BLUE DOLPHIN ENERGY CO
Form 10-K
March 13, 2009

Table of Contents

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549
FORM 10-K

(Mark One)

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

For the fiscal year ended December 31, 2008

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 No. 0-15905

BLUE DOLPHIN ENERGY COMPANY

(Exact name of registrant as specified in its charter)

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

801 Travis Street, Suite 2100
Houston, Texas 77002
(713) 568-4725

(Address and telephone number, including area code, of registrant s principal executive offices)

Securities registered pursuant to Section 12(b) of the Exchange Act:

Title of Each Class	Name of Each Exchange on Which Registered
Common Stock, par value $.01 per share	Nasdaq Capital Market

Securities registered pursuant to Section 12(g) of the Act:

None

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act. Yes o No þ

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Exchange Act. Yes o No þ

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 if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of registrant s knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K. þ

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

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

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

Aggregate market value of voting stock held by non-affiliates of the registrant as of June 30, 2008 was approximately $24.7 million based on the closing price of $2.12 per share on the NASDAQ Capital Market.

Number of shares of common stock outstanding as of March 10, 2009 11,745,299

Documents Incorporated By Reference

Certain sections of the registrant s definitive proxy statement for the 2009 Annual Meeting of Stockholders of the registrant (sections entitled Ownership of Securities of the Company, Election of Directors, Executive Compensation and Transactions With Related Persons), which is to be filed with the Securities and Exchange Commission pursuant to Regulation 14A, under the Securities and Exchange Act of 1934 within 120 days of the registrant s fiscal year ended December 31, 2008, are incorporated by reference in Part III of this report.

BLUE DOLPHIN ENERGY COMPANY
FORM 10-K REPORT INDEX

Table of Contents

PART I

Forward Looking Statements. Certain of the statements included in this annual report on Form 10-K, 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. Blue Dolphin Energy Company (referred to herein, with its predecessors and subsidiaries, as Blue Dolphin, we, us and our) cautions readers that these statements are not guarantees of future performance or results and such statements involve risks and uncertainties that may cause actual results and outcomes to differ materially from those indicated in forward-looking statements. Some of the important factors, risks and uncertainties that could cause actual results to vary from forward-looking statements include:

the level of utilization of our pipelines;

availability and cost of capital;

actions or inactions of third party operators for properties where we have an interest;

the risks associated with oil and gas exploration;

the level of production from oil and gas properties that we have interests in;

gas and oil price volatility;

uncertainties in the estimation of proved reserves, in the projection of future rates of production, the timing of development expenditures and the amount and timing of property abandonment;

regulatory developments; and

general economic conditions.

Additional factors that could cause actual results to differ materially from those indicated in the forward-looking statements are discussed in Item 1A Risk Factors. Readers are cautioned not to place undue reliance on these forward-looking statements which speak only as of the date hereof. We undertake no duty to update these forward-looking statements. Readers are urged to carefully review and consider the various disclosures made by us which attempt to advise interested parties of the additional factors which may affect our business, including the disclosures made under the caption Management s Discussion and Analysis of Financial Condition and Results of Operations in this report.

ITEM 1. BUSINESS

The Company

Blue Dolphin Energy Company, a Delaware corporation formed in 1986, is a holding company and conducts substantially all of its operations through its subsidiaries. We conduct our business activities in two primary business segments: (i) pipeline transportation and related services for producer/shippers, and (ii) oil and gas exploration and production. Substantially all of our assets consist of equity interests in our subsidiaries. Our operating subsidiaries are:

Blue Dolphin Pipe Line Company, a Delaware corporation;

Blue Dolphin Petroleum Company, a Delaware corporation;

Blue Dolphin Exploration Company, a Delaware corporation;

Blue Dolphin Services Co., a Texas corporation; and

Petroport, Inc., a Delaware corporation.

Table of Contents

Our principal executive office is located at 801 Travis Street, Suite 2100, Houston, Texas, 77002, and our telephone number is (713) 568-4725. All of our operations are in the Gulf of Mexico, except our onshore facilities which we own and operate to process and store natural gas and liquids to primarily serve our offshore operations. We have eight employees and two consultants. Our common stock is traded on the NASDAQ Capital Market under the ticker symbol BDCO. Our website address is http://www.blue-dolphin.com.

Certain terms that are commonly used in the oil and gas industry, including terms that define our rights and obligations with respect to our properties, are defined in the Glossary of Certain Oil and Gas Terms of this Form 10-K.

Recent Developments

The Blue Dolphin Pipeline System (BDPS) is currently transporting an aggregate of approximately 18 MMcf of gas per day from ten shippers and the GA 350 Pipeline is currently transporting an aggregate of approximately 22 MMcf of gas per day from six shippers. Annual revenues from pipeline operations were $2,448,831 in 2008. Throughput on the Blue Dolphin System and the GA 350 Pipeline increased during 2008 due to increases in production from three shippers that commenced deliveries in the second half of 2007, including delivery of production from one shipper on the Blue Dolphin System and two shippers on the GA 350 Pipeline.

In our oil and gas exploration and production segment, production from the High Island Block 37 A-2 well was restarted in December 2007 after experiencing production problems in April 2007. The well was shut-in for approximately eight months. Production from High Island Block 37 averaged approximately 1.7 MMcf of gas per day in 2008 as compared to approximately 5.4 MMcf of gas per day in 2007. We recognized net oil and gas sales revenues of approximately $246,000 in 2008 associated with our approximate 2.8% working interest in High Island Block 37. The B-1 well experienced production problems in January 2008 and is currently shut-in. The A-2 well resumed production in the first quarter of 2009 after being shut-in due to damage to third party onshore facilities resulting from Hurricane Ike in September 2008. We believe the A-2 well could continue to produce until early 2011, however, the well could deplete faster than currently projected or could develop production problems resulting in the cessation of production.

One well in High Island Block 115 commenced production in late November 2007. We had previously earned a 2.5% working interest in this well, which was drilled successfully in the second quarter 2007. We recognized net oil and gas sales revenues of approximately $294,000 from this well in 2008. The well resumed production in the first quarter of 2009, after being shut-in due to damage to third party onshore facilities resulting from Hurricane Ike in September 2008.

In December 2008, an exploratory well was drilled in Galveston Area Block 321 near our Blue Dolphin Pipeline System. We elected not to participate in this well; however, we maintained a 0.5% overriding royalty interest in the well. In January 2009, it was concluded the well was economically successful and it is expected to be connected to our system in the second quarter of 2009.

Pipeline Operations and Activities

All of our pipeline assets are held in, and operations conducted by, Blue Dolphin Pipe Line Company.

Table of Contents

The table below provides more information on our pipeline segments:

Pipeline Segment	Market	Ownership	Miles of Pipeline	Capacity (MMcf/d)	Storage (Bbls)[1]	Average Throughput (MMcf/d)		
						2008	2007	2006
BDPS	Gulf of Mexico	83.3%	34	160	85,000	22.6	22.3	17.3
GA 350	Gulf of Mexico	83.3%	13	65		23.8	22.6	9.1
Omega[2]	Gulf of Mexico	83.3%	18	110				

(1) Storage facility connected in Freeport, Texas.

(2) Inactive.

The economic return on our pipeline system investments and the fees chargeable for the services provided are dependent upon the amounts of gas and condensate gathered and transported. Currently, the level of throughput on our pipeline systems is significantly below maximum capacity. Competition for provision of gathering and transportation services similar to ours is intense in the market areas we serve. See Competition for additional information. Since contracts for gathering and transportation services with third party producer/shippers may be for specified time periods, there can be no assurance that current or future producer/shippers will not subsequently tie-in to alternative transportation systems or that current rates charged will be maintained in the future. We actively market our gathering and transportation services to producer/shippers operating in the vicinity of our pipeline systems. Future utilization of the pipelines and related facilities will depend upon the success of drilling programs around the pipelines, and the attraction, and retention, of producer/shippers to the systems.

Blue Dolphin Pipeline System The Blue Dolphin Pipeline System (the Blue Dolphin System) includes: the Blue Dolphin Pipeline, an offshore platform, the Buccaneer Pipeline, onshore facilities for condensate and gas separation and dehydration, 85,000 Bbls of above-ground tankage for storage of crude oil and condensate, a barge loading terminal on the Intracoastal Waterway and 360 acres of land in Brazoria County, Texas where the Blue Dolphin Pipeline comes ashore and where the pipeline system s onshore facilities, pipeline easements and rights-of-way are located. We own an 83% undivided interest in the Blue Dolphin System. The Blue Dolphin System gathers and transports gas and condensate from various offshore fields in the Galveston Area of the Gulf of Mexico to our onshore facilities located in Freeport, Texas. After processing, the gas is transported to an end user and a major intrastate pipeline system with further downstream tie-ins to other intrastate and interstate pipeline systems and end users.

The Blue Dolphin Pipeline consists of two segments, an offshore segment and an onshore segment. The offshore segment transports both gas and condensate and is comprised of approximately 34 miles of 20-inch pipeline originating at an offshore platform in Galveston Area Block 288 and running to shore. The offshore segment also includes the platform in Galveston Area Block 288 and 5 field gathering lines totaling approximately 27 miles connected to the main 20-inch line. An additional 2 miles of 20-inch pipeline onshore connects the offshore segment to the onshore facility at Freeport, Texas. The onshore segment also includes approximately 2 miles of 16-inch pipeline for transportation of gas from the onshore facility to a sales point at a chemical plant complex and intrastate pipeline system tie-in in Freeport, Texas. The Buccaneer Pipeline, an approximate 2 mile, 8-inch liquids pipeline, transports condensate from the onshore facility storage tanks to our barge-loading terminal on the Intracoastal Waterway near Freeport, Texas for sale to third parties.

Table of Contents

Various fees are charged to producer/shippers for provision of transportation and onshore facility services. The Blue Dolphin Pipeline has an aggregate capacity of approximately 160 MMcf of gas and 7,000 Bbls of crude oil and condensate per day. Unless otherwise stated, all gas and liquids volumes transported are attributable to production from third party producer/shippers.

Galveston Area Block 350 Pipeline We own an 83% undivided interest in the Galveston Area Block 350 Pipeline (the GA 350 Pipeline). The GA 350 Pipeline is an 8-inch, 13 mile offshore pipeline extending from Galveston Area Block 350 to an interconnect with a transmission pipeline in Galveston Area Block 391 located approximately 14 miles south of the Blue Dolphin Pipeline. Current system capacity on the GA 350 Pipeline is 65 MMcf of gas per day. Unless otherwise stated, all gas and liquids volumes transported are attributable to production from third party producer/shippers.

Other We also own an 83% undivided interest in a third offshore pipeline, the Omega Pipeline, which is currently inactive. The Omega Pipeline originates in the High Island Area, East Addition Block A-173 and extends to West Cameron Block 342, where it was previously connected to the High Island Offshore System. Reactivation of the Omega Pipeline will be dependent upon future drilling activity in the vicinity and successfully attracting producer/shippers to the system.

Oil and Gas Exploration and Production Activities

Although we sold substantially all of our producing oil and gas properties in 2002, we continue our oil and gas exploration and production activities, which include the exploration, acquisition, development, operation and, when appropriate, disposition of oil and gas properties. We focus our oil and gas activities in the western Gulf of Mexico off the Texas coast. We currently own seismic and other data that may be used to evaluate and develop prospects, including a non-exclusive license to approximately 200 blocks of 3-D seismic data covering 1,152,000 acres in the western Gulf of Mexico and a substantial inventory of close grid 2-D seismic data. Our oil and gas assets are held by Blue Dolphin Petroleum Company.

The leasehold interests we hold in properties are subject to royalty, overriding royalty and interests of others.

Oil and Gas Exploration and Production Assets and Activities. Following is a description of our oil and gas exploration and production assets and activities:

Galveston Area Block 321 Galveston Area Block 321 is located approximately 32 miles southeast of Galveston in an average water depth of approximately 66 feet. In December 2008, drilling of an exploratory well in Galveston Area Block 321 was commenced near our Blue Dolphin Pipeline System. We elected not to participate in this well. However, we maintained a 0.5% overriding royalty interest in the well. In January 2009, it was concluded that the well was successful and will be connected to our Blue Dolphin Pipeline System in second quarter 2009.

High Island Block 115 High Island Block 115 is located approximately 30 miles southeast of Bolivar Peninsula in an average water depth of approximately 38 feet. We own a 2.5% working interest in a single production zone in one well in this block. Production commenced in late November 2007. The well is currently producing. However, it was down for over four months due to damage to third party onshore facilities resulting from Hurricane Ike in September 2008.

High Island Block 37 High Island Block 37 is located approximately 15 miles south of Sabine Pass, offshore Texas, in an average water depth of approximately 36 feet. We own an approximate 2.8% working interest in this lease that covers 5,760 acres. The lease is operated by Seneca Resources Corporation and contains two wells. The A-2 well resumed production in the first quarter of 2009 after being shut-in due to damage to third party onshore facilities resulting from Hurricane Ike in

Table of Contents

September 2008. In early 2008, we elected to participate in an exploratory well for a 2.8% working interest. Drilling of the exploratory B-2 well commenced in mid-April 2008. The B-2 well was determined to be non-commercial and was plugged and abandoned in the third quarter of 2008.

See Note (8), Business Segment Information, in Item 8 Notes to Consolidated Financial Statements for additional information on revenues, operating income (loss), assets and depreciation, depletion and amortization on our business segments.

Proved Oil and Gas Reserves. We have prepared estimates of proved reserves, and discounted present value of future net revenues to our net interest as of December 31, 2008.

The quantities of proved oil and gas reserves presented below include only those amounts which we reasonably expect to recover in the future from known oil and gas reservoirs under existing economic and operating conditions. Therefore, proved reserves are limited to those quantities that are believed to be recoverable at prices and costs, and under regulatory practices and technology existing at the time of the estimate. Accordingly, changes in oil and gas prices, operation and development costs, regulations, technology, future production and other factors, many of which are beyond our control, could significantly affect the estimates of proved reserves and the discounted present value of future net revenues attributable thereto.

Estimates of production and future net revenues cannot be expected to represent accurately the actual production or revenues that may be recognized with respect to oil and gas properties or the actual present market value of such properties. See Note (9), Supplemental Oil and Gas Information, in Item 8 Notes to Consolidated Financial Statements for further information concerning our proved reserves, changes in proved reserves, estimated future net revenues and costs incurred in our oil and gas activities and the discounted present value of estimated future net revenues from our proved reserves.

The following table presents the estimates of proved reserves, proved developed reserves (as hereinafter defined) and the discounted present value of future net revenues or expenses from proved reserves after income taxes (in thousands) to our net interest in oil and gas properties as of December 31, 2008. The discounted present value of future net revenues or expenses is calculated using the SEC Method (defined below) and is not intended to represent the current market value of the oil and gas reserves we own.

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Table of Contents

Proved Reserves
As of December 31, 2008[1] [2]

	Net Oil Reserves (Mbbls)	Net Gas Reserves (MMcf)	Present Value of Future Net Cash Inflows (Outflows) [1] (in thousands)
Proved Reserves			
Galveston Area Block 321	0.3	14	81
High Island Block 115	0.4	129	383
High Island Block 37	0.1	15	46
Total Proved Reserves	0.8	158	$ 510
Proved Developed			
Galveston Area Block 321	0.3	14	81
High Island Block 115	0.4	129	383
High Island Block 37	0.1	15	46
Total Proved Developed	0.8	158	$ 510

(1) The estimated present value of future net cash outflows from our proved reserves has been determined by using prices of $44.60 per barrel of oil and $5.26 per Mcf of gas, representing the December 31, 2008 prices for oil and gas and discounted at a 10% annual rate in accordance with

requirements for reporting oil and gas reserves pursuant to regulations promulgated by the Securities and Exchange Commission (the SEC Method).

(2) As of December 31, 2008, we reported no proved undeveloped reserves.

Capital Expenditures for Proved Reserves. The following table presents information regarding the costs we expect to incur in activities associated with our proved reserves. These expenditures represent costs associated with the plugging and abandonment of wells. The information regarding proved reserves summarized in the preceding table assumes the following estimated undiscounted capital expenditures in the years indicated (in thousands).

Estimated Undiscounted Capital Expenditures
Associated with Plugging and Abandonment of Wells

	Years Ending December 31,				
	2009	2010	2011	2012	2013
Galveston Area Block 321					
High Island Block A-7		265			
High Island Block 37		73			
High Island Block 115			39		

8

Table of Contents

Production, Price and Cost Data. The following table presents information regarding production volumes and revenues, average sales prices and costs (after deduction of royalties and interests of others) with respect to crude oil, condensate, and gas attributable to our interest for each of the periods indicated.

Net Production, Price and Cost Data

	Years Ended December 31,		
	2008	2007	2006
Gas:			
Production (Mcf)	44,700	72,788	312,146
Revenue	$526,522	$476,224	$2,131,415
Average production per day (Mcf) (*)	122.5	199.4	772.3
Average sales price per Mcf	$ 11.78	$ 6.54	$ 6.83
Condensate:			
Production (Bbls)	117	177	1,823
Revenue	$ 14,057	$ 10,345	$ 114,114
Average production per day (Bbls) (*)	0.3	0.5	5.0
Average sales price per Bbl	$ 120.25	$ 58.45	$ 62.60
NGLs:			
Production (gallons)		36,372	137,139
Revenue	$	$ 30,842	$ 113,285
Average production per day (gallons) (*)		99.7	375.7
Average sales price per gallon	$	$ 0.85	$ 0.83
Production costs (**):			
Per Mcfe:	$ 5.36	$ 3.04	$ 1.34

(*) Average production is based on a 365 day year.

(**) Production costs, exclusive of work-over costs, are costs incurred to operate and maintain wells and equipment and to pay production taxes.

2008 Drilling Activity. In early 2008, we elected to participate in an exploratory well for a 2.8% working interest. Drilling of the exploratory B-2 well commenced in mid-April 2008. The B-2 well was determined to be non-commercial and was plugged and abandoned in the third quarter of 2008.

	Net Exploratory(1)	
	2008	2007
Wells Drilled		

Gulf of Mexico Productive		
Dry	1	
	1	

(1) Gross interest reflects the total wells we participated in, regardless of our ownership interest.

Table of Contents

Customers

We generated revenues from both of our business segments. Arena Offshore, W&T Offshore, Gryphon Exploration Co., and Apex Oil & Gas accounted for approximately 17%, 16%, 12%, and 11%, respectively, of our revenues in 2008. Revenues from customers exceeding 10% of revenues were as follows for 2008 and 2007:

	Oil and Gas Sales	Pipeline Operations	Total
Year Ended December 31, 2008:			
Arena Offshore	$	$513,634	$513,634
W&T Offshore	$	$488,083	$488,083
Gryphon Exploration Co.	$	$367,153	$367,153
Apex Oil & Gas	$	$338,836	$338,836
Year Ended December 31, 2007:			
Apex Oil & Gas	$	$809,420	$809,420
W&T Offshore	$	$519,866	$519,866
Gryphon Exploration Co.	$	$341,406	$341,406

Markets & Competition

The availability of a ready market for oil and natural gas, and the prices of oil and natural gas, depends upon a number of factors which are beyond our control. These include, among other things:

- the level of domestic production;
- actions taken by foreign oil and gas producing nations;
- the availability of pipelines with adequate capacity;
- the availability of vessels for direct shipment;
- lightering, transshipment and other means of transportation;
- the availability and marketing of other competitive fuels;
- fluctuating and seasonal demand for oil, natural gas and refined products; and
- the extent of governmental regulation and taxation (under both present and future legislation) of the production, importation, refining, transportation, pricing, use and allocation of oil, gas, refined products and alternative fuels.

In view of the many uncertainties affecting the supply and demand for crude oil, condensate, natural gas and refined petroleum products, it is not possible to predict accurately the prices or marketability of the oil and natural gas produced for sale or prices chargeable for transportation and storage services, which we provide. Our sale of natural gas is generally made at the market prices at the time of sale. Therefore, even though we sell natural gas to major purchasers, we believe other purchasers would be willing to buy our natural gas at comparable market prices. Vigorous competition occurs among oil, gas and other energy sources, and between producers, transporters, and distributors of oil and gas. Our pipeline business faces competition from other pipelines in the markets that we serve. The principal elements of competition among pipelines are rates, terms of service, access to markets, flexibility and reliability of service. Our oil and natural gas business competes for the acquisition of oil and natural gas properties with numerous entities, including major oil companies, independent oil and natural gas concerns and individual producers and operators, primarily on the basis of the price to be paid for such properties. Many of these competitors

are large, well-established companies that have financial and other resources that are substantially greater than ours, which give them an

Table of Contents

advantage over us in evaluating and obtaining properties and prospects. Our ability to acquire additional pipelines and oil and natural gas properties and to discover reserves in the future will depend upon our ability to evaluate and select suitable properties and consummate transactions in a highly competitive environment. There is also competition for the hiring of experienced personnel to manage and operate our assets. Several highly competitive alternative transportation and delivery options exist for current and potential customers of our traditional gas and oil gathering and transportation business. Competition also exists with other industries in supplying the energy and fuel needs of consumers.

Governmental Regulation

The production, processing, marketing, and transportation of oil and gas by us are subject to federal, state and local regulations which can have a significant impact upon our overall operations.

Federal Regulation of Natural Gas Transportation. The transportation and resale of gas in interstate commerce have been regulated by the Natural Gas Act (NGA), the Natural Gas Policy Act (NGPA), and the rules and regulations promulgated by the Federal Energy Regulatory Commission (FERC). In the past, the federal government has regulated the prices at which gas could be sold. In 1989, Congress enacted the Natural Gas Wellhead Decontrol Act, which removed all remaining Natural Gas Act and Natural Gas Policy Act price and non-price controls affecting producer sales of gas, effective January 1, 1993. The Energy Policy Act of 2005 did not alter our non-FERC-jurisdictional status, but has greatly expanded FERC s authority, including enforcement authority against market manipulation in connection with FERC-jurisdictional transactions. FERC has undertaken vigorous enforcement actions against a number of entities, including those not subject to direct FERC regulation, and, to increase transparency in natural gas markets, has taken steps to require reporting by interstate, major non-interstate and potentially certain intrastate pipelines. Additionally, energy pricing has attracted renewed political interest. Thus Congress could reenact regulatory controls in the future. The rates, terms and conditions applicable to interstate transportation of gas by pipelines are regulated by the FERC under the NGA, as well as under Section 311 of the NGPA. In February 2007, FERC issued a policy order acknowledging its lack of jurisdiction over offshore gathering, but stating that FERC would intervene in the event that interstate pipelines with affiliated offshore gathering lines engage in anticompetitive behavior, such conditioning access to interstate pipeline service upon use of the affiliated gathering line.

All of our pipelines located offshore in federal waters are subject to the requirements of the Outer Continental Shelf Lands Act (OCSLA). The FERC has stated that non-jurisdictional gathering lines, as well as interstate pipelines, are fully subject to the open access and nondiscrimination requirements of OCSLA s Section 5, which generally authorizes the FERC to insure that gas pipelines on the Outer Continental Shelf (OCS) will transport for non-owner shippers in a nondiscriminatory manner and will be operated in accordance with certain pro-competitive principles. Since all of our offshore pipelines fall within the exemption for feeder facilities and already operate on the basis required under OCSLA, we do not anticipate significant changes directly resulting from requirements concerning nondiscriminatory open access transportation.

Aside from the OCSLA requirements and federal safety and operational regulations, regulation of gas gathering activities is primarily a matter of state oversight. Regulation of gathering activities in Texas includes various transportation, safety, environmental and non-discriminatory purchase/transport requirements.

Federal Regulation of Oil Pipelines. Our operation of the Buccaneer Pipeline has been subject to a variety of regulations promulgated by the FERC and imposed on all oil pipelines pursuant to federal law. Recently, however, oil pipelines have been granted permanent exemptions from certain FERC filing requirements because of rulings that oil pipeline transportation tariff movements of crude petroleum occurring solely on or across the OCS, or across the OCS to onshore points where transportation ends are not subject to FERC jurisdiction under the OCSLA or the Interstate Commerce Act.

Table of Contents

Safety and Operational Regulations. Our operations are generally subject to safety and operational regulations administered primarily by the United States Minerals Management Service (MMS), the U.S. Department of Transportation, the U.S. Coast Guard, the FERC and/or various state agencies. In addition, the OCSLA authorizes regulations relating to safety and environmental protection applicable to leases and permittees operating on the OCS. Specific design and operational standards may apply to OCS vessels, rigs, platforms and structures. Violations of lease conditions or regulations issued pursuant to the OCSLA can result in substantial civil and criminal penalties, as well as potential court injunctions curtailing operations and the cancellation of leases. Such enforcement liabilities can result from either governmental or private prosecution. Currently, we believe that we are in material compliance with the various safety and operational regulations that we are subject to. However, as safety and operational regulations are frequently changed, we are unable to predict the future effect changes in these regulations will have on our operations, if any.

Federal Oil and Gas Leases. All of our exploration and production operations are currently located on federal oil and gas leases in the OCS, which are administered by the MMS. Such leases are issued through competitive bidding, contain relatively standardized terms and require compliance with detailed MMS regulations and orders pursuant to the OCSLA that are subject to interpretation and change by the MMS. For offshore operations, lessees must obtain MMS approval for exploration plans and development and production plans prior to the commencement of such operations. In addition to permits required from other agencies such as the Coast Guard, the Army Corps of Engineers and the Environmental Protection Agency, lessees must obtain a permit from the MMS prior to the commencement of drilling. The MMS has promulgated regulations requiring offshore production facilities located on the OCS to meet stringent engineering and construction specifications. To cover the various obligations of lessees on the OCS, the MMS generally requires that lessees have substantial net worth or post bonds or other acceptable assurance that such obligations will be met. The cost of these bonds or other surety can be substantial, and there is no assurance that bonds or other surety can be obtained in all cases. We are currently in compliance with the bonding requirements of the MMS. Under some circumstances, the MMS may require any of our operations on federal leases to be suspended or terminated. Any such suspension or termination could materially adversely affect our financial condition and results of operations.

With respect to our operations conducted on offshore federal leases, liability may generally be imposed under OCSLA for costs of clean-up and damages caused by pollution resulting from such operations, other than damages caused by acts of war or the negligence of third parties. Under certain circumstances, including but not limited to conditions deemed a threat or harm to the environment, the MMS may also require any of our operations on federal leases to be suspended or terminated in the affected area. Furthermore, the MMS generally requires that offshore facilities be dismantled and removed within one year after production ceases or the lease expires.

Environmental Regulation. Our activities with respect to (1) exploration, development and production of oil and natural gas and (2) the operation and construction of pipelines, plants, and other facilities for the transportation and processing, and storage of oil and natural gas are subject to stringent environmental regulation by local, state and federal authorities, including the U.S. Environmental Protection Agency (EPA). Such regulation has increased the cost of planning, designing, drilling, operating and in some instances, abandoning wells and related equipment. Similarly, such regulation has also increased the cost of design, construction, and operation of crude oil and natural gas pipelines and processing facilities. Although we believe that compliance with existing environmental regulations will not have a material adverse effect on operations or earnings, there can be no assurance that significant costs and liabilities, including civil and criminal penalties, will not be incurred. Moreover, future developments, such as stricter environmental laws and regulations or claims for personal injury or property damage resulting from our operations, could result in substantial costs and liabilities. It is not anticipated that, in response to such regulation, we will be required in the near future to expend amounts that are material relative to our total capital structure.

Table of Contents

The Comprehensive Environmental Response, Compensation and Liability Act (CERCLA) imposes liability, without regard to fault or the legality of the original conduct, on responsible parties with respect to the release or threatened release of a hazardous substance into the environment. Responsible parties, which include the present owner or operator of a site where the release occurred, the owner or operator of the site at the time of disposal of the hazardous substance, and persons that disposed or arranged for the disposal of a hazardous substance at the site, are liable for response and remediation costs and for damages to natural resources. Petroleum and natural gas are excluded from the definition of hazardous substances ; however, this exclusion does not apply to all materials used in our operations. At this time, neither we nor any of our predecessors have been designated as a potentially responsible party under CERCLA.

The federal Resource Conservation and Recovery Act (RCRA) and its state counterparts regulate solid and hazardous wastes and impose civil and criminal penalties for improper handling and disposal of such wastes. EPA and various state agencies have promulgated regulations that limit the disposal options for such wastes. Certain wastes generated by our oil and gas operations are currently exempt from regulation as hazardous wastes, but in the future could be designated as hazardous wastes under RCRA or other applicable statutes and therefore may become subject to more rigorous and costly requirements.

We currently own or lease, or have in the past owned or leased, various properties used for the exploration and production of oil and gas or used to store and maintain equipment regularly used in these operations. Although our past operating and disposal practices at these properties were standard for the industry at the time, hydrocarbons or other substances may have been disposed of or released on or under these properties or on or under other locations. In addition, many of these properties have been operated by third parties whose waste handling activities were not under our control. These properties and any waste disposed thereon may be subject to CERCLA, RCRA, and state laws which could require us to remove or remediate wastes and other contamination or to perform remedial plugging operations to prevent future contamination.

The Oil Pollution Act of 1990 (OPA) and regulations promulgated thereunder include a variety of requirements related to the prevention of oil spills and impose liability for damages resulting from such spills. OPA imposes liability on owners and operators of onshore and offshore facilities and pipelines for removal costs and certain public and private damages arising from a spill. OPA establishes a liability limit for onshore facilities of $350 million and for offshore facilities of all removal costs plus $75 million, and lesser liability limits for vessels depending upon their size. A party cannot take advantage of the liability limits if the spill is caused by gross negligence or willful misconduct or resulted from a violation of federal safety, construction, or operating regulations. If a party fails to report a spill or cooperate in the cleanup, liability limits likewise do not apply. OPA imposes ongoing requirements on responsible parties, including proof of financial responsibility for potential spills. The amount of financial responsibility required depends upon a variety of factors including the type of facility or vessel, its size, storage capacity, oil throughput, proximity to sensitive areas, type of oil handled, history of discharges, worst-case spill potential and other factors. We believe we have established adequate financial responsibility. While the financial responsibility requirements under OPA may be amended to impose additional costs on us, the impact of such a change is not expected to be any more burdensome on us than on others similarly situated.

The Clean Air Act and state air quality laws and regulations contain provisions that impose pollution control requirements on emissions to the air and require permits for construction and operation of certain emissions sources, including sources located offshore. We may be required to incur capital expenditures for air pollution control equipment in connection with maintaining or obtaining operating permits and approvals addressing emission-related issues, although we do not expect to be materially adversely affected by such expenditures.

Table of Contents

The Clean Water Act (CWA) regulates the discharge of pollutants to waters of the United States and imposes permit requirements on such discharges, including discharges to wetlands. Federal regulations under the CWA and OPA require certain owners or operators of facilities that store or otherwise handle oil, to prepare and implement spill prevention, control and countermeasure plans and facility response plans relating to the possible discharge of oil into surface waters. With respect to certain of our operations, we are required to prepare and comply with such plans and to obtain and comply with permits. The CWA also prohibits spills of oil and hazardous substances to waters of the United States in excess of levels set by regulations and imposes liability in the event of a spill. State laws further provide varying civil and criminal penalties and liabilities for the spills to both surface and ground waters. We believe we are in substantial compliance with the requirements of the CWA, OPA, and state laws, and that any non-compliance would not have a material adverse effect on us.

Various federal and state programs regulate the conservation and development of coastal resources. The federal Coastal Zone Management Act was passed to preserve and, where possible, restore the natural resources of the coastal zone of the United States of America and to provide for federal grants for state management programs that regulate land use, water use and coastal development. Under the Louisiana Coastal Zone Management Program, coastal use permits are required for certain activities, even if the activity only partially infringes on the coastal zone. Among other things, projects involving use of state lands and water bottoms, dredge or fill activities that intersect with more than one body of water, mineral activities, including the exploration and production of oil and gas, and pipelines for the gathering, transportation or transmission of oil, gas and other minerals require such permits. General permits, which entail a reduced administrative burden, are available for a number of routine oil and gas activities. The Texas Coastal Coordination Act (CCA) establishes the Texas Coastal Management Program that applies in the nineteen Texas counties that border the Gulf of Mexico and its tidal bays. The CCA provides for the review of state and federal agency rules and agency actions for consistency with the goals and policies of the Coastal Management Plan. These coastal programs may affect agency permitting of our facilities.

Legislation and Rulemaking. In October 1996, the U.S. Congress enacted the Coast Guard Authorization Act of 1996 (P.L. 104-324) which amended the OPA to establish requirements for evidence of financial responsibility for certain offshore facilities. The amount required is $35 million for certain types of offshore facilities located seaward of the seaward boundary of a state, including properties used for oil transportation. We currently maintain this statutory $35 million coverage.

Federal and state legislative rules and regulations are pending that, if enacted, could significantly affect the oil and gas industry. It is impossible to predict which of those federal and state proposals and rules, if any, will be adopted and what effect, if any, they would have on our operations.

In addition, various federal, state and local laws and regulations covering the discharge of materials into the environment, occupational health and safety issues, or otherwise relating to the protection of public health and the environment, may affect our operations, expenses and costs. The trend in such regulation has been to place more restrictions and limitations on activities that may impact the general or work environment, such as emissions of pollutants, generation and disposal of wastes, and use and handling of chemical substances. It is not anticipated that, in response to such regulation, we will be required in the near future to expend amounts that are material relative to our total capital structure. However, it is possible that the costs of compliance with environmental and health and safety laws and regulations will continue to increase. Given the frequent changes made to environmental and health and safety regulations and laws, we are unable to predict the ultimate cost of compliance.

Table of Contents

Employees

We have a total of eight employees and two consultants. Our employees supervise and coordinate the operation and administration of our oil and gas properties, pipelines and other assets. From time to time, major maintenance, engineering and construction projects are contracted to third-party engineering and service companies.

Environmental

A description of our environmental activities is included in Part II, Item 8 Financial Statement & Supplementary Data.

Executive Officers of the Registrant

Our executive officers as of March 12, 2009 are listed below:

Name	Office	Officer Since	Age
Ivar Siem	Chairman of the Board and Chief Executive Officer	1989	62
Michael J. Jacobson	President	1990	62
Thomas W. Heath	Executive Vice President and Secretary	2007	46
T. Scott Howard	Accounting Manager, Treasurer and Assistant Secretary	2006	37

Ivar Siem has served as Chairman of the Board of Directors of the Company since 1989 and was appointed as Chief Executive Officer in 2004. Since 2000 he has also served as Chairman of the Board of Directors and President of Drillmar, Inc., a well construction and intervention company. From 1995 to 2000 Mr. Siem served on the Board of Directors of Grey Wolf, Inc., during which time he served as Chairman from 1995 to 1998 and as interim President in 1995 during its restructuring. Since 1981, he has been an international consultant in energy, technology and finance. From 1974 to 1981, Mr. Siem managed the oil and gas interests of Fred. Olsen and from 1977 he managed their drilling operation, Dolphin International, Inc. Mr. Siem holds a Bachelor of Science in Mechanical Engineering from the University of California, Berkeley, and has completed an executive MBA program at Amos Tuck School of Business, Dartmouth University.

Michael J. Jacobson has served as President of the Company since 1990 having also served in dual capacities as Chief Executive Officer from 1990 to 2004 and as Secretary from 2005 to 2006 and again in 2008. Mr. Jacobson also served as Treasurer in 2008. Prior to joining the Company, Mr. Jacobson served in various senior management positions in the energy industry, including Senior Vice President and Chief Financial and Administrative Officer for Creole International, Inc. and its subsidiaries, international providers of engineering and technical services to the energy sector, Vice President of Operations for the parent holding company, and Vice President and Chief Financial Officer of Volvo Petroleum, Inc. and certain Fred. Olsen oil and gas interests. Mr. Jacobson began his career with Shell Oil Company in 1968, where he served in various analytical and management capacities in the exploration and production organization until 1974. Mr. Jacobson received his Bachelor of Science in Finance from the University of Colorado.

Table of Contents

Thomas W. Heath was appointed as Executive Vice President of the Company in 2007. From 2004 to 2007 he served as a Vice President of Union Bank of California, N.A., an affiliate of Bank of Tokyo-Mitsubishi UFJ, Ltd., where he developed and implemented an energy derivatives desk supporting Energy Capital Services. From 1988 to 2004 Mr. Heath held a variety of management and executive level positions with the evolving marketing units of Acadian Gas Pipeline System, Coral Energy, L.P. (formerly Shell Trading Gas & Power), Sempra Energy Trading Corp. and Tejas Gas Corporation. Mr. Heath began his career in 1983 with Columbia Gulf Transmission Company where he served in various operational and commercial positions until 1988. He is an alumnus of the University of Houston.

T. Scott Howard was appointed as Treasurer in February 2009 and Assistant Secretary of the Company in April 2008. He has served as Accounting Manager of the Company since 2006. From 1996 to 2006 he held a variety of management level positions: Audit Manager with DRDA, P.C., an independent public accounting firm in Houston, Texas from 2002 to 2006, Trust Officer with Frost National Bank in Houston, Texas from 2000 to 2002 and Controller for Hall s Insurance Agency, Inc. in Dickinson, Texas from 1996 to 2000. He began his career in 1994 as a Staff Accountant for Griffin, Iles, Masel & Duval, LLP, a public accounting firm, until 1996. Mr. Howard, who is a Certified Public Accountant in Texas, received his Bachelor of Business Administration in Accounting from St. Edward s University.

Available Information

Our website is http://www.blue-dolphin.com. We make available, free of charge on or through our website, our annual, quarterly and current reports, and any amendments to those reports, as soon as is reasonably possible after these reports are filed with the SEC. Information about each of our Board members, as well as each of our Board s standing committee charters, our Corporate Governance Guidelines and our Code of Business Conduct are also available, free of charge, through our website. Information contained on our website is not part of this report.

GLOSSARY OF CERTAIN OIL AND GAS TERMS

The following are abbreviations and definitions of certain terms commonly used in the oil and gas industry.

Back-in After Payout Interest. A contractual right of a non-participating partner to participate in a well or wells after the wells have produced enough for the participating partners to recover their capital costs of drilling, completing, and operating the wells.

Bbl. One stock tank barrel, or 42 U.S. gallons of liquid volume, used in reference to oil or other liquid hydrocarbons.

Bcf. One billion cubic feet of gas.

Btu or British Thermal Unit. The quantity of heat required to raise the temperature of one pound of water by one degree Fahrenheit.

Condensate. Liquid hydrocarbons associated with the production of a primarily gas reserve.

Development Well. A well drilled within the proved area of a gas or oil reservoir to the depth of a stratigraphic horizon known to be productive.

Exploratory Well. A well drilled to find and produce gas or oil in an unproved area, to find a new reservoir in a field previously found to be productive of gas or oil in another reservoir or to extend a known reservoir.