

VALERO ENERGY CORP/TX
Form 10-Q
May 09, 2006
Table of Contents

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

(Mark One)

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

For the quarterly period ended March 31, 2006

OR

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 1-13175

VALERO ENERGY CORPORATION

(Exact name of registrant as specified in its charter)

Delaware
(State or other jurisdiction of
incorporation or organization)

One Valero Way
San Antonio, Texas

74-1828067
(I.R.S. Employer
Identification No.)

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(Address of principal executive offices)

78249

(Zip Code)

(210) 345-2000

(Registrant's telephone number, including area code)

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes No

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

Large accelerated filer

Accelerated filer

Non-accelerated filer

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

The number of shares of the registrant's only class of common stock, \$0.01 par value, outstanding as of April 30, 2006 was 615,453,161.

Table of Contents

VALERO ENERGY CORPORATION AND SUBSIDIARIES

INDEX

| | Page |
|---|-------------|
| PART I - FINANCIAL INFORMATION | |
| Item 1. Financial Statements | |
| <u>Consolidated Balance Sheets as of March 31, 2006 and December 31, 2005</u> | 3 |
| <u>Consolidated Statements of Income for the Three Months Ended March 31, 2006 and 2005</u> | 4 |
| <u>Consolidated Statements of Cash Flows for the Three Months Ended March 31, 2006 and 2005</u> | 5 |
| <u>Consolidated Statements of Comprehensive Income for the Three Months Ended March 31, 2006 and 2005</u> | 6 |
| <u>Condensed Notes to Consolidated Financial Statements</u> | 7 |
| <u>Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations</u> | 28 |
| <u>Item 3. Quantitative and Qualitative Disclosures About Market Risk</u> | 41 |
| <u>Item 4. Controls and Procedures</u> | 45 |
| <u>PART II - OTHER INFORMATION</u> | |
| <u>Item 1. Legal Proceedings</u> | 45 |
| <u>Item 2. Unregistered Sales of Equity Securities and Use of Proceeds</u> | 46 |
| <u>Item 6. Exhibits</u> | 47 |
| <u>SIGNATURE</u> | 48 |

Table of Contents**PART I - FINANCIAL INFORMATION****Item 1. Financial Statements****VALERO ENERGY CORPORATION AND SUBSIDIARIES****CONSOLIDATED BALANCE SHEETS**

(Millions of Dollars, Except Par Value)

| | March 31, 2006 (Unaudited) | December 31, 2005 |
|---|----------------------------------|----------------------|
| ASSETS | | |
| Current assets: | | |
| Cash and temporary cash investments | \$ 436 | \$ 436 |
| Restricted cash | 30 | 30 |
| Receivables, net | 3,115 | 3,564 |
| Inventories | 4,381 | 4,039 |
| Deferred income taxes | 145 | 142 |
| Prepaid expenses and other | 74 | 65 |
| Total current assets | 8,181 | 8,276 |
| Property, plant and equipment, at cost | 21,131 | 20,388 |
| Accumulated depreciation | (2,707) | (2,532) |
| Property, plant and equipment, net | 18,424 | 17,856 |
| Intangible assets, net | 289 | 298 |
| Goodwill | 4,924 | 4,926 |
| Investment in Valero L.P. | 326 | 327 |
| Deferred charges and other assets, net | 1,159 | 1,045 |
| Total assets | \$ 33,303 | \$ 32,728 |
| LIABILITIES AND STOCKHOLDERS EQUITY | | |
| Current liabilities: | | |
| Current portion of long-term debt and capital lease obligations | \$ 3 | \$ 222 |
| Accounts payable | 6,167 | 5,563 |
| Accrued expenses | 394 | 581 |
| Taxes other than income taxes | 487 | 595 |
| Income taxes payable | 117 | 39 |
| Deferred income taxes | 276 | 305 |
| Total current liabilities | 7,444 | 7,305 |
| Long-term debt, less current portion | 5,089 | 5,109 |
| Capital lease obligations, less current portion | 46 | 47 |
| Deferred income taxes | 3,756 | 3,615 |

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| | | |
|--|------------------|------------------|
| Other long-term liabilities | 1,570 | 1,602 |
| Commitments and contingencies (Note 15) | | |
| Stockholders' equity: | | |
| Preferred stock, \$0.01 par value; 20,000,000 shares authorized; 2,451,116 and 3,164,151 shares issued and outstanding | 53 | 68 |
| Common stock, \$0.01 par value; 1,200,000,000 shares authorized; 622,643,499 and 621,230,266 shares issued | 6 | 6 |
| Additional paid-in capital | 7,952 | 8,164 |
| Treasury stock, at cost; 7,502,147 and 3,807,976 common shares | (420) | (196) |
| Retained earnings | 7,484 | 6,673 |
| Accumulated other comprehensive income | 323 | 335 |
| Total stockholders' equity | 15,398 | 15,050 |
| Total liabilities and stockholders' equity | \$ 33,303 | \$ 32,728 |

See Condensed Notes to Consolidated Financial Statements.

Table of Contents**VALERO ENERGY CORPORATION AND SUBSIDIARIES****CONSOLIDATED STATEMENTS OF INCOME****(Millions of Dollars, Except per Share Amounts and Supplemental Information)****(Unaudited)**

| | Three Months Ended March 31, | |
|---|-------------------------------------|-------------|
| | 2006 | 2005 |
| Operating revenues (1) (2) | \$ 20,941 | \$ 14,953 |
| Costs and expenses: | | |
| Cost of sales (1) | 18,082 | 13,072 |
| Refining operating expenses | 926 | 580 |
| Retail selling expenses | 189 | 172 |
| General and administrative expenses | 151 | 104 |
| Depreciation and amortization expense | 260 | 179 |
| Total costs and expenses | 19,608 | 14,107 |
| Operating income | 1,333 | 846 |
| Equity in earnings of Valero L.P. | 12 | 9 |
| Other expense, net | | (2) |
| Interest and debt expense: | | |
| Incurred | (96) | (74) |
| Capitalized | 37 | 11 |
| Income before income tax expense | 1,286 | 790 |
| Income tax expense | 437 | 256 |
| Net income | 849 | 534 |
| Preferred stock dividends | 1 | 4 |
| Net income applicable to common stock | \$ 848 | \$ 530 |
| Earnings per common share | \$ 1.37 | \$ 1.03 |
| Weighted-average common shares outstanding (in millions) | 619 | 512 |
| Earnings per common share assuming dilution | \$ 1.32 | \$ 0.96 |
| Weighted-average common equivalent shares outstanding (in millions) | 644 | 556 |
| Dividends per common share | \$ 0.06 | \$ 0.04 |

Supplemental information (billions of dollars):

(1) Includes the following amounts related to crude oil buy/sell arrangements
(see Note 2, EITF Issue No. 04-13):

| | | |
|--|--------|--------|
| Operating revenues | N/A | \$ 1.2 |
| Cost of sales | N/A | 1.2 |
| (2) Includes excise taxes on sales by our U.S. retail system | \$ 0.2 | 0.2 |

See Condensed Notes to Consolidated Financial Statements.

Table of Contents**VALERO ENERGY CORPORATION AND SUBSIDIARIES****CONSOLIDATED STATEMENTS OF CASH FLOWS**

(Millions of Dollars)

(Unaudited)

| | Three Months Ended March 31, | |
|---|-------------------------------------|---------------|
| | 2006 | 2005 |
| Cash flows from operating activities: | | |
| Net income | \$ 849 | \$ 534 |
| Adjustments to reconcile net income to net cash provided by operating activities: | | |
| Depreciation and amortization expense | 260 | 179 |
| Stock-based compensation expense | 23 | 14 |
| Deferred income tax expense | 120 | 102 |
| Changes in current assets and current liabilities | 537 | (14) |
| Changes in deferred charges and credits and other, net | (49) | (11) |
| Net cash provided by operating activities | 1,740 | 804 |
| Cash flows from investing activities: | | |
| Capital expenditures | (775) | (338) |
| Deferred turnaround and catalyst costs | (199) | (107) |
| Contingent payments in connection with acquisitions | (50) | (50) |
| Other investing activities, net | 11 | (34) |
| Net cash used in investing activities | (1,013) | (529) |
| Cash flows from financing activities: | | |
| Long-term debt borrowings, net of issuance costs | 31 | 35 |
| Long-term debt repayments | (251) | (313) |
| Issuance of common stock in connection with employee benefit plans | 32 | 26 |
| Benefit from tax deduction in excess of recognized stock-based compensation cost | 89 | |
| Common and preferred stock dividends | (38) | (22) |
| Purchase of treasury stock | (590) | (177) |
| Net cash used in financing activities | (727) | (451) |
| Effect of foreign exchange rate changes on cash | | (2) |
| Net increase (decrease) in cash and temporary cash investments | | (178) |
| Cash and temporary cash investments at beginning of period | 436 | 864 |
| Cash and temporary cash investments at end of period | \$ 436 | \$ 686 |

See Condensed Notes to Consolidated Financial Statements.

Table of Contents

VALERO ENERGY CORPORATION AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME

(Millions of Dollars)

(Unaudited)

| | Three Months Ended March 31, | |
|---|-------------------------------------|-------------|
| | 2006 | 2005 |
| Net income | \$ 849 | \$ 534 |
| Other comprehensive income (loss): | | |
| Foreign currency translation adjustment | (8) | (13) |
| Net gain (loss) on derivative instruments designated and qualifying as cash flow hedges: | | |
| Net gain (loss) arising during the period, net of income tax (expense) benefit of \$(1) and \$122 | 2 | (226) |
| Net (gain) loss reclassified into income, net of income tax expense (benefit) of \$3 and \$(23) | (6) | 43 |
| Net loss on cash flow hedges | (4) | (183) |
| Other comprehensive loss | (12) | (196) |
| Comprehensive income | \$ 837 | \$ 338 |

See Condensed Notes to Consolidated Financial Statements.

Table of Contents

VALERO ENERGY CORPORATION AND SUBSIDIARIES

CONDENSED NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

1. BASIS OF PRESENTATION, PRINCIPLES OF CONSOLIDATION AND SIGNIFICANT ACCOUNTING POLICIES

As used in this report, the terms Valero, we, us, or our may refer to Valero Energy Corporation, one or more of our consolidated subsidiaries, or all of them taken as a whole.

These unaudited consolidated financial statements include the accounts of Valero and subsidiaries in which Valero has a controlling interest. Intercompany balances and transactions have been eliminated in consolidation. Investments in 50% or less owned entities are accounted for using the equity method of accounting.

These unaudited consolidated financial statements have been prepared in accordance with United States generally accepted accounting principles (GAAP) for interim financial information and with the instructions to Form 10-Q and Article 10 of Regulation S-X of the Securities Exchange Act of 1934. Accordingly, they do not include all of the information and notes required by GAAP for complete consolidated financial statements. In the opinion of management, all adjustments considered necessary for a fair presentation have been included. All such adjustments are of a normal recurring nature unless disclosed otherwise. Financial information for the three months ended March 31, 2006 and 2005 included in these Condensed Notes to Consolidated Financial Statements is derived from our unaudited consolidated financial statements. Operating results for the three months ended March 31, 2006 are not necessarily indicative of the results that may be expected for the year ending December 31, 2006.

The consolidated balance sheet as of December 31, 2005 has been derived from the audited financial statements as of that date. For further information, refer to the consolidated financial statements and notes thereto included in our Annual Report on Form 10-K for the year ended December 31, 2005.

Share and per share data (except par value) presented for 2005 reflect the effect of a two-for-one stock split which was effected in the form of a common stock dividend distributed on December 15, 2005, as discussed in Note 8 under *2005 Common Stock Split*.

Table of Contents**VALERO ENERGY CORPORATION AND SUBSIDIARIES****CONDENSED NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

Certain previously reported amounts have been reclassified to conform to the 2006 presentation. These reclassifications included amounts previously reported in 2005 for refining operating expenses, retail selling expenses, general and administrative expenses, and depreciation and amortization expense which were reclassified due to the following changes that took effect on January 1, 2006: (i) information services costs that were previously allocated to the operating units are now being reported as general and administrative expenses to better reflect the area responsible for such costs and (ii) Statement No. 123R (discussed in Note 2) was implemented, which resulted in amounts previously reported as amortization expense now being reported as operating, selling or general and administrative expenses. The reclassified amounts were as follows (in millions):

| | Three Months Ended March 31, 2005 | | |
|-------------------------------------|--|--------------------------|------------------|
| | Previously | | Currently |
| | Reported | Reclassifications | Reported |
| Refining operating expenses | \$ 591 | \$ (11) | \$ 580 |
| Retail selling expenses | 175 | (3) | 172 |
| General and administrative expenses | 83 | | |