PATTERSON UTI ENERGY INC
Form 10-Q/A
March 27, 2006

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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 September 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	**75-2504748**
(State or other jurisdiction of incorporation or organization)	*(I.R.S. Employer Identification No.)*

4510 Lamesa Highway, Snyder, Texas 79549
(Address of principal executive offices) (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 þ No o

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 þ Accelerated filer o Non-accelerated filer o

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

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

172,801,959 shares of common stock, $0.01 par value, as of October 26, 2005

PATTERSON-UTI ENERGY, INC. AND SUBSIDIARIES
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PART I FINANCIAL INFORMATION

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 September 30, 2005, initially filed with the United States Securities and Exchange Commission (SEC) on October 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	September 30, 2005	December 31, 2004
Assets	$ (66,952)	$ (56,133)
Liabilities(1)	(24,836)	(20,848)
Retained Earnings & Stockholders Equity	$ (42,116)	$ (35,285)

(1) Consists of increases in Federal and state income taxes payable of $2.6 million and $1.3 million at September 30, 2005 and December 31, 2004, respectively and decreases in deferred tax liabilities of $27.4 million and $22.2 million at September 30, 2005 and December 31, 2004, respectively.

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

	Three Months Ended September 30,		Nine Months Ended September 30,	
Operating Income:	**2005**	**2004**	**2005**	**2004**
As previously reported	$ 173,511	$ 47,408	$ 390,179	$ 110,717
Adjustment for effects of embezzlement	(4,721)	(4,642)	(10,819)	(13,125)
Other adjustments	(1,344)	(1,024)	(3,430)	(2,953)
As restated	$ 167,446	$ 41,742	$ 375,930	$ 94,639

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

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2005	**2004**	**2005**	**2004**
Net Income:				
As previously reported	$ 110,135	$ 29,964	$ 247,548	$ 70,253
Adjustments:				
Embezzled funds expense	(5,431)	(4,759)	(12,193)	(13,479)
Embezzled amounts previously expensed as depreciation and selling, general and administrative	710	117	1,374	354
Other adjustments	(1,344)	(1,024)	(3,430)	(2,953)
Tax benefits	2,235	2,100	5,252	5,946
Net adjustment	(3,830)	(3,566)	(8,997)	(10,132)
Net income, as restated	$ 106,305	$ 26,398	$ 238,551	$ 60,121
Net income per common share:				
Basic:				
As previously reported	$ 0.64	$ 0.18	$ 1.46	$ 0.42
Adjustment for effects of embezzlement	$ (0.02)	$ (0.02)	$ (0.04)	$ (0.05)
Other adjustments	$	$	$ (0.01)	$ (0.01)
As restated	$ 0.62	$ 0.16	$ 1.40	$ 0.36
Diluted:				
As previously reported	$ 0.63	$ 0.18	$ 1.43	$ 0.42
Adjustment for effects of embezzlement	$ (0.02)	$ (0.02)	$ (0.04)	$ (0.05)
Other adjustments	$	$	$ (0.01)	$ (0.01)
As restated	$ 0.61	$ 0.16	$ 1.38	$ 0.36

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.

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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
(Unaudited)

	Restated (See Note 2) September 30, 2005	December 31, 2004
	(In thousands, except share data)	
ASSETS		
Current assets:		
Cash and cash equivalents	$ 131,211	$ 112,371
Accounts receivable, net of allowance for doubtful accounts of $2,431 at September 30, 2005 and $1,909 at December 31, 2004	362,976	214,097
Inventory	20,916	17,738
Deferred tax assets, net	19,688	15,991
Other	26,738	26,836
Total current assets	561,529	387,033
Property and equipment, at cost, net	980,456	765,019
Goodwill	99,056	99,056
Other	5,065	5,677
Total assets	$ 1,646,106	$ 1,256,785
LIABILITIES AND STOCKHOLDERS EQUITY		
Current liabilities:		
Accounts payable:		
Trade	$ 99,964	$ 54,553
Accrued revenue distributions	14,379	11,297
Other	2,956	2,309
Accrued federal and state income taxes payable	33,618	4,231
Accrued expenses	102,493	79,163
Total current liabilities	253,410	151,553
Deferred tax liabilities, net	139,177	140,475
Other	4,122	3,256
Total liabilities	396,709	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 175,791,288 and 171,625,841 issued and 172,678,192 and 168,512,745 outstanding at September 30, 2005 and December 31, 2004, respectively	1,758	1,716
Additional paid-in capital	671,303	597,280
Deferred compensation	(11,018)	(5,420)
Retained earnings	591,822	373,712
Accumulated other comprehensive income	8,669	7,350
Treasury stock, at cost, 3,113,096 shares	(13,137)	(13,137)
Total stockholders equity	1,249,397	961,501
Total liabilities and stockholders equity	$ 1,646,106	$ 1,256,785

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

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PATTERSON-UTI ENERGY, INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF INCOME
(Unaudited)

	Restated (See Note 2)			
	Three Months Ended September 30,		Nine Months Ended September 30,	
	2005	2004	2005	2004
	(In thousands, except per share amounts)			
Operating revenues:				
Contract drilling	$ 401,046	$ 206,454	$ 1,025,938	$ 573,851
Pressure pumping	27,640	19,663	66,358	48,490
Drilling and completion fluids	29,819	23,455	88,812	65,018
Oil and natural gas	10,234	9,602	28,146	25,104
	468,739	259,174	1,209,254	712,463
Operating costs and expenses:				
Contract drilling	202,956	140,608	558,607	402,986
Pressure pumping	15,662	10,455	38,648	26,871
Drilling and completion fluids	24,062	19,851	71,857	55,327
Oil and natural gas	2,365	1,715	6,953	6,051
Depreciation, depletion and impairment	39,545	31,661	112,319	91,037
Selling, general and administrative	10,565	8,303	30,157	22,999
Bad debt expense	50	192	416	499
Embezzled funds expense	5,431	4,759	12,193	13,479
Other (including gain or loss on sale of assets)	657	(112)	2,174	(1,425)
	301,293	217,432	833,324	617,824
Operating income	167,446	41,742	375,930	94,639
Other income (expense):				
Interest income	944	233	2,011	688
Interest expense	(56)	(75)	(179)	(205)
Other	19	56	39	313
	907	214	1,871	796
Income before income taxes	168,353	41,956	377,801	95,435
Income tax expense (benefit):				
Current	66,574	12,023	145,513	31,298
Deferred	(4,526)	3,535	(6,263)	4,016
	62,048	15,558	139,250	35,314

Net income	$ 106,305	$ 26,398	$ 238,551	$ 60,121
Net income per common share:				
Basic	$ 0.62	$ 0.16	$ 1.40	$ 0.36
Diluted	$ 0.61	$ 0.16	$ 1.38	$ 0.36
Weighted average number of common shares outstanding:				
Basic	171,613	167,006	169,846	165,744
Diluted	174,587	169,664	173,211	168,795

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

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

	Common Stock							
	Number of Shares	Amount	Additional Paid-In Capital	Deferred Compensation	Retained Earnings	Accumulated Other Comprehensive Income	Treasury Stock	Total
				(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)					(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	305	3	8,040	(8,043)				
Amortization of deferred compensation expense				2,121				2,121
Forfeitures of restricted shares	(17)		(324)	324				
Exercise of stock options	3,877	39	42,260					42,299
Tax benefit related to exercise of stock options			24,047					24,047
Foreign currency translation adjustment, net of tax of $749, as restated						1,319		1,319
					(20,441)			(20,441)

Payment of cash dividend								
Net income, as restated					238,551			238,551
September 30, 2005, as restated	175,791	$ 1,758	$ 671,303	$ (11,018)	$ 591,822	$ 8,669	$ (13,137)	$ 1,249,397

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

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

	Restated (See Note 2)	
	Nine Months Ended September 30,	
	2005	2004
	(In thousands)	
Cash flows from operating activities:		
Net income	$ 238,551	$ 60,121
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation, depletion and impairment	112,319	91,037
Provision for bad debts	416	499
Deferred income tax expense	(6,263)	4,016
Tax benefit related to exercise of stock options	24,047	6,682
Amortization of deferred compensation expense	2,121	749
Gain on sale of assets	(1,253)	(1,425)
Changes in operating assets and liabilities, net of business acquired:		
Accounts receivable	(148,825)	(34,480)
Income taxes receivable		21,923
Inventory and other current assets	(4,044)	(6,997)
Accounts payable	48,568	2,820
Income taxes payable	29,660	
Accrued expenses	22,662	(5,416)
Other liabilities	1,513	(6,729)
Net cash provided by operating activities	319,472	132,800
Cash flows from investing activities:		
Acquisitions, net of cash acquired	(73,577)	(30,387)
Purchases of property and equipment	(262,723)	(125,501)
Proceeds from sales of property and equipment	12,502	2,631
Restricted cash deposited to collateralize retained insurance losses		(11,316)
Change in other assets	1,766	
Net cash used in investing activities	(322,032)	(164,573)
Cash flows from financing activities:		
Purchase of treasury stock		(1,482)
Dividends paid	(20,441)	(6,674)
Proceeds from exercise of stock options	42,299	9,293
Net cash provided by financing activities	21,858	1,137
Effect of foreign exchange rate changes on cash	(458)	(81)

Net increase (decrease) in cash and cash equivalents		18,840		(30,717)
Cash and cash equivalents at beginning of period		112,371		100,483
Cash and cash equivalents at end of period	$	131,211	$	69,766
Supplemental disclosure of cash flow information:				
Net cash paid during the period for:				
Interest expense	$	179	$	205
Income taxes	$	85,824	$	500

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

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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, warrants and restricted shares, less the number of treasury shares assumed to be purchased with the exercise proceeds. For the three and nine months ended September 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 share for the three and nine months ended September 30, 2005 and 2004 as

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

well as cash dividends per share paid during the three and nine months ended September 30, 2005 and 2004 (in thousands, except per share amounts).

	Restated (See Note 2)			
	Three Months Ended September 30,		Nine Months Ended September 30,	
	2005	2004	2005	2004
Net income	$ 106,305	$ 26,398	$ 238,551	$ 60,121
Weighted average common shares outstanding	171,613	167,006	169,846	165,744
Basic earnings per share	$ 0.62	$ 0.16	$ 1.40	$ 0.36
Weighted average common shares outstanding	171,613	167,006	169,846	165,744
Dilutive effect of stock options and restricted shares	2,974	2,658	3,365	3,051
Weighted average dilutive common shares outstanding	174,587	169,664	173,211	168,795
Diluted earnings per share	$ 0.61	$ 0.16	$ 1.38	$ 0.36
Cash dividends per share(a)	$ 0.04	$ 0.02	$ 0.12	$ 0.04

(a) During March, June and September of 2005, cash dividends of $6.7 million, $6.8 million and $6.9 million, respectively, were paid on outstanding shares of 168,679,334, 169,741,460 and 172,591,361, respectively. During June and September of 2004, cash dividends of $3.3 million were paid on outstanding shares of 166,786,254 and 166,988,651, respectively.

The results of operations for the three and nine months ended September 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 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 results to date of its ongoing internal investigation into the facts and circumstances surrounding the embezzlement by Nelson, the Company would 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,

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

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.

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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	Effect of Other Adjustments	Restated
September 30, 2005:				
Property and equipment:				
At cost	$ 1,701,246	$ (67,386)	$ 1,626	$ 1,635,486
Accumulated depreciation	(652,685)	2,704	(5,049)	(655,030)
Net	1,048,561	(64,682)	(3,423)	980,456
Goodwill	101,326	(2,270)		99,056
Total assets	1,716,481	(66,952)	(3,423)	1,646,106
Accounts payable, trade	89,964		10,000	99,964
Federal and state income taxes payable	30,854	2,603	161	33,618
Deferred tax liabilities, net	171,542	(27,439)	(4,926)	139,177
Liabilities	416,310	(24,836)	5,235	396,709
Retained earnings	642,596	(42,116)	(8,658)	591,822
Stockholders equity	1,300,171	(42,116)	(8,658)	1,249,397
December 31, 2004:				
Property and 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 and 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

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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 September 30,			
	Previously Reported	Effect of Adjustment for Embezzlement	Effect of Other Adjustments	Restated
2005:				
Depreciation, depletion and impairment	$ 39,216	$ (704)	$ 1,033	$ 39,545
Selling, general and administrative	10,571	(6)		10,565
Other (including gain or loss on sale of assets)	346		311	657
Embezzled funds expense		5,431		5,431
Operating income	173,511	(4,721)	(1,344)	167,446
Income before income taxes	174,418	(4,721)	(1,344)	168,353
Income tax expense	64,283	(1,740)	(495)	62,048
Net income	110,135	(2,981)	(849)	106,305
Per common share:				
Basic	0.64	(0.02)		0.62
Diluted	0.63	(0.02)		0.61
Net cash provided by (used in):				
Operating activities	165,779	(5,425)		160,354
Investing activities	(110,462)	5,425		(105,037)
Purchases of property and equipment	105,949	(5,425)		100,524
2004:				
Depreciation, depletion and impairment	$ 30,789	$ (111)	$ 983	$ 31,661
Selling, general and administrative	8,309	(6)		8,303
Other (including gain or loss on sale of assets)	(153)		41	(112)
Embezzled funds expense		4,759		4,759
Operating income	47,408	(4,642)	(1,024)	41,742
Income before income taxes	47,622	(4,642)	(1,024)	41,956
Income tax expense	17,658	(1,721)	(379)	15,558
Net income	29,964	(2,921)	(645)	26,398
Per common share:				
Basic	0.18	(0.02)		0.16
Diluted	0.18	(0.02)		0.16
Net cash provided by (used in):				
Operating activities	55,577	(4,753)		50,824
Investing activities	(46,467)	4,753		(41,714)
Purchases of property and equipment	47,112	(4,753)		42,359

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	Nine Months Ended September 30,			
	Previously Reported	Effect of Adjustment for Embezzlement	Effect of Other Adjustments	Restated
	(In thousands, except per share amounts)			
2005:				
Depreciation, depletion and impairment	$ 110,575	$ (1,356)	$ 3,100	$ 112,319
Selling, general and administrative	30,175	(18)		30,157
Other (including gain or loss on sale of assets)	1,844		330	2,174
Embezzled funds expense		12,193		12,193
Operating income	390,179	(10,819)	(3,430)	375,930
Income before income taxes	392,050	(10,819)	(3,430)	377,801
Income tax expense	144,502	(3,988)	(1,264)	139,250
Net income	247,548	(6,831)	(2,166)	238,551
Per common share:				
Basic	1.46	(0.04)	(0.01)	1.40
Diluted	1.43	(0.04)	(0.01)	1.38
Net cash provided by (used in):				
Operating activities	321,647	(12,175)	10,000	319,472
Investing activities	(324,207)	12,175	(10,000)	(322,032)
Purchases of property & equipment	264,898	(12,175)	10,000	262,723
2004:				
Depreciation, depletion and impairment	$ 88,523	$ (336)	$ 2,850	$ 91,037
Selling, general and administrative	23,017	(18)		22,999
Other (including gain or loss on sale of assets)	(1,528)		103	(1,425)
Embezzled funds expense		13,479		13,479
Operating income	110,717	(13,125)	(2,953)	94,639
Income before income taxes	111,513	(13,125)	(2,953)	95,435
Income tax expense	41,260	(4,854)	(1,092)	35,314
Net income	70,253	(8,271)	(1,861)	60,121
Per common share:				
Basic	0.42	(0.05)	(0.01)	0.36
Diluted	0.42	(0.05)	(0.01)	0.36
Net cash provided by (used in):				
Operating activities	146,261	(13,461)		132,800
Investing activities	(178,034)	13,461		(164,573)
Acquisitions	32,514	(2,127)		30,387
Purchases of property & equipment	136,835	(11,334)		125,501

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 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.

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On September 29, 2005, the Company acquired five land-based drilling rigs and related drilling equipment for $8.2 million. The transaction 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.

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 its 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 and the third quarter of 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 nine months ended September 30, 2005, compensation expense of $639,000 and $1.3 million, net of $29,000 and $160,000 of forfeitures and of $374,000 and $782,000 of taxes, respectively, was included as a reduction in net income. Compensation expense of $306,000 and $471,000, net of $180,000 and $278,000 of taxes, was included as a reduction in net income for the three and nine months ended September 30, 2004, respectively. 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 September 30,		Nine Months Ended September 30,	
	2005	2004	2005	2004
Net income, as reported	$ 106,305	$ 26,398	$ 238,551	$ 60,121
Add: Stock-based employee compensation expense recorded, net of forfeitures and taxes	639	306	1,339	471
Deduct: Total stock-based employee compensation expense determined under the fair value based method for all awards, net of related tax effects	(3,426)	(3,468)	(9,484)	(9,794)
Pro-forma net income	$ 103,518	$ 23,236	$ 230,406	$ 50,798
Net income per common share:				
Basic, as reported	$ 0.62	$ 0.16	$ 1.40	$ 0.36
Basic, pro-forma	$ 0.60	$ 0.14	$ 1.36	$ 0.31

Diluted, as reported	$	0.61	$	0.16	$	1.38	$	0.36
Diluted, pro-forma	$	0.60	$	0.14	$	1.34	$	0.30

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5. Comprehensive Income

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

	Restated (See Note 2)			
	Three Months Ended September 30,		Nine Months Ended September 30,	
	2005	2004	2005	2004
Net income	$ 106,305	$ 26,398	$ 238,551	$ 60,121
Other comprehensive income (expense):				
Foreign currency translation adjustment related to our Canadian operations, net of tax	2,286	1,872	1,319	675
Comprehensive income, net of tax	$ 108,591	$ 28,270	$ 239,870	$ 60,796

6. Property and Equipment

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

	Restated (See Note 2)	
	September 30, 2005	December 31, 2004
Equipment	$ 1,537,197	$ 1,239,519
Oil and natural gas properties	77,349	82,711
Buildings	15,654	12,892
Land	5,286	3,649
	1,635,486	1,338,771
Less accumulated depreciation and depletion	(655,030)	(573,752)
	$ 980,456	$ 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

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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 September 30,		Nine Months Ended September 30,	
	2005	2004	2005	2004
Revenues:				
Contract drilling(a)	$ 401,626	$ 207,808	$ 1,028,230	$ 577,824
Pressure pumping	27,640	19,663	66,358	48,490
Drilling and completion fluids(b)	29,842	23,475	88,994	65,146
Oil and natural gas	10,234	9,602	28,146	25,104
Total segment revenues	469,342	260,548	1,211,728	716,564
Elimination of intercompany revenues(a)(b)	603	1,374	2,474	4,101
Total revenues	$ 468,739	$ 259,174	$ 1,209,254	$ 712,463
Income before income taxes:				
Contract drilling	$ 163,109	$ 38,752	$ 367,721	$ 92,697
Pressure pumping	7,691	6,199	15,779	12,787
Drilling and completion fluids	2,546	1,110	8,061	2,518
Oil and natural gas	4,098	3,674	10,532	7,217
	177,444	49,735	402,093	115,219
Corporate and other	(3,892)	(3,234)	(10,743)	(7,101)
Other operating	(675)		(3,227)	
Embezzled funds expense(c)	(5,431)	(4,759)	(12,193)	(13,479)
Interest income	944	233	2,011	688
Interest expense	(56)	(75)	(179)	(205)
Other	19	56	39	313
Income before income taxes	$ 168,353	$ 41,956	$ 377,801	$ 95,435

	Restated (See Note 2)	
	September 30, 2005	December 31, 2004
Identifiable assets:		
Contract drilling	$ 1,301,286	$ 961,873

Pressure pumping		70,919		49,145
Drilling and completion fluids		75,787		62,970
Oil and natural gas		59,781		62,984
		1,507,773		1,136,972
Corporate and other(d)		138,333		119,813
Total assets	$	1,646,106	$	1,256,785

(a) Includes contract drilling intercompany revenues of approximately $580,000 and $1.4 million for the three months ended September 30, 2005 and 2004, respectively, and approximately $2.3 million and $4.0 million for the nine months ended September 30, 2005 and 2004, respectively.

(b) Includes drilling and completion fluids intercompany revenues of approximately $23,000 and $20,000 for the three months ended September 30, 2005 and 2004, respectively, and approximately $182,000 and $128,000 for the nine months ended September 30, 2005 and 2004, respectively.

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(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 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 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 its 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.

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

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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.

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 September 30, 2005 and December 31, 2004 is as follows (in thousands):

	Restated (See Note 2)	
	September 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 September 30, 2005 and December 31, 2004 (in thousands):

	September 30, 2005	**December 31, 2004**
Salaries, wages, payroll taxes and benefits	$ 31,036	$ 21,245
Workers compensation liability	42,277	38,677
Sales, use and other taxes	11,659	5,863
Insurance, other than workers compensation	9,542	7,061
Other	7,979	6,317

	$	102,493	$	79,163

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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 nine months ended September 30, 2005 and 2004 (in thousands):

	2005	2004
Balance at beginning of year	$ 2,358	$ 1,163
Liabilities incurred*	61	1,242
Liabilities settled	(801)	(144)
Accretion expense	55	52
Asset retirement obligation at end of period	$ 1,673	$ 2,313

* The 2004 amount includes $1,091 of liabilities assumed in the acquisition 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.

The Company has signed non-cancelable commitments to purchase $93.0 million of equipment to be received throughout 2006.

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, April 27, 2005 and July 27, 2005, the Company s Board of Directors approved cash dividends on its common stock in the amount of $0.04 per share. The cash dividends of approximately $6.7 million, $6.8 million and $6.9 million were paid on March 4, 2005, June 1, 2005 and September 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.