

Testimony of Harold Hamm  
Chairman and Chief Executive Officer  
Continental Resources, Inc.

U.S. Independent Exploration and Production Companies:  
Leading the Development of Reliable U.S. Energy Resources and  
Reducing U.S. Dependence on Foreign Oil  
For the U.S. House Committee on Ways and Means

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Continental Resources, Inc. (NYSE: CLR) is an independent producer of crude oil and natural gas, operating primarily in the Rockies and Mid-Continental United States. Based in Enid, Oklahoma, the Company has 425 direct employees, as well as employing thousands of indirect contractors (drilling, etc.). The Company is the third largest producer of crude oil in the Rocky Mountain Region and its 2009 production was 74% crude oil and 26% natural gas.

## OVERVIEW:

U.S. independent exploration and production companies have been the leaders – not “Big Oil,” the integrated refiners – in increasing U.S. production and finding significant new reserves of crude oil and natural gas in the past decade. Because of the success of the independents, the United States is today the #1 producer of natural gas in the world and the #3 producer of crude oil and natural gas liquids.

This “quiet energy revolution,” involving advanced technologies such as horizontal/directional drilling and high-pressure fracture stimulation, has significantly increased U.S. production and reserves in recent years, and at the same time reduced imports of petroleum liquids. The application of advanced technologies and U.S. entrepreneurial investment are decreasing our dependence on foreign oil.

In contrast to conventional wisdom, world and U.S. petroleum reserves are also increasing, with world crude oil reserves now sufficient to meet growth in demand through the 21<sup>st</sup> century. Only a few years ago, we feared that U.S. natural gas reserves would be exhausted in about a decade. Now we are measuring them in at least a century of usage, because of domestic shale gas development.

These positive trends are supported by recent changes in the SEC reserve rules that finally recognized the increased scope of oil and gas reserves in continuous geological accumulation plays, such as the Bakken, Barnett and Haynesville shales. Crude oil and natural gas reserves in the United States can now be projected realistically on the same terms as those of other countries.

The United States is also moving forward in the developing of renewable energy technologies, and some are approaching market readiness. Domestic E&P companies, however, are the “boots on the ground” in developing the hydrocarbon energy resources that will remain the primary foundation of our country’s energy system for the 21<sup>st</sup> century.

The United States has the opportunity, taking advantage of new technologies and recent discoveries by domestic E&P companies, to continue increasing domestic production and reduce petroleum imports to less than 50% of consumption by 2018. We should continue investing in the development of additional advanced energy technologies and creating sustainable, long-term American jobs.

Independent exploration and production companies (E&Ps) are leading the development of huge new domestic reserves of crude oil and natural gas in the United States, not the major integrated producers and refiners, such as ExxonMobil.

Independent E&Ps drilled 90% of all oil and gas wells drilled in the lower 48 United States in 2008-2009. They produce 86% of all natural gas and 68% of all crude oil in the United States.

**The tax preferences targeted by the Administration disproportionately affect domestic, independent oil and gas producers, and if enacted would be devastating to the industry.**

**The effect of eliminating these preferences will be to decrease the amount of oil and gas produced in the U. S. and increase, not decrease our reliance on imported oil during the transition period to greener energy sources. One of the most significant preferences, percentage depletion, is only available to domestic independent producers and may not be utilized by major, integrated oil companies. Another of the significant preferences, intangible drilling costs, is only fully available to domestic independent producers and can only be partially used by major, integrated oil companies and then only for their domestic activities.**

Independents, not Big Oil, were the essential players with the service companies in developing the advanced technologies – horizontal/directional drilling and high-pressure fracing -- that resulted in the “quiet energy revolution.” (“The Quiet Energy Revolution,” by Max Schulz, *The American* magazine, February 2010) Independents also led in the development of the key U.S. shale plays – Barnett, Fayetteville, Bakken, Haynesville, Marcellus, etc. -- that have transformed domestic energy production and reserves.

Contrary to conventional wisdom, the U.S. is becoming increasingly self-sufficient by growing domestic production and reserves of crude oil, natural gas and natural gas liquids. We are reducing the percentage of petroleum liquid imports needed to meet demand.

Although one often hears, “The U.S. imports 70% of the crude oil, mainly from hostile, unstable countries,” this is misleading on a number of levels. Crude oil and natural gas liquids – not just crude oil – are the key inputs in the U.S. refinery complex, and U.S. production of each is growing. With the growth in U.S. natural gas production, U.S.-produced NGLs now constitute 40% of the overall input stream.

As a result, in the second half of 2009, U.S. production of crude oil and natural gas liquids equaled 47% of national consumption of 18.6 million barrels per day. Imports constituted only 53%, and that number is declining. (U.S. Energy Information Agency, February 2010)

The EIA projects that U.S. reliance on imported oil as a share of U.S. liquids use will decline to 45% by 2035. (EIA, Annual Energy Outlook 2010)

As for imports from “hostile countries,” in November 2009 Canada remained our largest source for net petroleum imports, accounting for 2.3 million barrels per day. This was more than the combined totals for Venezuela (#3), Saudi Arabia (#4) and Russia (#8). Nigeria was our second largest source of net imports, and Mexico is #5.

The 2009 change in SEC rules to recognize the extent of continuous accumulation resource plays will move the U.S. crude oil reserve base to the more realistic number of 10% of the world’s actual proved reserves, mirroring our production volumes.

Another often-stated misunderstanding is that we are running out of crude oil and natural gas. World and U.S. reserves are actually increasing, driven by advances in exploration and well-completion technology and the efforts of U.S. independent exploration and production companies.

As of November 2009, the United States was the third largest liquid petroleum producer in the world (9.3 million barrels per day), behind Russia (10.1 million) and Saudi Arabia (9.9 million). (U.S. Energy Information Administration, 2010)

U.S. production is also increasing. U.S. crude oil production averaged 5.5 million barrels per day in November 2009, compared to 5.0 million Bpd in November 2007 and 4.8 million Bpd in November 2005. This four-year positive trend reversed decades of falling U.S. production in the United States, and relates directly to advances in drilling and well-completion technology that have enabled new discoveries in the last decade, such as shale plays, to be economically developed. (EIA, U.S. Field Production of Crude Oil).

“Assuming that in the near future consumption returned to 2008 levels and then stayed constant, our planet’s proven reserves of oil – currently estimated at between 1.1 trillion and 1.3 trillion barrels – would have about 40 years to go. (However) advanced exploration and extraction methods can keep oil production growing for decades to come and could allow oil supplies to last at least another century.” (“Squeezing More Oil from the Ground,” by Leonardo Maugeri, Scientific American magazine, October 2009)

In late 2009, the United States overtook Russia as the #1 producer of natural gas in the world. (EIA, February 2010)

Estimated U.S. natural gas supplies have increased 35% in the last two years as a result of technological advances in horizontal drilling and well completion. “When the Petroleum Gas Committee’s results are combined with the U.S. Department of Energy’s latest available determination of proved gas reserves, 238 trillion cubic feet as of year-end 2007, the United States has a total available future supply of 2,073 Tcf, an increase of 542 Tcf over the previous evaluation.” (Colorado School of Mines, Potential Gas Committee release, June 18, 2009)

The Bakken Shale Play of North Dakota and Montana is a clear example of American entrepreneurial investment, technology development and resourcefulness. The Bakken illustrates the path to reducing our dependence on imported petroleum, while providing high-paying jobs to U.S. workers.

In 1995, the U.S. Geological Survey (Department of the Interior) assessed the Bakken Shale Play as having recoverable reserves of 150 million barrels of oil, based on current technology at that time. (USGS, National Assessment of Oil and Gas Fact Sheet, April 2008.)

However, the advent of horizontal/directional drilling and multi-stage fracture stimulation technologies in the last 15 years greatly increased the productivity of the tight shale rock of the Bakken play. As a result, in April 2008 – only 13 years later – the USGS re-assessed the Bakken Shale Play as having recoverable reserves of 3 billion to 4.3 billion barrels of crude oil, using current technology, or 28 times the 1995 estimate. The Bakken is the largest oil accumulation in the onshore, lower-48 states ever assessed by the USGS. (USGS, National Assessment of Oil and Gas Fact Sheet, April 2008.)

Since the April 2008 assessment, Continental has led in the development of a second reservoir, the Three Forks/Sanish Formation, which underlies the traditional target – the Middle Bakken

shale – in most of the Bakken Shale Play. The industry now estimates that the likely amount of recoverable oil in the Bakken may be double the USGS’s 2008 estimate.

As a result of the Bakken Shale ‘s development, crude oil production in North Dakota averaged 245,490 barrels per day in November 2009, a 78% increase over the average production of 137,642 bpd in January 2008.

As of year-end 2007, the oil and gas industry in North Dakota accounted for 39,702 direct and indirect jobs, approximately 9% of the state’s total nonfarm employment base. (North Dakota Policy Council)

North Dakota is one of only four states currently that do not have budget shortfalls – the others being South Dakota, Montana and Wyoming. All four states benefit significantly from hydrocarbon energy revenues. (The Kiplinger Letter, January 29, 2010)

As of late summer 2009, North Dakota had a budget surplus of \$1.2 billion, the nation’s lowest unemployment rate at 4.2%, and more than 9,000 unfilled jobs. (“In N.D., the Road to Economic Recovery,” Washington Post, August 14, 2009)

The U.S. energy industry has an excellent track record of finding and developing new domestic energy reserves, minimizing environmental impact and creating high-paying jobs. For two decades, U.S. independents have consistently led the technology revolution in the oil patch, especially in horizontal drilling and hydro-fracture stimulation, using environmentally-sound and industry-proven safe practices.

Horizontal drilling minimizes the number of surface holes that are drilled in an unconventional resource play, resulting in a reduced surface footprint while accessing a large, oil-or-gas bearing formation. Continental has trademarked the term “ECO-Pad” in our North Dakota Bakken development. Instead of one five-acre pad per well, we are drilling four wells per seven-acre drilling pad, greatly reducing surface disturbance.

The U.S. oil and natural gas industry has also been an engine for growth in the U.S. economy, accounting for 9.2 million jobs and adding \$1 trillion. (American Petroleum Institute, 2009).

The United States cannot quickly transition from a hydrocarbon-based energy system to renewable energy sources. Energy system conversions require decades of technology and infrastructure development as new energy technologies become market-ready.

While non-fossil energy use is expected to grow rapidly, the EIA projects that fossil fuels will still account for 78% of U.S. energy consumption in 2035 – two and a half decades from today. (EIA, Annual Energy Outlook 2010) Crude oil currently supplies 94% of the nation’s transportation fuel. The EIA estimates that by 2035, crude oil will still account for 85% of transportation fuel, despite advances in natural-gas and battery-powered engines.

“Energy transitions from established prime movers to new converters take place across time spans measured in decades, not in a decade... In the case of primary energy supply, the time span needed for significant market penetration is mostly the function of financing, developing, and perfecting necessarily massive and expensive infrastructures. For example,

the world oil industry annually handles more than 30 billion barrels, or four billion tons, of liquids and gases; it extracts the fuel in more than 100 countries and its facilities range from self-propelled geophysical exploration rigs to sprawling refineries, and include about 3,000 large tankers and more than 300,000 miles of pipelines. Even if an immediate alternative were available, writing off this colossal infrastructure that took more than a century to build would amount to discarding an investment worth well over \$5 trillion—but it is quite obvious that its energy output could not be replicated by any alternative in a decade or two.” (“Moore’s Curse and the Great Energy Delusion,” by Vaclav Smil, University of Manitoba, The American, A Magazine of Ideas, November 19, 2008)

“New promises of rapid shifts in energy sources and new anticipations of early massive gains from the deployment of new conversion techniques create expectations that will not be met and distract us from pursuing real solutions. Unfortunately, there is no shortage of these unrealistic calls, such as the popular claim that America should seek to generate 30% of its electricity supply from wind power by 2030.” (Ibid, Vaclav Smil)

We have the technology to continue reducing pollutant emissions from burning hydrocarbon fuels, and we should continue to invest in the development of these, as well as investing in the development of renewable alternatives.

We should encourage increased U.S. production growth, targeting the reduction of energy imports to less than 50% of our consumption by 2018. We should continue investing in the development of additional advanced energy technologies, and, in the case of all fuel technologies, the creation of sustainable, long-term jobs.

According to the preliminary summary of EIA’s “Annual Energy Outlook 2010,” U.S. production of petroleum liquids and biofuels is expected to surpass 50% of U.S. consumption in 2026. If we maintained the pace of improvement achieved from 2008 to 2009, we would hit the 50% mark in 2018. How would this benefit the United States?

1. More domestic production would strengthen the U.S. economy and the U.S. dollar worldwide.
2. Less dependence on imported oil will strengthen U.S. national security and reduce currency transfers to unstable countries in the Middle East.
3. Less dependence on imported oil will improve the U.S. trade balance.
4. Increased U.S. production will reduce commodity price volatility and increase U.S. employment.
5. Increased U.S. production will generate a pro-American psychological lift for the American public/consumer.

## CONCLUSION

U.S. supplies of both crude oil and natural gas have been underdeveloped for the past 50 years. Development was curtailed by the huge influx of cheap foreign oil, regulated only by the whims of OPEC, and by harmful regulations and anti-development energy policies. These included windfall profits taxes and the elimination of most of the depletion allowance, despite the fact that 136 other mineral producers receive depletion allowances, including such non-strategic elements as sand and gravel. Government policy also scaled back intangible drilling cost treatment from the integrated oil companies and imposed tax measures that incentivized companies to find and develop oil and gas resources outside the United States. Throughout most of the last 50 years, oil and gas commodity prices remained at sub-economic lows below U.S. development thresholds.

As a result, the oil and gas exploration and production industry has operated at half capacity or less for a lengthy time, preserving much of the remaining U.S. supply. The combination of these factors resulted in the much bally-hoed “energy crisis” of 2008, which is now a fading memory. Gasoline at the pump is less than \$3 per gallon, and natural gas reserves have surged 50% in the past five years. Our U.S. crude oil supply is on the upswing as the largest ever onshore, lower-48 field – the Bakken Shale Play of North Dakota and Montana -- is developed.

We have the strategic opportunity and the technology to develop the Bakken field, as well as other shale plays, but to do so we must have an economic and regulatory environment that supports development of this vital U.S. resource. Market disruption from additional new Canadian pipeline deliveries must be properly managed and sufficient take-away capacity must be provided. A sound domestic pipeline and refining infrastructure is crucial for the growth and development of U.S. supply.

With a positive focus on U.S. oil and natural gas supply development, we can make meaningful additional strides toward reducing our dependence on foreign imports over the next decade. **Punitive tax policy changes that single out crude oil and natural gas producers will delay this development. The bottom line is that if it is the intention of the Administration to decrease our reliance on imported oil, eliminating particular tax preferences for domestic independent producers will not accomplish the Administration’s objective.** As has been demonstrated these past few years, our domestic oil and gas potential is large and development imminent if the U.S. energy industry is not further burdened with punitive regulations and market manipulation.