the Company's and Pioneer Southwest's credit facilities are calculated using a discounted cash flow model based on (i) forecasted contractual interest and fee payments, (ii) forward active market-quoted United States Treasury Bill rate (in the case of the Company's credit facility) or LIBOR (in the case of the Pioneer Southwest credit facility) yield curves and (iii) the applicable credit-adjustments.

Senior notes. The Company's senior notes represent debt securities that are not actively traded on major exchanges. The fair values of the Company's senior notes are based on their periodic values as quoted on the major exchanges.

The Company has other financial instruments consisting primarily of cash equivalents, short-term receivables, prepaids, payables and other current assets and liabilities that approximate fair value due to the nature of the instrument and relatively short maturities. Non-financial assets and liabilities initially measured at fair value include certain assets acquired and liabilities assumed in a business combination, goodwill and asset retirement obligations.

NOTE F. Income Taxes

The Company's income tax (provisions) benefits attributable to income from continuing operations consisted of the following for the three and nine months ended September 30, 2012 and 2011:

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2012	2011	2012	2011
	(in thousands)			
Current	$ 13,052	$ (3,035)	$ (6,927)	$ (8,075)
Deferred	(21,438)	(179,693)	(241,608)	(270,657)
Income tax provision	$ (8,386)	$ (182,728)	$ (248,535)	$ (278,732)

At the end of each interim reporting period, the Company updates its estimate of the annual effective tax rate. Tax items included in the annual effective tax rate are pro-rated for the full year and tax items discrete to a specific quarter are included in the effective tax rate for that quarter. The estimate used in providing for income taxes on a year-to-date basis may change in subsequent interim periods as new facts or circumstances become known. The annual effective tax rate represents the income tax benefit or provision divided by the income or loss from continuing operations before income taxes excluding the effect of net income attributable to noncontrolling interests. For the three months ended September 30, 2012 and 2011, the Company's effective tax rates are (119) percent and 34 percent, respectively, and for the nine months ended September 30, 2012 and 2011, the effective tax rates are 38 percent and 34 percent, respectively. The Company's effective tax rate for the three months ended September 30, 2012, as compared to the same period of the prior year, is primarily due to the impact of non-deductible items and state taxes on a pretax loss, excluding net income attributable to noncontrolling interests, of $7.0 million for the three months ended September 30, 2012, as compared to the impact of similar components on pretax income, excluding net income attributable to noncontrolling interests, of $533.9 million for the three months ended September 30, 2011.

The Company files income tax returns in the U.S. federal and various state and foreign jurisdictions. With few exceptions, the Company believes that it is no longer subject to examinations by state and foreign tax authorities for years before 2006. The Internal Revenue Service has closed examinations of the 2010 and prior tax years. As of September 30, 2012, no adjustments had been proposed in any jurisdiction that would have a significant effect on the Company's liquidity, future results of operations or financial position.

NOTE G. Long-term Debt

The Company's long-term debt consists of senior notes and revolving credit facilities, including the effects of net deferred fair value hedge losses and issuance discounts. As of September 30, 2012, the Company and Pioneer Southwest were in compliance with all of their debt covenants.

Credit facility. During March 2011, the Company entered into a Second Amended and Restated 5-Year Revolving Credit Agreement (the "Credit Facility") with a syndicate of financial institutions that matures in March 2016, unless extended in accordance with the terms of the Credit Facility. As of September 30, 2012, the Company had $360.0 million of outstanding borrowings under the Credit Facility and $2.2 million of undrawn letters of credit, all of which were commitments under the Credit Facility, leaving the Company with $887.8 million of unused borrowing capacity under the Credit Facility.

Pioneer Southwest credit facility. During March 2012, Pioneer Southwest entered into an Amended and Restated 5-Year Revolving Credit Agreement (the "Pioneer Southwest Credit Facility") with a syndicate of financial institutions that matures in March 2017, unless extended in accordance with the terms of the Pioneer Southwest Credit Facility. The Pioneer Southwest Credit Facility provides for aggregate loan commitments of $300 million. As of September 30, 2012, Pioneer Southwest had $88.0 million of outstanding borrowings and $212.0 million of unused borrowing capacity under the Pioneer Southwest Credit Facility.

The Pioneer Southwest Credit Facility is available for general partnership purposes, including working capital, capital expenditures and distributions. Borrowings under the Pioneer Southwest Credit Facility may be in the form of Eurodollar rate loans, base rate committed loans or swing line loans. The Pioneer Southwest Credit Facility contains certain financial covenants, including (i) the maintenance of a quarter end maximum leverage ratio of not more than 3.5 to 1.00 and (ii) the maintenance of a ratio of the net present value of Pioneer Southwest's projected future cash flows from its oil and gas properties to total debt of at least 1.75 to 1.0.

Senior notes. During June 2012, the Company issued $600 million of 3.95% Senior Notes due 2022 and received proceeds, net of $8.5 million of offering discounts and costs, of $591.5 million. The Company used the net proceeds to reduce outstanding borrowings under the Credit Facility.

Convertible senior notes. As of September 30, 2012 and December 31, 2011, the Company had $479.9 million of 2.875% Convertible Senior Notes outstanding. The 2.875% Convertible Senior Notes are convertible under certain circumstances, using a net share settlement process, into a combination of cash and the Company's common stock based on a formula set forth in the indenture supplement pursuant to which the 2.875% Convertible Senior Notes were issued.

The Company's stock prices during each of March 2012 and March 2011 met the average price threshold that caused the Company's 2.875% Convertible Senior Notes to become convertible at the option of the holders during the three month periods ended June 30, 2012 and 2011. Associated therewith, certain holders of the 2.875% Convertible Senior Notes tendered $15 thousand and $70 thousand principal amounts of the notes for conversion during the three months ended June 30, 2012 and 2011, respectively. In accordance with the terms of the 2.875% Convertible Senior Notes indenture supplement, the Company paid the tendering holders $15 thousand cash and issued to the tendering holders 55 shares of the Company's common stock during 2012 and paid the tendering holders a total of $71 thousand cash and issued to the tendering holders 340 shares of the Company's common stock during 2011.

The Company's stock prices during September 2012 also met the price threshold that causes the 2.875% Convertible Senior Notes to be convertible at the option of the holders for the three months ended December 31, 2012, and may become convertible in future quarters depending on the Company's stock price or other conditions.

On January 15, 2013, the 2.875% Convertible Senior Notes become redeemable at the option of the Company and on January 15, 2013, January 15, 2018, January 15, 2023, January 15, 2028 and January 15, 2033 the holders may require the Company to repurchase the notes for cash. The Company has the intent and ability to fund cash payments that may be required upon the conversion, redemption or repurchase of the 2.875% Convertible Senior Notes with borrowing capacity under the Credit Facility. Accordingly, the 2.875% Convertible Senior Notes are classified as long-term debt in the accompanying balance sheets. If all of the 2.875% Convertible Senior Notes had been converted on September 30, 2012, the note holders would have received $479.9

million of cash and approximately 3.3 million shares of the Company's common stock, which was valued at $345.8 million on September 30, 2012.

NOTE H. Derivative Financial Instruments

The Company utilizes commodity swap contracts, collar contracts and collar contracts with short puts to (i) reduce the effect of price volatility on the commodities the Company produces and sells or consumes, (ii) support the Company's annual capital budgeting and expenditure plans and (iii) reduce commodity price risk associated with certain capital projects. The Company also, from time to time, utilizes interest rate contracts to reduce the effect of interest rate volatility on the Company's indebtedness.

Oil production derivative activities. All material physical sales contracts governing the Company's oil production are tied directly to, or are highly correlated with, New York Mercantile Exchange ("NYMEX") West Texas Intermediate ("WTI") oil prices.

The following table sets forth the volumes per day in barrels ("BBLs") outstanding as of September 30, 2012 under the Company's oil derivative contracts and the weighted average oil prices per BBL for those contracts:

	Three Months Ending December 31,	Twelve Months Ending December 31,		
	2012	2013	2014	2015
Collar contracts with short puts:				
Volume (BBL) (a)	53,110	54,029	60,000	26,000
Average price per BBL:				
Ceiling	$118.85	$119.60	$117.06	$104.45
Floor	$85.09	$89.71	$92.67	$95.00
Short put	$69.44	$73.74	$76.58	$80.00
Collar contracts:				
Volume (BBL)	2,000	—	—	—
Average price per BBL:				
Ceiling	$127.00	$—	$—	$—
Floor	$90.00	$—	$—	$—
Swap contracts:				
Volume (BBL) (a)	11,000	20,000	—	—
Average price per BBL	$89.34	$97.27	$—	$—
Rollfactor swap contracts:				
Volume (BBL)	—	6,000	—	—
NYMEX roll price (b)	$—	$0.43	$—	$—
Basis swap contracts:				
Index swap volume (BBL)	20,000	—	—	—
Average price per BBL (c)	$(1.15)	$—	$—	$—

(a) Subsequent to September 30, 2012, the Company converted NYMEX swap contracts for 17,000 BBLs per day of 2013 production with a price of $100.14 per BBL into collar contracts with short puts for 17,000 BBLs per day of 2013 production with a ceiling price of $120.29 per BBL, a floor price of $100.41 per BBL and a short put price of $75.99 per BBL.

(b) Represents swaps that fix the difference between (i) each day's price per BBL of WTI for the first nearby month less (ii) the price per BBL of WTI for the second nearby NYMEX month, multiplied by .6667; plus (iii) each day's price per BBL of WTI for the first nearby month less (iv) the price per BBL of WTI for the third nearby NYMEX month, multiplied by .3333.

(c) Basis differential price between Midland WTI and Cushing WTI.

Table of Contents
PIONEER NATURAL RESOURCES COMPANY
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
September 30, 2012
(Unaudited)

NGL production derivative activities. All material physical sales contracts governing the Company's NGL production are tied directly or indirectly to either Mont Belvieu or Conway fractionation facilities' NGL product component prices.
The following table sets forth the volumes per day in BBLs outstanding as of September 30, 2012 under the Company's NGL derivative contracts and the weighted average NGL prices per BBL for those contracts:

	Three Months Ending December 31,	Twelve Months Ending December 31,	
	2012	2013	2014
Collar contracts with short puts:			
Volume (BBL)	3,000	1,000	1,000
Average price per BBL:			
Ceiling	$79.99	$112.00	$109.50
Floor	$67.70	$95.00	$95.00
Short put	$55.76	$80.00	$80.00
Swap contracts:			
Volume (BBL)	2,750	—	—
Average price per BBL	$67.85	$—	$—

(a) Subsequent to September 30, 2012, the Company converted the 2013 collar contracts with short puts for 1,000 BBLs per day into collar contracts with short puts for 1,064 BBLs per day of 2013 natural gasoline production with a ceiling price of $105.28 per BBL, a floor price of $89.30 per BBL and a short put price of $75.20 per BBL.

Gas production derivative activities. All material physical sales contracts governing the Company's gas production are tied directly or indirectly to regional index prices where the gas is sold. The Company uses derivative contracts to manage gas price volatility and reduce basis risk between NYMEX Henry Hub ("HH") prices and actual index prices at which the gas is sold.

Table of Contents
PIONEER NATURAL RESOURCES COMPANY
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
September 30, 2012
(Unaudited)

The following table sets forth the volumes per day in millions of British thermal units ("MMBTU") outstanding as of September 30, 2012 under the Company's gas derivative contracts and the weighted average gas prices per MMBTU for those contracts:

	Three Months Ending December 31,	Twelve Months Ending December 31,		
	2012	2013	2014	2015
Collar contracts with short puts:				
Volume (MMBTU) (a)	—	—	—	155,000
Price per MMBTU:				
Ceiling	$—	$—	$—	$4.97
Floor	$—	$—	$—	$4.00
Short put	$—	$—	$—	$3.00
Collar contracts:				
Volume (MMBTU)	65,000	150,000	—	—
Price per MMBTU:				
Ceiling	$6.60	$6.25	$—	$—
Floor	$5.00	$5.00	$—	$—
Swap contracts:				
Volume (MMBTU) (a)	275,000	112,500	105,000	—
Price per MMBTU	$4.97	$5.62	$4.03	$—
Basis swap contracts:				
Volume (MMBTU)	136,000	142,500	—	—
Price per MMBTU	$(0.34)	$(0.22)	$—	$—

(a) Subsequent to September 30, 2012, the Company entered into additional (i) 2013 swap contracts for 50,000 MMBTU per day priced at $4.01 per MMBTU and (ii) 2015 collar contracts with short puts for 70,000 MMBTU per day with a ceiling price of $5.35 per MMBTU, a floor price of $4.00 per MMBTU and a short put price of $3.00 per MMBTU.

Marketing and basis transfer derivative activities. Periodically, the Company enters into gas buy and sell marketing arrangements to utilize unused firm pipeline transportation commitments. Associated with these gas marketing arrangements, the Company may enter into gas index swaps to mitigate the related price risk. From time to time, the Company also enters into long and short gas swap contracts that transfer gas basis risk from one sales index to another sales index.

The following table sets forth the contract volumes outstanding as of September 30, 2012 under the Company's marketing and basis transfer derivative contracts and the weighted average gas prices per MMBTU for those contracts:

	Three Months Ending December 31, 2012	Twelve Months Ending December 31, 2013
Average Daily Gas Production Associated with Marketing Derivatives:		
Basis swap contracts:		
Index swap volume (MMBTU)	43,370	9,863
Price differential ($/MMBTU)	$0.24	$0.25

Average Daily Gas Production Associated with Basis Transfer Derivatives:		
Basis swap contracts:		
Short index swap volume (MMBTU)	1,685	—
NGI-So Cal Border Monthly price differential to NYMEX HH ($/MMBTU)	$ 0.12	$ —
Long index swap volume (MMBTU)	(1,685)	—
IF-HSC price differential to NYMEX HH ($/MMBTU)	$ (0.05)	$ —

22

Table of Contents
PIONEER NATURAL RESOURCES COMPANY
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
September 30, 2012
(Unaudited)

Interest rates. As of September 30, 2012, the Company was a party to interest rate derivative contracts that lock in a fixed forward annual interest rate of 3.21 percent, for a 10-year period ending in December 2025, on a notional amount of $250 million. These derivative contracts mature and settle by their terms during December 2015.
Tabular disclosure of derivative financial instruments. All of the Company's derivatives are accounted for as non-hedge derivatives as of September 30, 2012 and December 31, 2011. The following tables provide disclosure of the Company's derivative instruments:

Fair Value of Derivative Instruments as of September 30, 2012

Type	Asset Derivatives (a) Balance Sheet Location	Fair Value (in thousands)	Liability Derivatives (a) Balance Sheet Location	Fair Value (in thousands)
Derivatives not designated as hedging instruments				
Commodity price derivatives	Derivatives - current	$234,231	Derivatives - current	$23,145
Commodity price derivatives	Derivatives - noncurrent	108,819	Derivatives - noncurrent	24,201
Interest rate derivatives	Derivatives - noncurrent	—	Derivatives - noncurrent	11,534
		$343,050		$58,880

Fair Value of Derivative Instruments as of December 31, 2011

Type	Asset Derivatives (a) Balance Sheet Location	Fair Value (in thousands)	Liability Derivatives (a) Balance Sheet Location	Fair Value (in thousands)
Derivatives not designated as hedging instruments				
Commodity price derivatives	Derivatives - current	$248,809	Derivatives - current	$68,735
Interest rate derivatives	Derivatives - current	—	Derivatives - current	15,654
Commodity price derivatives	Derivatives - noncurrent	257,368	Derivatives - noncurrent	47,689
		$506,177		$132,078

(a) Derivative assets and liabilities shown in the tables above are presented as gross assets and liabilities, without regard to master netting arrangements which are considered in the presentations of derivative assets and liabilities in the accompanying consolidated balance sheets.

Derivatives in Cash Flow Hedging Relationships	Location of Gain/(Loss) Reclassified from AOCI into Earnings	Amount of Gain/(Loss) Reclassified from AOCI into Earnings Three Months Ended September 30, 2012	2011	Nine Months Ended September 30, 2012	2011
		(in thousands)			
Commodity price derivatives	Oil and gas revenue	$—	$8,295	$(3,156)	$24,627
Interest rate derivatives	Interest expense	—	(71)	(1,699)	(209)
Total		$—	$8,224	$(4,855)	$24,418

23

Table of Contents
PIONEER NATURAL RESOURCES COMPANY
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
September 30, 2012
(Unaudited)

Derivatives Not Designated as Hedging Instruments	Location of Gain (Loss) Recognized in Earnings on Derivatives	Amount of Gain (Loss) Recognized in Earnings on Derivatives			
		Three Months Ended September 30,		Nine Months Ended September 30,	
		2012	2011	2012	2011
		(in thousands)			
Commodity price derivatives	Derivative gains (losses), net	$(118,795)	$407,407	$267,806	$380,030
Interest rate derivatives	Derivative gains (losses), net	(5,199)	(6,335)	(24,238)	6,088
Total		$(123,994)	$401,072	$243,568	$386,118

Derivative counterparties. The Company uses credit and other financial criteria to evaluate the credit standing of, and to select, counterparties to its derivative instruments. Although the Company does not obtain collateral or otherwise secure the fair value of its derivative instruments, associated credit risk is mitigated by the Company's credit risk policies and procedures.

The following table provides the Company's net derivative assets or liabilities by counterparty as of September 30, 2012:

	Net Assets (Liabilities) (in thousands)
Citibank, N.A.	$66,329
JP Morgan Chase	57,419
Barclays Capital	32,920
J. Aron & Company	20,846
BNP Paribas	20,061
BMO Financial Group	19,187
Credit Suisse	16,605
Toronto Dominion	15,144
Societe Generale	13,218
Morgan Stanley	8,852
Merrill Lynch	7,726
Den Norske Bank	6,161
Credit Agricole	2,099
Wells Fargo Bank, N.A.	756
BP Corporation North America	462
Macquarie Bank	454
Vitol	154
Royal Bank of Canada	(362)
Deutsche Bank	(766)
UBS	(3,095)
Total	$284,170

NOTE I. Asset Retirement Obligations

The Company's asset retirement obligations primarily relate to the future plugging and abandonment of wells and facilities. Market risk premiums associated with asset retirement obligations are estimated to represent a component of the Company's credit-adjusted risk-free rate that is utilized in the calculations of asset retirement obligations.

Table of Contents

PIONEER NATURAL RESOURCES COMPANY
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
September 30, 2012
(Unaudited)

The following table summarizes the Company's asset retirement obligation activity during the three and nine months ended September 30, 2012 and 2011:

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2012	2011	2012	2011
	(in thousands)			
Beginning asset retirement obligations	$ 145,457	$ 151,970	$ 136,742	$ 152,291
Liabilities assumed in acquisitions	—	—	8,515	6
New wells placed on production	1,251	1,132	3,662	3,206
Changes in estimates	48	(5,453)	1,651	(5,331)
Liabilities reclassified to discontinued operations held for sale	(5,919)	—	(5,919)	—
Disposition of wells	(2,536)	—	(2,536)	(448)
Liabilities settled	(4,506)	(2,808)	(13,248)	(10,277)
Accretion of discount from continuing operations	2,369	1,993	6,994	5,930
Accretion of discount from integrated services (a)	23	—	77	—
Accretion of discount from discontinued operations	127	813	376	2,270
Ending asset retirement obligations	$ 136,314	$ 147,647	$ 136,314	$ 147,647

(a) Accretion of discount from integrated services includes Premier Silica accretion expense, which is recorded as a reduction in third-party income from vertical integration services in interest and other income in the Company's accompanying consolidated statements of operations. See Note M for more information about interest and other income.

The Company records the current and noncurrent portions of asset retirement obligations in other current liabilities and other liabilities, respectively, in the accompanying consolidated balance sheets. As of September 30, 2012 and December 31, 2011, the current portions of the Company's asset retirement obligations were $16.1 million and $14.2 million, respectively.

NOTE J. Incentive Plans

Stock-based compensation

For the three and nine months ended September 30, 2012, the Company recorded $22.8 million and $66.0 million, respectively, of stock-based compensation expense for all plans, as compared to $11.7 million and $38.1 million for the same respective periods of 2011. As of September 30, 2012, there was $143.9 million of unrecognized compensation expense related to unvested share- and unit-based compensation plan awards, including $28.3 million attributable to stock-based awards that are expected to be settled in cash on their vesting date, rather than in equity shares ("Liability Awards"). This compensation will be recognized over the remaining vesting periods of the awards, which is a period of less than three years on a weighted average basis. As of September 30, 2012 and December 31, 2011, accounts payable – due to affiliates includes $13.5 million and $9.2 million, respectively, of liabilities attributable to Liability Awards.

The Company's issued shares, as reflected in the consolidated balance sheets at September 30, 2012 and December 31, 2011, do not include 304,260 and 533,125 common shares, respectively, associated with unvested stock-based compensation awards that have voting rights.

Table of Contents
PIONEER NATURAL RESOURCES COMPANY
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
September 30, 2012
(Unaudited)

The following table summarizes the activity that occurred during the nine months ended September 30, 2012, for each type of share-based incentive award issued by Pioneer:

	Restricted Stock Equity Awards	Restricted Stock Liability Awards	Performance Units	Stock Options	Pioneer Southwest LTIP Restricted Units	Pioneer Southwest LTIP Phantom Units
Outstanding at December 31, 2011	1,857,612	322,925	114,128	564,044	7,492	65,157
Awards granted	912,543	240,524	47,875	98,819	7,496	37,487
Awards vested	(1,220,841)	(127,919)	—	—	(7,492)	—
Options exercised	—	—	—	(190,377)	—	—
Awards forfeited	(21,472)	(18,360)	—	—	—	—
Outstanding as of September 30, 2012	1,527,842	417,170	162,003	472,486	7,496	102,644

Postretirement Benefit Obligations

As of September 30, 2012 and December 31, 2011, the Company had $8.1 million and $7.5 million, respectively, of unfunded accumulated postretirement benefit obligations, the current and noncurrent portions of which are included in other current liabilities and other liabilities in the accompanying consolidated balance sheets. These obligations are comprised of five unfunded plans, of which four relate to predecessor entities that the Company acquired in prior years, and two funded plans that the Company assumed sponsorship for in conjunction with the acquisition of Premier Silica.

The unfunded plans had no assets as of September 30, 2012 or December 31, 2011. The Company's funding policy for the Premier Silica plans is to contribute amounts sufficient to meet legal funding requirements, plus any additional amounts that the Company may determine to be appropriate considering the funded status of the plan, tax deductibility, the cash flow generated by the Company, and other factors. The Company continually reassesses the amount and timing of any discretionary contributions and may elect to make such contributions in future periods.

NOTE K. Commitments and Contingencies

The Company is a party to various proceedings and claims incidental to its business. While many of these matters involve inherent uncertainty, the Company believes that the amount of the liability, if any, ultimately incurred with respect to such proceedings and claims will not have a material adverse effect on the Company's consolidated financial position as a whole or on its liquidity, capital resources or future annual results of operations. The Company records reserves for contingencies when information available indicates that a loss is probable and the amount of the loss can be reasonably estimated.

NOTE L. Net Income (Loss) Per Share

The Company uses the two-class method of calculating net income (loss) per share because certain of the Company's and its consolidated subsidiaries' unvested share-based awards qualify as participating securities. Participating securities participate in the Company's dividend or partnership distributions and are assumed to participate in the Company's undistributed income proportionate to weighted average outstanding common shares, but are not assumed to participate in the Company's net losses because they are not contractually obligated to do so. Accordingly, allocations of earnings to participating securities are included in the Company's calculations of basic and diluted earnings per share from continuing operations, discontinued operations and net income attributable to common stockholders.

During periods in which the Company realizes a loss from continuing operations attributable to common stockholders, securities or other contracts to issue common stock would be dilutive to loss per share from continuing operations; therefore, conversion into common stock is assumed not to occur.

26

Table of Contents
PIONEER NATURAL RESOURCES COMPANY
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
September 30, 2012
(Unaudited)

The following tables reconcile the Company's net income (loss) attributable to common stockholders to basic net income (loss) attributable to common stockholders and diluted net income (loss) attributable to common stockholders for the three and nine months ended September 30, 2012 and 2011:

	Three Months Ended September 30, 2012			Nine Months Ended September 30, 2012		
	Continuing Operations	Discontinued Operations	Total	Continuing Operations	Discontinued Operations	Total
	(in thousands)					
Net income (loss) attributable to common stockholders	$ (15,426)	$ 34,650	$ 19,224	$ 403,925	$ (240,474)	$ 163,451
Participating basic earnings	—	(357)	(357)	(2,499)	—	(2,499)
Basic net income (loss) attributable to common stockholders	(15,426)	34,293	18,867	401,426	(240,474)	160,952
Reallocation of participating earnings	—	—	—	134	—	134
Diluted income (loss) attributable to common stockholders	$ (15,426)	$ 34,293	$ 18,867	$ 401,560	$ (240,474)	$ 161,086

	Three Months Ended September 30, 2011		Nine Months Ended September 30, 2011
	Continuing Operations	Discontinued Operations	