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NUEVO ENERGY CO
Form 10-Q
May 15, 2002

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

FORM 10-Q

(Mark One)

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

FOR THE QUARTERLY PERIOD ENDED MARCH 31, 2002

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 1-10537

NUEVO ENERGY COMPANY
(Exact Name of Registrant as Specified in Its Charter)

DELAWARE
(State or other jurisdiction of
incorporation or organization)

76-0304436
(I.R.S. Employer Identification No.)

1021 MAIN, SUITE 2100, HOUSTON, TEXAS
(Address of principal executive offices)

77002
(Zip Code)

Registrant's telephone number, including area code: (713) 652-0706

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 No

Indicate the number of shares outstanding of each of the issuer's classes of common stock, as of the latest practicable date.

Common Stock, par value \$.01 per share. Shares outstanding on May 10, 2002:

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17,083,426.

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NUEVO ENERGY COMPANY
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PART I - FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS

NUEVO ENERGY COMPANY
CONDENSED CONSOLIDATED STATEMENTS OF INCOME
(IN THOUSANDS, EXCEPT PER SHARE DATA)
(UNAUDITED)

Quarter Ended
March 31,

2002

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| | | |
|--|-----------|-------|
| Revenues | | |
| Crude oil and liquids | \$ 70,925 | \$ |
| Natural gas | 7,201 | |
| Other income | 6 | |
| | ----- | ----- |
| | 78,132 | |
| | ----- | ----- |
| Costs and expenses | | |
| Lease operating expenses | 38,064 | |
| Exploration costs | 1,058 | |
| General and administrative expenses | 6,083 | |
| Depreciation, depletion and amortization | 19,158 | |
| Other | 24 | |
| Loss on disposition of properties | -- | |
| | ----- | ----- |
| | 64,387 | |
| | ----- | ----- |
| Income from operations | 13,745 | |
| Derivative gain (loss) | (756) | |
| Interest income | 108 | |
| Interest expense | (9,004) | |
| Dividends on Company-Obligated Mandatorily Redeemable Convertible Preferred Securities of Nuevo Financing I (TECONS) | (1,653) | |
| | ----- | ----- |
| Income before income tax | 2,440 | |
| Income tax expense | | |
| Current | -- | |
| Deferred | 978 | |
| | ----- | ----- |
| | 978 | |
| | ----- | ----- |
| Net income | \$ 1,462 | \$ |
| | ===== | ===== |
| Earnings per common share | | |
| Basic | \$ 0.09 | \$ |
| | ===== | ===== |
| Diluted | \$ 0.08 | \$ |
| | ===== | ===== |
| Weighted average shares outstanding | | |
| Basic | 17,000 | |
| | ===== | ===== |
| Diluted | 17,176 | |
| | ===== | ===== |

See accompanying notes.

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| | | Ma |
|---|--|--------------------------------------|
| | | (UN |
| | | ASSETS |
| Current assets | | |
| Cash and cash equivalents | | \$ |
| Accounts receivable, net | | |
| Inventory | | |
| Assets held for sale | | |
| Assets from price risk management activities | | |
| Prepaid expenses and other | | |
| Total current assets | | |
| Property and equipment, at cost | | |
| Land | | |
| Oil and gas properties (successful efforts method) | | 1 |
| Gas plant facilities | | |
| Other facilities | | |
| Accumulated depreciation, depletion and amortization | | 1 |
| Total property and equipment, net | | |
| Deferred tax assets, net | | |
| Other assets | | |
| Total assets | | \$ ===== |
| | | LIABILITIES AND STOCKHOLDERS' EQUITY |
| Current liabilities | | |
| Accounts payable | | \$ |
| Accrued interest | | |
| Other accrued liabilities | | |
| Total current liabilities | | |
| Long-term debt (Note 4) | | |
| Other long-term liabilities | | |
| TECONS | | |
| Commitments and contingencies (Note 7) | | |
| Stockholders' equity | | |
| Preferred stock, 7% Cumulative Convertible, \$1.00 par value, 10,000,000 shares authorized; none issued and outstanding in 2002 and 2001 | | |
| Common stock, \$0.01 par value, authorized 50,000,000 shares; issued 20,998,662 shares in 2002 and 20,905,796 shares in 2001 | | |
| Additional paid-in capital | | |
| Treasury stock (at cost) 3,877,077 shares in 2002 and 3,902,721 shares in 2001 ... | | |
| Stock held by benefit trust, 61,209 shares in 2002 and 122,995 shares in 2001 | | |
| Deferred stock compensation | | |
| Accumulated other comprehensive income (loss) | | |
| Accumulated deficit | | |
| Total stockholders' equity | | |

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Total liabilities and stockholders' equity \$

See accompanying notes.

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NUEVO ENERGY COMPANY
 CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
 (IN THOUSANDS)
 (UNAUDITED)

| | Quarter Ended March 2002 | |
|---|-----------------------------|-------|
| | ----- | ----- |
| Cash flows from operating activities | | |
| Net income | \$ 1,462 | \$ |
| Adjustments to reconcile net income to net cash provided by operating activities | | |
| Depreciation, depletion and amortization | 19,158 | |
| Dry hole costs | 90 | |
| Amortization of debt financing costs | 602 | |
| Loss on sale of assets, net | -- | |
| Deferred income taxes | 978 | |
| Other | 797 | |
| | ----- | ----- |
| | 23,087 | |
| Working capital changes, net of non-cash transactions | | |
| Accounts receivable | 3,765 | |
| Accounts payable | (7,813) | |
| Other | (6,717) | |
| | ----- | ----- |
| Net cash provided by operating activities | 12,322 | |
| | ----- | ----- |
| Cash flows from investing activities | | |
| Additions to oil and gas properties | (15,354) | |
| Acquisitions of oil and gas properties | -- | |
| Additions to gas plant and other facilities | (1,013) | |
| | ----- | ----- |
| Net cash used in investing activities | (16,367) | |
| | ----- | ----- |
| Cash flows from financing activities | | |
| Debt issuance and modification costs | -- | |
| Payments of long-term debt | -- | |
| Net repayments of credit facility | (1,525) | |
| Proceeds from exercise of stock options | 759 | |
| Purchase of treasury shares | -- | |
| | ----- | ----- |
| Net cash used in financing activities | (766) | |
| | ----- | ----- |

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| | | |
|---|----------|-------|
| Decrease in cash and cash equivalents | (4,811) | |
| Cash and cash equivalents | | |
| Beginning of period | 7,110 | |
| | ----- | |
| End of period | \$ 2,299 | \$ |
| | ===== | ===== |

See accompanying notes.

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NUEVO ENERGY COMPANY
CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME (LOSS)

(IN THOUSANDS)
(UNAUDITED)

| | | |
|--|--|-------|
| | | Quar |
| | | 200 |
| | | ----- |
| Net income | | \$ |
| Unrealized gains (losses) from cash flow hedging activity: | | |
| Cumulative-effect transition adjustment (net of tax of \$10,784 in 2001) | | |
| Reclassification of initial cumulative effect transition adjustment at original value (net of tax of \$1,122 in 2002 and \$6,084 in 2001) | | (|
| Additional reclassification adjustments for changes in initial value to settlement date (net of tax of \$766 in 2002 and \$1,328 in 2001) | | (|
| Changes in fair value of derivative instruments during the period (net of tax of \$7,905 in 2002 and \$6,883 in 2001) | | (1 |
| | | ----- |
| Other comprehensive income (loss) | | (1 |
| | | ----- |
| Comprehensive income (loss) | | \$ (1 |
| | | ===== |

See accompanying notes.

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NUEVO ENERGY COMPANY
NOTES TO THE CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

1. BASIS OF PRESENTATION

Our 2001 Annual Report on Form 10-K includes a summary of our significant accounting policies and other disclosures. You should read it in conjunction with this Quarterly Report on Form 10-Q. The financial statements as of March 31, 2002, and for the quarters ended March 31, 2002 and 2001, are

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unaudited. The balance sheet as of December 31, 2001, is derived from the audited balance sheet filed in the Form 10-K. These financial statements have been prepared pursuant to the rules and regulations of the U.S. Securities and Exchange Commission and do not include all disclosures required by accounting principles generally accepted in the United States. In our opinion, we have made all adjustments, all of which are of a normal, recurring nature, to fairly present our interim period results. Information for interim periods may not necessarily indicate the results of operations for the entire year due to the seasonal nature of our business. The prior period information also includes reclassifications which were made to conform to the current period presentation. These reclassifications have no effect on our reported net income, cash flows or stockholders' equity.

Our accounting policies are consistent with those discussed in our Form 10-K, except as discussed below. You should refer to our Form 10-K for a further discussion of those policies.

Accounting for the Impairment or Disposal of Long-Lived Assets.

In October 2001, the Financial Accounting Standards Board ("FASB") issued Statement of Financial Accounting Standards ("SFAS") No. 144, Accounting for the Impairment or Disposal of Long-Lived Assets. This Statement requires that long-lived assets that are to be disposed of by sale be measured at the lower of book value or fair value less cost to sell. The standard also expanded the scope of discontinued operations to include all components of an entity with operations that can be distinguished from the rest of the entity and that will be eliminated from the ongoing operations of the entity in a disposal transaction. We adopted the provisions of this statement effective January 1, 2002 and it had no impact on our financial statements.

Accounting for Asset Retirement Obligations.

In August 2001, the FASB issued SFAS No. 143, Accounting for Asset Retirement Obligations. This Statement requires companies to record a liability relating to the retirement and removal of assets used in their business. The liability is discounted to its present value, and the related asset value is increased by the amount of the resulting liability. Over the life of the asset, the liability will be accreted to its future value and eventually extinguished when the asset is taken out of service. The provisions of this Statement are effective for fiscal years beginning after June 15, 2002. We are currently evaluating the effects of this pronouncement

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2. RESTRUCTURING CHARGES

Termination of Outsourcing Agreements.

Effective March 15, 2002, we terminated two outsourcing agreements with the objective of exercising greater control over certain operating functions and lowering our costs. The terminated outsourcing agreements related to the California field operations and human resources. We now employ a majority of the field employees currently working on our California properties and the human resources function was brought in-house.

Reorganization of Exploration and Production Operations.

We have reorganized our exploration and production operations in an effort to create a smaller, more focused exploitation program and eliminated our

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California exploration program. In connection with the reorganization, approximately 20 technical positions were eliminated in late 2001.

The following table details the amounts related to our restructuring:

| | Liability at December 31, 2001 | Payments in 2002 | Liability at March 31, 2002 |
|------------------------------|--------------------------------------|---------------------|-----------------------------------|
| | (In thousands) | | |
| Severance and benefits | \$ 1,675 | \$ 1,452 | \$ 223 |
| Contract termination | 2,681 | 2,512 | 169 |
| | \$ 4,356 | \$ 3,964 | \$ 392 |

We expect that the balance of the restructuring liability will be paid during the second quarter of 2002.

3. EARNINGS PER SHARE

SFAS No. 128, Earnings per Share, requires a reconciliation of the numerator (income) and denominator (shares) of the basic earnings per share computation to the numerator and denominator of the diluted earnings per share computation. The reconciliation is as follows:

| | Quarter Ended March | | |
|--|---------------------|--------|--------|
| | 2002 | | |
| | Net Income | Shares | Net In |
| | (In thousands) | | |
| Earnings - Basic | \$ 1,462 | 17,000 | \$ |
| Effect of dilutive securities | | | |
| Stock options and restricted stock | -- | 122 | |
| Shares held by benefit trust | (38) | 54 | |
| Earnings - Diluted | \$ 1,424 | 17,176 | \$ |

4. LONG-TERM DEBT

Our long-term debt consisted of the following:

| | March 31, 2002 |
|--|-------------------|
| | (In thous |
| 9 3/8% Senior Subordinated Notes due 2010 | \$ 150,000 |
| 9 1/2 % Senior Subordinated Notes due 2008 | 257,210 |

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| | |
|--|------------|
| 9 1/2 % Senior Subordinated Notes due 2006 | 2,367 |
| Bank credit facility (3.58% on March 31, 2002 and 3.71% on December 31, 2001) | 39,975 |
| | ----- |
| Total debt | 449,552 |
| Interest rate swaps fair value adjustment | (7,763) |
| | ----- |
| Long-term debt | \$ 441,789 |
| | ===== |

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5. FINANCIAL INSTRUMENTS

We have entered into commodity swaps, put options and interest rate swaps. The commodity swaps and put options are designated as cash flow hedges and the interest rate swaps are designated as fair value hedges in accordance with SFAS 133. Quantities covered by the commodity swaps and put options are based on West Texas Intermediate ("WTI") barrels. Our production is expected to average 72% of WTI, therefore, each WTI barrel hedges 1.37 barrels of our production.

Derivative Instruments Designated as Cash Flow Hedges

At March 31, 2002, we had entered into the following cash flow hedges:

| | WTI Barrels Per Day ----- | Average Price / Bbl ----- |
|---------------------------|------------------------------------|---------------------------------|
| Swaps | | |
| Second quarter 2002 | 13,000 | 24.45 |
| Third quarter 2002 | 13,000 | 23.95 |
| Fourth quarter 2002 | 13,000 | 24.12 |
| First quarter 2003 | 8,000 | 23.59 |
| Second quarter 2003 | 6,000 | 23.30 |
| Third quarter 2003 | 6,000 | 23.21 |
| Put Options | | |
| Second quarter 2002 | 14,000 | 22.00 |
| Third quarter 2002 | 9,000 | 22.00 |
| Fourth quarter 2002 | 9,000 | 22.00 |

Subsequent to March 31, 2002, we entered into the following cash flow hedges:

| | WTI Barrels Per Day ----- | Average Price / Bbl ----- |
|---------------------------|------------------------------------|---------------------------------|
| Second quarter 2002 | 4,000 | \$ 26.56 |
| Third quarter 2002 | 5,000 | 26.55 |

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| | | |
|---------------------------|-------|-------|
| Fourth quarter 2002 | 4,000 | 26.07 |
| First quarter 2003 | 2,000 | 24.50 |
| Second quarter 2003 | 4,000 | 24.13 |
| Third quarter 2003 | 4,000 | 23.91 |
| Fourth quarter 2003 | 8,000 | 23.34 |

Derivative Instruments Designated as Fair Value Hedges

We have entered into three interest rate swap agreements with notional amounts totaling \$200 million, to hedge the fair value of our 9 1/2% Notes due 2008 and our 9 3/8 % Notes due 2010. These swaps are designated as fair value hedges and are reflected as a reduction of long-term debt of \$7.8 million as of March 31, 2002, with a corresponding increase in other long-term liabilities. Under the terms of the agreements for the 9 3/8 % Notes, the counterparty pays us a weighted average fixed annual rate of 9 3/8 % on total notional amounts of \$150 million, and we pay the counterparty a variable annual rate equal to the six-month and three-month LIBOR rate plus a weighted average rate of 3.49%. Under the terms of the agreement for the 9 1/2% Notes, the counterparty pays us a weighted average fixed annual rate of 9 1/2% on total notional amounts of \$50 million, and we pay the counterparty a variable annual rate equal to the six-month LIBOR rate plus a weighted average rate of 3.92%.

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Derivative Instruments Not Designated as Hedges

In December 2001, Enron Corp. ("Enron") and certain of its affiliates filed voluntary petitions for reorganization under Chapter 11 of the United States Bankruptcy Code. Once a deterioration in creditworthiness creates uncertainty as to whether the future cash flows from the hedging instrument will be highly effective in offsetting the hedged risk, the derivative instrument is no longer considered highly effective and no longer qualifies for hedge accounting treatment. At such time, the fair value of the derivative asset or liability is adjusted to its new fair value, with the change in value being charged to current earnings. The net gain or loss of the derivative instruments previously reported in other comprehensive income remains in accumulated other comprehensive income and is reclassified into earnings during the period in which the originally designated hedge items affect earnings. At March 31, 2002, a deferred gain of \$2.2 million remains in accumulated other comprehensive income related to the outstanding Enron options, which will be reclassified into earnings when the hedged production occurs, during the remainder of 2002.

In 2001 and 2000, we entered into call spreads with the anticipation of using the proceeds to offset the Unocal Contingent payment. Subsequent to entering into the call spreads, the market fell and as a result, offsetting call spreads were purchased to economically nullify the trade. All of our existing call spreads had been offset through the purchase of a mirror spread, however, the call spread with Enron was cancelled. The remaining mirror call spread is not designated as a hedge instrument and is marked-to-market with changes in fair value recognized in earnings. The value decreased during the quarter ended March 31, 2002 and we recorded a loss of \$0.6 million. At March 31, 2002, \$1.7 million is reflected in other long-term liabilities.

6. SEGMENTS

Our operations are the exploration for and production of crude oil and natural gas. For segment reporting purposes, domestic producing areas have been aggregated as one reportable segment due to similarities in their operations as allowed by SFAS No. 131, Disclosures About Segments of an Enterprise and Related

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Information. Financial information by reportable segment is presented below:

| | For the Quarter Ended March | | |
|--|-----------------------------|------------------------|---------|
| | Oil and Gas Domestic | Oil and Gas Foreign | Other (|
| | (In thousands) | | |
| Revenues from external customers | \$ 70,728 | \$ 7,398 | \$ |
| Operating income before income tax | 18,126 | 2,344 | (18 |

| | For the Quarter Ended March | | |
|--|-----------------------------|------------------------|---------|
| | Oil and Gas Domestic | Oil and Gas Foreign | Other (|
| | (In thousands) | | |
| Revenues from external customers | \$ 112,161 | \$ 4,992 | \$ |
| Operating income before income tax | 38,114 | (510) | (21 |

(1) Includes unallocated corporate expenses.

7. CONTINGENCIES AND OTHER MATTERS

On September 22, 2000, we were named as a defendant in the lawsuit Thomas Wachtell et al. versus Nuevo Energy Company in the Superior Court of Los Angeles County, California. We successfully removed this lawsuit to the United States District Court for the Central District of California. The plaintiffs, who own certain interests in the Point Pedernales properties, have asserted numerous causes of action including breach of contract, fraud and conspiracy in connection with the plaintiff's allegation that: (i) royalties have not been properly paid to them for production from the Point Pedernales field, (ii) payments have not been made to them related to production from the Pescado and Sacate field, and (iii) we have failed to recognize the plaintiff's interests in the Tranquillon Ridge project. The plaintiffs have not specified damages. We intend to vigorously contest these claims.

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We have been named as a defendant in certain other lawsuits incidental to our business. However, these actions and claims in the aggregate seek substantial damages against us and are subject to the inherent uncertainties in any litigation. We are defending ourselves vigorously in all such matters.

We have reserved an amount that we deem adequate to cover any potential losses related to the matters discussed above. This amount is reviewed periodically and changes may be made, as appropriate. Any additional costs related to these potential losses are not expected to be material to our operating results, financial condition or liquidity.

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In September 1997, there was a spill of crude oil into the Santa Barbara Channel from a pipeline that connects our Point Pedernales field with shore-based processing facilities. The volume of the spill was estimated to be 163 barrels of oil. Repairs were completed by the end of 1997, and production recommenced in December 1997. The costs of the clean up and the cost to repair the pipeline either have been or are expected to be covered by our insurance, less a deductible of \$0.1 million. As of March 31, 2002, we had received insurance reimbursements of \$4.2 million, with a remaining insurance receivable of \$0.5 million. We also have exposure to costs that may not be recoverable from insurance, including certain fines, penalties, and damages and certain legal fees. Such costs are not quantifiable at this time, but are not expected to be material to our operating results, financial condition or liquidity.

Our international investments involve risks typically associated with investments in emerging markets such as an uncertain political, economic, legal and tax environment and expropriation and nationalization of assets. In addition, if a dispute arises in our foreign operations, we may be subject to the exclusive jurisdiction of foreign courts or may not be successful in subjecting foreign persons to the jurisdiction of the United States. We attempt to conduct our business and financial affairs to protect against political and economic risks applicable to operations in the various countries where we operate, but there can be no assurance that we will be successful in so protecting ourselves. A portion of our investment in the Congo is insured through political risk insurance provided by Overseas Private Investment Company ("OPIC"). The political risk insurance through OPIC covers up to \$25.0 million relating to expropriation and political violence, which is the maximum coverage available through OPIC. We have no deductible for this insurance.

In connection with our February 1995 acquisitions of two subsidiaries (each a "Congo subsidiary") owning interests in the Yombo field offshore Congo, we and a wholly-owned subsidiary of CMS NOMEKO Oil & Gas Co. ("CMS") agreed with the seller of the subsidiaries not to claim certain tax losses ("dual consolidated losses") incurred by such subsidiaries prior to the acquisitions. Under the tax law in the Congo, as it existed when this acquisition took place, if an entity is acquired in its entirety and that entity has certain tax attributes, for example tax loss carryforwards from operations in the Republic of Congo, the subsequent owners of that entity can continue to utilize those losses without restriction. Pursuant to the agreement, we and CMS may be liable to the seller for the recapture of dual consolidated losses (net operating losses of any domestic corporation that are subject to an income tax of a foreign country without regard to the source of its income or on a residence basis) utilized by the seller in years prior to the acquisitions if certain triggering events occur, including (i) a disposition by either us or CMS of its respective Congo subsidiary, (ii) either Congo subsidiary's sale of its interest in the Yombo field, (iii) the acquisition of us or CMS by another consolidated group or (iv) the failure of us or CMS's Congo subsidiary to continue as a member of its respective consolidated group. A triggering event will not occur, however, if a subsequent purchaser enters into certain agreements specified in the consolidated return regulations intended to ensure that such dual consolidated losses will not be claimed. The only time limit associated with the occurrence of a triggering event relates to the utilization of a dual consolidated loss in a foreign jurisdiction. A dual consolidated loss that is utilized to offset income in a foreign jurisdiction is only subject to recapture for 15 years following the year in which the dual consolidated loss was incurred for U.S. income tax purposes. We and CMS have agreed that the party responsible for the triggering event shall indemnify the other for any liability to the seller as a result of such triggering event. Our potential direct liability could be as much as \$38.5 million if a triggering event occurs. Additionally, we believe that CMS's liability (for which we would be jointly liable with an indemnification right against CMS) could be as much as \$56.2 million. We do not expect a triggering event to occur with respect to us or CMS and do not believe

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the agreement will have a material adverse effect upon us.

ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

RESULTS OF OPERATIONS

Our results of operations are significantly affected by fluctuations in oil and gas prices. Success in acquiring oil and gas properties and our ability to maintain or increase production through exploitation activities has also significantly affected our operating results. The following table reflects our production and average prices for oil and natural gas:

| | Quarter Ended March 31, 2000 | 2001 |
|---------------------------|---------------------------------|-----------|
| | ----- | ----- |
| Crude Oil and Liquids | | |
| Sales Volumes (MBbls/day) | | |
| Domestic | 41.5 | 43.7 |
| Foreign | 5.0 | 2.8 |
| | ----- | ----- |
| Total | 46.5 | 46.5 |
| | ===== | ===== |
| Sales Prices (\$/Bbl) | | |
| Unhedged | \$ 15.82 | \$ 20.99 |
| Hedged | 16.94 | 15.86 |
| Revenues (\$/thousands) | | |
| Domestic | \$ 59,038 | \$ 83,168 |
| Foreign | 7,651 | 6,039 |
| Congo Earnout | (253) | (1,047) |
| Marketing Fees | (194) | (253) |
| Hedging | 4,683 | (21,477) |
| | ----- | ----- |
| Total | \$ 70,925 | \$ 66,430 |
| | ===== | ===== |
| Natural Gas | | |
| Sales Volumes (MMcf/day) | | |
| Domestic | 36.2 | 42.5 |
| | ===== | ===== |
| Sales Prices (\$/Mcf) | | |
| Unhedged | \$ 2.21 | \$ 13.26 |
| Revenues (\$/thousands) | | |
| Domestic | \$ 7,289 | \$ 51,112 |
| Marketing Fees | (88) | (389) |
| | ----- | ----- |
| Total | \$ 7,201 | \$ 50,723 |
| | ===== | ===== |

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Below is a list of terms commonly used in the oil and gas industry.

| | | |
|-------|---|--|
| /d | = | per day |
| Bbl | = | barrel of crude oil or other liquid hydrocarbons |
| Bcf | = | billion cubic feet of natural gas |
| Bcfe | = | billion cubic feet of natural gas equivalent |
| BOE | = | barrel of oil equivalent, converting gas to oil at the ratio of 6 Mcf of gas to 1 Bbl of oil |
| BOPD | = | barrel of oil per day |
| MBbl | = | thousand barrels |
| Mcf | = | thousand cubic feet of natural gas |
| MMBbl | = | million barrels of oil or other liquid hydrocarbons. |
| MMcf | = | million cubic feet of natural gas |
| MBOE | = | thousand barrels of oil equivalent |
| MMBOE | = | million barrels of oil equivalent |

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QUARTER ENDED MARCH 31, 2002 COMPARED TO QUARTER ENDED MARCH 31, 2001

We had net income of \$1.5 million, or \$0.08 per diluted share for the quarter ended March 31, 2002 as compared to net income of \$9.6 million, or \$0.57 per diluted share in the same period of 2001.

Revenues

Oil and Gas Revenues. Oil and gas revenues decreased 33% to \$78.1 million for the quarter ended March 31, 2002 from \$117.2 million in the same period of 2001 due to significantly lower natural gas prices and lower production which was partially offset by hedging gains in 2002. The realized oil price in the first quarter of 2002 was \$16.94 per Bbl, an increase of \$1.08 per Bbl from the same period in 2001. Oil production in the Congo increased 2.2 MBbls per day due to the favorable results of development drilling last year. The increase was offset by a 2.2 MBbls per day decrease in domestic oil production where production was lower from our thermal properties which is continuing to rise in response to the resumption of steaming in the second half of last year. We had hedging gains of \$4.7 million in the first quarter of 2002 compared to a hedging loss of \$21.5 million in same period of 2001. Natural gas production averaged 36.2 MMcf per day in the first quarter of 2002, declining 15% from the 2001 period of 42.5 MMcf per day. The decline was primarily due to lower domestic production onshore and offshore California. The first quarter 2002 realized natural gas price was \$2.21 per Mcf, which decreased 83% from \$13.26 per Mcf in the prior year period.

Costs and Expenses

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Costs and Expenses. Lease operating expenses ("LOE") for the quarter ended March 31, 2002 totaled \$38.1 million, as compared to \$57.3 million for the 2001 period. The 34% decrease in LOE is principally due to lower steam and workover costs in our California operations. Exploration costs were \$1.1 million in the quarter ended March 31, 2002, a decrease from \$2.7 million in the same period of 2001 which had \$1.5 million of dry hole costs associated with our exploratory well offshore the Republic of Ghana. Depreciation, depletion and amortization ("DD&A") decreased to \$19.2 million in first quarter of 2002 primarily due to lower gas production. The DD&A rate was \$4.05 per BOE in the 2002 period compared to \$4.07 per BOE in 2001. General and administrative expense of \$6.1 million in 2002 was \$1.2 million lower than the comparable period in 2001 due to lower headcount and the timing of expenses.

Derivative Gain (Loss). Our derivative loss for the quarter ended March 31, 2002 is comprised of a loss on our mark-to-market derivatives of \$0.6 million and \$0.1 million of ineffectiveness on our hedges.

Interest Expense. Interest expense of \$9.0 million in the quarter ended March 31, 2002 decreased 19% compared to interest expense of \$11.1 million in the same period of 2001. The decrease is primarily due to the benefit of our interest rate swaps in 2002 of \$1.9 million which more than offset higher average borrowings.

Dividends. Dividends on the TECONS were \$1.7 million in both quarters ended March 31, 2002 and 2001. The TECONS pay dividends at a rate of 5.75% and were issued in December 1996.

Income Tax. We had income tax expense of \$1.0 million in the quarter ended March 31, 2002 compared to an expense of \$6.5 million in the prior year period. Our effective income tax rate was 40.1% in 2002 and 40.3% in 2001.

CAPITAL RESOURCES AND LIQUIDITY

We have grown and diversified our operations through a series of disciplined, low-cost acquisitions of oil and gas properties and the subsequent exploitation and development of these properties. We have historically funded our operations and acquisitions with operating cash flows, bank financing, private and public placements of debt and equity securities, property divestitures and joint ventures with industry participants.

Net cash provided by operating activities was \$12.3 million in the quarter ended March 31, 2002. During that time period, we invested \$15.4 million in oil and gas properties and \$1.0 million on gas plant and other facilities.

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We believe our working capital, cash flow from operations and available financing sources are sufficient to meet our obligations as they become due and to finance our capital budget through 2002. We have a \$225 million borrowing base under our Credit Agreement. Under the most restrictive covenant, \$100 million is available at March 31, 2002 of which we had drawn \$40.0 million under the agreement. In late December 2001 and early January 2002, we entered into interest rate swaps totaling \$200 million; \$150 million on our 9 3/8 % Notes and \$50 million on our 9 1/2% Notes.

CONTINGENCIES AND OTHER MATTERS

Legal Proceedings

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On September 14, 2001, during an annual inspection, we discovered fractures in the heat affected zone of certain flanges on our pipeline that connects the Point Pedernales field with onshore processing facilities. We voluntarily elected to shut-in production in the field while repairs were being made. The daily net production from this field was approximately 5,000 barrels of crude oil and 1.2 MMcf of natural gas, representing approximately 11% of our daily production. We replaced the damaged flanges, as well as others which had not shown signs of damage. Certain costs of repair and costs related to business interruption are expected to be partially covered by insurance. We may have exposure to costs that may not be recoverable from insurance, including those associated with the repair of undamaged equipment. We resumed production in January 2002.

On June 15, 2001, we experienced a failure of a carbon dioxide treatment vessel at the Rincon Onshore Separation Facility ("ROSF") located in Ventura County, California. There were no injuries associated with this event. Crude oil and natural gas produced from three fields offshore California are transported onshore by pipeline to the ROSF plant where crude oil and water are separated and treated, and carbon dioxide is removed from the natural gas stream. The daily net production associated with these fields is 3,000 barrels of crude oil and 2.4 MMcf of natural gas, representing approximately 6% of our daily production. Crude oil production resumed in early July and full gas sales resumed by mid August. The cost of repair, less a \$50,000 deductible, is expected to be covered by insurance. We may have exposure to costs that may not be recoverable from insurance.

On September 22, 2000, we were named as a defendant in the lawsuit Thomas Wachtell et al. versus Nuevo Energy Company in the Superior Court of Los Angeles County, California. We successfully removed this lawsuit to the United States District Court for the Central District of California. The plaintiffs, who own certain interests in the Point Pedernales properties, have asserted numerous causes of action including breach of contract, fraud and conspiracy in connection with the plaintiffs' allegation that: (i) royalties have not been properly paid to them for production from the Point Pedernales field, (ii) payments have not been made to them related to production from the Pescado and Sacate fields and (iii) we have failed to recognize the plaintiffs' interests in the Tranquillon Ridge project. The plaintiffs have not specified damages. We intend to vigorously contest these claims.

On April 5, 2000, we filed a lawsuit against ExxonMobil Corporation in the United States District Court for the Central District of California, Western Division. The Company and ExxonMobil each own a 50% interest in the Sacate field, offshore Santa Barbara County, California. We have alleged that by grossly inflating the fee that ExxonMobil insists we must pay to use an existing ExxonMobil platform and production infrastructure, ExxonMobil failed to submit a proposal for the development of the Sacate field consistent with the unit operating agreement. We, therefore believe that we have been denied a reasonable opportunity to exercise our rights under the unit operating agreement. We have alleged that ExxonMobil's actions breach the unit operating agreement and the covenant of good faith and fair dealing. We are seeking damages and a declaratory judgment as to the payment that must be made to access ExxonMobil's platform and facilities.

We have been named as a defendant in certain other lawsuits incidental to our business. Management does not believe that the outcome of such litigation will have a material adverse impact on our operating results, financial condition or liquidity above the amounts we have reserved to cover any potential losses. However, these actions and claims in the aggregate seek substantial damages against us and are subject to the inherent uncertainties in any litigation. We are defending ourselves vigorously in all such matters.

In September 1997, there was a spill of crude oil into the Santa

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Barbara Channel from a pipeline that connects our Point Pedernales field with shore-based processing facilities. The volume of the spill was estimated to be 163 Bbls of oil. Repairs were completed by the end of 1997 and production recommenced in December

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1997. The costs of the clean-up and the cost to repair the pipeline either have been or are expected to be covered by our insurance, less a deductible of \$0.1 million. As of December 31, 2001, we had received insurance reimbursements of \$4.2 million, with a remaining insurance receivable of \$0.5 million. We also have exposure to costs that may not be recoverable from insurance, including certain fines, penalties, and damages and certain legal fees. Such costs are not quantifiable at this time, but are not expected to be material to our operating results, financial condition or liquidity.

Our international investments involve risks typically associated with investments in emerging markets such as an uncertain political, economic, legal and tax environment and expropriation and nationalization of assets. In addition, if a dispute arises in our foreign operations, we may be subject to the exclusive jurisdiction of foreign courts or may not be successful in subjecting foreign persons to the jurisdiction of the United States. We attempt to conduct our business and financial affairs so as to protect against political and economic risks applicable to operations in the various countries where we operate, but there can be no assurance that we will be successful in so protecting ourselves. A portion of our investment in the Congo is insured through political risk insurance provided by the Overseas Private Investment Corporation ("OPIC"). The political risk insurance through OPIC covers up to \$25.0 million relating to expropriation and political violence, which is the maximum coverage available through OPIC. We have no deductible for this insurance.

In connection with our February 1995 acquisitions of two subsidiaries owning interests in the Yombo field offshore Congo, we and a wholly-owned subsidiary of CMS Gas Co. agreed with the seller of the subsidiaries not to claim certain tax losses ("dual consolidated losses") incurred by such subsidiaries prior to the acquisitions. Under the tax law in the Congo, as it existed when this acquisition took place, if an entity is acquired in its entirety and that entity has certain tax attributes, for example tax loss carryforwards from operations in the Republic of Congo, the subsequent owners of that entity can continue to utilize those losses without restriction. Pursuant to the agreement, we and CMS may be liable to the seller for the recapture of dual consolidated losses (net operating losses of any domestic corporation that are subject to an income tax of a foreign country without regard to the source of its income or on a residence basis) utilized by the seller in years prior to the acquisitions if certain triggering events occur, including:

- o a disposition by either us or CMS of its respective Congo subsidiary,
- o either Congo subsidiary's sale of its interest in the Yombo field,
- o the acquisition of us or CMS by another consolidated group or
- o the failure of CMS's Congo subsidiary or us to continue as a member of its respective consolidated group.

A triggering event will not occur, however, if a subsequent purchaser enters into certain agreements specified in the consolidated return regulations intended to ensure that such dual consolidated losses will not be claimed. The

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only time limit associated with the occurrence of a triggering event relates to the utilization of a dual consolidated loss in a foreign jurisdiction. A dual consolidated loss that is utilized to offset income in a foreign jurisdiction is only subject to recapture for 15 years following the year in which the dual consolidated loss was incurred for U.S. income tax purposes. We and CMS have agreed among ourselves that the party responsible for the triggering event shall indemnify the other for any liability to the seller as a result of such triggering event. Our potential direct liability could be as much as \$38.5 million if a triggering event with respect to us occurs. Additionally, we believe that CMS's liability (for which we would be jointly liable with an indemnification right against CMS) could be as much as \$56.2 million. We do not expect a triggering event to occur with respect to us or CMS and do not believe the agreement will have a material adverse effect upon us.

During 1997, a new government was established in the Congo. Although the political situation in the Congo has not to date had a material adverse effect on our operations in the Congo, no assurances can be made that continued political unrest in West Africa will not have a material adverse effect on us or our operations in the Congo in the future.

In 1996, the Congo government requested that the convention governing the Marine 1 Exploitation Permit be converted to a Production Sharing Agreement ("PSA"). We are under no obligation to convert to a PSA, and our existing convention is valid and protected by law. Our position is that any conversion to a PSA would have no detrimental impact to us, otherwise, we will not agree to any such conversion. Discussions with the government have been ongoing intermittently since early 1997. To date, no final agreement has been reached concerning conversion to a PSA.

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ACCOUNTING PRONOUNCEMENTS NOT YET ADOPTED

Accounting for Asset Retirement Obligations. In August 2001, the FASB issued SFAS No. 143, Accounting for Asset Retirement Obligations. This Statement requires companies to record a liability relating to the retirement and removal of assets used in their business. The liability is discounted to its present value, and the related asset value is increased by the amount of the resulting liability. Over the life of the asset, the liability will be accreted to its future value and eventually extinguished when the asset is taken out of service. The provisions of this Statement are effective for fiscal years beginning after June 15, 2002. We are currently evaluating the effects of this pronouncement.

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CAUTIONARY STATEMENT FOR PURPOSES OF THE "SAFE HARBOR" PROVISIONS OF THE PRIVATE SECURITIES LITIGATION REFORM ACT OF 1995

This report contains or incorporates by reference forward looking statements within the meaning of Section 27A of the Securities Act of 1933, as amended, Section 21E of the Securities Exchange Act of 1934 and the Private Securities Litigation Reform Act of 1995. All statements other than statements of historical facts included in this document, including without limitation, statements in Item 7, Management's Discussion and Analysis of Financial Condition and Results of Operations regarding our financial position, estimated

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quantities and net present values of reserves, business strategy, plans and objectives of our management for future operations and covenant compliance, are forward looking statements. We can give no assurances that the assumptions upon which such forward-looking statements are based will prove to be correct. Important factors that could cause actual results to differ materially from our expectations are included throughout this document. The cautionary statements expressly qualify all subsequent written and oral forward-looking statements attributable to us or persons acting on our behalf.

ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

The information contained in this item updates, and should be read in conjunction with Part II, Item 7A of our Annual Report on Form 10-K for the year ended December 31, 2001.

There are no material changes in our quantitative and qualitative disclosures about market risks from those reported in our Annual Report on Form 10-K for the year ended December 31, 2001.

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PART II - OTHER INFORMATION

ITEM 1. LEGAL PROCEEDINGS

See Part I, Item 1, Financial Statements, Note 7, which is incorporated herein by reference.

ITEM 2. CHANGES IN SECURITIES AND USE OF PROCEEDS

None.

ITEM 3. DEFAULTS UPON SENIOR SECURITIES

None.

ITEM 4. SUBMISSION OF MATTERS TO A VOTE OF SECURITY-HOLDERS

None.

ITEM 5. OTHER INFORMATION

None.

ITEM 6. EXHIBITS AND REPORTS ON FORM 8-K

(a) EXHIBITS

None.

(b) REPORTS ON FORM 8-K:

None.

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SIGNATURES

Pursuant to the requirements of Section 13 or 15(d) the Securities Exchange Act of 1934, the Registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

NUEVO ENERGY COMPANY
(Registrant)

Date: May 15, 2002

By: /s/ James L. Payne

James L. Payne
Chairman, President and
Chief Executive Officer

Date: May 15, 2002

By: /s/ Janet F. Clark

Janet F. Clark
Senior Vice President and
Chief Financial Officer