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BLUE DOLPHIN ENERGY CO
Form 10QSB
May 14, 2002

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

FORM 10-QSB

Quarterly Report Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934

For the quarterly period ended: March 31, 2002

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: 0-15905

BLUE DOLPHIN ENERGY COMPANY
(Exact name of small business issuer as specified in its charter)

Delaware 73-1268729
(State or other jurisdiction of (I.R.S. Employer
incorporation or organization) Identification No.)

801 Travis, Suite 2100, Houston, Texas 77002
(Address of principal executive offices) (Zip Code)

(713) 227-7660
(Issuer's telephone number, including area code)

(Former name, former address and former fiscal year,
if changed since last report.)

APPLICABLE ONLY TO ISSUERS INVOLVED IN BANKRUPTCY
PROCEEDINGS DURING THE PRECEDING FIVE YEARS

Check whether the registrant filed all documents and reports required to be filed by Section 12, 13 or 15(d) of the Exchange Act after the distribution of securities under a plan confirmed by a court.

YES NO

APPLICABLE ONLY TO CORPORATE ISSUERS:

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

6,371,845 shares of the registrants' common stock, par value \$.01 per share, were outstanding at May 3, 2002.

Transitional Small Business Disclosure Format (Check one): Yes No

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BLUE DOLPHIN ENERGY COMPANY AND SUBSIDIARIES
CONDENSED CONSOLIDATED BALANCE SHEET -UNAUDITED

March 31, 2002
BLUE DOLPHIN ENERGY COMPANY AND SUBSIDIARIES

PART I. FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS

The condensed consolidated financial statements of Blue Dolphin Energy Company and subsidiaries (the "Company") included herein have been prepared by the Company, without audit, pursuant to the rules and regulations of the Securities and Exchange Commission ("SEC") and, in the opinion of management, reflect all adjustments necessary to present a fair statement of operations, financial position and cash flows. The Company follows the full-cost method of accounting for oil and gas properties, wherein costs incurred in the acquisition, exploration and development of oil and gas reserves are capitalized. The Company believes that the disclosures are adequate and the information presented is not misleading, although certain information and footnote disclosures normally included in financial statements prepared in accordance with generally accepted accounting principles have been condensed or omitted pursuant to such rules and regulations.

The accompanying condensed consolidated financial statements of the Company should be read in conjunction with the consolidated financial statements and notes thereto included in the Annual Report on Form 10-KSB for the year ended December 31, 2001.

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BLUE DOLPHIN ENERGY COMPANY AND SUBSIDIARIES
CONDENSED CONSOLIDATED BALANCE SHEET - UNAUDITED

ASSETS

Current assets:

Cash and cash equivalents	\$ 2,345,880
Accounts receivable, net of allowance of \$197,500	1,060,318
Prepaid expenses and other assets	278,111

TOTAL CURRENT ASSETS	3,684,309

Property and Equipment at cost:

Oil and Gas properties, including \$221,832	
of unproved leasehold cost (full-cost method)	27,126,133
Pipelines	3,580,910
Onshore separation and handling facilities	1,664,128
Land	860,275

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Other property and equipment	272,091	

	33,503,537	
Accumulated depletion, depreciation and amortization	(27,117,808)	

	6,385,729	
Deferred federal income tax	244,444	
Other assets	463,189	

TOTAL ASSETS	\$ 10,777,671	=====
LIABILITIES AND STOCKHOLDERS' EQUITY		
Current liabilities:		
Trade accounts payable	\$ 818,555	
Accrued expenses and other liabilities	4,983,527	

TOTAL CURRENT LIABILITIES	5,802,082	
Note payable	750,000	
Contingencies	--	
Common Stock, (\$.01 par value, 10,000,000 shares authorized, 6,371,845 shares issued and outstanding)	63,720	
Additional Paid-in Capital	26,107,139	
Accumulated Deficit	(21,945,270)	

TOTAL LIABILITES AND STOCKHOLDERS' EQUITY	4,225,589	
	\$ 10,777,671	=====

See accompanying notes to the condensed consolidated financial statements.

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BLUE DOLPHIN ENERGY COMPANY AND SUBSIDIARIES

CONDENSED CONSOLODATED STATEMENTS OF OPERATIONS - UNAUDITED

	Three Months Ended March 31,	
	2002	2001
	-----	-----
Revenue from operations:		
Oil and gas sales	\$ 578,269	\$ 1,790,852
Pipeline operations	329,297	322,198

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	-----	-----
	907,566	2,113,050
	-----	-----
Cost of operations:		
Lease operating expenses	217,647	333,764
Pipeline operating expenses	144,716	150,738
Depletion, depreciation, amortization and abandonment	289,567	649,012
Impairment of assets	339,984	1,000,000
General and administrative	584,615	629,569
	-----	-----
	1,576,529	2,763,083
	-----	-----
LOSS FROM OPERATIONS	(668,963)	(650,033)
Other income (expense):		
Interest and other expense	(15,792)	(165,240)
Bad debt expense	(197,500)	--
Gain on sale of assets	--	1,417,626
Interest and other income	14,590	53,121
	-----	-----
INCOME (LOSS) BEFORE MINORITY INTEREST, AND INCOME TAXES	(867,665)	655,474
Minority interest	(55,746)	(102,560)
Income taxes	--	--
	-----	-----
Net income (loss)	\$ (923,411)	\$ 552,914
	=====	=====
Earnings (loss) per common share-basic	\$ (0.15)	\$ 0.09
	=====	=====
Earnings (loss) per common share-diluted	\$ (0.15)	\$ 0.09
	=====	=====
Weighted average number of common shares outstanding:		
Basic	6,213,324	6,016,829
	-----	-----
Diluted	6,213,324	6,036,437
	=====	=====

See accompanying notes to the condensed consolidated financial statements.

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BLUE DOLPHIN ENERGY COMPANY AND SUBSIDIARIES

CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS - UNAUDITED

	Three Months Ended March 31,	
	2002	2001
OPERATING ACTIVITIES		
Net income (loss)	\$ (923,411)	\$ 55,100
Adjustments to reconcile net income (loss) to net cash provided by operating activities:		
Depletion, depreciation, amortization, abandonment	289,567	64,100
Minority interests	55,746	10,000
Gain on sale of assets	--	(1,410)
Impairment of assets	339,984	1,000
Bad debt expense	197,500	--
Changes in operating assets and liabilities:		
Accounts receivable	421	(900)
Prepaid expenses and other assets	(114,286)	(290)
Abandonment costs incurred	--	(1,380)
Trade accounts payable, accrued expenses, and other current liabilities	(160,823)	1,960
NET CASH PROVIDED BY (USED IN) OPERATING ACTIVITIES	(315,302)	26,000
INVESTING ACTIVITIES		
Purchases of property and equipment	(103,979)	(92,000)
Exploration and development costs	(331,313)	(23,000)
Net proceeds from sale of assets	--	4,620
Other assets	(4,302)	(19,000)
Purchase of minority interest from subsidiary	(254,786)	--
NET CASH PROVIDED BY (USED IN) INVESTING ACTIVITIES	(694,380)	3,260
FINANCING ACTIVITIES		
Payments on borrowings	--	(2,210)
Other	12,002	(1,000)
NET CASH PROVIDED BY (USED IN) FINANCING ACTIVITIES	12,002	(2,210)
INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS	(997,680)	1,300
CASH AND CASH EQUIVALENTS AT BEGINNING OF PERIOD	3,343,560	2,070
CASH AND CASH EQUIVALENTS AT END OF PERIOD	\$ 2,345,880	\$ 3,370
SUPPLEMENTARY CASH FLOW INFORMATION		
Interest paid	\$ --	\$ 900

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NON CASH INVESTING AND FINANCING ACTIVITIES:

Purchases of property and equipment financed with debt	\$ 750,000	\$
	=====	=====

See accompanying notes to the condensed consolidated financial statements.

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BLUE DOLPHIN ENERGY COMPANY AND SUBSIDIARIES

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS UNAUDITED

1. Related Party Transactions

In May 2002, the Company terminated its agreement with Drillmar, effective as of May 1, 2002, whereby it provided office space and certain management and administrative services to Drillmar for approximately \$40,000 per month. Drillmar will owe the Company approximately \$235,000 as of May 1, 2002.

Also in May 2002, the Company and Drillmar entered into a new agreement effective as of May 1, 2002, whereby the Company will provide office space and minimal accounting and administrative services to Drillmar for \$2,000 per month. The agreement can be terminated upon 30 days notice or by the mutual agreement of the parties.

Due to Drillmar's working capital deficiency and delays in securing capital funding, the Company has elected to record a full impairment of its investment in Drillmar of approximately \$340,000 and a full reserve for the accounts receivable amount owed from Drillmar, \$197,500 at March 31, 2002. Except for an initial contribution of approximately \$125,000 cash, the Company's investment in Drillmar and the accounts receivable emanated primarily from a contribution of services for which the Company incurred essentially no incremental cost.

Ivar Siem, Chairman of the Company, and Harris A. Kaffie, a Director of the Company, are owners of 30.3% and 30.6%, respectively, of Drillmar's common stock. As of March 31, 2002, Messrs. Siem and Kaffie provided funding to Drillmar of \$525,000 and \$425,000, respectively, and were issued unsecured promissory notes from Drillmar. The promissory notes are due June 30, 2002 and bear interest at the rate of 10% per annum. Along with the promissory notes, Drillmar issued detachable warrants to Messrs. Siem and Kaffie of 52,500 and 42,500, respectively. Each warrant provides for the purchase of one share of Drillmar common stock at \$5 per share and are exercisable for three years from issuance. The promissory notes issued by Drillmar are nonrecourse to the Company.

2. Contingencies

As a result of the decision to cease operating activities in the Buccaneer Field, the Company's leases in or on the Buccaneer Field terminated in January 2001. The Company must plug and abandon all remaining wells and remove platform facilities within one year from the termination of the leases. In 2001, the Company plugged its remaining wells at a cost of approximately \$1.4 million. During 2001 the Company also commenced operations to remove the Buccaneer Field platform complexes at a cost of approximately \$0.4 million. After the Company commenced removal operations, discussions were initiated with the Texas Parks and Wildlife ("TP&W") in an effort to leave certain of the underwater portions

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of the platform complexes in place as artificial reefs. In December 2001, operations to remove the platform complexes were suspended while the Company continues its discussions with the TP&W.

The Company expects that the TP&W will make a decision whether the Company can leave portions of the Buccaneer Field platform complexes in place as artificial reefs late in the second quarter 2002. If one or both of the platform complexes are left in place as an artificial reef, certain site clearance costs would be eliminated. The Company requested and has received an extension from the MMS until October 1, 2002 to complete the removal and site clearance of the platform complexes. The Company still believes that its provision for abandonment costs of \$4.6 million at December 31, 2001 is adequate.

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BLUE DOLPHIN ENERGY COMPANY AND SUBSIDIARIES

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS UNAUDITED (Continued)

On May 8, 2000, American Resources and its former Chief Financial Officer were named in a lawsuit in the United States District Court for the Southern District of Texas, Houston Division, styled H&N Gas, Limited Partnership, et al. v. Richard Hale, et al (Case No H-00-1371). The lawsuit alleges, among other things, that H&N Gas ("H&N") was defrauded by American Resources in connection with gas purchase options and gas price swap contracts entered into from February 1998 through September 1999. H&N alleges unlawful collusion between American Resources' prior management and the then president of H&N, Richard Hale ("Hale"), to the detriment of H&N. H&N generally alleges that Hale directed H&N to purchase illusory options from American Resources that bore no relation to any physical gas business and that American Resources did not have the financial resources and/or sufficient quantity of gas to perform. H&N further alleges that American Resources and Hale colluded with respect to swap transactions that were designed to benefit American Resources at the expense of H&N. H&N further alleges civil conspiracy against all the defendants. H&N is seeking approximately \$6.2 million in actual damages plus treble damages, punitive damages and prejudgment interest against American Resources directly. As a result of its conspiracy allegation, H&N also contends that all defendants are jointly and severally liable for over \$40.0 million in actual damages plus treble damages, punitive damages and prejudgment interest. Settlement discussions with H&N are currently in progress; however, if these discussions are unsuccessful, American Resources intends to vigorously defend this claim.

The Company is involved in various other claims and legal actions arising in the ordinary course of business. In the opinion of management, the ultimate disposition of these matters will not have a material effect on the Company's financial position, results of operations or cash flows.

3. Acquisition of assets

In February 2002, the Company acquired a 1/3 interest in the Blue Dolphin Pipeline System and the inactive Omega Pipeline from MCNIC Pipeline and Processing Company ("MCNIC"). Pursuant to the terms of the purchase and sales agreement, Blue Dolphin issued MCNIC a \$750,000 promissory note due December 31, 2006, with required monthly payments to be made out of 90% of the net revenues of the interest acquired. The note bears interest at the rate of 6% per annum and is secured by the interest acquired. Additionally, a contingent payment of up to \$750,000 will be made, if the promissory note is retired before its

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maturity date, payable annually after the promissory note is retired until December 31, 2006 out of 50% of the net revenues from the interest acquired. The termination date, December 31, 2006, will be extended by one additional year, up to a maximum of two years, for years in which non-recurring, extraordinary expenditures attributable to the interest acquired exceeds \$200,000, in the aggregate, during any year.

On December 2, 1999, the Company, through Blue Dolphin Exploration, acquired a 75% ownership interest in American Resources by purchasing approximately 39.5 million shares of American Resources common stock. On February 19, 2002, the Company completed its acquisition of American Resources, pursuant to the Amended and Restated Agreement and Plan of Merger dated as of December 19, 2001 (the "Merger Agreement"). Pursuant to the Merger Agreement, American Resources became a wholly owned subsidiary of the Company and each outstanding share of (i) American Resources common stock, par value \$.00001 per share, was converted into

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BLUE DOLPHIN ENERGY COMPANY AND SUBSIDIARIES

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

UNAUDITED

(Continued)

the right to receive, at the option of the holder, either \$.06 per share in cash or .0362 of a share of the Company's Common Stock, par value \$.01 per share (the "Common Stock"), and (ii) American Resources Series 1993 Preferred Stock, par value \$12.00 per share, was converted into the right to receive, at the option of the holder, either \$.07 in cash or .0301 of a share of Common Stock.

As a result of elections made by American Resources' stockholders, the Company issued 273,336 shares of Common Stock and paid approximately \$255,000 in cash.

4. Other Liabilities

In December 1999, American Resources received approximately \$4.5 million from Blue Dolphin Exploration for American Resources common stock representing a 75% ownership interest and \$24.2 million from Fidelity Oil for an 80% interest in its Gulf of Mexico assets. American Resources senior secured debt was held by Den norske Bank ("Den norske"). Den norske sold the senior debt to the Company for the right to receive a possible future payment. A payment of approximately \$.8 million is owed by American Resources. The original due date of this obligation has been extended by Den norske from March 15 to May 31, 2002. The Company and Den norske are currently negotiating an extended payment arrangement of this obligation.

5. Earnings Per Share

The Company applies the provisions of Statement of Financial Accounting Standards No. 128 ("SFAS 128"), "Earnings per Share". SFAS 128 requires the presentation of basic earnings per share ("EPS") which excludes dilution and is computed by dividing income (loss) available to common stockholders by the weighted-average number of shares of common stock outstanding for the period. SFAS 128 requires dual presentation of basic EPS and diluted EPS on the face of the income statement and requires a reconciliation of the numerators and denominators of basic EPS and diluted EPS.

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The following table provides a reconciliation between basic and diluted earnings per share:

	Net Income (Loss)	Weighted- Average Number of Common Shares Outstanding and Potential Dilutive Common Shares	Per Share Amount
	-----	-----	-----
Quarter ended March 31, 2002			
Basic and diluted loss per share	\$ (923,411)	6,213,324	\$ (0.15)
	=====	=====	=====
Quarter ended March 31, 2001			
Basic earnings per share	\$ 552,914	6,016,829	\$ 0.09
Effect of dilutive stock options		19,608	
	-----	-----	-----
Diluted earnings per share	\$ 552,914	6,036,437	\$ 0.09
	=====	=====	=====

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BLUE DOLPHIN ENERGY COMPANY AND SUBSIDIARIES

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS UNAUDITED (Continued)

6. Business Segment Information

The Company's income producing operations are conducted in two principal business segments: oil and gas exploration and production; and pipeline operations. There were no intersegment revenues during the periods presented. Information concerning these segments for the quarters ended March 31, 2002 and 2001, and at March 31, 2002 are as follows:

	Revenues (3)	Operating Income (Loss) (1) (3)
	-----	-----
Quarter ended March 31, 2002:		
Oil and gas exploration and production	\$ 578,269	(44,601)
Pipeline operations	329,297	34,408
Other	--	(658,770)
	-----	-----
Consolidated	907,566	(688,963)
	-----	-----
Other expense		(198,702)

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Loss before minority interest and income taxes		(867,665)
Quarter ended March 31, 2001:		
Oil and gas exploration and production	\$ 1,790,852	(442,651)
Pipeline operations	332,198	1,478,499
Other	--	(268,255)
Consolidated	2,113,050	767,593
Other expense		(112,119)
Income before minority interest and income taxes		655,474

	March 31, 2002
Identifiable assets:	
Oil and Gas exploration and production	\$ 4,117,803
Pipeline operations	4,953,117
Other	1,706,751
Consolidated	\$10,777,671

1. Consolidated income (loss) from operations includes \$313,431 and \$257,193 in unallocated general and administrative expenses, and unallocated depletion, depreciation and amortization of \$5,356 and \$11,063 for the quarters ended March 31, 2002 and 2001, respectively.

2. Pipeline depreciation and amortization includes a provision for pipeline abandonment of \$8,225 and \$4,935 for the quarters ended March 31, 2002 and 2001, respectively. In addition, the Company recorded an impairment expense of \$339,984 for the three months ended March 31, 2002, of its investment in Drillmar, and an expense of approximately

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BLUE DOLPHIN ENERGY COMPANY AND SUBSIDIARIES

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS UNAUDITED (Continued)

\$1.0 million for the three months ended March 31, 2001, as a result of a change in the estimated abandonment costs associated with the Buccaneer Field.

3. Pipeline revenues include \$49,640 for the quarter ended March 31, 2001 from the Black Marlin Pipeline System. Pipeline operations include \$50,107 of operating expenses and depreciation for the quarter ended March 31, 2001 from the Black Marlin Pipeline System.

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7. Recently Issued Accounting Pronouncements

In July 2001, the FASB issued Statement No. 141 ("SFAS 141"), "Business Combinations," and Statement No. 142, "Goodwill and Other Intangible Assets" ("SFAS 142"). SFAS 141 requires that the purchase method of accounting be used for all business combinations initiated after June 30, 2001. SFAS 141 also specifies criteria intangible assets acquired in a purchase method business combination must meet to be recognized and reported apart from goodwill. SFAS 142 requires that goodwill and intangible assets with indefinite useful lives no longer be amortized, but instead tested for impairment at least annually in accordance with the provisions of SFAS 142. SFAS 142 also requires that intangible assets with definite useful lives be amortized over their respective estimated useful lives to their estimated residual values, and reviewed for impairment in accordance with SFAS 144, "Accounting for the Impairment or Disposal of Long-Lived Assets". Upon adoption of SFAS 142 on January 1, 2002, the Company did not have unamortized goodwill, unamortized identifiable assets, or unamortized negative goodwill.

In August 2001, the FASB issued Statement No. 143 ("SFAS 143"), "Accounting for Asset Retirement Obligations," which addresses financial accounting and reporting for obligations associated with the retirement of tangible long-lived assets and the associated asset retirement costs. The standard applies to legal obligations associated with the retirement of long-lived assets that result from the acquisition, construction, development and/or normal use of the asset.

SFAS 143 requires that the fair value of a liability for an asset retirement obligation be recognized in the period in which it is incurred if a reasonable estimate of fair value can be made. The fair value of the liability is added to the carrying amount of the associated asset and this additional carrying amount is depreciated over the life of the asset. If the obligation is settled for other than the carrying amount of the liability, the Company will recognize a gain or loss on settlement.

The Company is required and plans to adopt the provisions of SFAS 143 for the quarter ending March 31, 2003. To accomplish this, the Company must identify all legal obligations for asset retirement obligations and determine the fair value of these obligations on the date of adoption. The determination of fair value is complex and will require the Company to gather market information and develop cash flow models. Additionally, the Company will be required to develop processes to track and monitor these obligations. Because of the effort necessary to comply with the adoption of SFAS 143, it is not practicable for management to estimate the impact of adopting this Statement at the date of this report.

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BLUE DOLPHIN ENERGY COMPANY AND SUBSIDIARIES

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
UNAUDITED
(Continued)

In October 2001, the FASB issued Statement No. 144 ("SFAS 144"), "Accounting for the Impairment or Disposal of Long-Lived Assets". SFAS 144 provides that long-lived assets to be disposed of by sale be measured at the lower of carrying amount or fair value less cost to sell, whether reported in continuing operations or in discontinued operations, and broadens the reporting of discontinued operations to include all components of an entity with operations that can be distinguished from the rest of the entity and that will be

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eliminated from the ongoing operations of the entity in a disposal transaction. SFAS 144 is effective for fiscal years beginning after December 15, 2001. SFAS 144 did not have a material effect on the Company's financial condition and results of operations.

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BLUE DOLPHIN ENERGY COMPANY AND SUBSIDIARIES

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

CAUTIONARY NOTE REGARDING FORWARD LOOKING STATEMENTS

Forward Looking Statements. Certain of the statements included in this quarterly report on Form 10-QSB, including those regarding future financial performance or results or that are not historical facts, are "forward-looking" statements as that term is defined in Section 21E of the Securities Exchange Act of 1934, as amended, and Section 27A of the Securities Act of 1933, as amended. The words "expect", "plan", "believe", "anticipate", "project", "estimate", and similar expressions are intended to identify forward-looking statements. The Company cautions readers that any such statements are not guarantees of future performance or events and such statements involve risks and uncertainties that may cause actual results and outcomes to differ materially from those indicated in the forward-looking statements. Some of the important factors, risks and uncertainties that could cause actual results to vary from the forward-looking statements include:

- o the risks associated with exploration;
- o gas and oil price volatility;
- o uncertainties in the estimation of proved reserves and in the projection of future rates of production and timing of development expenditures;
- o availability and cost of capital;
- o actions or inactions of third party operators for properties where the Company has an interest;
- o regulatory developments; and
- o general economic conditions.

Additional factors that could cause actual results to differ materially from those indicated in the forward-looking statements are discussed under the caption "Risk Factors" in the Company's Form 10-KSB for the fiscal year ended December 31, 2001. Readers are cautioned not to place undue reliance on these forward-looking statements which speak only as of the date hereof. The Company undertakes no duty to update these forward-looking statements. Readers are urged to carefully review and consider the various disclosures made by the Company which attempt to advise interested parties of the additional factors which may affect the Company's business, including the disclosures made under the caption "Management's Discussion and Analysis of Financial Condition and Results of Operations" in this report.

LIQUIDITY AND CAPITAL RESOURCES

At March 31, 2002 the Company's working capital deficit was approximately \$2.1 million. In order to satisfy its working capital and capital expenditure requirements for the remainder of 2002, the Company believes that it will need to raise between \$2.0 to \$3.0 million of capital. The Company will need to seek

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external financing and/or sell assets to raise the necessary capital. Historically, the Company has relied on the proceeds from the sale of assets and capital raised from the issuance of debt and equity securities to individual investors and related parties to sustain its operations. There can be no assurance that the Company will be able to obtain financing or sell assets on commercially reasonable terms. The Company's inability to raise capital may have a material adverse effect on its financial condition, ability to meet its obligations and operating needs and results of operations. In addition, the

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BLUE DOLPHIN ENERGY COMPANY AND SUBSIDIARIES

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

Company's audit report as of and for the year ended December 31, 2001 contained a qualification as to the Company's ability to continue as a going concern due to its financing needs. The consolidated financial statements do not include any adjustments that might result from the outcome of this uncertainty.

The following table summarizes certain of the Company's contractual cash obligations and other commercial cash commitments at March 31, 2002 (amounts in thousands).

Contractual Obligations	Total	Less than 1 year	Payments Due by Period		
			1-3 years	4-5 years	After 5 years
Long-Term Debt	\$ 750	--	--	750	--
Other Contractual Obligations	5,010	2,986	1,877	147	--
Total Contractual Cash Obligations	\$ 5,760	2,986	1,877	897	--

Other Commercial Commitments	Total	Less than 1 year	Amount of Commitment Expiration Per Period		
			1-3 years	4-5 years	After 5 years
Long-Term Debt	\$ --	--	--	--	--
Other Commercial Obligations	2,000	2,000	--	--	--
Total Commercial Cash Obligations	\$ 2,000	2,000	--	--	--

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BLUE DOLPHIN ENERGY COMPANY AND SUBSIDIARIES

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

The following table summarizes the Company's financial position at March 31, 2002 and December 31, 2001 (dollars in thousands):

	March 31,		December 31,	
	2002		2001	
	Amount	%	Amount	%
Property and equipment, net	\$ 6,386	90	\$ 5,980	85
Other noncurrent assets	708	10	1,043	15
Total	\$ 7,094	100	\$ 7,023	100
Working capital	\$ 2,118	30	\$ 1,197	17
Minority interest	--	0	1,065	15
Long term debt	750	10	--	0
Stockholders' equity	4,226	60	4,761	68
Total	\$ 7,094	100	\$ 7,023	100

The change in the Company's financial position from December 31, 2001 to March 31, 2002, was primarily due to acquisitions of the 23% minority interest in American Resources and the 1/3 interest in the Blue Dolphin Pipeline System.

Historically, the Company has relied on the proceeds from financing activities and the sale of assets to supplement its capital requirements. During the three months ended March 31, 2002 ("current period"), the Company financed its activities from revenues generated from its operating activities and working capital.

The Company's future cash flows are subject to a number of variables, including the level of production from oil and natural gas properties that the Company has an interest in, utilization of its pipeline systems and commodity prices among others.

The net cash provided by or used in our operating, investing and financing activities is summarized below (amounts in thousands):

Three Months Ended	
March 31	
2002	2001

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Net cash provided by (used in):	\$ (315)	\$ 262
Investing activities	(695)	3,268
Financing activities	12	(2,225)
Net increase (decrease) in cash	\$ (998)	\$ 1,305

The Company's cash flow from operating activities decreased by \$0.6 million in the current period compared to the three months ended March 31, 2001 ("previous period"), due primarily to a decrease in oil and gas revenues of approximately \$1.2 million.

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BLUE DOLPHIN ENERGY COMPANY AND SUBSIDIARIES

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

Cash flow used in investing activities during the current period decreased by approximately \$4.0 million compared to the previous period due primarily to proceeds received from the sale of the Black Marlin Pipeline System in the prior period of approximately \$4.6 million.

The Company previously announced a gas discovery in High Island Area Block A-7, in the Gulf of Mexico. The Company owns an 8.9% reversionary working interest in this field and it will begin to receive revenues from its reversionary interest after "payout" occurs. Payout occurs after all of the other working interest owners have recovered their costs and expenses associated with developing the field from sales of gas and oil production from the field. In mid 2001, there were three wells producing in this field at a combined rate of approximately 60 Mmcf of natural gas per day. However, two of the three wells stopped producing and the remaining well is currently producing approximately 14 Mmcf of natural gas per day. Additionally, two unsuccessful exploratory wells were drilled in late 2001. The Company expected to begin to receive revenues from its reversionary working interest in this field in late 2001, however, as a result of the above mentioned occurrences the Company does not expect to receive revenues until 2005.

In November 2000, the Company elected to abandon the Buccaneer field due to adverse developments in the field. The Company reached an agreement with Tetra Applied Technologies, Inc. ("Tetra"), to plug and abandon the wells located in the Buccaneer Field which was completed in the first quarter of 2001 for approximately \$1.4 million. In addition, Maritech Resources, Inc. ("Maritech") an affiliate of Tetra purchased an adjacent lease from Apache Corporation on which the Company provided production operating services. In December 2000, as a result of the Company's plans to abandon the Buccaneer Field platform facilities, the Company and Maritech terminated the operating agreement. The Company installed a new platform in 2001 at a cost of \$1.7 million net to its interest, to operate and maintain the Blue Dolphin Pipeline System, as well as handle the production from Maritech's lease. The Blue Dolphin System was previously tied into and operated from the Buccaneer Field platforms.

In August 2001, the Company reached an agreement with Tetra to remove the Buccaneer Field platforms for a cost of approximately \$2.6 million. Pursuant to the agreement, Tetra and the Company agreed to extended payment terms, whereby the Company will pay 20% upon completion and 5% per month for twelve months, with the remaining balance due in the thirteenth month. To provide security for

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the extended payment terms, the Company provided Tetra with a first lien on its 50% interest in the Blue Dolphin Pipeline System. Operations to remove the platforms commenced in August 2001 and were suspended in December 2001, while the Company continues its discussions with the Texas Parks and Wildlife to leave the underwater portion of the platforms in place as artificial reefs. The Company expects that the Texas Parks and Wildlife will make a decision as to whether the Company will be able to leave any of the Buccaneer Field platforms in place as artificial reefs, in late second quarter 2002. The Company requested and has received an extension from the Minerals Management Service until October 1, 2002, to complete the removal and site clearance of the platform complexes. After the decision is made by the Texas Parks and Wildlife, Tetra will resume its removal operations. If a platform complex is left in place as an artificial reef, certain site clearance operations would be eliminated. The Company believes that its provision for abandonment costs of \$4.6 million at March 31, 2002 is adequate. The Company expects to finance the remaining abandonment costs from working capital, the private placement of debt or equity securities, or the sale of assets.

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BLUE DOLPHIN ENERGY COMPANY AND SUBSIDIARIES

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

In January 2001, the Company and its partners sold the Black Marlin Pipeline System for \$7.3 million and the High Island Block A-5 pipeline for \$2.0 million to Williams Field Services; \$3.6 million and \$1.0 million, respectively, net to the Company's interest.

The Company's proved reserves and future net revenues reported at December 31, 2001 reflect capital expenditures totaling \$150,000, for the year ending December 31, 2002. Management will continue to evaluate its capital expenditure program based on, among other things, field reservoir performance, availability and cost of drilling and workover equipment, and demand and prices obtainable for the Company's production, as well as availability of capital resources. There can be no assurance that reserves will be developed as currently planned. For the three months ended March 31, 2002, the Company incurred capital expenditures of approximately \$331,000, including approximately \$133,000 for its share of drilling costs for an exploratory well in High Island Block 34 which is currently being drilled. In May 2002, the Company sold its interest in the High Island Block 34 field for approximately \$150,000. The Company is currently not aware of any further planned capital expenditures associated with its proved reserves.

In February 2002, the Company acquired a 1/3 interest in the Blue Dolphin Pipeline System and the inactive Omega Pipeline from MCNIC. Pursuant to the terms of the purchase and sales agreement, Blue Dolphin issued MCNIC a \$750,000 promissory note due December 31, 2006, with required monthly payments to be made out of 90% of the net revenues of the interest acquired. See Note 3. Acquisition of Assets, in Part 1., Item 1.

On December 2, 1999, the Company, through Blue Dolphin Exploration, acquired a 75% ownership interest in American Resources by purchasing approximately 39.5 million shares of American Resources common stock. On February 19, 2002, the Company completed its acquisition of American Resources, pursuant to the Amended and Restated Agreement and Plan of Merger dated as of December 19, 2001 (the "Merger Agreement"). Pursuant to the Merger Agreement, American Resources became a wholly owned subsidiary of the Company and each outstanding share of (i) American Resources common stock, par value \$.00001 per share, was converted into

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the right to receive, at the option of the holder, either \$.06 per share in cash or .0362 of a share of the Company's Common Stock, par value \$.01 per share (the "Common Stock"), and (ii) American Resources Series 1993 Preferred Stock, par value \$12.00 per share, was converted into the right to receive, at the option of the holder, either \$.07 in cash or .0301 of a share of Common Stock.

As a result of elections made by American Resources' stockholders, the Company issued 273,336 shares of Common Stock and paid approximately \$255,000 in cash.

In December 1999, American Resources received approximately \$4.5 million from Blue Dolphin Exploration for American Resources common stock representing a 75% ownership interest and \$24.2 million from Fidelity Oil for an 80% interest in its Gulf of Mexico assets. American Resources senior secured debt was held by Den norske Bank ("Den norske"). Den norske sold the senior debt to the Company for the right to receive a possible future payment. A payment of approximately \$.8 million is owed by American Resources. The original due date of this obligation has been extended by Den norske from March 15 to May 31, 2002. The Company and Den norske are currently negotiating an extended payment arrangement of this obligation.

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

RESULTS OF OPERATIONS

The Company reported a net loss for the current period of \$923,411, compared to net income of \$552,914 reported for the previous period. The decrease is primarily due to a decline in revenues from oil and gas sales of \$1.2 million, the impairment of the Company's investment in Drillmar of \$.3 million and the reserve recorded against the account receivable from Drillmar of \$.2 million. In 2001, the Company recorded a gain on the sale of the Black Marlin Pipeline system of \$1.4 million, offset in part by an increase of \$1.0 million in the Company's Buccaneer Field abandonment obligations.

Revenues:

Current period revenues from oil and gas sales decreased by \$1,212,583 from those of the previous period. The change was due to a 55% decrease in gas prices resulting in a reduction of revenues of approximately \$710,000, and a decrease of 28% in production volumes resulting in a reduction of revenues of approximately \$500,000.

Costs and Expenses:

Current period lease operating expenses decreased by \$116,117 or 35% from the previous period. The decrease was primarily due to elimination of costs associated with maintaining the Buccaneer Field platform facilities.

Current period depletion, depreciation, amortization and abandonment decreased \$359,445 or 55% from the previous period. The decrease was primarily due to a decrease in production of approximately 72% and a 14% decrease in the depletion rate in the current period.

Impairment of assets included an impairment of the Company's investment in Drillmar of \$339,984 in the current period and an increase in the estimated cost associated with the Buccaneer Field abandonment of \$1,000,000 recorded in the

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previous period.

General and administrative expenses for the current period decreased \$44,954, or 7% from the previous period. In the current period, the Company's cost reduction plan resulted in a reduction in staff costs of approximately \$155,000, offset in part by an increase in contract labor of approximately \$46,000, and elimination of management fees received in the previous period for managing Fidelity Oil's interest in properties acquired from American Resources of \$40,000 and MCNIC's 1/3 interest in the Blue Dolphin Pipeline System of \$19,200.

The gain on sale of assets in the previous period represents the gain on the sale of the Black Marlin Pipeline System of \$1,417,626.

Interest and other expense decreased in the current period by \$149,448. The previous period included a charge for the contingent payment due to Den norske Bank of \$150,000.

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BLUE DOLPHIN ENERGY COMPANY AND SUBSIDIARIES

ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET PRICE

The Company is exposed to market risk, including adverse changes in commodity prices and interest rates as discussed below.

Commodity Price Risk- The Company produces and sells natural gas, crude oil, and natural gas liquids. As a result, the Company's financial results can be significantly affected if these commodity prices fluctuate widely in response to changing market forces. The Company does not use derivative products to manage commodity price risk.

Interest Rate Risk- The Company currently has no short-term or long-term debt with floating interest rates, and thus currently is not subject to risk of interest rate changes.

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BLUE DOLPHIN ENERGY COMPANY AND SUBSIDIARIES

PART II. OTHER INFORMATION

ITEM 1. LEGAL PROCEEDINGS

On May 8, 2000, American Resources and its former Chief Financial Officer, were named in a lawsuit in the United States District Court for the Southern District of Texas, Houston Division, styled H&N Gas, Limited Partnership, et al. v. Richard Hale, et al (Case No H-00-1371). The lawsuit alleges, among other things, that H&N Gas ("H&N") was defrauded by American Resources in connection with gas purchase options and gas price swap contracts entered into from February 1998 through September 1999. H&N alleges unlawful collusion between American Resources' prior management and the then president of H&N, Richard Hale ("Hale"), to the detriment of H&N. H&N generally alleges that Hale directed H&N to purchase illusory options from American Resources that bore no relation to any physical gas business and that American Resources did not have the financial resources and/or sufficient quantity of gas to perform. H&N further alleges that

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American Resources and Hale colluded with respect to swap transactions that were designed to benefit American Resources at the expense of H&N. H&N further alleges civil conspiracy against all the defendants. H&N is seeking approximately \$6.2 million in actual damages plus treble damages, punitive damages and prejudgment interest against American Resources directly. As a result of its conspiracy allegation, H&N also contends that all defendants are jointly and severally liable for over \$40.0 million in actual damages plus treble damages, punitive damages and prejudgment interest. Settlement discussions with H&N are currently underway; however, if these discussions are unsuccessful, American Resources intends to vigorously defend this claim.

ITEM 6. EXHIBITS AND REPORT ON FORM 8-K

- A) No Exhibits
- B) Reports on Form 8-K

On February 25, 2002, the Company filed a current report on Form 8-K dated February 15, 2002, reporting a change in Certifying Accountant. The items reported in such current report were Item 4 (Change in Registrant's Certifying Accountant).

On March 1, 2002, the Company filed a current report on Form 8-K dated February 19, 2002, reporting it completed the acquisition of American Resources Offshore, Inc. The items in such current report were Item 2 (Acquisition or Disposition of Assets).

On March 13, 2002, the Company filed a current report on Form 8-K dated February 28, 2002, reporting the acquisition of an additional 1/3 interest in the Blue Dolphin Pipeline System from MCNIC Pipeline & Processing Company. The items reported in such current report were Item 5 (Other Events).

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BLUE DOLPHIN ENERGY COMPANY AND SUBSIDIARIES

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.

By: BLUE DOLPHIN ENERGY COMPANY

Date: May 14, 2002

/s/ Michael J. Jacobson

Michael J. Jacobson
President and Chief Executive Officer

/s/ G. Brian Lloyd

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G. Brian Lloyd
Vice President, Treasurer
(Principal Accounting Officer)