

PATTERSON UTI ENERGY INC

Form 10-Q/A

March 27, 2006

Table of Contents

UNITED STATES SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549
Form 10-Q/A
(Amendment No. 1)

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

For the quarterly period ended June 30, 2005

OR

o **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 0-22664
PATTERSON-UTI ENERGY, INC.
(Exact name of registrant as specified in its charter)

DELAWARE
(State or other jurisdiction of incorporation or organization)

75-2504748
(I.R.S. Employer Identification No.)

4510 LAMESA HIGHWAY, SNYDER, TEXAS
(Address of principal executive offices)

79549
(Zip Code)

(325) 574-6300
(Registrant's telephone number, including area code)
N/A

(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 No

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

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). Yes No

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

171,706,441 shares of common stock, \$0.01 par value, as of July 28, 2005

**PATTERSON-UTI ENERGY, INC. AND SUBSIDIARIES
TABLE OF CONTENTS**

	Page
<u>Explanatory Note</u>	3
<u>PART I Financial Information</u>	
<u>ITEM 1. Financial Statements</u>	
<u>Unaudited condensed consolidated balance sheets</u>	5
<u>Unaudited condensed consolidated statements of income</u>	6
<u>Unaudited condensed consolidated statement of changes in stockholders' equity</u>	7
<u>Unaudited condensed consolidated statements of changes in cash flows</u>	8
<u>Notes to unaudited condensed consolidated financial statements</u>	9
<u>ITEM 2. Management's Discussion and Analysis of Financial Condition and Results of Operations</u>	23
<u>ITEM 3. Quantitative and Qualitative Disclosures About Market Risk</u>	32
<u>ITEM 4. Controls and Procedures</u>	33
<u>Forward Looking Statements and Cautionary Statements for Purposes of the Safe Harbor Provisions of the Private Securities Litigation Reform Act of 1995</u>	35
<u>PART II Other Information</u>	
<u>ITEM 4. Submission of Matters to a Vote of Security Holders</u>	36
<u>ITEM 6. Exhibits</u>	37
<u>Signatures</u>	38
<u>Certification of CEO Pursuant to Rule 13a-14(a)/15d-14(a)</u>	
<u>Certification of CFO Pursuant to Rule 13a-14(a)-15d-14(a)</u>	
<u>Certification of CEO & CFO Pursuant to 18 USC Section 1350</u>	

Table of Contents**Explanatory Note**

This Amendment No. 1 on Form 10-Q/A (Form 10-Q/A) to our previously filed Quarterly Report on Form 10-Q for the quarterly period ended June 30, 2005, initially filed with the United States Securities and Exchange Commission (SEC) on July 28, 2005 (Original Filing), reflects a restatement of our unaudited interim condensed consolidated financial statements as discussed in Note 2 of the Notes to Unaudited Condensed Consolidated Financial Statements. Previously issued financial statements are being restated to properly reflect losses incurred as a result of an embezzlement whereby payments were made to or for the benefit of Jonathan D. Nelson (Nelson), our former Chief Financial Officer (CFO), that had been reflected in previously issued financial statements as payments for assets and services that were not received by the Company. Previously issued financial statements are also being restated for the effects of the correction of other errors that are immaterial both individually and in the aggregate. These other adjustments relate primarily to previously reported property and equipment balances that resulted from our review of our property and equipment records and the underlying physical assets in connection with investigation of the embezzlement.

The total amount embezzled was approximately \$77.5 million in cash, excluding any tax effects, beginning with the year ended December 31, 1998 through November 3, 2005 as follows (in thousands):

From 1998 to December 31, 2004	\$ 58,961
From January 1, 2005 to September 30, 2005	12,193
Total through September 30, 2005	71,154
From October 1, 2005 to November 3, 2005 (net of \$1,500 repayment)	6,350
Total embezzlement	\$ 77,504

On November 16, 2005 the SEC obtained a freeze order on Nelson's assets (including assets held by entities controlled by him) and a Receiver was appointed to collect those assets. The Company understands that the Receiver will ultimately liquidate the assets and propose a plan to distribute the proceeds. While the Company believes it has a claim for at least the full amount embezzled, other creditors have or may assert claims on the assets held by the Receiver. As a result, recovery by the Company from the Receiver is uncertain as to timing and amount, if any. Recoveries, if any, will be recognized when they are considered collectable.

The effects of the embezzlement on the Company's financial position follow (in thousands):

Decrease in Amounts Previously Reported	June 30, 2005	December 31, 2004
Assets	\$ (62,231)	\$ (56,133)
Liabilities(1)	(23,096)	(20,848)
Retained Earnings & Stockholders' Equity	\$ (39,135)	\$ (35,285)

(1) Consists of increases in Federal and state income taxes payable of \$2.2 million and \$1.3 million at June 30, 2005 and December 31, 2004, respectively, and decreases in deferred tax liabilities of \$25.3 million and \$22.2 million at June 30, 2005 and December 31, 2004, respectively.

Table of Contents

The effects of the restatement due to the embezzlement and other adjustments on operating income as previously reported for the three and six months ended June 30, 2005 and 2004 follow (in thousands):

	Three Months Ended June 30,		Six Months Ended June 30,	
	2005	2004	2005	2004
Operating income:				
As previously reported	\$ 122,416	\$ 30,799	\$ 216,668	\$ 63,309
Adjustment for effects of embezzlement	(4,717)	(3,470)	(6,098)	(8,483)
Other adjustments	(1,048)	(1,002)	(2,086)	(1,929)
As restated	\$ 116,651	\$ 26,327	\$ 208,484	\$ 52,897

The effects of the restatement due to the embezzlement and other adjustments on net income as previously reported for the three and six months ended June 30, 2005 and 2004 follow (in thousands):

	Three Months Ended June 30,		Six Months Ended June 30,	
	2005	2004	2005	2004
Net income:				
As previously reported	\$ 77,665	\$ 19,607	\$ 137,413	\$ 40,289
Adjustments:				
Embezzled funds expense	(5,156)	(3,587)	(6,762)	(8,720)
Embezzled amounts previously expensed as depreciation and selling, general and administrative	439	117	664	237
Other adjustments	(1,048)	(1,002)	(2,086)	(1,929)
Tax benefits	2,126	1,655	3,017	3,846
Net adjustments	(3,639)	(2,817)	(5,167)	(6,566)
Net income, as restated	\$ 74,026	\$ 16,790	\$ 132,246	\$ 33,723

Net income per common share:

Basic:				
As previously reported	\$ 0.46	\$ 0.12	\$ 0.81	\$ 0.24
Adjustment for effects of embezzlement	\$ (0.02)	\$ (0.01)	\$ (0.02)	\$ (0.03)
Other adjustments	\$	\$	\$ (0.01)	\$ (0.01)
As restated	\$ 0.44	\$ 0.10	\$ 0.78	\$ 0.20
Diluted:				
As previously reported	\$ 0.45	\$ 0.12	\$ 0.80	\$ 0.24
Adjustment for effects of embezzlement	\$ (0.02)	\$ (0.01)	\$ (0.02)	\$ (0.03)
Other adjustments	\$	\$	\$ (0.01)	\$ (0.01)
As restated	\$ 0.43	\$ 0.10	\$ 0.77	\$ 0.20

Except for the foregoing amended information, this Form 10-Q/A continues to speak as of the date of the Original Filing and the Company has not updated the disclosure contained herein to reflect events that occurred at a later date.

Table of Contents**PART I FINANCIAL INFORMATION****ITEM 1. Financial Statements**

The following unaudited condensed consolidated financial statements include all adjustments which, in the opinion of management, are necessary in order to make such financial statements not misleading.

**PATTERSON-UTI ENERGY, INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATED BALANCE SHEETS**

	Restated (See Note 2)	
	June 30, 2005	December 31, 2004
	(Unaudited) (In thousands, except share data)	
ASSETS		
Current assets:		
Cash and cash equivalents	\$ 70,077	\$ 112,371
Accounts receivable, net of allowance for doubtful accounts of \$2,859 at June 30, 2005 and \$1,909 at December 31, 2004	298,802	214,097
Inventory	21,920	17,738
Deferred tax assets, net	17,919	15,991
Other	28,401	26,836
Total current assets	437,119	387,033
Property and equipment, at cost, net	911,898	765,019
Goodwill	99,056	99,056
Other	5,135	5,677
Total assets	\$ 1,453,208	\$ 1,256,785
LIABILITIES AND STOCKHOLDERS EQUITY		
Current liabilities:		
Accounts payable:		
Trade	\$ 68,717	\$ 54,553
Accrued revenue distributions	11,388	11,297
Other	3,816	2,309
Accrued federal and state income taxes payable	12,615	4,231
Accrued expenses	85,280	79,163
Total current liabilities	181,816	151,553
Deferred tax liabilities, net	140,106	140,475
Other	4,351	3,256
Total liabilities	326,273	295,284
Commitments and contingencies		

Stockholders' equity:

Preferred stock, par value \$.01; authorized 1,000,000 shares, no shares issued		
Common stock, par value \$.01; authorized 300,000,000 shares with 174,734,503 and 171,625,841 issued and 171,621,407 and 168,512,745 outstanding at June 30, 2005 and December 31, 2004, respectively	1,748	1,716
Additional paid-in capital	651,615	597,280
Deferred compensation	(12,095)	(5,420)
Retained earnings	492,421	373,712
Accumulated other comprehensive income, net of tax	6,383	7,350
Treasury stock, at cost, 3,113,096 shares respectively	(13,137)	(13,137)
Total stockholders' equity	1,126,935	961,501
Total liabilities and stockholders' equity	\$ 1,453,208	\$ 1,256,785

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

Table of Contents**PATTERSON-UTI ENERGY, INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF INCOME**

Restated (See Note 2)

	Three Months Ended June 30,		Six Months Ended June 30,	
	2005	2004	2005	2004
(Unaudited) (In thousands, except per share amounts)				
Operating revenues:				
Contract drilling	\$ 329,503	\$ 188,222	\$ 624,892	\$ 367,397
Pressure pumping	22,025	14,577	38,718	28,827
Drilling and completion fluids	29,587	23,424	58,993	41,563
Oil and natural gas	8,807	8,287	17,912	15,502
	389,922	234,510	740,515	453,289
Operating costs and expenses:				
Contract drilling	180,185	134,387	355,651	262,378
Pressure pumping	12,622	8,328	22,986	16,416
Drilling and completion fluids	23,846	19,837	47,795	35,476
Oil and natural gas	2,418	2,768	4,588	4,336
Depreciation, depletion and impairment	37,559	31,295	72,774	59,376
Selling, general and administrative	9,919	7,904	19,592	14,696
Bad debt expense	143	217	366	307
Embezzled funds expense	5,156	3,587	6,762	8,720
Other (including gain or loss on sale of assets)	1,423	(140)	1,517	(1,313)
	273,271	208,183	532,031	400,392
Operating income	116,651	26,327	208,484	52,897
Other income (expense):				
Interest income	634	204	1,067	455
Interest expense	(57)	(54)	(123)	(130)
Other	16	172	20	257
	593	322	964	582
Income before income taxes	117,244	26,649	209,448	53,479
Income tax expense (benefit):				
Current	45,410	14,689	78,939	19,275
Deferred	(2,192)	(4,830)	(1,737)	481
	43,218	9,859	77,202	19,756

Edgar Filing: PATTERSON UTI ENERGY INC - Form 10-Q/A

Net income	\$ 74,026	\$ 16,790	\$ 132,246	\$ 33,723
Net income per common share:				
Basic	\$ 0.44	\$ 0.10	\$ 0.78	\$ 0.20
Diluted	\$ 0.43	\$ 0.10	\$ 0.77	\$ 0.20
Weighted average number of common shares outstanding:				
Basic	169,992	166,681	169,378	165,211
Diluted	173,162	169,062	172,648	168,005

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

Table of Contents

PATTERSON-UTI ENERGY, INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENT OF CHANGES IN STOCKHOLDERS EQUITY

	Common Stock		Additional		Accumulated			
	Number	Amount	Paid-In	Deferred	Retained	Other	Treasury	Total
	of		Capital	Compensation	Earnings	Income	Stock	
	Shares							
(Unaudited)								
(In thousands)								
December 31, 2004, as previously reported	171,626	\$ 1,716	\$ 597,280	\$ (5,420)	\$ 415,489	\$ 11,611	\$ (13,137)	\$ 1,007,539
Adjustment for effects of embezzlement (net of applicable income tax benefit of \$20,848) (See Note 2)					(35,285)			(35,285)
Other adjustments (net of applicable income tax benefit of \$3,501) (See Note 2)					(6,492)	(4,261)		(10,753)
December 31, 2004, As restated	171,626	1,716	597,280	(5,420)	373,712	7,350	(13,137)	961,501
Issuance of restricted stock	301	3	7,911	(7,914)				
Amortization of deferred compensation expense				1,108				1,108
Forfeitures of restricted shares	(9)		(131)	131				
Exercise of stock options	2,816	29	29,285					29,314
Tax benefit related to exercise of stock options			17,270					17,270
Foreign currency translation adjustment, net of tax of \$560, as restated						(967)		(967)

Payment of cash dividend					(13,537)				(13,537)
Net income, as restated					132,246				132,246
June 30, 2005, as restated	174,734	\$ 1,748	\$ 651,615	\$ (12,095)	\$ 492,421	\$ 6,383	\$ (13,137)		\$ 1,126,935

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

Table of Contents

PATTERSON-UTI ENERGY, INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF CHANGES IN CASH FLOWS

	Restated (See Note 2)	
	Six Months Ended June 30,	
	2005	2004
	(Unaudited)	
	(In thousands)	
Cash flows from operating activities:		
Net income	\$ 132,246	\$ 33,723
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation, depletion and impairment	72,774	59,376
Provision for bad debts	366	307
Deferred income tax expense	(1,737)	481
Tax benefit related to exercise of stock options	17,270	8,396
Amortization of deferred compensation expense	1,108	263
Gain on sale of assets	(1,034)	(1,313)
Changes in operating assets and liabilities, net of business acquired:		
Accounts receivable	(85,417)	(21,969)
Income taxes receivable		17,024
Inventory and other current assets	(6,990)	(2,206)
Accounts payable	14,481	5,260
Income taxes payable	8,393	
Accrued expenses	5,056	(13,333)
Other liabilities	2,602	(4,033)
Net cash provided by operating activities	159,118	81,976
Cash flows from investing activities:		
Acquisitions, net of cash acquired	(65,401)	(30,387)
Purchases of property and equipment	(162,199)	(83,142)
Proceeds from sales of property and equipment	8,839	1,986
Restricted cash deposited to collateralize retained insurance losses		(11,316)
Change in other assets	1,766	
Net cash used in investing activities	(216,995)	(122,859)
Cash flows from financing activities:		
Purchase of treasury stock		(1,482)
Dividends paid	(13,537)	(3,336)
Proceeds from exercise of stock options	29,314	8,698
Net cash provided by financing activities	15,777	3,880
Effect of foreign exchange rate changes on cash	(194)	(127)

Net decrease in cash and cash equivalents	(42,294)	(37,130)
Cash and cash equivalents at beginning of period	112,371	100,483
Cash and cash equivalents at end of period	\$ 70,077	\$ 63,353
Supplemental disclosure of cash flow information:		
Net cash received (paid) during the period for:		
Interest expense	\$ (123)	\$ (130)
Income taxes	\$ (48,585)	\$ 8,000

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

Table of Contents

**PATTERSON-UTI ENERGY, INC. AND SUBSIDIARIES
NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**

1. Basis of Consolidation and Presentation

The interim condensed consolidated financial statements include the accounts of Patterson-UTI Energy, Inc. (the Company) and its wholly-owned subsidiaries. All significant intercompany accounts and transactions have been eliminated.

The interim condensed consolidated financial statements have been prepared by management of the Company, without audit, pursuant to the rules and regulations of the Securities and Exchange Commission. Certain information and footnote disclosures normally included in financial statements prepared in accordance with accounting principles generally accepted in the United States of America have been omitted pursuant to such rules and regulations, although the Company believes the disclosures included herein are adequate to make the information presented not misleading. In the opinion of management, all adjustments which are of a normal recurring nature considered necessary for presentation of the information have been included.

The Company's former Chief Financial Officer (CFO), Jonathan D. Nelson (Nelson), perpetrated an embezzlement over a period of more than five years. The accompanying interim unaudited condensed consolidated financial statements have been restated to reflect the effects of losses incurred as a result of the embezzlement in the periods of occurrence. Payments related to the embezzlement previously capitalized as property and equipment and goodwill acquired, and the related depreciation and other amounts expensed have been reversed from the Company's accounting records. Embezzled payments have been recognized as expense in the periods they were embezzled. The cumulative effects of the embezzlement prior to 2004, have been recognized as a reduction of retained earnings. The accompanying interim unaudited condensed consolidated financial statements have also been restated for the effects of the correction of other errors that are immaterial both individually and in the aggregate (See Note 2).

The unaudited condensed consolidated balance sheet as of December 31, 2004, as presented herein, was derived from the audited balance sheet of the Company. These unaudited condensed consolidated financial statements should be read in conjunction with the consolidated financial statements and related notes included in the Company's Annual Report on Form 10-K/A for the year ended December 31, 2004.

The U.S. dollar is the functional currency for all of the Company's operations except for its Canadian operations, which use the Canadian dollar as their functional currency. The effects of exchange rate changes are reflected in accumulated other comprehensive income, which is a separate component of stockholders' equity (see Note 5 of these Notes to Unaudited Condensed Consolidated Financial Statements).

The Company provides a dual presentation of its earnings per share in its Unaudited Condensed Consolidated Statements of Income: Basic Earnings per Share (Basic EPS) and Diluted Earnings per Share (Diluted EPS). Basic EPS excludes dilution and is computed by dividing net income by the weighted average number of common shares outstanding. Diluted EPS is based on the weighted-average number of common shares outstanding and the assumed exercise of dilutive instruments, including stock options and warrants, less the number of treasury shares assumed to be purchased with the exercise proceeds. For the three and six months ended June 30, 2005 and 2004, all potentially dilutive options and warrants were included in the calculation of Diluted EPS. The following table presents information necessary to calculate earnings per

Table of Contents**PATTERSON-UTI ENERGY, INC. AND SUBSIDIARIES****NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

share for the three and six months ended June 30, 2005 and 2004 as well as dividends per share paid for the three and six months ended June 30, 2005 (in thousands, except per share amounts).

	Restated (See Note 2)			
	Three Months Ended June 30,		Six Months Ended June 30,	
	2005	2004	2005	2004
Net income	\$ 74,026	\$ 16,790	\$ 132,246	\$ 33,723
Weighted average common shares outstanding	169,992	166,681	169,378	165,211
Basic earnings per share	\$ 0.44	\$ 0.10	\$ 0.78	\$ 0.20
Weighted average common shares outstanding	169,992	166,681	169,378	165,211
Assumed exercise of stock options	3,170	2,381	3,270	2,794
Weighted average dilutive common shares outstanding	173,162	169,062	172,648	168,005
Diluted earnings per share	\$ 0.43	\$ 0.10	\$ 0.77	\$ 0.20
Cash dividends per share(a)	\$ 0.04	\$ 0.02	\$ 0.08	\$ 0.02

(a) During March 2005 and June 2005, cash dividends of \$6.7 million and \$6.8 million, respectively, were paid on outstanding shares of 168,679,334 and 169,741,460, respectively. During June 2004, a cash dividend of \$3.3 million was paid on outstanding shares of 166,786,254.

The results of operations for the three and six months ended June 30, 2005 are not necessarily indicative of the results to be expected for the full year.

Certain reclassifications have been made to the 2004 consolidated financial statements in order for them to conform with the 2005 presentation.

2. Embezzlement and Restatements

On November 3, 2005, the Company announced the resignation of its CFO, Jonathan D. Nelson. On November 10, 2005, the Company announced that, based on information received by Company senior management on November 9, 2005, the Audit Committee of the Company's Board of Directors began an investigation into an embezzlement from the Company by Nelson.

Most of the embezzled funds result from Nelson causing the wiring of Company funds aggregating approximately \$72.3 million, to, or for the benefit of, entities owned and controlled by him. Nelson was originally able to initiate these wire transfers by requesting the wire transfers himself in telephone calls to one of the Company's banks. After changes to the Company's internal controls and procedures in 2004, Nelson initiated the wire transfers through instructions to one of his subordinates and by the creation of fraudulent invoices containing forged senior management approvals. This false documentation was created by our former CFO to conceal the true nature of these transactions from the Company and its independent registered public accountants.

Nelson also instructed certain former employees, who worked under his supervision, to alter management reports related to property and equipment expenditures and created fictitious property and equipment approval forms with forged signatures.

On December 22, 2005, upon recommendation of Company management and the Audit Committee of its Board of Directors, the Company announced that based on the result to date of its ongoing internal investigation into the facts and circumstances surrounding the embezzlement by Nelson, the Company would

Table of Contents**PATTERSON-UTI ENERGY, INC. AND SUBSIDIARIES****NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

restate its previously issued financial statements and amend its previously issued Annual Report on Form 10-K for the year ended December 31, 2004 and Quarterly Reports on Form 10-Q for the periods ended March 31, June 30 and September 30, 2005. These restatements reflect losses incurred as a result of payments made to or for the benefit of Nelson that had been recognized in the Company's accounting records and previously issued financial statements as payments for assets and services that were not received by the Company.

The total amount embezzled was approximately \$77.5 million in cash, excluding any tax effects, beginning with the year ended December 31, 1998 through November 3, 2005 as follows (in thousands):

From 1998 to December 31, 2004	\$ 58,961
From January 1, 2005 to September 30, 2005	12,193
Total through September 30, 2005	71,154
From October 1, 2005 to November 3, 2005 (net of \$1,500 repayment)	6,350
Total embezzlement	\$ 77,504

The Company promptly advised the United States Securities and Exchange Commission (SEC) when it became aware of the embezzlement. The SEC promptly obtained a freeze order on Nelson's assets (including assets held by entities controlled by him) and a Receiver was appointed to collect those assets. The United States attorney for the Northern District of Texas obtained an indictment against Nelson and investigation of this matter continues.

The Company understands that the Receiver will ultimately liquidate the assets and propose a plan to distribute the proceeds. While the Company believes it has a claim for at least the full amount embezzled, other creditors have or may assert claims on the assets held by the Receiver. As a result, recovery by the Company from the Receiver is uncertain as to timing and amount, if any. Recoveries, if any, will be recognized when they are considered collectable.

Table of Contents**PATTERSON-UTI ENERGY, INC. AND SUBSIDIARIES****NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

The accompanying unaudited condensed consolidated financial statements have been restated to provide for, net of related tax effects, (1) the effects of losses incurred as a result of the former CFO's embezzlement and (2) the effects of the correction of other errors that are immaterial both individually and in the aggregate. These other adjustments relate primarily to previously reported property and equipment balances that resulted from our review of the Company's property and equipment records and the underlying physical assets in connection with the investigation of the embezzlement as well as the tax effects of our foreign currency translation adjustment. The effects of the embezzlement and other adjustments on the Company's financial position follow (in thousands):

	Previously Reported	Effect of Adjustment for Embezzlement	Effects of Other Adjustments	Restated
June 30, 2005:				
Property & equipment:				
At cost	\$ 1,591,078	\$ (61,961)	\$ 2,566	\$ 1,531,683
Accumulated depreciation	(617,140)	2,000	(4,645)	(619,785)
Net	973,938	(59,961)	(2,079)	911,898
Goodwill	101,326	(2,270)		99,056
Total assets	1,517,518	(62,231)	(2,079)	1,453,208
Accounts payable, trade	58,717		10,000	68,717
Federal & state income taxes payable	10,278	2,174	163	12,615
Deferred tax liabilities, net	169,809	(25,270)	(4,433)	140,106
Liabilities	343,639	(23,096)	5,730	326,273
Retained earnings	539,365	(39,135)	(7,809)	492,421
Stockholders' equity	1,173,879	(39,135)	(7,809)	1,126,935
December 31, 2004:				
Property & equipment:				
At cost	1,400,848	(55,211)	(6,866)	1,338,771
Accumulated depreciation	(571,973)	1,348	(3,127)	(573,752)
Net	828,875	(53,863)	(9,993)	765,019
Goodwill	101,326	(2,270)		99,056
Total assets	1,322,911	(56,133)	(9,993)	1,256,785
Federal & state income taxes payable	2,754	1,311	166	4,231
Deferred tax liabilities, net	162,040	(22,159)	594	140,475
Liabilities	315,372	(20,848)	760	295,284
Retained earnings	415,489	(35,285)	(6,492)	373,712
Accumulated other comprehensive income	11,611		(4,261)	7,350
Stockholders' equity	1,007,539	(35,285)	(10,753)	961,501

Table of Contents**PATTERSON-UTI ENERGY, INC. AND SUBSIDIARIES****NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

The effects of the embezzlement and other adjustments on the Company's results of operations and cash flows follow (In thousands, except per share amounts):

	Three Months Ended June 30,			
	Previously Reported	Effect of Adjustment for Embezzlement	Effect of Other Adjustments	Restated
2005:				
Depreciation, depletion, and impairment	\$ 36,959	\$ (433)	\$ 1,033	\$ 37,559
Selling, general and administrative	9,925	(6)		9,919
Other (including gain or loss on sale of assets)	1,408		15	1,423
Embezzled funds expense		5,156		5,156
Operating income	122,416	(4,717)	(1,048)	116,651
Income before income taxes	123,009	(4,717)	(1,048)	117,244
Income tax expense	45,344	(1,739)	(387)	43,218
Net income	77,665	(2,978)	(661)	74,026
Per common share:				
Basic	0.46	(0.02)		0.44
Diluted	0.45	(0.02)		0.43
Net cash provided by (used in):				
Operating activities	70,961	(5,150)	10,000	75,811
Investing activities	(84,113)	5,150	(10,000)	(88,963)
Purchases of property & equipment	81,149	(5,150)	10,000	85,999
2004:				
Depreciation, depletion, and impairment	\$ 30,451	\$ (111)	\$ 955	\$ 31,295
Selling, general and administrative	7,910	(6)		7,904
Other (including gain or loss on sale of assets)	187		(47)	140
Embezzled funds expense		3,587		3,587
Operating income	30,799	(3,470)	(1,002)	26,327
Income before income taxes	31,121	(3,470)	(1,002)	26,649
Income tax expense	11,514	(1,284)	(371)	9,859
Net income	19,607	(2,186)	(631)	16,790
Per common share:				
Basic	0.12	(0.01)		0.10
Diluted	0.12	(0.01)		0.10
Net cash provided by (used in):				
Operating activities	36,853	(3,581)		33,272
Investing activities	(62,368)	3,581		(58,787)
Purchases of property & equipment	51,778	(3,581)		48,197

Table of Contents

PATTERSON-UTI ENERGY, INC. AND SUBSIDIARIES
NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

	Six Months Ended June 30,			
	Previously	Effect of	Effect of	
	Reported	Adjustment	Other	Restated
		for	Adjustments	
		Embezzlement		
(In thousands, except per share amounts)				
2005:				
Depreciation, depletion, and impairment	\$ 71,359	\$ (652)	\$ 2,067	\$ 72,774
Selling, general and administrative	19,604	(12)		19,592
Other (including gain or loss on sale of assets)	1,498		19	1,517
Embezzled funds expense		6,762		6,762
Operating income	216,668	(6,098)	(2,086)	208,484
Income before income taxes	217,632	(6,098)	(2,086)	209,448
Income tax expense	80,219	(2,248)	(769)	77,202
Net income	137,413	(3,850)	(1,317)	132,246
Per common share:				
Basic	0.81	(0.02)	(0.01)	0.78
Diluted	0.80	(0.02)	(0.01)	0.77
Net cash provided by (used in):				
Operating activities	155,868	(6,750)	10,000	159,118
Investing activities	(213,745)	6,750	(10,000)	(216,995)
Purchases of property & equipment	158,949	(6,750)	10,000	162,199
2004:				
Depreciation, depletion, and impairment	\$ 57,734	\$ (225)	\$ 1,867	\$ 59,376
Selling, general and administrative	14,708	(12)		14,696
Other (including gain or loss on sale of assets)	1,375		(62)	1,313
Embezzled funds expense		8,720		8,720
Operating income	63,309	(8,483)	(1,929)	52,897
Income before income taxes	63,891	(8,483)	(1,929)	53,479
Income tax expense	23,602	(3,133)	(713)	19,756
Net income	40,289	(5,350)	(1,216)	33,723
Per common share:				
Basic	0.24	(0.03)	(0.01)	0.20
Diluted	0.24	(0.03)	(0.01)	0.20
Net cash provided by (used in):				
Operating activities	90,684	(8,708)		81,976
Investing activities	(131,567)	8,708		(122,859)
Acquisitions	32,514	(2,127)		30,387
Purchases of property & equipment	89,723	(6,581)		83,142

3. Recent Acquisitions

On January 15, 2005, the Company purchased land drilling assets from Key Energy Services, Inc. for \$61.8 million. The assets included 25 active and 10 stacked land-based drilling rigs, related drilling equipment, yard facilities and a rig moving fleet consisting of approximately 45 trucks and 100 trailers. The transaction

Table of Contents**PATTERSON-UTI ENERGY, INC. AND SUBSIDIARIES****NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

was accounted for as an acquisition of assets and the purchase price was allocated among the assets acquired based on their estimated fair market values.

On June 17, 2005, the Company acquired one land-based drilling rig for \$3.6 million. The transaction was accounted for as an acquisition of assets and the purchase price was allocated to the acquired drilling rig.

4. Stock-based Compensation

During June 2005, the Company's shareholders approved the Patterson-UTI Energy, Inc. 2005 Long-Term Incentive Plan (the 2005 Plan). In addition, the Board of Directors adopted a resolution that no future grants would be made under any of the previously existing equity plans of the Company. The Company accounts for activity under the 2005 Plan and previous activity of other equity plans using the recognition and measurement principles of APB Opinion No. 25, *Accounting for Stock Issued to Employees* (APB 25), and related interpretations. During the second quarters of 2004 and 2005, the Company granted restricted shares of the Company's common stock (the Restricted Shares) to certain key employees under the Patterson-UTI Energy, Inc 1997 Long-Term Incentive Plan, as amended, and the 2005 Plan. As required by APB 25, the Restricted Shares were valued based upon the market price of the Company's common stock on the date of the grant. The resulting value is being amortized over the vesting period of the stock. For the three and six months ended June 30, 2005, compensation expense of \$399,000 and \$700,000, net of \$56,000 and \$131,000 of forfeitures and of \$233,000 and \$408,000 of taxes, respectively, was included as a reduction in net income. Compensation expense of \$165,000, net of \$97,000 of taxes, was included as a reduction in net income for the three and six months ended June 30, 2004. Other than the Restricted Shares discussed above, no additional stock-based employee compensation expense is reflected in net income, as all options granted under the plans discussed above had an exercise price equal to the market value of the underlying common stock on the date of grant. The following table illustrates the effect on net income and net income per share if the Company had applied the fair value recognition provisions of Financial Accounting Standards Board Statement No. 123, *Accounting for Stock-Based Compensation* (SFAS 123), to stock-based employee compensation (in thousands, except per share amounts):

	Restated (See Note 2)			
	Three Months Ended June 30,		Six Months Ended June 30,	
	2005	2004	2005	2004
Net income, as reported	\$ 74,026	\$ 16,790	\$ 132,246	\$ 33,723
Add: Stock-based employee compensation expense recorded, net of forfeitures and taxes	399	165	700	165
Deduct: Total stock-based employee compensation expense determined under the fair value based method for all awards, net of related tax effects	(2,811)	(3,187)	(5,358)	(6,161)
Pro-forma net income	\$ 71,614	\$ 13,768	\$ 127,588	\$ 27,727
Net income per common share:				
Basic, as reported	\$ 0.44	\$ 0.10	\$ 0.78	\$ 0.20
Basic, pro-forma	\$ 0.42	\$ 0.08	\$ 0.75	\$ 0.17

Edgar Filing: PATTERSON UTI ENERGY INC - Form 10-Q/A

Diluted, as reported	\$ 0.43	\$ 0.10	\$ 0.77	\$ 0.20
Diluted, pro-forma	\$ 0.41	\$ 0.08	\$ 0.74	\$ 0.17

Table of Contents

PATTERSON-UTI ENERGY, INC. AND SUBSIDIARIES
NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

5. Comprehensive Income (Expense)

The following table illustrates the Company's comprehensive income (expense) including the effects of foreign currency translation adjustments for the three and six months ended June 30, 2005 and 2004 (in thousands):

	Restated (See Note 2)			
	Three Months Ended June 30,		Six Months Ended June 30,	
	2005	2004	2005	2004
Net income	\$ 74,026	\$ 16,790	\$ 132,246	\$ 33,723
Other comprehensive income (expense):				
Foreign currency translation adjustment related to our Canadian operations, net of tax	(631)	(902)	(967)	(1,197)
Comprehensive income, net of tax	\$ 73,395	\$ 15,888	\$ 131,279	\$ 32,526

6. Property and Equipment

Property and equipment consisted of the following at June 30, 2005 and December 31, 2004 (in thousands):

	Restated (See Note 2)	
	June 30, 2005	December 31, 2004
Equipment	\$ 1,433,253	\$ 1,239,519
Oil and natural gas properties	77,869	82,711
Buildings	15,288	12,892
Land	5,273	3,649
	1,531,683	1,338,771
Less accumulated depreciation and depletion	(619,785)	(573,752)
	\$ 911,898	\$ 765,019

7. Business Segments

Our revenues, operating profits and identifiable assets are primarily attributable to four business segments: (i) contract drilling of oil and natural gas wells, (ii) pressure pumping services, (iii) drilling and completion fluid services to operators in the oil and natural gas industry, and (iv) the exploration, development, acquisition and production of oil and natural gas. Each of these segments represents a distinct type of business based upon the type and nature of services and products offered. These segments have separate management teams which report to the Company's chief executive officer and have distinct and

Table of Contents**PATTERSON-UTI ENERGY, INC. AND SUBSIDIARIES****NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

identifiable revenues and expenses. Separate financial data for each of our four business segments is provided below (in thousands).

	Restated (See Note 2)			
	Three Months Ended June 30,		Six Months Ended June 30,	
	2005	2004	2005	2004
Revenues:				
Contract drilling(a)	\$ 330,027	\$ 189,691	\$ 626,604	\$ 370,016
Pressure pumping	22,025	14,577	38,718	28,827
Drilling and completion fluids(b)	29,726	23,507	59,152	41,671
Oil and natural gas	8,807	8,287	17,912	15,502
Total segment revenues	390,585	236,062	742,386	456,016
Elimination of intercompany revenues(a)(b)	663	1,552	1,871	2,727
Total revenues	\$ 389,922	\$ 234,510	\$ 740,515	\$ 453,289
Income before income taxes:				
Contract drilling	\$ 115,729	\$ 27,659	\$ 204,612	\$ 53,945
Pressure pumping	5,533	3,364	8,088	6,588
Drilling and completion fluids	2,803	1,176	5,515	1,408
Oil and natural gas	3,106	767	6,434	3,543
	127,171	32,966	224,649	65,484
Corporate and other	(2,812)	(3,052)	(6,851)	(3,867)
Other operating	(2,552)		(2,552)	
Embezzled funds expense(c)	(5,156)	(3,587)	(6,762)	(8,720)
Interest income	634	204	1,067	455
Interest expense	(57)	(54)	(123)	(130)
Other	16	172	20	257
Income before income taxes	\$ 117,244	\$ 26,649	\$ 209,448	\$ 53,479

Restated (See Note 2)

	June 30, 2005	December 31, 2004
	Identifiable assets:	
Contract drilling	\$ 1,179,223	\$ 961,873
Pressure pumping	66,108	49,145

Edgar Filing: PATTERSON UTI ENERGY INC - Form 10-Q/A

Drilling and completion fluids	73,915	62,970
Oil and natural gas	57,624	62,984
	1,376,870	1,136,972
Corporate and other(d)	76,338	119,813
Total assets	\$ 1,453,208	\$ 1,256,785

- (a) Includes contract drilling intercompany revenues of approximately \$524,000 and \$1.5 million for the three months ended June 30, 2005 and 2004, respectively, and approximately \$1.7 million and \$2.6 million for the six months ended June 30, 2005 and 2004, respectively.

Table of Contents

PATTERSON-UTI ENERGY, INC. AND SUBSIDIARIES
NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

- (b) Includes drilling and completion fluids intercompany revenues of approximately \$139,000 and \$83,000 for the three months ended June 30, 2005 and 2004, respectively, and approximately \$159,000 and \$108,000 for the six months ended June 30, 2005 and 2004, respectively.
- (c) The Company's former CFO perpetrated an embezzlement over a period of more than five years. Embezzled funds expense includes adjustments to eliminate payments related to the embezzlement previously capitalized as property and equipment and goodwill acquired. The related depreciation and other amounts expensed have also been reversed from the Company's accounting records (see Note 2).
- (d) Corporate assets primarily include cash on hand managed by the parent corporation and certain deferred federal income tax assets.

8. Recently Issued Accounting Standards

The Financial Accounting Standards Board (FASB) issued Staff Position Financial Accounting Standard 19-1, *Accounting for Suspended Well Costs* (FAS 19-1), in April 2005. FAS 19-1 provides guidance on accounting for exploratory well costs for entities that use the successful efforts method of accounting as described in Statement of Financial Accounting Standard No. 19, *Financial Accounting and Reporting by Oil and Gas Producing Companies*, (SFAS 19). Exploration activities are frequently performed in more remote areas, to greater depths, and in more complex geological formations than the exploration activities that occurred when SFAS 19 was issued in 1977. These changes in exploration activities have resulted in an increased frequency of exploratory wells that successfully find reserves that cannot be recognized as proved when drilling is completed and a lengthened evaluation period for determining whether the reserves qualify as proved. The FASB staff believes that exploratory well costs should continue to be capitalized when the well has found a sufficient quantity of reserves to justify its completion as a producing well and the enterprise is making sufficient progress assessing the reserves and the economic and operating viability of the project and SFAS 19 is amended to clarify this position. The Company intends to adopt these accounting and disclosure requirements prospectively to existing and newly capitalized exploratory well costs in the third quarter of 2005 and does not expect a significant impact on financial position or results of operations.

The FASB issued Staff Position FIN 46(R)-5, *Implicit Variable Interests Under FASB Interpretation No. 46 (revised December 2003)*, in March 2005. It addresses whether a reporting enterprise should consider whether it holds an implicit variable interest in a variable interest entity (VIE) or potential VIE when specific conditions exist. The Company does not expect any impact on its financial position or results of operations as a result of its adoption of FIN 46(R)-5 in the second quarter of 2005.

The FASB issued Staff Position FIN 47, *Accounting for Conditional Asset Retirement Obligations*, an interpretation of FASB Statement No. 143, in March 2005. The Interpretation is effective no later than the end of fiscal years ending after December 15, 2005. The statement clarifies the term conditional asset retirement obligation as used in FASB 143. The Company believes that it is already in compliance with the statement and does not expect any impact on financial position or results of operations when adopted.

The FASB issued Statement of Financial Accounting Standard No. 123 (revised 2004), *Share-Based Payment* (SFAS 123(R)), in December 2004; it replaces SFAS 123, and supersedes APB 25. Under SFAS 123(R), companies would have been required to implement the standard as of the beginning of the first interim reporting period that begins after June 15, 2005. However, in April 2005, the SEC announced the adoption of an Amendment to Rule 4-01(a) of Regulation S-X regarding the compliance date for SFAS 123(R) that amends the compliance dates and allows companies to implement SFAS 123(R) beginning with the first annual reporting period beginning on or after June 15, 2005. The Company intends to adopt SFAS 123(R) in its fiscal year beginning January 1, 2006.

Table of Contents

PATTERSON-UTI ENERGY, INC. AND SUBSIDIARIES

NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

The Company currently uses the intrinsic value method to value stock options, and accordingly, no compensation expense has been recognized for stock options since the Company grants stock options with exercise prices equal to the Company's common stock market price on the date of the grant. SFAS 123(R) requires the expensing of all stock-based compensation, including stock options and restricted shares, using the fair value method. The Company intends to expense stock options using the Modified Prospective Transition method as described in SFAS 123(R). This method will require expense to be recognized for stock options over their respective remaining vesting periods. No expense will be recognized for stock options vested in periods prior to the adoption of SFAS 123(R). The Company is evaluating the impact of its adoption of SFAS 123(R) on its results of operations and financial position. Adoption is not expected to have a material effect on the Company's financial position or results of operations.

The FASB issued Statement of Financial Accounting Standard No. 151, *Inventory Costs – an amendment of ARB No. 43, Chapter 4* (SFAS 151). SFAS 151 is effective, and will be adopted, for inventory costs incurred during fiscal years beginning after June 15, 2005 and is to be applied prospectively. SFAS 151 amends the guidance in ARB No. 43, Chapter 4, *Inventory Pricing*, to require current period recognition of abnormal amounts of idle facility expense, freight, handling costs and wasted material (spoilage). Adoption is not expected to have a material effect on the Company's financial position or results of operations.

The FASB issued Statement of Financial Accounting Standard No. 153, *Exchanges of Nonmonetary Assets – an amendment of APB Opinion No. 29* (SFAS 153). SFAS 153 is effective, and will be adopted, for nonmonetary asset exchanges occurring in fiscal periods beginning after June 15, 2005 and is to be applied prospectively. SFAS 153 eliminates the exception for fair value treatment of nonmonetary exchanges of similar productive assets and replaces it with a general exception for exchanges of nonmonetary assets that do not have commercial substance. A nonmonetary exchange has commercial substance if the future cash flows of the entity are expected to change significantly as a result of the exchange. Adoption is not expected to have a material effect on the Company's financial position or results of operations.

The FASB issued Statement of Financial Accounting Standards No. 154, *Accounting Changes and Error Corrections – a replacement of APB Opinion No. 20 and FASB Statement No. 3* (SFAS 154). SFAS 154 is effective, and will be adopted, for accounting changes made in fiscal years beginning after December 15, 2005 and is to be applied retrospectively. SFAS 154 requires that retroactive application of a change in accounting principle be limited to the direct effects of the change. Adoption is not expected to have a material effect on the Company's financial position or results of operations.

Table of Contents

PATTERSON-UTI ENERGY, INC. AND SUBSIDIARIES
NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

9. Goodwill

Goodwill is evaluated to determine if the fair value of an asset has decreased below its carrying value. At December 31, 2004 the Company performed its annual goodwill evaluation and determined no adjustment to impair goodwill was necessary. Goodwill as of June 30, 2005 and December 31, 2004 are as follows (in thousands):

	Restated (See Note 2)	
	June 30, 2005	December 31, 2004
Drilling:		
Goodwill at beginning of year	\$ 89,092	\$ 41,069
Changes to goodwill		48,020
Other		3
Goodwill at end of period	89,092	89,092
Drilling and completion fluids:		
Goodwill at beginning of year	9,964	9,964
Changes to goodwill		
Goodwill at end of period	9,964	9,964
Total goodwill	\$ 99,056	\$ 99,056

10. Accrued Expenses

Accrued expenses consisted of the following at June 30, 2005 and December 31, 2004 (in thousands):

	June 30, 2005	December 31, 2004
Salaries, wages, payroll taxes and benefits	\$ 23,865	\$ 21,245
Workers compensation liability	38,099	38,677
Sales, use and other taxes	6,258	5,863
Insurance, other than workers compensation	9,817	7,061
Other	7,241	6,317
	\$ 85,280	\$ 79,163

Table of Contents

PATTERSON-UTI ENERGY, INC. AND SUBSIDIARIES
NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

11. Asset Retirement Obligation

Statement of Financial Accounting Standards No. 143, Accounting for Asset Retirement Obligations, (SFAS No. 143), requires that the Company record a liability for the estimated costs to be incurred in connection with the abandonment of oil and natural gas properties in the future. The following table describes the changes to our asset retirement obligations during the six months ended June 30, 2005 and 2004 (in thousands):

	2005	2004
Balance at beginning of year	\$ 2,358	\$ 1,163
Liabilities incurred*	19	1,113
Liabilities settled	(511)	(70)
Accretion expense	37	15
Asset retirement obligation at end of period	\$ 1,903	\$ 2,221

* The 2004 amount includes \$1,091 of liabilities assumed in the acquisition of TMBR/ Sharp Drilling, Inc. (TMBR).

12. Commitments, Contingencies and Other Matters

The Company maintains letters of credit in the aggregate amount of approximately \$56 million for the benefit of various insurance companies as collateral for retrospective premiums and retained losses which could become payable under the terms of the underlying insurance contracts. These letters of credit expire at various times during each calendar year. No amounts have been drawn under the letters of credit.

We are also party to various legal proceedings arising in the normal course of our business. We do not believe that the outcome of these proceedings, either individually or in the aggregate, will have a material adverse effect on our financial condition.

13. Stockholders Equity

On February 16, 2005 and April 27, 2005, the Company's Board of Directors approved cash dividends on its common stock in the amount of \$0.04 per share. The dividends of approximately \$6.7 million and \$6.8 million were paid on March 4, 2005 and June 1, 2005, respectively. The amount and timing of all future dividend payments is subject to the discretion of the Board of Directors and will depend upon business conditions, results of operations, financial condition, terms of the Company's credit facilities and other factors.

Table of Contents

PATTERSON-UTI ENERGY, INC. AND SUBSIDIARIES

NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

During the second quarters of 2004 and 2005, the Company granted restricted shares of the Company's common stock to certain key employees under the Patterson-UTI Energy, Inc 1997 Long-Term Incentive Plan, as amended, and the 2005 Plan. As required by APB Opinion No. 25, the Restricted Shares were valued based upon the market price of the Company's common stock on the date of the grant. The resulting value is being amortized over the vesting period of the stock. For the three and six months ended June 30, 2005, compensation expense of \$399,000 and \$700,000, net of \$56,000 and \$131,000 of forfeitures and of \$233,000 and \$408,000 of taxes, respectively, was included as a reduction in net income. Compensation expense of \$165,000, net of \$97,000 taxes, was included as a reduction in net income for the three and six months ended June 30, 2004.

14. Subsequent Event

On July 27, 2005, the Company's Board of Directors approved a quarterly cash dividend of \$0.04 on each outstanding share of its common stock. The dividend is to be paid on September 1, 2005 to holders of record as of August 16, 2005.

Table of Contents**ITEM 2. Management's Discussion and Analysis of Financial Condition and Results of Operations**

This Quarterly Report on Form 10-Q/A for the three and six months ended June 30, 2005, amends and restates the financial statements and related financial information for all periods presented herein. The determination to restate these financial statements and other information was made as a result of management's identification of an embezzlement. Further information on the restatement can be found in Note 2 to Unaudited Condensed Consolidated Financial Statements.

Management Overview We are a leading provider of contract services to the North American oil and natural gas industry. Our services primarily involve the drilling, on a contract basis, of land-based oil and natural gas wells and, to a lesser extent, we provide pressure pumping services and drilling and completion fluid services. In addition to the aforementioned contract services, we also engage in the development, exploration, acquisition and production of oil and natural gas. For the three and six months ended June 30, 2005 and 2004, our operating revenues consisted of the following (dollars in thousands):

	Three Months Ended June 30,				Six Months Ended June 30,			
	2005		2004		2005		2004	
Contract drilling	\$ 329,503	84%	\$ 188,222	80%	\$ 624,892	84%	\$ 367,397	81%
Pressure pumping	22,025	6	14,577	6	38,718	5	28,827	6
Drilling and completion fluids	29,587	8	23,424	10	58,993	8	41,563	9
Oil and natural gas	8,807	2	8,287	4	17,912	3	15,502	4
	\$ 389,922	100%	\$ 234,510	100%	\$ 740,515	100%	\$ 453,289	100%

We provide our contract services to oil and natural gas operators in many of the oil and natural gas producing regions of North America. Our contract drilling operations are focused in various regions of Texas, New Mexico, Oklahoma, Louisiana, Mississippi, Colorado, Utah, Wyoming, Montana, North Dakota, South Dakota and Western Canada, while our pressure pumping services are focused primarily in the Appalachian Basin. Our drilling and completion fluids services are provided to operators in Texas, Southeastern New Mexico, Oklahoma, the Gulf Coast region of Louisiana and the Gulf of Mexico. Our oil and natural gas operations are primarily focused in West and South Texas, Southeastern New Mexico, Utah and Mississippi.

We have been a leading consolidator of the land-based contract drilling industry over the past several years, increasing our drilling fleet to 397 rigs as of June 30, 2005. Based on publicly available information, we believe we are the second largest owner of land-based drilling rigs in North America. Growth by acquisition has been a corporate strategy intended to expand both revenues and profits.

The profitability of our business is most readily assessed by two primary indicators: our average number of rigs operating and our average revenue per operating day. During the second quarter of 2005, our average number of rigs operating increased to 265 from 263 in the first quarter of 2005 and 203 in the second quarter of 2004. Our average revenue per operating day increased to \$13,690 in the second quarter of 2005 from \$12,490 in the first quarter of 2005 and \$10,190 in the second quarter of 2004. Primarily due to these improvements, we experienced an increase of approximately \$57.2 million, or 341%, in consolidated net income for the second quarter of 2005 as compared to the second quarter of 2004.

Our revenues, profitability and cash flows are highly dependent upon the market prices of oil and natural gas. During periods of improved commodity prices, the capital spending budgets of oil and natural gas operators tend to expand, which results in increased demand for our contract services. Conversely, in periods of time when these commodity prices deteriorate, the demand for our contract services generally weakens and we experience downward

pressure on pricing for our services. In addition, our operations are highly impacted by competition, the availability of excess equipment, labor issues and various other factors which are more fully described as risk factors in our Forward Looking Statements and Cautionary Statements for Purposes of the Safe Harbor Provisions of the Private Securities Litigation Reform Act of 1995 included in our Annual Report on Form 10-K/A for the year ended December 31, 2004, beginning on page 18.

Management believes that the liquidity of our balance sheet as of June 30, 2005, which includes approximately \$255 million in working capital (including \$70 million in cash), no long-term debt and

Table of Contents

\$144 million available under a \$200 million line of credit (availability of \$56 million is reserved for outstanding letters of credit), provides us with the ability to pursue acquisition opportunities, expand into new regions, make improvements to our assets and survive downturns in our industry.

Commitments and Contingencies The Company has no commitments or contingent liabilities which require disclosure in its financial statements other than letters of credit of approximately \$56 million at June 30, 2005, maintained for the benefit of various insurance companies as collateral for retrospective premiums and retained losses which may become payable under the terms of the underlying insurance contracts. No amounts have been drawn under the letters of credit.

Net income for the three months ended June 30, 2005 and 2004 includes embezzlement expense of approximately \$5.2 million and \$3.6 million, respectively. Net income for the six months ended June 30, 2005 and 2004 includes embezzlement expenses of approximately \$6.8 million and \$8.7 million, respectively. On November 16, 2005, the SEC obtained a freeze order on Nelson's assets (including assets held by entities controlled by him) and a Receiver was appointed to collect those assets. The Company understands that the Receiver will ultimately liquidate the assets and propose a plan to distribute the proceeds. While the Company believes it has a claim for at least the full amount embezzled, other creditors have or may assert claims on the assets held by the Receiver. As a result, recovery by the Company from the Receiver is uncertain as to timing and amount, if any. Recoveries, if any, will be recognized when they are considered collectable.

Trading and Investing We have not engaged in trading activities that include high-risk securities, such as derivatives and non-exchange traded contracts. We invest cash primarily in highly liquid, short-term investments such as overnight deposits, money markets, and highly rated municipal and commercial bonds.

Description of Business We conduct our contract drilling operations in Texas, New Mexico, Oklahoma, Louisiana, Mississippi, Colorado, Utah, Wyoming, Montana, North Dakota, South Dakota and Western Canada. As of June 30, 2005, we owned 397 drilling rigs. We provide pressure pumping services to oil and natural gas operators primarily in the Appalachian Basin. These services consist primarily of well stimulation and cementing for completion of new wells and remedial work on existing wells. We provide drilling fluids, completion fluids and related services to oil and natural gas operators in Texas, Southeastern New Mexico, Oklahoma, the Gulf Coast region of Louisiana and the Gulf of Mexico. Drilling and completion fluids are used by oil and natural gas operators during the drilling process to control pressure when drilling oil and natural gas wells. We are also engaged in the development, exploration, acquisition and production of oil and natural gas. Our oil and natural gas operations are focused primarily in producing regions in West and South Texas, Southeastern New Mexico, Utah and Mississippi.

The North American land drilling industry has experienced periods of downturn in demand over the last decade. During these periods, there have been substantially more drilling rigs available than necessary to meet demand. As a result, drilling contractors have had difficulty sustaining profit margins during the downturn periods.

In addition to adverse effects that future declines in demand could have on us, ongoing factors which could adversely affect utilization rates and pricing, even in an environment of stronger oil and natural gas prices and increased drilling activity, include:

- movement of drilling rigs from region to region,

- reactivation of land-based drilling rigs, or

- new construction of drilling rigs.

We cannot predict either the future level of demand for our contract drilling services or future conditions in the oil and natural gas contract drilling business.

Critical Accounting Policies

In addition to established accounting policies, our consolidated financial statements are impacted by certain estimates and assumptions made by management. The following is a discussion of our critical

Table of Contents

accounting policies pertaining to property and equipment, oil and natural gas properties, goodwill, revenue recognition, and the use of estimates.

Property and equipment Property and equipment, including betterments which extend the useful life of the asset, are stated at cost. Maintenance and repairs are charged to expense when incurred. We provide for the depreciation of our property and equipment using the straight-line method over their estimated useful lives. Our method of depreciation does not change when equipment becomes idle; we continue to depreciate idled equipment on a straight-line basis. No provision for salvage value is considered in determining depreciation of our property and equipment. We review our assets for impairment when events or changes in circumstances indicate that the carrying values of certain assets either exceed their respective fair values or may not be recovered over their estimated remaining useful lives. The cyclical nature of our industry has resulted in fluctuations in rig utilization over periods of time. Management believes that the contract drilling industry will continue to be cyclical and rig utilization will fluctuate. Based on management's expectations of future trends we estimate future cash flows in our assessment of impairment assuming the following four-year industry cycle: one year projected with low utilization, one year projected as a recovery period with improving utilization and the remaining two years projecting higher utilization. Provisions for asset impairment are charged to income when estimated future cash flows, on an undiscounted basis, are less than the asset's net book value. Impairment charges are recorded based on discounted cash flows. Other than to our oil and natural gas properties, there were no impairment charges to property and equipment during the six months ended June 30, 2005 or 2004.

Oil and natural gas properties Oil and natural gas properties are accounted for using the successful efforts method of accounting. Under the successful efforts method of accounting, exploration costs which result in the discovery of oil and natural gas reserves and all development costs are capitalized to the appropriate well. Exploration costs which do not result in discovering oil and natural gas reserves are charged to expense when such determination is made. In accordance with SFAS 19, costs of exploratory wells are initially capitalized to wells in progress until the outcome of the drilling is known. We review wells in progress quarterly to determine the related reserve classification. If the reserve classification is uncertain after one year following the completion of drilling, we consider the costs of the well to be impaired and recognize the costs as expense. Geological and geophysical costs, including seismic costs and costs to carry and retain undeveloped properties, are charged to expense when incurred. The capitalized costs of both developmental and successful exploratory type wells, consisting of lease and well equipment, lease acquisition costs, and intangible development costs, are depreciated, depleted, and amortized on the units-of-production method, based on petroleum engineer estimates of proved oil and natural gas reserves of each respective field. We review our proved oil and natural gas properties for impairment when an event occurs such as downward revisions in reserve estimates or decreases in oil and natural gas prices. Proved properties are grouped by field and undiscounted cash flow estimates are provided by our reserve engineer. If the net book value of a field exceeds its undiscounted cash flow estimate, impairment expense is measured and recognized as the difference between its net book value and discounted cash flow. Unproved oil and natural gas properties are reviewed quarterly to determine impairment. Our intent to drill, lease expiration, and abandonment of area are considered. Assessment of impairment is made on a lease-by-lease basis. If an unproved property is determined to be impaired, then costs related to that property are expensed. Impairment expense of approximately \$216,000 and \$818,000 for the three and six months ended June 30, 2005, respectively, and \$1.7 million and \$2.2 million for the three and six months ended June 30, 2004, respectively, is included in depreciation, depletion and impairment in the accompanying financial statements.

Goodwill Goodwill is considered to have an indefinite useful economic life and is not amortized. As such, we assess impairment of our goodwill annually or on an interim basis if events or circumstances indicate that the fair value of the asset has decreased below its carrying value.

Revenue recognition Revenues are recognized when services are performed, except for revenues earned under turnkey contract drilling arrangements which are recognized using the completed contract method of accounting, as described below. We follow the percentage-of-completion method of accounting for footage contract drilling arrangements. Under the percentage-of-completion method, management estimates are relied upon in the determination of the total estimated expenses to be incurred drilling the well. Due to the

Table of Contents

nature of turnkey contract drilling arrangements and risks therein, we follow the completed contract method of accounting for such arrangements. Under this method, all drilling revenues and expenses related to a well in progress are deferred and recognized in the period the well is completed. Provisions for losses on incomplete or in-process wells are made when estimated total expenses are expected to exceed estimated total revenues.

In accordance with Emerging Issues Task Force Issue No. 00-14, we recognize reimbursements due from third parties for out-of-pocket expenses incurred as revenues and account for out-of-pocket expenses as direct costs.

Use of estimates The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from such estimates.

Key estimates used by management include:

allowance for doubtful accounts,

total expenses to be incurred on footage and turnkey drilling contracts,

depreciation, depletion, and amortization,

asset impairment,

reserves for self-insured levels of insurance coverages, and

fair values of assets and liabilities assumed in acquisitions.

Liquidity and Capital Resources

As of June 30, 2005, we had working capital of approximately \$255 million, including cash and cash equivalents of \$70.1 million. For the six months ended June 30, 2005, our significant sources of cash flow included:

\$159.1 million provided by operations,

\$29.3 million from the exercise of stock options, and

\$8.8 million in proceeds from sales of property and equipment.

We used \$65.4 million to purchase land drilling assets from Key Energy Services, Inc. and one additional land-based drilling rig, \$13.5 million to pay dividends on the Company's common stock and \$162.2 million: to make capital expenditures for the betterment and refurbishment of our drilling rigs,

to acquire and procure drilling equipment,

to fund capital expenditures for our pressure pumping and drilling and completion fluids divisions, and

to fund leasehold acquisition and exploration and development of oil and natural gas properties.

In January 2005, the Company purchased land drilling assets of Key Energy Services, Inc. for \$61.8 million. The assets acquired included 25 active and 10 stacked land-based drilling rigs, related drilling equipment, yard facilities and a rig moving fleet consisting of approximately 45 trucks and 100 trailers. In June 2005, the Company acquired one land-based drilling rig for \$3.6 million. The transactions were accounted for as acquisitions of assets and the respective purchase price was allocated among the assets acquired based on their estimated fair market values.

On February 16, 2005 and April 27, 2005, the Company's Board of Directors approved cash dividends on its common stock in the amount of \$0.04 per share. The dividends of approximately \$6.7 million and \$6.8 million were paid on March 4, 2005 and June 1, 2005, respectively.

Table of Contents

On July 27, 2005, the Company's Board of Directors approved a quarterly cash dividend of \$0.04 on each outstanding share of its common stock to be paid on September 1, 2005 to holders of record as of August 16, 2005. The amount and timing of all future dividend payments is subject to the discretion of the Board of Directors and will depend upon business conditions, results of operations, financial condition, terms of the Company's credit facilities and other factors.

We believe that the current level of cash and short-term investments, together with cash generated from operations, should be sufficient to meet our capital needs. From time to time, acquisition opportunities are evaluated. The timing, size or success of any acquisition and the associated capital commitments are unpredictable. Should opportunities for growth requiring capital arise, we believe we would be able to satisfy these needs through a combination of working capital, cash generated from operations, our existing credit facility and additional debt or equity financing. However, there can be no assurance that such capital would be available.

Results of Operations

The following tables summarize operations by business segment for the three months ended June 30, 2005 and 2004:

Contract Drilling	Restated (See Note 2)		
	2005	2004	% Change
	(Dollars in thousands)		
Revenues	\$ 329,503	\$ 188,222	75.1%
Direct operating costs	\$ 180,185	\$ 134,387	34.1%
Selling, general and administrative	\$ 1,199	\$ 1,074	11.6%
Depreciation	\$ 32,390	\$ 25,102	29.0%
Operating income	\$ 115,729	\$ 27,659	318.4%
Operating days	24,074	18,473	30.3%
Average revenue per operating day	\$ 13.69	\$ 10.19	34.3%
Average direct operating costs per operating day	\$ 7.48	\$ 7.27	2.9%
Number of owned rigs at end of period	397	361	10.0%
Average number of rigs owned during period	396	361	9.7%
Average rigs operating	265	203	30.5%
Rig utilization percentage	67%	56%	19.6%
Capital expenditures	\$ 74,643	\$ 39,399	89.5%

Revenues and direct operating costs increased as a result of the increased number of operating days, as well as an increase in the average revenue and average direct operating costs per operating day. Operating days and average rigs operating increased as a result of increased demand for our contract drilling services and the acquisition of land drilling assets from Key Energy Services, Inc. in January 2005. Average revenue per operating day increased as a result of increased demand and pricing for our drilling services. Significant capital expenditures were incurred during the second quarter of 2005 to activate additional drilling rigs to meet increased demand, to modify and upgrade our existing drilling rigs and to acquire additional related equipment such as drill pipe, drill collars, engines, fluid circulating systems, rig hoisting systems and safety enhancement

Table of Contents

equipment. Increased depreciation expense was due to the acquisition described above and capital expenditures in 2004 and 2005.

Pressure Pumping	2005	2004	% Change
	(Dollars in thousands)		
Revenues	\$ 22,025	\$ 14,577	51.1%
Direct operating costs	\$ 12,622	\$ 8,328	51.6%
Selling, general and administrative	\$ 2,192	\$ 1,664	31.7%
Depreciation	\$ 1,678	\$ 1,221	37.4%
Operating income	\$ 5,533	\$ 3,364	64.5%
Total jobs	2,345	1,578	48.6%
Average revenue per job	\$ 9.39	\$ 9.24	1.6%
Average direct operating costs per job	\$ 5.38	\$ 5.28	1.9%
Capital expenditures	\$ 7,075	\$ 4,782	48.0%

Revenues and direct operating costs for our pressure pumping operations increased primarily as a result of the increased number of jobs. The increase in jobs was largely attributable to increased demand for our services and increased operating capacity which was added in 2004 and the first six months of 2005. Selling, general and administrative expenses increased largely as a result of the expanding operations of the pressure pumping segment. Increased depreciation expense for the 2005 quarter was largely due to the expansion of the pressure pumping segment through capital expenditures during 2004 and 2005. Significant capital expenditures were incurred during the second quarter of 2005 to modify and upgrade existing equipment and to add additional equipment to the segment's expanded operations to meet increased demand.

Drilling and Completion Fluids	Restated (See Note 2)		
	2005	2004	% Change
	(Dollars in thousands)		
Revenues	\$ 29,587	\$ 23,424	26.3%
Direct operating costs	\$ 23,846	\$ 19,837	20.2%
Selling, general and administrative	\$ 2,367	\$ 1,875	26.2%
Depreciation	\$ 571	\$ 536	6.5%
Operating income	\$ 2,803	\$ 1,176	138.4%
Total jobs	503	593	(15.2)%
Average revenue per job	\$ 58.82	\$ 39.50	48.9%
Average direct operating costs per job	\$ 47.41	\$ 33.45	41.7%
Capital expenditures	\$ 766	\$ 416	84.1%

Revenues and direct operating costs increased during the second quarter of 2005 compared to the second quarter of 2004 as a result of an increase in the average revenue and direct operating costs per job. Average revenue and direct operating costs per job increased primarily as a result of an increase in the number of larger jobs in the Gulf of Mexico and a decrease in the number of smaller land-based jobs during the second quarter.

Table of Contents

of 2005. Selling, general and administrative expense increased in 2005 primarily due to increased incentive compensation resulting from higher profitability levels.

Oil and Natural Gas Production and Exploration	2005	2004	% Change
	(Dollars in thousands, except sales prices)		
Revenues	\$ 8,807	\$ 8,287	6.3%
Direct operating costs	\$ 2,418	\$ 2,768	(12.6)%
Selling, general and administrative	\$ 552	\$ 427	29.3%
Depreciation, depletion and impairment	\$ 2,731	\$ 4,325	(36.9)%
Operating income	\$ 3,106	\$ 767	305.0%
Capital expenditures	\$ 3,407	\$ 3,600	(5.4)%
Average net daily oil production (Bbls)	795	1,171	(32.1)%
Average net daily gas production (Mcf)	7,253	7,335	(1.1)%
Average oil sales price (per Bbl)	\$ 51.52	\$ 37.94	35.8%
Average gas sales price (per Mcf)	\$ 6.44	\$ 5.31	21.3%

Revenues increased in the second quarter of 2005 compared to the second quarter of 2004, due to increased market prices received for oil and natural gas. Average net daily oil production decreased as a result of production declines and the sale of certain oil and gas properties during the second quarter of 2005. Depreciation, depletion and impairment expense includes approximately \$216,000 and \$1.7 million of expenses incurred during the three months ended June 30, 2005 and 2004, respectively, to impair certain oil and natural gas properties.

	Restated (See Note 2)		
Corporate and Other	2005	2004	% Change
	(In thousands)		
Selling, general and administrative	\$ 3,609	\$ 2,864	26.0%
Bad debt expense	\$ 143	\$ 217	(34.1)%
Depreciation	\$ 189	\$ 111	70.3%
Gain on sale of assets	\$ 1,129	\$ 140	706.4%
Embezzled funds expense	\$ 5,156	\$ 3,587	43.7%
Other	\$ 2,552	\$	N/A%
Interest income	\$ 634	\$ 204	210.8%
Interest expense	\$ 57	\$ 54	5.6%
Other income	\$ 16	\$ 172	(90.7)%
Capital expenditures	\$ 108	\$	N/A%

Selling, general and administrative expenses increased primarily as a result of payroll taxes attributable to the exercise of employee stock options, increased professional fees, and additional compensation expense related to the issuance of restricted shares to certain key employees in the second quarters of 2004 and 2005. Other in 2005 includes a charge of \$2.6 million to increase reserves related to the financial failure of a workers' compensation insurance carrier used previously by the Company. Embezzled funds expense includes payments made to or for the benefit of Jonathan D. Nelson, our former CFO, for assets and services that were not received by the Company.

Table of Contents

The following tables summarize operations by business segment for the six months ended June 30, 2005 and 2004:

Contract Drilling	Restated (See Note 2)		
	2005	2004	% Change
(Dollars in thousands)			
Revenues	\$ 624,892	\$ 367,397	70.1%
Direct operating costs	\$ 355,651	\$ 262,378	35.5%
Selling, general and administrative	\$ 2,415	\$ 2,163	11.7%
Depreciation and amortization	\$ 62,214	\$ 48,911	27.2%
Operating income	\$ 204,612	\$ 53,945	279.3%
Operating days	47,731	36,437	31.0%
Average revenue per operating day	\$ 13.09	\$ 10.08	29.9%
Average direct operating costs per operating day	\$ 7.45	\$ 7.20	3.5%
Number of owned rigs at end of period	397	361	10.0%
Average number of rigs owned during period	393	357	10.1%
Average rigs operating	264	200	32.0%
Rig utilization percentage	67%	56%	19.6%
Capital expenditures	\$ 132,378	\$ 64,779	104.4%

Revenues and direct operating costs increased as a result of the increased number of operating days, as well as an increase in the average revenue and average direct operating costs per operating day. Operating days and average rigs operating increased as a result of the increased demand for our contract drilling services, the acquisition of land drilling assets from Key Energy Services, Inc. in January 2005, and the acquisition of TMBR in February 2004. Average revenue per operating day increased as a result of increased demand and pricing for our drilling services. Significant capital expenditures were incurred during the first six months of 2005 to activate additional drilling rigs to meet increased demand, to modify and upgrade our existing drilling rigs and to acquire additional related equipment such as drill pipe, drill collars, engines, fluid circulating systems, rig hoisting systems and safety enhancement equipment. Increased depreciation expense was due to the acquisitions described above and capital expenditures in 2004 and 2005.

Pressure Pumping	2005	2004	% Change
(Dollars in thousands)			
Revenues	\$ 38,718	\$ 28,827	34.3%
Direct operating costs	\$ 22,986	\$ 16,416	40.0%
Selling, general and administrative	\$ 4,394	\$ 3,457	27.1%
Depreciation	\$ 3,250	\$ 2,366	37.4%
Operating income	\$ 8,088	\$ 6,588	22.8%
Total jobs	4,254	3,266	30.3%
Average revenue per job	\$ 9.10	\$ 8.83	3.1%
Average direct operating costs per job	\$ 5.40	\$ 5.03	7.4%
Capital expenditures	\$ 14,733	\$ 10,604	38.9%

Revenues and direct operating costs for our pressure pumping operations primarily increased as a result of the increased number of jobs. The increase in jobs was largely attributable to increased demand for our services and

increased operating capacity which was added in 2004 and the first six months of 2005. Selling, general and administrative expenses increased largely as a result of the expanding operations of the pressure

Table of Contents

pumping segment. Increased depreciation expense in 2005 was largely due to the expansion of the pressure pumping segment through capital expenditures during 2004 and the first six months of 2005.

Drilling and Completion Fluids	Restated (See Note 2)		
	2005	2004	% Change
	(Dollars in thousands)		
Revenues	\$ 58,993	\$ 41,563	41.9%
Direct operating costs	\$ 47,795	\$ 35,476	34.7%
Selling, general and administrative	\$ 4,562	\$ 3,585	27.3%
Depreciation and amortization	\$ 1,121	\$ 1,094	2.5%
Operating income	\$ 5,515	\$ 1,408	291.7%
Total jobs	1,030	1,111	(7.3)%
Average revenue per job	\$ 57.27	\$ 37.41	53.1%
Average direct operating costs per job	\$ 46.40	\$ 31.93	45.3%
Capital expenditures	\$ 1,352	\$ 627	115.6%

Revenues and direct operating costs increased during the first six months of 2005 compared to the first six months of 2004 as a result of an increase in the average revenue and direct operating costs per job. Average revenue and direct operating costs per job increased primarily as a result of an increase in the number of larger jobs in the Gulf of Mexico and a decrease in the number of smaller land-based jobs during 2005. Selling, general and administrative expense increased in 2005 primarily due to increased incentive compensation resulting from higher profitability levels.

Oil and Natural Gas Production and Exploration	% Change		
	2005	2004	% Change
	(Dollars in thousands, except sales prices)		
Revenues	\$ 17,912	\$ 15,502	15.5%
Direct operating costs	\$ 4,588	\$ 4,336	5.8%
Selling, general and administrative	\$ 1,053	\$ 840	25.4%
Depreciation, depletion and impairment	\$ 5,837	\$ 6,783	(13.9)%
Operating income	\$ 6,434	\$ 3,543	81.6%
Capital expenditures	\$ 8,428	\$ 7,132	18.2%
Average net daily oil production (Bbls)	846	1,050	(19.4)%
Average net daily gas production (Mcf)	7,922	7,488	5.8%
Average oil sales price (per Bbl)	\$ 49.00	\$ 36.14	35.6%
Average gas sales price (per Mcf)	\$ 6.16	\$ 5.35	15.1%

Revenues increased in 2005 compared to 2004, primarily due to increased market prices received for oil and natural gas. Depreciation, depletion and impairment expense includes approximately \$817,000 and

Table of Contents

\$2.2 million of expenses incurred during 2005 and 2004, respectively, to impair certain oil and natural gas properties.

Corporate and Other	Restated (See Note 2)		
	2005	2004	% Change
	(In thousands)		
Selling, general and administrative	\$ 7,168	\$ 4,651	54.1%
Bad debt expense	\$ 366	\$ 307	19.2%
Depreciation and amortization	\$ 352	\$ 222	58.6%
Gain on sale of assets	\$ 1,035	\$ 1,313	(21.2)%
Embezzled funds expense	\$ 6,762	\$ 8,720	(22.5)%
Other	\$ 2,552	\$	N/A%
Interest income	\$ 1,067	\$ 455	134.5%
Interest expense	\$ 123	\$ 130	(5.4)%
Other income	\$ 20	\$ 257	(92.2)%
Capital expenditures	\$ 5,308	\$	N/A%

Selling, general and administrative expenses increased primarily as a result of payroll taxes attributable to the exercise of employee stock options, increased professional fees, and additional compensation expense related to the issuance of restricted shares to certain key employees in the second quarters of 2004 and 2005. Other in 2005 includes a charge of \$2.6 million to increase reserves related to the financial failure of a worker's compensation insurance carrier used previously by the Company. Embezzled funds expense includes payments made to or for the benefit of Jonathan D. Nelson, our former CFO, for assets and services that were not received by the Company.

Volatility of Oil and Natural Gas Prices and its Impact on Operations

Our revenue, profitability, and future rate of growth are substantially dependent upon prevailing prices for oil and natural gas, with respect to all of our operating segments. For many years, oil and natural gas prices and markets have been volatile. Prices are affected by market supply and demand factors as well as international military, political and economic conditions, and the ability of OPEC, to set and maintain production and price targets. All of these factors are beyond our control. Natural gas prices fell from an average of \$6.23 per Mcf in the first quarter of 2001 to an average of \$2.51 per Mcf for the same period in 2002. During this same period, the average number of our rigs operating dropped by approximately 50%. The average market price of natural gas improved from \$3.36 in 2002 to \$5.45 in 2003 to \$5.95 in 2004 and \$6.94 in the second quarter of 2005, resulting in an increase in demand for our drilling services. Our average number of rigs operating increased from 126 in 2002 to 188 in 2003 to 211 in 2004 and 265 in the second quarter of 2005. We expect oil and natural gas prices to continue to be volatile and to affect our financial condition and operations and ability to access sources of capital.

The North American land drilling industry has experienced periods of downturn in demand over the last decade. During these periods, there have been substantially more drilling rigs available than necessary to meet demand. As a result, drilling contractors have had difficulty sustaining profit margins during the downturn periods.

Impact of Inflation

We believe that inflation will not have a significant near-term impact on our financial position.

ITEM 3. Quantitative and Qualitative Disclosures About Market Risk

We currently have no exposure to interest rate market risk as we have no outstanding balance under our credit facility. Should we incur a balance in the future, we would have exposure associated with the floating rate of the interest charged on that balance. The revolving credit facility calls for periodic interest payments at a floating rate ranging from LIBOR plus 0.625% to 1.0% or at the prime rate. The applicable rate above

Table of Contents

LIBOR is based upon our debt to capitalization ratio. Our exposure to interest rate risk due to changes in LIBOR is not expected to be material.

We conduct some business in Canadian dollars through our Canadian land-based drilling operations. The exchange rate between Canadian dollars and U.S. dollars has fluctuated during the last several years. If the value of the Canadian dollar against the U.S. dollar weakens, revenues and earnings of our Canadian operations will be reduced and the value of our Canadian net assets will decline when they are translated to U.S. dollars.

ITEM 4. Controls and Procedures

Background to the Fraud and Restatement In November 2005, the Company discovered that its former Chief Financial Officer, Jonathan D. Nelson (Nelson), had fraudulently diverted approximately \$78 million in Company funds for his own benefit. Nelson's fraudulent diversions began in 1998 and continued until the fourth quarter of 2005 when he resigned from the Company. The funds fraudulently diverted were recorded as payments for assets or services that were not actually received by the Company. The Audit Committee of the Board of Directors commenced an investigation into Nelson's activities and retained independent counsel and independent forensic accountants to assist with the investigation.

On December 22, 2005, the Company announced that the Audit Committee of the Board of Directors of the Company had concluded that it was necessary to restate its previously reported consolidated financial statements for the years ended December 31, 2004, 2003 and 2002, and for the first three quarters of 2005 and all quarters in 2004 and 2003.

As discussed in Note 2 to the consolidated financial statements included within this Quarterly Report on Form 10-Q/A for the quarterly period ended June 30, 2005, we have restated our previously issued financial statements.

Disclosure Controls and Procedures We maintain disclosure controls and procedures (as such terms are defined in Rules 13a-15(e) and 15d-15(e) promulgated under the Exchange Act) designed to ensure that the information required to be disclosed in the reports that we file with the SEC under the Exchange Act is recorded, processed, summarized and reported within the time periods specified in the SEC's rules and forms, and that such information is accumulated and communicated to our management, including our Chief Executive Officer (CEO) and current Chief Financial Officer (CFO), as appropriate, to allow timely decisions regarding required disclosure.

Under the supervision and with the participation of our management, including our CEO and current CFO, we conducted an evaluation of the effectiveness of our disclosure controls and procedures as of the end of the period covered by this Quarterly Report on Form 10-Q/A.

At the time of the filing of our Quarterly Report on Form 10-Q for the quarterly period ended June 30, 2005, our CEO and former CFO concluded that our disclosure controls and procedures were effective as of June 30, 2005. Subsequent to that evaluation, our CEO and current CFO concluded that our disclosure controls and procedures were not effective at a reasonable level of assurance, as of June 30, 2005, because of material weaknesses. For a discussion of the material weakness, see Item 9A of our Annual Report on Form 10-K/A for the year ended December 31, 2004. Based upon the substantial work performed during the restatement process, management has concluded that the Company's unaudited condensed consolidated financial statements for the periods covered by and included in this Quarterly Report on Form 10-Q/A are fairly stated in all material respects.

Changes in Internal Control Over Financial Reporting Our management is responsible for establishing and maintaining adequate internal control over financial reporting as such term is defined in Exchange Act Rule 13a-15(f). With the participation of our CEO and CFO, our management evaluates any changes in our internal control over financial reporting that occurred during each fiscal quarter which have materially

Table of Contents

affected, or are reasonably likely to materially affect, such internal control. At the time of the filing of our Quarterly Report on Form 10-Q for the quarterly period ended June 30, 2005, our management, including our CEO and former CFO, concluded that there were no changes in our internal control over financial reporting that occurred during the fiscal quarter ended June 30, 2005, that have materially affected or were reasonably likely to materially affect our internal control over financial reporting.

Our CEO and current CFO have subsequently concluded that the material weaknesses described in Item 9A of our Annual Report on Form 10-K/A for the year ended December 31, 2004 existed as of June 30, 2005.

You can find more information about the investigation, the material weaknesses and the actions that we have taken and are planning to take to remediate the material weaknesses in Item 9A of our Annual Report on Form 10-K/A, for the year ended December 31, 2004.

Table of Contents

**FORWARD LOOKING STATEMENTS AND CAUTIONARY STATEMENTS FOR
PURPOSES OF THE SAFE HARBOR PROVISIONS OF THE PRIVATE
SECURITIES LITIGATION REFORM ACT OF 1995**

Management's Discussion and Analysis of Financial Condition and Results of Operations included in Item 2 of this Report contains forward-looking statements which are made pursuant to the safe harbor provisions of the Private Securities Litigation Reform Act of 1995. These statements include, without limitation, statements relating to: liquidity; financing of operations; continued volatility of oil and natural gas prices; source and sufficiency of funds required for immediate capital needs and additional rig acquisitions (if further opportunities arise); and other matters. The words believes, plans, intends, expected, estimates or budgeted and similar expressions identify forward-looking statements. The forward-looking statements are based on certain assumptions and analyses we make in light of our experience and our perception of historical trends, current conditions, expected future developments and other factors we believe are appropriate in the circumstances. We do not undertake to update, revise or correct any of the forward-looking information. Factors that could cause actual results to differ materially from our expectations expressed in the forward-looking statements include, but are not limited to, the following:

Changes in prices and demand for oil and natural gas;

Changes in demand for contract drilling, pressure pumping and drilling and completion fluids services;

Shortages of drill pipe and other drilling equipment;

Labor shortages, primarily qualified drilling personnel;

Effects of competition from other drilling contractors and providers of pressure pumping and drilling and completion fluids services;

Occurrence of operating hazards and uninsured losses inherent in our business operations; and

Environmental and other governmental regulation.

For a more complete explanation of these various factors and others, see Forward Looking Statements and Cautionary Statements for Purposes of the Safe Harbor Provisions of the Private Securities Litigation Reform Act of 1995 included in our Annual Report on Form 10-K/A for the year ended December 31, 2004, beginning on page 18.

You are cautioned not to place undue reliance on any of our forward-looking statements, which speak only as of the date of this Report or, in the case of documents incorporated by reference, the date of those documents.

Table of Contents**PART II OTHER INFORMATION****ITEM 4. Submission of Matters to a Vote of Security Holders.**

On June 15, 2005, the Company held its Annual Meeting of Stockholders. At the meeting, the stockholders voted on the following matters:

1. The election of nine persons to serve as directors of the Company.
2. Approval of the adoption of the Patterson-UTI Energy, Inc. 2005 Long-Term Incentive Plan (the 2005 Plan).
3. Ratification of the appointment of PricewaterhouseCoopers LLP as the independent accountants of the Company for the fiscal year ending December 31, 2005.

The nine nominees to the Board of Directors of the Company were elected at the meeting, and the other proposals received the affirmative vote required for approval. The number of votes cast for, against or withheld, as well as the number of abstentions and broker non-votes, were as follows:

	Votes For	Votes Withheld		
1. Election of Directors				
Mark S. Siegel	155,764,040	2,664,759		
Cloyce A. Talbott	155,762,955	2,665,844		
A. Glenn Patterson	155,763,338	2,665,461		
Kenneth N. Berns	151,630,010	6,798,789		
Robert C. Gist	152,198,666	6,230,133		
Curtis W. Huff	157,004,971	1,423,828		
Terry H. Hunt	157,003,923	1,424,876		
Kenneth R. Peak	157,072,419	1,356,380		
Nadine C. Smith	157,070,786	1,358,013		
	Votes For	Votes Against	Abstentions	Broker Non-votes
2. Approval of the 2005 Plan	126,619,156	10,728,710	1,651,308	19,429,625
	Votes For	Votes Against	Abstentions	Broker Non-votes
3. Ratification of PricewaterhouseCoopers LLP as the Company's Independent Accountants	156,358,655	1,945,384	124,760	0

Table of Contents

ITEM 6. Exhibits

(a) Exhibits.

The following exhibits are filed herewith or incorporated by reference, as indicated:

- 3.1 Restated Certificate of Incorporation, as amended (filed August 9, 2004 as Exhibit 3.1 to the Company's Quarterly Report on Form 10-Q for the quarterly period ended June 30, 2004 and incorporated herein by reference).
- 3.2 Amendment to Restated Certificate of Incorporation, as amended (filed August 9, 2004 as Exhibit 3.2 to the Company's Quarterly Report on Form 10-Q for the quarterly period ended June 30, 2004 and incorporated herein by reference).
- 3.3 Amended and Restated Bylaws (filed March 19, 2002 as Exhibit 3.2 to the Company's Annual Report on Form 10-K for the fiscal year ended December 31, 2001 and incorporated herein by reference).
- 10.1 Patterson-UTI Energy, Inc. 2005 Long-Term Incentive Plan, including Form of Executive Officer Restricted Stock Award Agreement, Form of Executive Officer Stock Option Agreement, Form of Non-Employee Director Restricted Stock Award Agreement and Form of Non-Employee Director Stock Option Agreement (incorporated by reference to Exhibit 10.1 to Patterson-UTI Energy, Inc.'s Current Report on Form 8-K, dated June 15, 2005, as filed with the SEC on June 21, 2005).*
- 31.1 Certification of Chief Executive Officer pursuant to Rule 13a-14(a)/15d-14(a) of the Securities Exchange Act of 1934, as amended.
- 31.2 Certification of Chief Financial Officer pursuant to Rule 13a-14(a)/15d-14(a) of the Securities Exchange Act of 1934, as amended.
- 32.1 Certification of Chief Executive Officer and Chief Financial Officer pursuant to 18 USC Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
- 99.1 Controls and Procedures (filed March 17, 2006 as Item 9A to the Company's Annual Report on Form 10-K/A for the fiscal year ended December 31, 2004 and incorporated herein by reference).

* Management Contract or Compensatory Plan.

Table of Contents

SIGNATURES

Pursuant to the requirements of 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.

PATTERSON-UTI ENERGY, INC.

By: /s/ Cloyce A. Talbott

Cloyce A. Talbott

(Principal Executive Officer)

Chief Executive Officer

By: /s/ John E. Vollmer III

John E. Vollmer III

(Principal Accounting Officer)

Senior Vice President Corporate Development, Chief Financial
Officer, Secretary and Treasurer

DATED: March 27, 2006