ENERGY PARTNERS LTD
Form 10-Q
August 05, 2008
Table of Contents

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

(Mark One)

x **QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15 (d) OF THE SECURITIES EXCHANGE ACT OF 1934**
For the quarterly period ended June 30, 2008

OR

¨ **TRANSITION REPORT PURSUANT TO SECTION 13 OR 15 (d) OF THE SECURITIES EXCHANGE ACT OF 1934**
Commission file number: 001-16179

ENERGY PARTNERS, LTD.

(Exact Name of Registrant as Specified in Its Charter)

Delaware	**72-1409562**
(State or Other Jurisdiction of Incorporation or Organization)	**(I.R.S. Employer Identification Number)**
201 St. Charles Ave., Suite 3400 New Orleans, Louisiana	**70170**
(Address of principal executive offices)	**(Zip code)**

Registrant s telephone number, including area code: (504) 569-1875

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 x No ¨

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or smaller reporting company. See definitions of large accelerated filer , accelerated filer and smaller reporting company in Rule 12b-2 of the Exchange Act.

Large accelerated filer ¨	Accelerated filer x
Non-accelerated filer ¨ (Do not check if a smaller reporting company)	Smaller reporting company ¨

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

As of July 31, 2008, there were 32,052,384 shares of the Registrant s Common Stock, par value $0.01 per share, outstanding.

Table of Contents

TABLE OF CONTENTS

		Page
PART I FINANCIAL STATEMENTS		
Item 1.	Financial Statements:	3
	Consolidated Balance Sheets as of June 30, 2008 and December 31, 2007	3
	Consolidated Statements of Operations for the three and six months ended June 30, 2008 and 2007	4
	Consolidated Statements of Cash Flows for the six months ended June 30, 2008 and 2007	5
	Notes to Consolidated Financial Statements	6
Item 2.	Management s Discussion and Analysis of Financial Condition and Results of Operations	16
Item 3.	Quantitative and Qualitative Disclosures about Market Risk	23
Item 4.	Controls and Procedures	25
PART II OTHER INFORMATION		
Item 4.	Submission of Matters of the Vote of Security Holders	25
Item 6.	Exhibits	27

Table of Contents

Item 1. FINANCIAL STATEMENTS

ENERGY PARTNERS, LTD. AND SUBSIDIARIES

CONSOLIDATED BALANCE SHEETS

(In thousands, except share data)

	June 30, 2008 (Unaudited)	December 31, 2007
ASSETS		
Current assets:		
Cash and cash equivalents	$ 8,619	$ 8,864
Trade accounts receivable	53,122	47,081
Deferred tax assets	16,017	3,865
Prepaid expenses	5,943	6,698
Total current assets	83,701	66,508
Property and equipment, at cost under the successful efforts method of accounting for oil and natural gas properties	1,637,101	1,547,003
Less accumulated depreciation, depletion and amortization	(885,934)	(824,397)
Net property and equipment	751,167	722,606
Other assets	14,670	15,556
Deferred financing costs net of accumulated amortization of $2,938 in 2008 and $2,100 in 2007	9,503	10,186
	$ 859,041	$ 814,856
LIABILITIES AND STOCKHOLDERS EQUITY		
Current liabilities:		
Accounts payable	$ 22,789	$ 14,369
Accrued expenses	86,234	104,555
Fair value of commodity derivative instruments	42,730	9,124
Total current liabilities	151,753	128,048
Long-term debt	484,501	484,501
Deferred tax liabilities	36,134	20,880
Asset retirement obligation	73,006	73,350
Fair value of commodity derivative instruments		4,602
Other	1,428	1,505
	746,822	712,886
Stockholders equity:		
Preferred stock, $1 par value. Authorized 1,700,000 shares; no shares issued and outstanding		
Common stock, par value $0.01 per share. Authorized 100,000,000 shares; issued: 2008 44,268,718 shares; 2007 43,980,644 shares; outstanding, net of treasury shares: 2008 32,028,732 shares; 2007 31,740,658 shares	443	441
Additional paid-in capital	378,810	374,874
Accumulated deficit	(8,678)	(14,989)
Treasury stock, at cost. 2008 12,239,986 shares; 2007 12,239,986 shares	(258,356)	(258,356)
Total stockholders equity	112,219	101,970
Commitments and contingencies		

	$ 859,041	$ 814,856

See accompanying notes to consolidated financial statements.

Table of Contents

ENERGY PARTNERS, LTD. AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF OPERATIONS

(UNAUDITED)

(In thousands, except per share data)

	Three Months Ended June 30,		Six Months Ended June 30,	
	2008	2007	2008	2007
Revenue:				
Oil and natural gas	$ 125,642	$ 121,584	$ 223,097	$ 229,986
Other	46	82	87	143
	125,688	121,666	223,184	230,129
Costs and expenses:				
Lease operating	14,662	17,437	28,876	34,186
Transportation	260	606	666	1,065
Exploration expenditures, dry hole costs and impairments	5,271	37,375	28,480	59,176
Depreciation, depletion and amortization	33,244	44,053	62,054	91,973
Accretion	1,087	1,103	2,143	2,203
General and administrative	13,485	13,507	22,852	35,902
Taxes, other than on earnings	3,315	2,199	5,694	5,069
Gain on insurance recoveries				(8,084)
(Gain) loss on sale of assets	80	(7,020)	(6,594)	(7,020)
Other	62	(8)	1,158	(8)
Total costs and expenses	71,466	109,252	145,329	214,462
Business interuption recovery				9,084
Income from operations	54,222	12,414	77,855	24,751
Other income (expense):				
Interest income	66	390	367	570
Interest expense	(11,439)	(13,629)	(23,351)	(20,386)
Gain (loss) on derivative instruments	(36,483)	1,907	(44,809)	1,907
Loss on early extinguishment of debt		(10,838)		(10,838)
	(47,856)	(22,170)	(67,793)	(28,747)
Income (loss) before income taxes	6,366	(9,756)	10,062	(3,996)
Income taxes	(2,370)	3,486	(3,751)	1,422
Net income (loss)	3,996	(6,270)	6,311	(2,574)
Basic earnings (loss) per share	$ 0.13	$ (0.18)	$ 0.20	$ (0.07)
Diluted earnings (loss) per share	$ 0.12	$ (0.18)	$ 0.20	$ (0.07)
Weighted average common shares used in Computing earnings per share:				
Basic	31,950	34,581	31,861	37,364

Incremental common shares				
Stock options	108			
Restricted share units	83			
Performance shares			7	
Diluted	32,141	34,581	31,868	37,364

See accompanying notes to consolidated financial statements.

Table of Contents

ENERGY PARTNERS, LTD. AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF CASH FLOWS

(UNAUDITED)

(In thousands)

	Six Months Ended June 30,	
	2008	**2007**
Cash flows from operating activities:		
Net income (loss)	$ 6,311	$ (2,574)
Adjustments to reconcile net income (loss) to net cash provided by operating activities:		
Depreciation, depletion and amortization	62,054	91,973
Accretion	2,143	2,203
Unrealized (gain) loss on derivative contracts	29,004	(1,907)
Non cash-based compensation	2,802	4,604
Non cash loss on early extinguishment of debt		3,398
Deferred income taxes	3,101	(1,423)
Gain on sale of oil and natural gas assets	(6,611)	(7,020)
Exploration expenditures	23,749	51,788
Amortization of deferred financing costs	838	565
Gain on insurance recoveries		(8,084)
Other	937	830
Changes in operating assets and liabilities:		
Trade accounts receivable	(6,889)	7,877
Other receivables		56,346
Prepaid expenses	755	(4,772)
Other assets	886	(1,715)
Accounts payable and accrued expenses	4,485	(24,521)
Other liabilities	(4,142)	(264)
Net cash provided by operating activities	119,423	167,304
Cash flows used in investing activities:		
Insurance recoveries for property, plant and equipment		19,574
Property acquisitions	(20,197)	(1,115)
Exploration and development expenditures	(114,519)	(195,509)
Proceeds from sale of oil and natural gas assets	15,026	67,543
Other property and equipment additions	(505)	(459)
Net cash used in investing activities	(120,195)	(109,966)
Cash flows provided by (used in) financing activities:		
Deferred financing costs	(155)	(10,882)
Repayments of long-term debt	(70,000)	(445,499)
Proceeds from long-term debt	70,000	603,000
Purchase of shares into treasury		(200,100)
Exercise of stock options and warrants	682	766
Net cash provided by (used in) financing activities	527	(52,715)
Net increase (decrease) in cash and cash equivalents	(245)	4,623

Cash and cash equivalents at beginning of period		8,864		3,214
Cash and cash equivalents at end of period	$	8,619	$	7,837

See accompanying notes to consolidated financial statements.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(UNAUDITED)

(1) BASIS OF PRESENTATION

Certain information and footnote disclosures normally in financial statements prepared in accordance with generally accepted accounting principles have been condensed or omitted pursuant to rules and regulations of the Securities and Exchange Commission; however, management believes the disclosures which are made are adequate to make the information presented not misleading. These financial statements and footnotes should be read in conjunction with the financial statements and notes thereto included in Energy Partners, Ltd. s (the Company) Annual Report on Form 10-K for the year ended December 31, 2007 and Management s Discussion and Analysis of Financial Condition and Results of Operations. The Company maintains a website at www.eplweb.com which contains information about the Company including links to the Company s Annual Report on Form 10-K, quarterly reports on Form 10-Q and current reports on Form 8-K. The Company s website and the information contained in it and connected to it shall not be deemed incorporated by reference into this report on Form 10-Q.

The financial information as of June 30, 2008 and for the three and six month periods ended June 30, 2008 and 2007 has not been audited. However, in the opinion of management, all adjustments (which include only normal recurring adjustments) necessary to present fairly the results of operations for the periods presented have been included therein. The results of operations for the first six months of the year are not necessarily indicative of the results of operations which might be expected for the entire year.

(2) MERGERS, ACQUISITIONS AND DIVESTITURES

On March 26 and 27, 2008, the Company completed the sale of two Gulf of Mexico Shelf properties located in its Western offshore area for $15.0 million after giving effect to preliminary closing adjustments. The Company recorded a gain on the sale of $7.0 million in the first half of 2008.

On June 12, 2007, the Company completed the sale of substantially all of the Company s onshore South Louisiana assets for $68.6 million after giving effect to closing adjustments. The Company used the proceeds to pay down a portion of its revolving credit facility. As of the closing date, the estimated proved reserves of the disposed properties totaled approximately 2.1 million barrels of oil equivalent. The Company recorded a gain of $7.2 million on this sale in the second quarter of 2007.

On October 12, 2006 the Company announced that its Board of Directors (the Board) had directed the Company, assisted by its financial and legal advisors, to explore strategic alternatives to maximize stockholder value, including the possible sale of the Company. On March 12, 2007 the Company announced that the Board had concluded its strategic alternatives process. As a result of this process, the Board, with advice from its financial and legal advisors and management, determined to continue with the execution of the Company s strategic plan, augmented by a self-tender offer for up to 8,700,000 shares of its common stock at $23.00 per share, the refinancing of its bank credit facility and a tender offer for all of its existing $150 million aggregate principal amount of senior notes due 2010 (the Transactions), and the divestment of selected properties following the completion of the Transactions to reduce debt under the Company s new bank credit facility. In order to fund the Transactions, the Company undertook a private offering of $450 million of senior unsecured notes and entered into a new bank credit facility. The Company incurred $9.4 million of financial and legal advisory fees during the first half of 2007 related to the exploration of strategic alternatives and the tender offers.

(3) COMMON STOCK

On March 12, 2007, the Company s Board concluded its strategic alternatives process as discussed in note 2 above, which resulted in, among other things, an equity self-tender offer for up to 8,700,000 shares of its common stock at $23.00 per share and the authorization for the repurchase of up to $50 million of its common stock during the one year period following the completion of the equity self tender offer, subject to business and market conditions and any debt covenants restricting such repurchases. On April 23, 2007 the Company completed the equity self-tender offer and purchased 8,700,000 million shares of its common stock. In addition, during the year ended December 31, 2007 the Company acquired 59,500 shares of its common stock for $0.8 million, at an average price of $13.71 per share, in its stock repurchase program. All of these shares are reflected in treasury stock in the Consolidated Balance Sheets.

Table of Contents

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(UNAUDITED)

(4) EARNINGS PER SHARE

Basic earnings per share are computed by dividing income available to common stockholders by the weighted average number of common shares outstanding during the period. Diluted earnings per share is computed in the same manner as basic earnings per share except that the denominator is increased to include the number of additional common shares that could have been outstanding assuming the exercise of stock options and the potential shares associated with restricted share units and performance shares that would have a dilutive effect on earnings per share.

(5) DERIVATIVE TRANSACTIONS

The Company enters into derivative transactions with major financial institutions and others to reduce exposure to fluctuations in the price of oil and natural gas. While the use of these transactions limits the downside risk of adverse price movements, their use also may limit future revenues from favorable price movements. The Company s Board has set limitations on the percentage of proved production that the Company can hedge. Crude oil hedges are primarily settled based on the average of the reported settlement prices for West Texas Intermediate crude on the New York Mercantile Exchange (NYMEX) for each month. Natural gas hedges are primarily settled based on the average of the last three days of trading of the NYMEX Henry Hub natural gas contract for each month.

The Company has primarily used financially-settled crude oil and natural gas zero-cost collars and put options to provide floor prices with varying upside price participation. With a zero-cost collar, the counterparty is required to make a payment to the Company if the settlement price for any settlement period is below the floor price of the collar, and the Company is required to make a payment to the counterparty if the settlement price is above the cap price for the collar. With a put option, the counterparty is required to make a payment to the Company if the settlement price for any settlement period is below the strike price of the put and the Company has no obligations to the counterparty except for the payment of any option premium. On occasion, the Company may incorporate floors and/or collars into its production sales contracts which are settled under conventional marketing terms.

Prior to the second quarter of 2007, all derivative transactions that qualified for hedge accounting under Financial Accounting Standards No. 133 Accounting for Derivative Instruments and Hedging Activities, (Statement 133) as amended by Statement Nos. 137, 138 and 149 were designated on the date the Company entered into each transaction as a hedge of the variability in cash flows associated with the forecasted sale of future oil and natural gas production. After-tax changes in the fair value of a hedge that was highly effective and designated and qualified as a cash flow hedge, to the extent that the hedge was effective, were recorded as Accumulated Other Comprehensive Income (OCI) on the consolidated balance sheet until the sale of the hedged oil and natural gas production occurred. Upon the sale of the underlying hedged production, the net after-tax change in the fair value of the associated hedging transaction recorded in OCI was reversed and the resulting gain or loss on the settlement of the hedge, to the extent that it was effective, was reported in oil and natural gas revenues in the consolidated statement of operations. Once hedge accounting was discontinued prospectively effective April 2, 2007 for existing contracts and while the hedging contracts remained in effect they were carried at their fair value on the Consolidated Balance Sheets until settlement and all subsequent changes in fair value were recognized in the Consolidated Statements of Operations for the period in which the change occurred. All of these contracts were settled in 2007.

Effective April 2, 2007, the Company elected to discontinue hedge accounting on its existing contracts and elected not to designate any additional derivative contracts that were entered into subsequent to that date as cash flow hedges under Statement 133, as amended. Derivative contracts are carried at their fair value on the Consolidated Balance Sheets as Fair value of commodity derivative instruments and all unrealized gains and losses are recorded in Gain (loss) on derivative instruments in Other income (expense) in the Statements of Operations and realized gains and losses related to contract settlements subsequent to April 2, 2007 are recognized in Other income (expense) in the Consolidated Statements of Operations.

Table of Contents

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(UNAUDITED)

The Company had the following derivative contracts as of June 30, 2008:

Natural Gas Positions

Remaining Contract Term	Contract Type	Strike Price ($/Mmbtu)	Volume (Mmbtu) Daily	Volume (Mmbtu) Total
11/08 12/08	Collar	$6.82/$15.38	20,000	1,220,000
01/09 03/09	Collar	$6.75/$17.15	10,000	900,000

Crude Oil Positions

Remaining Contract Term	Contract Type	Strike Price ($/Bbl)	Volume (Bbls) Daily	Volume (Bbls) Total
07/08 9/08	Put	$55.00	2,000	184,000
07/08 10/08	Collar	$55.00/$85.65	500	61,500
11/08 12/08	Collar	$55.00/$86.80	2,500	152,500
1/09 06/09	Collar	$55.00/$87.17	3,000	543,000

The following table presents information about the components of gain (loss) on derivative instruments for the indicated periods.

	Three Months Ended June 30,		Six Months Ended June 30,	
	2008	2007	2008	2007
Derivative contracts:				
Unrealized gain (loss) due to change in fair market value	$ (25,907)	$ 1,907	$ (29,004)	$ 1,907
Realized loss on settlement	(10,576)		(15,805)	
Total gain (loss) on derivative instruments	$ (36,483)	$ 1,907	$ (44,809)	$ 1,907

(6) OIL AND GAS PROPERTIES

At June 30, 2008, the Company had two projects whose exploratory well costs in the amount of $35.1 million were suspended and were capitalized for a period greater than one year. At June 30, 2007, the Company had one project whose exploratory well costs in the amount of $17.0 million were suspended and were capitalized for a period greater than one year.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(UNAUDITED)

(7) ASSET RETIREMENT OBLIGATION

Accounting and reporting standards require entities to record the fair value of a liability for an asset retirement obligation in the period in which it is incurred and a corresponding increase in the carrying amount of the related long-lived asset. The following table reconciles the beginning and ending aggregate recorded amount of the asset retirement obligation for the six months ended June 30, 2008.

	Six Months Ended June 30, 2008 (in thousands)
December 31, 2007	$ 77,898
Accretion expense	2,143
Sale of properties	(321)
Revisions	1,162
Liabilities incurred	2,523
Liabilities settled	(4,064)
June 30, 2008	$ 79,341

At June 30, 2008, and included above, asset retirement obligations required to be settled within the next twelve months of $6.3 million were included in accrued expenses on the Consolidated Balance Sheets.

(8) INDEBTEDNESS

On April 23, 2007 the Company refinanced its bank credit facility with a new $300 million revolving credit facility (the bank credit facility) with an initial availability of $225 million and a borrowing base of $200 million. Concurrently with the 2007 sale of assets described in Note 2, the availability under the bank credit facility was automatically reduced to the $200 million borrowing base amount. On May 6, 2008, the Company s bank credit facility was redetermined with a borrowing base of $150 million. The bank credit facility is secured by substantially all of the Company s assets. The bank credit facility permits both prime rate borrowings and London InterBank Offered Rate (LIBOR) borrowings plus a floating spread. The spread will float up or down based on utilization of the bank credit facility. The spread can range from 1.00% to 2.50% above LIBOR and 0% to 0.50% above prime. At June 30, 2008, the Company had $30 million outstanding under the bank credit facility and $120 million available under its borrowing base. In addition, the Company pays an annual fee on the unused portion of the bank credit facility ranging between 0.25% to 0.50% based on utilization. The bank credit facility contains customary events of default and various financial covenants, which require the Company to: (i) maintain a minimum current ratio, as defined by the bank credit facility, of 1.0x, (ii) maintain a minimum Consolidated EBITDAX to interest ratio, as defined by the bank credit facility, of 2.5x, and (iii) maintain a ratio of long-term debt to Consolidated EBITDAX below 3.0x. The Company was in compliance with the bank credit facility covenants as of June 30, 2008. The borrowing base remains subject to redetermination based on the proved reserves of the oil and natural gas properties that serve as collateral for the bank credit facility as set out in the reserve report delivered to the banks on or about each April 1 and October 1.

On April 23, 2007 the Company completed a private placement of $450 million aggregate principal amount of senior unsecured notes (the Senior Unsecured Notes), consisting of $300 million aggregate principal amount of 9.75% Senior Notes due 2014 (the Fixed Rate Notes), with interest payable semi-annually on April 15 and October 15 beginning on October 15, 2007, and $150 million aggregate principal amount of Senior Floating Rate Notes due 2013 (the Floating Rate Notes). The interest rate on the Floating Rate Notes for a particular interest period will be an annual rate equal to the three-month LIBOR plus 5.125%. Interest on the Floating Rate Notes is payable quarterly on January 15, April 15, July 15 and October 15, beginning in July of 2007. The Company may redeem the Senior Unsecured Notes, in whole or in part, prior to their maturity at specific redemption prices, including premiums ranging from 4.875% to 0% from 2011 to 2013 and thereafter for the Fixed Rate Notes and premiums ranging from 2% to 0% from 2008 to 2010 and thereafter for the Floating Rate Notes. The indenture governing the Senior Unsecured Notes contains customary covenants, including but not limited to a covenant limiting the creation of liens securing indebtedness. The Senior Unsecured Notes are not subject to any sinking fund requirements. In November 2007 the Company consummated an exchange offer pursuant to which it exchanged registered senior unsecured notes having substantially identical terms as the privately placed Senior Unsecured Notes.

9

Table of Contents

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(UNAUDITED)

On May 4, 2007, the Company completed a cash tender offer for its $150 million 8.75% Senior Notes due 2010 (the Senior Notes). Approximately $145.5 million of these Senior Notes were repurchased and substantially all of their covenants have been removed.

A loss on early extinguishment of debt for the refinancing of the bank credit facility and the repurchase of the Senior Notes of approximately $10.8 million was recorded during the second quarter 2007. It included the write-off of unamortized deferred financing costs related to the bank credit facility and the Senior Notes as well as the consent fees relating to the tender for the Senior Notes.

(9) FAIR VALUE MEASUREMENTS

In September 2006, the FASB issued Statement of Accounting Standards No. 157, Fair Value Measurements (Statement 157). Statement 157 defines fair value, establishes a framework for measuring fair value in generally accepted accounting principles, and expands disclosures about fair value measurements. The Company adopted Statement 157 effective January 1, 2008. Certain of the Company s assets and liabilities are reported at fair value in the accompanying Consolidated Balance Sheets which include amounts for both financial and nonfinancial instruments. The FASB agreed to a one year deferral of Statement 157 s fair value measurement requirements for nonfinancial assets and liabilities that are not required or permitted to be measured at fair value on a recurring basis such as asset retirement obligations and oil and natural gas property and equipment. The following tables provide fair value measurement information for such assets and liabilities as of June 30, 2008.

The carrying values of cash and cash equivalents, trade accounts receivable and accounts payable (including income taxes payable and accrued expenses) included in the accompanying Consolidated Balance Sheets approximated fair value at June 30, 2008. These assets and liabilities are not presented in the following tables.

	As of June 30, 2008				
			Fair Value Measurements Using:		
	Carrying Amount (In thousands)	Total Fair Value	Quoted Prices in Active Markets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Financial Assets (Liabilities):					
Oil and natural gas puts and collars	$ 42,730	$ 42,730	$	$ 42,730	$
Debt	$ 484,501	$ 452,480	$ 422,480	$ 30,000	$

Statement 157 establishes a fair value hierarchy that prioritizes the inputs to valuation techniques used to measure fair value. As presented in the table above, this hierarchy consists of three broad levels. Level 1 inputs on the hierarchy consist of unadjusted quoted prices in active markets for identical assets and liabilities and have the highest priority. Level 2 inputs are other than quoted prices in active markets included in Level 1, and Level 3 inputs have the lowest priority and include significant inputs that are generally less observable from objective sources. When available, the Company measures fair value using Level 1 inputs because they generally provide the most reliable evidence of fair value. The Company currently does not use Level 3 inputs to measure fair value.

Table of Contents

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(UNAUDITED)

The following methods and assumptions were used to estimate the fair values of the assets and liabilities in the table above.

Level 1 Fair Value Measurements

Debt The Fixed Rate Notes and the Floating Rate Notes are actively traded in an established market. The fair values of these debt instruments are based on quotes obtained through financial information services and/or major financial institutions.

Level 2 Fair Value Measurements

Debt The fair value of the bank credit facility is estimated to approximate the carrying amount because the interest rates paid on such debt are generally set for periods of three months or less.

Oil and natural gas puts and collars The fair values of some of the oil and natural gas puts and collars are estimated using similar, observable NYMEX published settlements.

(10) TROPICAL WEATHER

As a result of Hurricanes Katrina and Rita and three other hurricanes that traversed the Gulf of Mexico and adjacent land areas in 2005, nearly all of the Company s production was shut in at one time or another during the third quarter of 2005 and into 2006. The Company maintained business interruption insurance during this period on its significant properties, including its East Bay field on which recovery of lost revenue continued to accrue until October 2006. Through March 31, 2007, the total business interruption claim on these fields was $62.6 million (all of which had been collected as of that date). In the first quarter of 2007, the Company settled and collected all remaining claims related to Hurricanes Katrina and Rita and recognized business interruption income of $9.1 million and a gain of $8.1 million on a property damage settlement.

(11) NEW ACCOUNTING PRONOUNCEMENTS

In May 2008, the FASB issued Statement of Financial Accounting Standard No. 162, The Hierarchy of Generally Accepted Accounting Principles (Statement 162). Statement 162 identifies the sources of accounting principles and the framework for selecting the principles to be used in the preparation of financial statements that are presented in conformity with generally accepted accounting principles in the U.S. Statement 162 is effective 60 days following the SEC s approval of the Public Company Accounting Oversight Board amendments to Au Section 411, *The Meaning of* Present Fairly in Conformity with Generally Accepted Accounting Principles. The Company is currently assessing what impact Statement 162 may have on the Company s financial position, results of operations or cash flows.

In March 2008, the FASB issued Statement of Accounting Standards No. 161, Disclosures about Derivative Instruments and Hedging Activities an amendment of FASB Statement No. 133 (Statement 161). Statement 161 changes the disclosure requirements for derivative instruments and hedging activities. Entities are required to provide enhanced disclosures about (a) how and why an entity uses derivative instruments, (b) how derivative instruments and related hedged items are accounted for under Statement 133 and its related interpretations, and (c) how derivative instruments and related hedged items affect an entity s financial position, financial performance, and cash flows. Statement 161 is effective for financial statements issued for fiscal years and interim periods beginning after November 15, 2008, with early application encouraged. Statement 161 encourages, but does not require, comparative disclosures for earlier periods at initial adoption. The Company is currently assessing what impact Statement 161 may have on the Company s financial disclosures.

In December 2007, the FASB issued Statement of Accounting Standards No. 141R, Business Combinations (Statement 141R). Statement 141R establishes principles and requirements for how an acquirer recognizes and measures in its financial statements the identifiable assets acquired, the liabilities assumed, any non-controlling interest in the acquiree and the goodwill acquired. This statement also establishes disclosure requirements which will enable users to evaluate the nature and financial effects of the business combination. Statement 141R applies prospectively to business combinations for which the acquisition date is on or after the beginning of the first annual reporting period beginning on or after December 15, 2008. The Company is assessing what impact Statement 141R may have on its financial position, results of operations or cash flows should it complete a business combination after the effective date of Statement 141R.

(12) RELATED PARTY

One of the Company s former directors (through May 29, 2008) is a senior managing director of Evercore Partners, Inc. an affiliate of Evercore Group L.L.C. (Evercore). Evercore provided financial advisory services to the Company in connection with a subsequently terminated merger agreement in 2006 with Stone Energy Corporation, an unsolicited cash tender offer in 2006 by a U.S. Subsidiary of Woodside Petroleum, Ltd. that subsequently expired and the Company s exploration of strategic alternatives. A $7.0 million fee was due to Evercore upon the earlier of the consummation of a transaction or September 5, 2007, of which $2.3 million was accrued during 2006 and the remaining $4.7 million was accrued in the first quarter of 2007 and paid in September 2007.

Table of Contents

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(UNAUDITED)

(13) SUPPLEMENTAL CONDENSED CONSOLIDATING FINANCIAL INFORMATION

In connection with the sale of the Senior Unsecured Notes discussed above, all of the Company s current active subsidiaries (the Guarantor Subsidiaries) jointly, severally and unconditionally guaranteed the payment obligations under the Senior Unsecured Notes. The following supplemental financial information sets forth, on a consolidating basis, the balance sheet, statement of operations and cash flow information for Energy Partners, Ltd. (parent company only) and for the Guarantor Subsidiaries. The Company has not presented separate financial statements and other disclosures concerning the Guarantor Subsidiaries because management has determined that such information is not material to investors.

The supplemental condensed consolidating financial information has been prepared pursuant to the rules and regulations for condensed financial information and does not include all disclosures included in annual financial statements, although the Company believes that the disclosures made are adequate to make the information presented not misleading. Certain reclassifications were made to conform all of the financial information to the financial presentation on a consolidated basis. The principal eliminating entries eliminate investments in subsidiaries, intercompany balances and intercompany revenues and expenses.

Table of Contents

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(UNAUDITED)

Supplemental Condensed Consolidating Balance Sheet

As of June 30, 2008

	Parent Company Only	Guarantor Subsidiaries	Eliminations	Consolidated
	(in thousands)			
ASSETS				
Current assets:				
Cash and cash equivalents	$ 8,619	$	$	$ 8,619
Accounts receivable	40,252	10,730	2,140	53,122
Other current assets	21,827	133		21,960
Total current assets	70,698	10,863	2,140	83,701
Property and equipment	1,383,565	253,536		1,637,101
Less accumulated depreciation, depletion and amortization	(756,479)	(129,455)		(885,934)
Net property and equipment	627,086	124,081		751,167
Investment in affiliates	93,102	1,597	(94,699)	
Notes receivable, long-term		115,531	(115,531)	
Other assets	24,083	90		24,173
	$ 814,969	$ 252,162	$ (208,090)	$ 859,041
LIABILITIES AND STOCKHOLDERS EQUITY				
Current liabilities:				
Accounts payable and accrued expenses	$ 107,565	$ 1,458	$	$ 109,023
Fair value of commodity derivative instruments	42,730			42,730
Total current liabilities	150,295	1,458		151,753
Long-term debt	484,501	115,531	(115,531)	484,501
Other liabilities	67,954	42,614		110,568
	702,750	159,603	(115,531)	746,822
Stockholders equity:				
Preferred stock		3	(3)	
Common stock	443	98	(98)	443
Additional paid-in capital	378,810	68	(68)	378,810
Retained earnings (accumulated deficit)	(8,678)	92,390	(92,390)	(8,678)
Treasury stock	(258,356)			(258,356)
Total stockholders equity	112,219	92,559	(92,559)	112,219
	$ 814,969	$ 252,162	$ (208,090)	$ 859,041

Table of Contents

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(UNAUDITED)

Supplemental Condensed Consolidated Statement of Operations

Six Months Ended June 30, 2008

	Parent Company Only	Guarantor Subsidiaries	Eliminations	Consolidated
		(in thousands)		
Revenue:				
Oil and natural gas	$ 168,321	$ 54,776	$	$ 223,097
Other	26,464	75	(26,452)	87
	194,785			