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[McDermott International Inc](#) · 10-Q · For 3/31/01

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5/15/01	McDermott International Inc	10-Q	3/31/01	2:60

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2: EX-3.2	Amended & Restated By-Laws	6	35K

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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 period ended March 31, 2001

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 No. 1-8430

McDERMOTT INTERNATIONAL, INC.

 (Exact name of registrant as specified in its charter)

REPUBLIC OF PANAMA

72-0593134

 (State or Other Jurisdiction of
 Incorporation or Organization)

(I.R.S. Employer Identification No.)

1450 Poydras Street, New Orleans, Louisiana

70112-6050

 (Address of Principal Executive Offices)

(Zip Code)

Registrant's Telephone Number, Including Area Code (504) 587-5400

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 and (2) has been subject to such filing requirements for the past 90 days.

Yes [**X**]

No []

The number of shares outstanding of the Company's Common Stock at April 30, 2001 was 61,184,820.

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McDERMOTT INTERNATIONAL, INC.

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PART I

McDERMOTT INTERNATIONAL, INC.

FINANCIAL INFORMATION

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McDERMOTT INTERNATIONAL, INC.
CONDENSED CONSOLIDATED BALANCE SHEETS

[\[Enlarge/Download Table\]](#)

<i>ASSETS</i>	<i>March 31, 2001</i>	<i>December 31, 2000</i>
	<i>(Unaudited)</i>	<i>(Unaudited)</i>
	<i>(In thousands)</i>	<i>(In thousands)</i>
Current Assets:		
Cash and cash equivalents	\$ 57,037	\$ 84,620
Investments	--	34,440
Accounts receivable - trade, net	169,434	181,422
Accounts receivable from The Babcock & Wilcox Company	28,491	30,501
Accounts receivable - unconsolidated affiliates	49,777	31,155
Accounts receivable - other	59,249	54,662
Environmental and products liabilities recoverable - current	1,264	1,527
<u>Contracts</u> in progress	94,307	90,142
Inventories	10,233	11,733
Deferred income taxes	57,502	56,805
Other current assets	18,375	28,022
	-----	-----
Total Current Assets	545,669	605,029
	-----	-----
Property, Plant and Equipment	1,238,782	1,239,554
Less accumulated depreciation	875,210	874,198
	-----	-----
Net Property, Plant and Equipment	363,572	365,356
	-----	-----
Investments:		
Government obligations	273,932	280,208
Other investments	49,045	46,547
	-----	-----
Total Investments	322,977	326,755
	-----	-----
Investment in The Babcock & Wilcox Company	186,966	186,966
	-----	-----
Goodwill less Accumulated Amortization of \$55,498,000 at <u>March 31, 2001</u> and \$50,579,000 at December 31, 2000	345,772	350,939
	-----	-----
Prepaid Pension Costs	141,487	134,307
	-----	-----
Other Assets	90,918	86,275
	-----	-----
TOTAL	\$ 1,997,361	\$ 2,055,627
	=====	=====

See accompanying notes to condensed consolidated financial statements.

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LIABILITIES AND STOCKHOLDERS' EQUITY

[\[Enlarge/Download Table\]](#)

	<i>March 31, 2001</i>	<i>December 31, 2000</i>
	-----	-----
	<i>(Unaudited)</i>	
	<i>(In thousands)</i>	
Current Liabilities:		
Notes payable and current maturities of long-term debt	\$ 47,500	\$ 96,346
Accounts payable	114,365	114,184
Accounts and notes payable to The Babcock & Wilcox Company	45,769	53,073
Environmental and products liabilities - current	4,430	6,162
Accrued employee benefits	51,914	57,578
Accrued contract costs	31,128	32,867
Advance billings on contracts	92,423	71,612
Other current liabilities	237,804	258,405
	-----	-----
Total Current Liabilities	625,333	690,227
	-----	-----
Long-Term Debt	322,207	323,157
	-----	-----
Accumulated Postretirement Benefit Obligation	28,425	28,276
	-----	-----
Environmental and Products Liabilities	10,112	10,294
	-----	-----
Other Liabilities	228,154	227,070
	-----	-----
Commitments and Contingencies		
Stockholders' Equity:		
Common stock, par value \$1.00 per share, authorized 150,000,000 shares; issued 63,053,834 at March 31, 2001 and 62,582,382 at December 31, 2000	63,054	62,582
Capital in excess of par value	1,068,047	1,062,511
Accumulated deficit	(235,335)	(230,902)
Treasury stock at cost, 2,005,042 shares at March 31, 2001 and December 31, 2000	(62,736)	(62,736)
Accumulated other comprehensive loss	(49,900)	(54,852)
	-----	-----
Total Stockholders' Equity	783,130	776,603
	-----	-----
TOTAL	\$ 1,997,361	\$ 2,055,627
	=====	=====

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McDERMOTT INTERNATIONAL, INC.
CONDENSED CONSOLIDATED STATEMENTS OF INCOME (LOSS)

[\[Download Table\]](#)

	<i>Three Months Ended</i>	
	<i>March 31,</i>	
	<i>2001</i>	<i>2000</i>
	-----	-----
	<i>(Unaudited)</i>	
	<i>(In thousands, except per share amounts)</i>	
Revenues	\$ 432,735	\$ 591,711
	-----	-----
Costs and Expenses:		
Cost of operations	388,124	514,760
Selling, general and administrative expenses	43,611	60,279
Equity in (income) loss of investees	(4,957)	6,223
	-----	-----
Total Costs and Expenses	426,778	581,262
	-----	-----
Operating Income	5,957	10,449
	-----	-----
Other Income (Expense):		
Interest income	5,848	7,145
Interest expense	(10,131)	(8,823)
Other-net	(2,172)	2,413
	-----	-----
Total Other Income (Expense)	(6,455)	735
	-----	-----
Income (Loss) before Provision for Income Taxes	(498)	11,184
Provision for Income Taxes	3,935	3,317
	-----	-----
Net Income (Loss)	\$ (4,433)	\$ 7,867
	-----	-----
Earnings (Loss) per Common Share:		
Basic	\$ (0.07)	\$ 0.13
Diluted	\$ (0.07)	\$ 0.13
	=====	=====
Cash Dividends:		
Per Common Share	\$ --	\$ 0.05
	=====	=====

See accompanying notes to condensed consolidated financial statements.

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McDERMOTT INTERNATIONAL, INC.
CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME

[\[Enlarge/Download Table\]](#)

	<i>Three Months Ended</i>	
	<i>March 31,</i>	
	<i>2001</i>	<i>2000</i>

	<i>(Unaudited)</i>	
	<i>(In thousands)</i>	

Net Income (Loss)	\$ (4,433)	\$ 7,867

Other Comprehensive Income:		
Currency translation adjustments:		
Foreign currency translation adjustments	120	2,832
Unrealized losses on derivative financial instruments	(1,200)	--
Unrealized gains (losses) on investments:		
Unrealized gains (losses) arising during the period, net of taxes		
(benefits) of \$30,000 at March 31, 2001		
and (\$8,000) at March 31, 2000	4,077	(491)
Reclassification adjustment for (gains) losses		
included in net income, net of tax benefit of		
\$162,000 at March 31, 2001	1,955	(1)

Other Comprehensive Income	4,952	2,340

Comprehensive Income	\$ 519	\$ 10,207
	=====	

See accompanying notes to condensed consolidated financial statements.

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McDERMOTT INTERNATIONAL, INC.
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS

[\[Download Table\]](#)

	<i>Three Months Ended</i>	
	<i>March 31,</i>	
	<i>2001</i>	<i>2000</i>
	-----	-----
	<i>(Unaudited)</i>	
	<i>(In thousands)</i>	
CASH FLOWS FROM OPERATING ACTIVITIES:		
Net Income (Loss)	\$ (4,433)	\$ 7,867
	-----	-----
Adjustments to reconcile net income to net cash used in operating activities:		
Depreciation and amortization	14,623	17,133
Income or loss of investees, less dividends	(3,551)	7,333
Gain on asset disposals and impairments - net	(525)	(1,059)
Provision for deferred taxes	760	8,180
Deconsolidation of the Babcock & Wilcox Company	--	(19,424)
Other	4,690	2,176
Changes in assets and liabilities, net of effects of acquisitions and divestitures:		
Accounts receivable	(12,862)	81,498
Net contracts in progress and advance billings	16,947	(41,716)
Accounts payable	(4,358)	15,618
Accrued and other current liabilities	(19,427)	(32,267)
Products and environmental liabilities	(1,651)	(6,725)
Other, net	(3,026)	(56,447)
Proceeds from insurance for products liability claims	--	26,427
Payments of products liability claims	--	(23,782)
	-----	-----
NET CASH USED IN OPERATING ACTIVITIES	(12,813)	(15,188)
	-----	-----
CASH FLOWS FROM INVESTING ACTIVITIES:		
Purchases of property, plant and equipment	(7,764)	(16,972)
Purchases of available-for-sale securities	(348,883)	(5,229)
Sales of available-for-sale securities	355,875	--
Maturities of available-for-sale securities	33,026	2,997
Proceeds from asset disposals	543	1,166
Other	(1,366)	500
	-----	-----
NET CASH PROVIDED BY (USED IN) INVESTING ACTIVITIES	31,431	(17,538)
	-----	-----

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	<i>Three Months Ended</i>	
	<i>March 31,</i>	
	<i>2001</i>	<i>2000</i>

	<i>(Unaudited)</i>	
	<i>(In thousands)</i>	
CASH FLOWS FROM FINANCING ACTIVITIES:		
Payment of long-term debt	\$ (27)	\$ (2)
Increase (decrease) in short-term borrowing	(48,838)	803
Issuance of common stock	180	--
Dividends paid	--	(2,979)
Other	3,101	10

NET CASH USED IN FINANCING ACTIVITIES	(45,584)	(2,168)

EFFECTS OF EXCHANGE RATE CHANGES ON CASH	(617)	(2,100)

NET DECREASE IN CASH AND CASH EQUIVALENTS	(27,583)	(36,994)
CASH AND CASH EQUIVALENTS AT BEGINNING OF PERIOD	84,620	162,734

CASH AND CASH EQUIVALENTS AT END OF PERIOD	\$ 57,037	\$ 125,740

SUPPLEMENTAL DISCLOSURES OF CASH FLOW INFORMATION:		
Cash paid during the period for:		
Interest (net of amount capitalized)	\$ 14,317	\$ 14,494
Income taxes - net	\$ 2,146	\$ 2,559

SUPPLEMENTAL SCHEDULE OF NON-CASH FINANCING ACTIVITIES		
Deconsolidation of The Babcock & Wilcox Company debt	\$ --	\$ 4,760
	=====	=====

See accompanying notes to condensed consolidated financial statements.

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McDERMOTT INTERNATIONAL, INC.
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
MARCH 31, 2001

NOTE 1 - BASIS OF PRESENTATION

We have presented our condensed consolidated financial statements in U.S. Dollars in accordance with accounting principles generally accepted in the United States ("*GAAP*") for interim financial information. Accordingly, they do not include all of the information and footnotes required by GAAP for complete financial statements. We have included all adjustments that we consider necessary for a fair presentation. These condensed consolidated financial statements include the accounts of McDermott International, Inc. and its [subsidiaries](#) and controlled joint ventures. We use the equity method to account for investments in joint ventures and other entities we do not control, but have significant influence over. We have eliminated all significant intercompany transactions and accounts. We have reclassified certain amounts previously reported to conform with the presentation at and for the three month period ended March 31, 2001.

McDermott International, Inc. ("*MII*") is the parent company of the McDermott group of companies, which includes:

- o J. Ray McDermott, S.A. ("*JRM*"), a Panamanian subsidiary of MII, and its consolidated [subsidiaries](#);
- o McDermott Incorporated ("*MI*"), a Delaware subsidiary of MII, and its consolidated [subsidiaries](#);
- o Babcock & Wilcox Investment Company ("*BWICO*"), a Delaware subsidiary of MI;
- o BWX Technologies, Inc. ("*BWXT*"), a Delaware subsidiary of BWICO, and its consolidated [subsidiaries](#); and
- o The Babcock & Wilcox Company ("*B&W*"), an unconsolidated Delaware subsidiary of BWICO.

Operating results for the three months ended March 31, 2001 are not necessarily indicative of the results that may be expected for the year ended December 31, 2001. For further information, refer to the consolidated financial statements and footnotes thereto, included in MII's annual report on Form 10-K for the year ended December 31, 2000.

On February 22, 2000, B&W and certain of its [subsidiaries](#) filed a voluntary petition in the U.S. Bankruptcy Court for the Eastern District of Louisiana in New Orleans (the "*Bankruptcy Court*") to reorganize under Chapter 11 of the U.S. Bankruptcy Code. B&W and these [subsidiaries](#) took this action as a means to determine and comprehensively resolve their asbestos liability. B&W and its [subsidiaries](#) are committed to operating their businesses as normal, delivering products and services as usual and pursuing new [contracts](#) and growth opportunities. However, as of February 22, 2000, B&W's operations

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are subject to the jurisdiction of the Bankruptcy Court and, as a result, our access to cash flows of B&W and its [subsidiaries](#) is restricted.

Due to the bankruptcy filing, beginning on [February 22, 2000](#), we no longer consolidate B&W's financial results in our condensed consolidated financial statements, and our investment in B&W is presented on the cost method. When B&W emerges from the jurisdiction of the Bankruptcy Court, the subsequent accounting will be determined based on the applicable circumstances and facts at such time, including the terms of any [plan of reorganization](#). The filing results in increased uncertainty with respect to the amounts, means and timing of the ultimate settlement of asbestos claims and the recovery of MII's net investment in B&W which was \$186,966,000 at [March 31, 2001](#) and is subject to periodic reviews for recoverability. At [March 31, 2001](#), MII's investment exceeds the underlying net assets of B&W by \$8,346,000. See Note 8 for condensed consolidated financial information of B&W.

Effective [January 1, 2001](#), we adopted Statement of Financial Accounting Standards ("*SFAS*") No. 133, "*Accounting for Derivative Instruments and Hedging Activities*," as amended by SFAS No. 138, which adds to the guidance related to accounting for derivative instruments and hedging activities. SFAS No. 133 requires us to recognize all derivatives on our consolidated balance sheet at their fair values. The initial adoption of SFAS No. 133, as amended by SFAS No. 138, had no material effect on our consolidated financial position or results of operations.

NOTE 2 - INVENTORIES

Inventories are summarized below:

[\[Download Table\]](#)

	<i>March 31,</i> <i>2001</i>	<i>December 31,</i> <i>2000</i>
	-----	-----
	<i>(Unaudited)</i>	
	<i>(In thousands)</i>	
Raw Materials and Supplies	\$ 6,767	\$ 7,412
Work in Progress	1,244	1,895
Finished Goods	2,222	2,426
	-----	-----
Total Inventories	\$ 10,233	\$ 11,733
	=====	=====

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NOTE 3 - ACCUMULATED OTHER COMPREHENSIVE LOSS

The components of accumulated other comprehensive loss included in stockholders' equity are as follows:

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	<u>March 31,</u> <u>2001</u>	<u>December 31,</u> <u>2000</u>
	-----	-----
	(Unaudited)	
	(In thousands)	
Currency Translation Adjustments	\$ (46,969)	\$ (47,089)
Net Unrealized Gain (Loss) on Investments	1,190	(4,842)
Net Unrealized Loss on Derivative Financial Instruments	(1,200)	--
Minimum Pension Liability	(2,921)	(2,921)
	-----	-----
Accumulated Other Comprehensive Loss	\$ (49,900)	\$ (54,852)
	=====	=====

NOTE 4 - INVESTIGATIONS AND LITIGATION

In March 1997, we, with the help of outside counsel, began an investigation into allegations of wrongdoing by a limited number of former employees of MII and JRM and others. The allegations concerned the heavy-lift business of JRM's HeereMac joint venture ("*HeereMac*") with Heerema Offshore Construction Group, Inc. ("*Heerema*") and the heavy-lift business of JRM. Upon becoming aware of these allegations, we notified authorities, including the Antitrust Division of the Department of Justice ("*DOJ*"), the Securities and Exchange Commission ("*SEC*") and the European Commission. As a result of our prompt disclosure of the allegations, MII and JRM and their officers, directors and employees at the time of the disclosure were granted immunity from criminal prosecution by the DOJ for any anti-competitive acts involving worldwide heavy-lift activities. In June 1999, the DOJ agreed to our request to expand the scope of the immunity to include a broader range of our marine construction activities and affiliates. We have cooperated fully with the investigations of the DOJ and the SEC into these matters. In February 2001, we were advised that the SEC has terminated its investigation and no enforcement action has been recommended.

On becoming aware of the allegations involving HeereMac, we initiated action to terminate JRM's interest in HeereMac, and, on [December 19, 1997](#), Heerema acquired JRM's interest in exchange for cash and title to several pieces of equipment. On [December 21, 1997](#), HeereMac and one of its employees pled guilty to criminal charges by the DOJ that they and others had participated in a conspiracy to rig bids in connection with the heavy-lift business of HeereMac in the Gulf of Mexico, the North Sea and the Far

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East. HeereMac and the HeereMac employee were fined \$49,000,000 and \$100,000, respectively. As part of the plea, both HeereMac and certain employees of HeereMac agreed to cooperate fully with the DOJ investigation. Neither MII, JRM nor any of their officers, directors or employees was a party to those proceedings.

In July 1999, a former JRM officer pled guilty to charges brought by the DOJ that he participated in a bid-rigging conspiracy for the sale of marine construction services in the U.S. Gulf of Mexico and elsewhere. In May 2000, another former JRM officer was indicted by the DOJ for participating in a bid-rigging conspiracy for the sale of marine construction services in the Gulf of Mexico. His trial was held in February 2001 and at the conclusion of the Government's case, the presiding Judge directed a judgment of acquittal. Also in February 2001, we were advised that the SEC has terminated its investigation and no enforcement action has been recommended.

We have cooperated with the DOJ in its investigation. The DOJ also has requested additional information from us relating to possible anti-competitive activity in the marine construction business of McDermott-ETPM East, Inc., one of the operating companies within JRM's former McDermott-ETPM joint venture with ETPM S.A., a French company. In connection with the termination of the McDermott-ETPM joint venture on [April 3, 1998](#), JRM assumed 100% ownership of McDermott-ETPM East, Inc., which was renamed J. Ray McDermott Middle East, Inc.

In June 1998, Phillips Petroleum Company (individually and on behalf of certain co-venturers) and several related entities (the "*Phillips Plaintiffs*") filed a lawsuit in the United States District Court for the Southern District of Texas against MII, JRM, MI, McDermott-ETPM, Inc., certain JRM [subsidiaries](#), HeereMac, Heerema, certain Heerema affiliates and others, alleging that the defendants engaged in anti-competitive acts in violation of Sections 1 and 2 of the Sherman Act and Sections 15.05 (a) and (b) of the Texas Business and Commerce Code, engaged in fraudulent activity and tortiously interfered with the plaintiffs' businesses in connection with certain offshore transportation and installation projects in the Gulf of Mexico, the North Sea and the Far East (the "*Phillips Litigation*"). In December 1998, Den norske stats oljeselskap a.s., individually and on behalf of certain of its ventures and its participants (collectively "*Statoil*"), filed a similar lawsuit in the same court (the "*Statoil Litigation*"). In addition to seeking injunctive relief, actual damages and attorneys' fees, the plaintiffs in the Phillips Litigation and Statoil Litigation have requested punitive as well as treble damages. In January 1999, the court dismissed without prejudice, due to the court's lack of subject matter jurisdiction, the claims of the Phillips Plaintiffs relating to alleged injuries sustained on any foreign projects. In July 1999, the court also dismissed the Statoil Litigation for lack of subject matter jurisdiction. Statoil appealed this dismissal to

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the Fifth Circuit Court of Appeals. The Fifth Circuit affirmed the district court decision in February 2000. Statoil filed a motion for rehearing en banc which was denied on [March 12, 2001](#). In September 1999, the Phillips Plaintiffs filed notice of their request to dismiss their remaining domestic claims in the lawsuit in order to seek an appeal of the dismissal of their claims on foreign projects, which request was subsequently denied.

In June 1998, Shell Offshore, Inc. and several related entities also filed a lawsuit in the United States District Court for the Southern District of Texas against MII, JRM, MI, McDermott-ETPM, Inc., certain JRM [subsidiaries](#), HeereMac, Heerema and others, alleging that the defendants engaged in anti-competitive acts in violation of Sections 1 and 2 of the Sherman Act (the "*Shell Litigation*"). Subsequently, the following parties (acting for themselves and, in certain cases, on behalf of their respective co-venturers and for whom they operate) intervened as plaintiffs in the Shell Litigation: Amoco Production Company and B.P. Exploration & Oil, Inc.; Amerada Hess Corporation; Conoco Inc. and certain of its affiliates; Texaco Exploration and Production Inc. and certain of its affiliates; Elf Exploration UK PLC and Elf Norge a.s.; Burlington Resources Offshore, Inc.; The Louisiana Land & Exploration Company; Marathon Oil Company and certain of its affiliates; VK-Main Pass Gathering Company, L.L.C., Green Canyon Pipeline Company, L.L.C.; Delos Gathering Company, L.L.C.; Chevron U.S.A. Inc. and Chevron Overseas Petroleum Inc.; Shell U.K. Limited and certain of its affiliates; Woodside Energy, Ltd; and Saga Petroleum, S.A.. Also, in December 1998, Total Oil Marine p.l.c. and Norsk Hydro Produksjon a.s., individually and on behalf of their respective co-venturers, filed similar lawsuits in the same court, which lawsuits were consolidated with the Shell Litigation. In addition to seeking injunctive relief, actual damages and attorneys' fees, the plaintiffs in the Shell Litigation request treble damages. In February 1999, we filed a motion to dismiss the foreign project claims of the plaintiffs in the Shell Litigation due to the Texas district court's lack of subject matter jurisdiction, which motion is pending before the court. Subsequently, the Shell Litigation plaintiffs were allowed to amend their complaint to include non-heavy lift marine construction activity claims against the defendants. Currently, we are awaiting the court's decision on our motion to dismiss the foreign claims. In the meantime, the Court has allowed limited discovery.

We recently learned that on [December 15, 2000](#), lawsuits were filed by a number of Norwegian oil companies against MII, Heeremac, Heerema and Saipem S.p.A. for violations of the Norwegian Pricing Act of 1953 in connection with projects in Norway. Plaintiffs include Norwegian affiliates of various of the plaintiffs in the Shell civil case pending in Houston. Most of the projects were performed by Saipem S.p.A. or its affiliates, with some by Heerema/HeereMac and none by MII. We understand that the

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conduct alleged by plaintiffs is the same conduct which plaintiffs allege in the U.S. civil cases. The first appearance is scheduled for [October 4, 2001](#) in Oslo.

As a result of the initial allegations of wrongdoing in March 1997, we formed and have continued to maintain a special committee of our Board of Directors to monitor and oversee our investigation into all of these matters.

It is not possible to predict the ultimate outcome of the DOJ investigation, our internal investigation, the above-referenced lawsuits or any actions that may be taken by others as a result of HeereMac's guilty plea or otherwise. These matters could result in civil and criminal liability and have a material adverse effect on our consolidated financial position and results of operations.

B&W and Atlantic Richfield Company ("*ARCO*") are defendants in a lawsuit filed by Donald F. Hall, Mary Ann Hall and others in the United States District Court for the Western District of Pennsylvania. The suit involves approximately 300 separate claims for compensatory and punitive damages relating to the operation of two former nuclear fuel processing facilities located in Pennsylvania (the "*Hall Litigation*"). The plaintiffs in the Hall Litigation allege, among other things, that they suffered personal injury, property damage and other damages as a result of radioactive emissions from these facilities. In September 1998, a jury found B&W and ARCO liable to eight plaintiffs in the first cases brought to trial, awarding \$36,700,000 in compensatory damages. In June 1999, the district court set aside the \$36,700,000 judgment and ordered a new trial on all issues. In November 1999, the district court allowed an interlocutory appeal by the plaintiffs of certain issues, including the granting of the new trial and the court's rulings on certain evidentiary matters, which, following B&W's bankruptcy filing, the Third Circuit Court of Appeals declined to accept for review. The plaintiffs' claims against B&W in the Hall Litigation have been automatically stayed as a result of the B&W bankruptcy filing. B&W has also filed a complaint for declaratory and injunctive relief with the Bankruptcy Court seeking to stay the pursuit of the Hall Litigation against ARCO during the pendency of B&W's bankruptcy proceeding due to common insurance coverage and the risk to B&W of issue or claim preclusion, which stay the Bankruptcy Court denied in October 2000. B&W has appealed this decision.

In 1998, B&W settled all pending and future punitive damage claims in the Hall Litigation for \$8,000,000 for which it seeks reimbursement from other parties. There is a controversy between B&W and its insurers as to the amount of coverage available under the liability insurance policies covering the facilities. B&W filed a declaratory judgment action in a Pennsylvania State Court seeking a judicial determination as to the amount of coverage available under the policies. On [April 28, 2001](#), in response to

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cross-motions for partial summary judgment, the Pennsylvania State Court issued its ruling regarding: (i) the applicable trigger of coverage under the Nuclear Energy Liability Policies issued by B&W's nuclear insurers; and (ii) the scope of the nuclear insurers' defense obligations to B&W under these policies. With respect to the trigger of coverage, the Pennsylvania State Court held that a "manifestation" trigger applied to the underlying claims at issue. Although the Court did not make any determination of coverage with respect to any of the underlying claims, we believe the effect of its ruling is to increase the amount of coverage potentially available to B&W under the policies at issue to \$320,000,000. With respect to the nuclear insurers' duty to defend B&W, the Court held that B&W is entitled to separate and independent counsel funded by the nuclear insurers. We believe that all claims under the Hall Litigation will be resolved within the limits of coverage of our insurance policies; but our insurance coverage may not be adequate and we may be materially adversely impacted if our liabilities exceed our coverage. B&W transferred the two facilities subject to the Hall Litigation to BWXT in June 1997 in connection with BWXT's formation and an overall corporate restructuring.

In December 1999 and early 2000, several persons who allegedly purchased shares of our common stock during the period from [May 21, 1999](#) through [November 11, 1999](#) filed four purported class action complaints against MII and two of its executive officers, Roger E. Tetrault and Daniel R. Gaubert, in the United States District Court for the Eastern District of Louisiana. Each of the complaints alleged that the defendants violated federal securities laws by disseminating materially false and misleading information and/or concealing material adverse information relating to our estimated liability for asbestos-related claims. Each complaint sought relief, including unspecified compensatory damages and an award for costs and expenses. The four cases were subsequently consolidated. In June 2000, the plaintiffs filed a consolidated amended complaint, and in July 2000, we filed a motion to dismiss all claims asserted in that complaint. In September 2000, the District Court dismissed with prejudice the plaintiffs' consolidated amended complaint for failure to state a claim upon which relief can be granted, which dismissal the plaintiffs appealed to the U.S. Fifth Circuit Court of Appeals in October 2000. On [April 25, 2001](#), the plaintiffs-appellants filed a motion to voluntarily dismiss their appeal and the appeal was dismissed by the U.S. Fifth Circuit Court on [April 26, 2001](#).

In December 1998, JRM was in the process of installing a deck module on a compliant tower in the Gulf of Mexico for Texaco Exploration and Production, Inc. ("Texaco") when the main hoist load line failed, resulting in the loss of the module. As a result, Texaco has withheld payment to JRM of \$23,000,000 due under the installation [contract](#), and, in January 2000, JRM instituted an arbitration proceeding against

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Texaco seeking the amount owed. Texaco has countered in the arbitration, claiming consequential damages for delays resulting from the incident, as well as costs incurred to complete the project with another contractor. Texaco has also filed a lawsuit against a number of other parties, claiming that they are responsible for the incident. It is our position that the [contract](#) between the parties prohibits Texaco's claims against JRM and JRM is entitled to the amount withheld.

In early April 2001, a group of insurance underwriters who have previously provided insurance to B&W under our excess liability policies filed (1) a complaint for declaratory judgment and damages against MII in the U.S. District Court for the Eastern District of Louisiana and (2) a declaratory judgment complaint against B&W in the U.S. Bankruptcy Court for the Eastern District of Louisiana. The insurance policies at issue in this litigation provide a significant portion of B&W's excess liability coverage available for the resolution of the asbestos-related claims that are the subject of the B&W Chapter 11 proceeding. The complaints contain substantially identical factual allegations. These include allegations that, in the course of settlement discussions with the representatives of the asbestos claimants in the B&W bankruptcy proceeding, MII and B&W breached the confidentiality provisions of an agreement they entered into with these insurers relating to insurance payments of the insurers as a result of asbestos claims. They also allege that MII and B&W have wrongfully attempted to expand the underwriters' obligations under that agreement and the applicable policies through the filing of a plan of reorganization in the B&W bankruptcy proceeding that contemplates the transfer of rights under that agreement and those policies to a trust that will manage the pending and future asbestos-related claims against B&W and certain of its affiliates. The complaints seek declarations that, among other things, the defendants are in material breach of the agreement with the insurers and that the plaintiff underwriters owe no further obligations to MII and B&W under that agreement. With respect to the insurance policies, if the insurers should succeed in terminating the agreement, they seek to litigate issues under the policies in order to reduce their coverage obligations. The complaint in the District Court case also seeks a recovery of unspecified compensatory damages. Management believes these complaints and the substantive allegations they contain are without merit. Management intends to contest and defend against these actions vigorously. In management's opinion, these complaints will not have a material adverse effect on our consolidated financial position or results of operations.

On [April 30, 2001](#), B&W filed a declaratory judgment action in its Chapter 11 proceeding against MI, BWICO, BWXT, Hudson Products Corporation and McDermott Technologies, Inc. seeking a judgment, among other things, that B&W was not insolvent at the time of, or rendered insolvent as a result of, a corporate reorganization that we completed in the fiscal year ended [March 31, 1999](#), which involved

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B&W's cancellation of a \$313,000,000 note receivable and B&W's transfer of all the capital stock of Hudson Products Corporation, Tracy Power, BWXT and McDermott Technologies, Inc. to BWICO, and that the transfers are not voidable. As an alternative, and only in the event that the Bankruptcy Court finds B&W insolvent at a pertinent time, the action preserves B&W's claims against the defendants. We believe that B&W was solvent at the time of the transfers and that the transfers are not voidable. However, if the declaratory judgment were adversely decided by the Bankruptcy Court, it could have a material adverse effect on our consolidated financial position and results of operations.

Additionally, due to the nature of our business, we are, from time to time, involved in routine litigation or subject to disputes or claims related to our business activities, including performance or warranty related matters under our customer and supplier [contracts](#) and other business arrangements. In our management's opinion, none of this litigation or disputes and claims will have a material adverse effect on our consolidated financial position or results of operations.

See Note 8 to the condensed consolidated financial statements regarding B&W's potential liability for non-employee asbestos claims and the Chapter 11 reorganization proceedings commenced by B&W and certain of its [subsidiaries](#) on [February 22, 2000](#).

NOTE 5 - SEGMENT REPORTING

Our reportable segments are Marine Construction Services, Power Generation Systems, Government Operations and Industrial Operations. These segments are managed separately and are unique in technology, services and customer class.

Marine Construction Services, which includes the results of JRM, supplies worldwide services for the offshore oil and gas exploration, production and hydrocarbon processing industries and to other marine construction companies. Principal activities include the design, engineering, fabrication and installation of offshore drilling and production platforms, specialized structures, modular facilities, marine pipelines and subsea production systems. JRM also provides project management services, engineering services, procurement activities, and removal, salvage and refurbishment services of offshore fixed platforms.

Government Operations supplies nuclear reactor components and nuclear fuel assemblies to the U.S. Government, manages and operates government-owned facilities and supplies commercial nuclear environmental services and other government and commercial nuclear services.

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Industrial Operations is comprised of the engineering and construction activities and plant outage maintenance of certain Canadian operations and manufacturing of auxiliary equipment such as air-cooled heat exchangers and replacement parts. Industrial Operations also includes [contract](#) research activities.

Power Generation Systems supplies engineered-to-order services, products and systems for energy conversion, and fabricates replacement nuclear steam generators and environmental control systems. In addition, this segment provides aftermarket services including replacement parts, engineered upgrades, construction, maintenance and field technical services to electric power plants and industrial facilities. This segment also provides power through cogeneration, refuse-fueled power plants and other independent power producing facilities. The Power Generation Systems segment's operations are conducted primarily through B&W. Due to B&W's Chapter 11 filing, effective [February 22, 2000](#), we no longer consolidate B&W's and its [subsidiaries](#)' results of operations in our condensed consolidated financial statements. Through [February 21, 2000](#), B&W's and its [subsidiaries](#)' results are reported as Power Generation Systems - B&W in the segment information that follows. See Note 8 for the condensed consolidated results of B&W and its [subsidiaries](#).

We account for intersegment sales at prices that we generally establish by reference to similar transactions with unaffiliated customers. Other reconciling items to income before provision for income taxes are interest income, interest expense, minority interest and other-net. We have allocated amortization of goodwill to the reportable segments for all periods presented. Income from over-funded pension plans of discontinued businesses are included in corporate for both periods presented.

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Segment Information for the Three Months Ended [March 31, 2001](#) and [2000](#).

[\[Download Table\]](#)

	Three Months Ended	
	March 31,	
	2001	2000
	-----	-----
	(Unaudited)	
	(In thousands)	
REVENUES		
Marine Construction Services	\$ 134,680	\$ 206,635
Government Operations	120,863	114,720
Industrial Operations	168,928	115,242
Power Generation Systems - B&W	--	155,774
Power Generation Systems	8,434	82
Adjustments and Eliminations(1)	(170)	(742)
	-----	-----
	\$ 432,735	\$ 591,711
	=====	=====

(1) Segment revenues are net of the following intersegment transfers and other adjustments:

[\[Download Table\]](#)

Marine Construction Services Transfers	\$ 34	\$ 437
Government Operations Transfers	112	194
Industrial Operations Transfers	24	52
Power Generation Systems Transfers - B&W	--	59
	-----	-----
	\$ 170	\$ 742
	=====	=====

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[\[Enlarge/Download Table\]](#)

	Three Months Ended	
	March 31,	
	2001	2000

	(Unaudited)	
	(In thousands)	
OPERATING INCOME (LOSS) :		
Segment Operating Income:		
Marine Construction Services	\$ (10,416)	\$ (5,787)
Government Operations	11,047	13,343
Industrial Operations	2,162	2,235
Power Generation Systems - B&W	--	7,172
Power Generation Systems	(585)	(220)
	-----	-----
	\$ 2,208	\$ 16,743
	=====	=====
Gain (Loss) on Asset Disposal and Impairments - Net:		
Marine Construction Services	\$ 522	\$ 1,085
Government Operations	3	--
Industrial Operations	--	7
Power Generation Systems - B&W	--	(33)
	-----	-----
	\$ 525	\$ 1,059
	=====	=====
Income (Loss) from Investees:		
Marine Construction Services	\$ (46)	\$ (7,546)
Government Operations	4,702	1,352
Industrial Operations	66	24
Power Generation Systems - B&W	--	812
Power Generation Systems	235	(865)
	-----	-----
	\$ 4,957	\$ (6,223)
	=====	=====
SEGMENT INCOME :		
Marine Construction Services	\$ (9,940)	\$ (12,248)
Government Operations	15,752	14,695
Industrial Operations	2,228	2,266
Power Generation Systems - B&W	--	7,951
Power Generation Systems	(350)	(1,085)
	-----	-----
	7,690	11,579
Corporate	(1,733)	(1,130)
	-----	-----
TOTAL	\$ 5,957	\$ 10,449
	=====	=====

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NOTE 6 - EARNINGS (LOSS) PER SHARE

The following table sets forth the computation of basic and diluted earnings (loss) per share:

[\[Download Table\]](#)

	<i>Three Months Ended</i>	
	<i>March 31,</i>	
	<i>2001</i>	<i>2000</i>
	-----	-----
	<i>(Unaudited)</i>	
	<i>(In thousands, except shares and per share amounts)</i>	
Basic:		
Net income (loss)	\$ (4,433)	\$ 7,867
Weighted average common shares	60,144,541	59,396,332
Basic earnings (loss) per common share	\$ (0.07)	\$ 0.13
Diluted:		
Net income (loss)	\$ (4,433)	\$ 7,867
Weighted average common shares (basic)	60,144,541	59,396,332
Effect of dilutive securities:		
Stock options and restricted stock	--	435,908
	-----	-----
Adjusted weighted average common shares and assumed conversions	60,144,541	59,832,240
	-----	-----
Diluted earnings (loss) per common share	\$ (0.07)	\$ 0.13
	-----	-----

At March 31 2001, incremental shares of 2,426,431 related to stock options and restricted stock were excluded from the diluted share calculation as their effect would have been anti-dilutive.

NOTE 7 - DERIVATIVE FINANCIAL INSTRUMENTS

Effective [January 1, 2001](#), we adopted Statement of Financial Accounting Standards ("*SFAS*") No. 133, "*Accounting for Derivative Instruments and Hedging Activities*," as amended by SFAS No. 138, which adds to the guidance related to accounting for derivative instruments and hedging activities. SFAS No. 133 requires us to recognize all derivatives on our consolidated balance sheet at their fair values. The initial adoption of SFAS No. 133, as amended by SFAS No. 138, had no material effect on our consolidated financial position or results of operations.

Our worldwide operations give rise to exposure to market risks from changes in foreign exchange rates. We use derivative financial instruments, primarily forward [contracts](#), to reduce the impact of changes in foreign exchange rates on our operating results. We use these instruments primarily to hedge our

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exposure associated with revenues or costs on our long-term [contracts](#) which are denominated in currencies other than our operating entities' functional currencies. We do not hold or issue derivative financial instruments for trading or other speculative purposes.

We enter into forward [contracts](#) primarily as hedges of certain firm purchase and sale commitments denominated in foreign currencies. We record these [contracts](#) at fair value on our consolidated balance sheet. Depending on the hedge designation at the inception of the [contract](#), the related gains and losses on these [contracts](#) are either offset against the change in fair value of the hedged firm commitment through earnings or deferred in stockholders' equity (as a component of accumulated other comprehensive loss) until the hedged item is recognized in earnings. The ineffective portion of a derivative's change in fair value is immediately recognized in earnings. The gain or loss on a derivative financial instrument not designated as a hedging instrument is also immediately recognized in earnings. Gains and losses on forward [contracts](#) that require immediate recognition are included as a component of other-net in our condensed consolidated statement of income (loss).

At [March 31, 2001](#), we had forward [contracts](#) to purchase \$25,733,000 in foreign currencies (primarily Euro and Australian Dollar), and to sell \$1,326,000 in foreign currencies (primarily Pound Sterling), at varying maturities from 2001 through 2002. At [March 31, 2001](#), we had deferred approximately \$1,200,000 of net losses on these forward [contracts](#), of which 38% is expected to be recognized in income over the next twelve months. For the three months ended [March 31, 2001](#), the net loss on forward [contracts](#) recognized immediately was not significant.

We are exposed to credit-related losses in the event of nonperformance by counterparties to derivative financial instruments. We mitigate this risk by using major financial institutions with high credit ratings.

NOTE 8 - THE BABCOCK & WILCOX COMPANY

General

As a result of asbestos-containing commercial boilers and other products B&W and certain of its [subsidiaries](#) sold, installed or serviced in prior decades, B&W is subject to a substantial volume of non-employee liability claims asserting asbestos-related injuries. All of these claims are similar in nature, the primary difference being the type of alleged injury or illness suffered by the plaintiff as a result of the exposure to asbestos fibers (e.g., mesothelioma, lung cancer, other types of cancer, asbestosis or pleural changes).

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Beginning in the third quarter of calendar 1999, B&W experienced a significant increase in the amount demanded by several plaintiffs' attorneys to settle certain types of asbestos products liability claims. These increased demands significantly impaired B&W's ability to continue to resolve its asbestos products liability through out-of-court settlements.

On [February 22, 2000](#), B&W and certain of its [subsidiaries](#) filed a voluntary petition in the Bankruptcy Court to reorganize under Chapter 11 of the U.S. Bankruptcy Code. Included in the filing are B&W and its [subsidiaries](#) American, Inc., Babcock & Wilcox Construction Co., Inc. and Diamond Power International, Inc. B&W and these [subsidiaries](#) took this action as a means to determine and comprehensively resolve all pending and future asbestos liability claims against them. As a result of the filing, the Bankruptcy Court issued a temporary restraining order prohibiting asbestos liability lawsuits and other actions for which there is shared insurance from being brought against non-filing affiliates of B&W, including MI, JRM and MII. The temporary restraining order was converted to a preliminary injunction, which is subject to periodic hearings before the Bankruptcy Court for extension. Currently, the preliminary injunction runs through [July 17, 2001](#). On [February 20, 2001](#), the Bankruptcy Court appointed a mediator to facilitate negotiations among the debtors and the committee representing the asbestos claimants to reach a final determination of the debtors' ultimate liability for asbestos related claims. The mediator's appointment extends through [May 23, 2001](#).

On [February 22, 2001](#), B&W and its debtors filed a [plan of reorganization](#) and a disclosure statement. The [plan of reorganization](#) contemplates a resolution under either the settlement process or a strategy of litigating asbestos claims. Under the settlement process, there would be a consensual agreement of 75% of the asbestos personal injury claimants. A trust would be formed and assigned all of B&W's and its filing [subsidiaries](#)' insurance rights with an aggregate products liability value of approximately \$1,150,000,000. In addition, \$50,000,000 cash and a \$100,000,000 subordinated 10-year note payable would be transferred into the trust. The debtors will consent to the assignment of the insurance and will release and void any right that they have to the insurance. The trust's rights to the insurance would be protected and could be dedicated solely to the resolution of the asbestos claims. As a result of the creation of the trust, B&W and all affiliates would be released and discharged from all present and future liability for asbestos claims arising out of exposure to B&W's products.

Under the litigation strategy, if B&W is not able to reach a consensual agreement with the plaintiffs, a cram-down option is available. The claims would still be channeled through a trust with \$50,000,000 cash and a \$100,000,000 subordinated 10-year note payable, but the debtors and their

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affiliates would not transfer their insurance rights. The debtors would manage the insurance rights and claims would be handled through the litigation process by the trust. Funding of the trust would be from the insurance, the cash, the note payable, and equity of the debtors, if necessary.

Prior to its bankruptcy filing, B&W and its [subsidiaries](#) had engaged in a strategy of negotiating and settling asbestos products liability claims brought against them and billing the settled amounts to insurers for reimbursement. The average amount per settled claim over the three calendar years prior to the Chapter 11 filing was approximately \$7,900. Reimbursed amounts are subject to varying insurance limits based upon the year of coverage, insurer solvency and collection delays (due primarily to agreed payment schedules with specific insurers delaying reimbursement for three months or more). No claims have been paid since the bankruptcy filing. Claims paid during the year ended [December 31, 2000](#), prior to the bankruptcy filing, were \$23,640,000 of which \$20,121,000 has been recovered or is due from insurers. At [March 31, 2001](#), receivables of \$29,091,000 were due from insurers for reimbursement of settled claims. Currently, certain insurers are refusing to reimburse B&W for settled claims until B&W's assumption, in bankruptcy, of its pre-bankruptcy filing contractual reimbursement arrangements with such insurers. To date, this has not had a material adverse impact on B&W's liquidity or the conduct of its business and we do not expect it to in the future. We anticipate that B&W will eventually recover these insurance reimbursements.

At [February 21, 2000](#), the day prior to the bankruptcy filing, B&W had recorded an asbestos products liability of \$1,307,583,000 and an asbestos products liability insurance recoverable of \$1,153,619,000. Historically, B&W's estimated liabilities for pending and future non-employee products liability asbestos claims have been derived from its prior claims history. Inherent in the estimate of such liabilities were expected trend claim severity, frequency, and other factors. B&W's estimated liabilities were based on the assumption that B&W would continue to settle claims rather than litigate them, that new claims would conclude by 2012, that there would be a significant decline in new claims received after 2003, and that the average cost per claim would continue to increase only moderately. During the fiscal year ended [March 31, 1999](#), we revised our estimate of the liability for pending and future non-employee asbestos claims and recorded an additional liability of \$902,847,000, additional estimated insurance recoveries of \$817,662,000 and a loss of \$85,185,000 for future claims for which recovery from insurance carriers was not considered probable.

In early April 2001, a group of insurance underwriters who have previously provided insurance to B&W under our excess liability policies filed (1) a complaint for declaratory judgment and damages against MII in the U.S. District Court for the Eastern District of Louisiana and (2) a declaratory judgment complaint

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against B&W in the U.S. Bankruptcy Court for the Eastern District of Louisiana. The insurance policies at issue in this litigation provide a significant portion of B&W's excess liability coverage available for the resolution of the asbestos-related claims that are the subject of the B&W Chapter 11 proceeding. The complaints contain substantially identical factual allegations. These include allegations that, in the course of settlement discussions with the representatives of the asbestos claimants in the B&W bankruptcy proceeding, MII and B&W breached the confidentiality provisions of an agreement they entered into with these insurers relating to insurance payments of the insurers as a result of asbestos claims. They also allege that MII and B&W have wrongfully attempted to expand the underwriters' obligations under that agreement and the applicable policies through the filing of a [plan of reorganization](#) in the B&W bankruptcy proceeding that contemplates the transfer of rights under that agreement and those policies to a trust that will manage the pending and future asbestos-related claims against B&W and certain of its affiliates. The complaints seek declarations that, among other things, the defendants are in material breach of the agreement with the insurers and that the plaintiff underwriters owe no further obligations to MII and B&W under that agreement. With respect to the insurance policies, if the insurers should succeed in terminating the agreement, they seek to litigate issues under the policies in order to reduce their coverage obligations. The complaint in the District Court case also seeks a recovery of unspecified compensatory damages. Management believes these complaints and the substantive allegations they contain are without merit. Management intends to contest and defend against these actions vigorously. In management's opinion, these complaints will not have a material adverse effect on our consolidated financial position or results of operations.

Pursuant to the Bankruptcy Court's order, a [March 29, 2001](#) bar date was set for the submission of allegedly settled asbestos claims and a [July 30, 2001](#) bar date was set for all other personal injury claims including unsettled asbestos claims against B&W and its filing [subsidiaries](#). As of the [March 29, 2001](#), bar date over 49,000 allegedly settled claims had been filed. While the B&W Chapter 11 reorganization proceedings continue to progress, there are a number of issues and matters related to

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B&W's asbestos liability to be resolved prior to its emergence from the proceedings. Remaining issues and matters to be resolved include, but are not limited:

- o the ultimate asbestos liability of B&W and its [subsidiaries](#);
- o the outcome of negotiations with the asbestos claimants committee, the future claimants representative and other participants in the Chapter 11, concerning, among other things, the size and structure of a trust to satisfy the asbestos liability and the means for funding that trust;
- o the outcome of the declaratory judgment actions filed by certain insurers and negotiations with our insurers as to additional amounts of coverage of B&W and its [subsidiaries](#) and their participation in a plan to fund the settlement trust;
- o the Bankruptcy Court's decisions relating to numerous substantive and procedural aspects of the Chapter 11 proceedings, including the Court's periodic determinations as to whether to extend the existing preliminary injunction that prohibits asbestos liability lawsuits and other actions for which there is shared insurance from being brought against non-filing affiliates of B&W, including MI, JRM and MII; and
- o the possible need for an extension of the three-year term of the \$300,000,000 debtor-in-possession revolving credit and letter of credit facility ("*DIP Credit Facility*"), which is scheduled to expire in February 2003, to accommodate the issuance of letters of credit expiring after that date in connection with new construction and other [contracts](#) on which B&W intends to bid.

The timing and ultimate outcome of the Chapter 11 proceedings are uncertain. Any changes in the estimate of B&W's non-employee asbestos liability and insurance recoverables, and differences between the proportion of such liabilities covered by insurance and that experienced in the past, could result in material adjustments to the B&W financial statements and could negatively impact our ability to realize our net investment in B&W totaling \$186,966,000.

In addition, if the asbestos liability of B&W and its [subsidiaries](#) is ultimately determined to be substantially in excess of the amount we have estimated and reflected in our net investment in B&W, B&W, the asbestos claimants and/or other creditors in the B&W Chapter 11 proceedings may pursue claims against other entities within MI based on allegations relating to various pre-petition transfers by B&W to BWICO and other entities within MI. Although no formal claims of this nature have been made by the asbestos claimants committee in the B&W Chapter 11 proceedings, representatives of the asbestos claimants committee have asserted that the corporate reorganization that we completed in the fiscal year ended [March 31, 1999](#), which involved B&W's cancellation of a \$313,000,000 note receivable and B&W's transfer of all the capital stock of Hudson Products Corporation, Tracy Power, BWXT and

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McDermott Technologies, Inc. to BWICO, included transfers which may be voided under applicable federal bankruptcy and/or state law. On [April 30, 2001](#), B&W filed a declaratory judgment action in the Chapter 11 proceedings against MI, BWICO, BWXT, Hudson Products Corporation and McDermott Technologies, Inc. seeking a judgment, among other things, that B&W was not insolvent at the time of, or rendered insolvent as a result of, the transfers and cancellation of the note receivable and that the transfers are not voidable under applicable law. As an alternative, and only in the event that the Bankruptcy Court finds B&W insolvent at a pertinent time and the transfers are voidable, the action preserves B&W's claims against the defendants. We believe that B&W was solvent at the time of the transfers and that the transfers are not voidable. However, if the declaratory judgment were adversely decided by the Bankruptcy Court, it could have a material adverse effect on our consolidated financial position and results of operations.

Debtor-In-Possession Financing

In connection with the bankruptcy filing, B&W and its filing [subsidiaries](#) entered into the DIP Credit facility with Citibank, N.A. and Salomon Smith Barney Inc. with a three-year term. The Bankruptcy Court approved the full amount of this facility, giving all amounts owed under the facility a super-priority administrative expense status in bankruptcy. B&W's and its filing [subsidiaries'](#) obligations under the facility are (1) guaranteed by substantially all of B&W's other domestic [subsidiaries](#) and B&W Canada Ltd. and (2) secured by a security interest on B&W Canada Ltd.'s assets. Additionally, B&W and substantially all of its domestic [subsidiaries](#) executed a pledge and security agreement pursuant to which they have granted a security interest in their assets to the lenders under the DIP Credit Facility upon the defeasance or refinancing of MI's public debt. The DIP Credit Facility generally provides for borrowings by B&W and its filing [subsidiaries](#) for working capital and other general corporate purposes and the issuance of letters of credit, except that the total of all borrowings and non-performance letters of credit issued under the facility cannot exceed \$100,000,000 in the aggregate. The DIP Credit Facility also imposes certain financial and non-financial covenants on B&W and its [subsidiaries](#). There were no borrowings under this facility at [March 31, 2001](#). A permitted use of the DIP Credit Facility is the issuance of new letters of credit to backstop or replace pre-existing letters of credit issued in connection with B&W's and its [subsidiaries'](#) business operations, but for which MII, MI or BWICO was a maker or guarantor. As of [February 22, 2000](#), the aggregate amount

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of all such pre-existing letters of credit totaled approximately \$172,000,000 (the "Pre-existing LCs"). MII, MI and BWICO have agreed to indemnify and reimburse B&W and its filing [subsidiaries](#) for any customer draw on any letter of credit issued under the DIP Credit Facility to backstop or replace any Pre-existing LC for which it already has exposure and for the associated letter of credit fees paid under the facility. As of [March 31, 2001](#), approximately \$75,672,000 in letters of credit have been issued under the DIP Credit Facility of which approximately \$51,353,000 were to replace or backstop Pre-existing LCs.

Financial Results and Reorganization Items

The B&W condensed consolidated financial statements set forth below have been prepared in conformity with the American Institute of Certified Public Accountants' Statement of Position 90-7, "*Financial Reporting by Entities in Reorganization Under the Bankruptcy Code*," issued November 19, 1990 ("*SOP 90-7*"). SOP 90-7 requires a segregation of liabilities subject to compromise by the Bankruptcy Court as of the bankruptcy filing date and identification of all transactions and events that are directly associated with the reorganization. Liabilities subject to compromise include prepetition unsecured claims, which may be settled at amounts which differ from those recorded in the B&W condensed consolidated financial statements.

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THE BABCOCK & WILCOX COMPANY
DEBTOR-IN-POSSESSION
CONDENSED CONSOLIDATED STATEMENTS OF INCOME

[\[Download Table\]](#)

	<i>Three Months Ended</i>	
	<i>March 31,</i>	
	<i>2001</i>	<i>2000</i>
	-----	-----
	<i>(Unaudited)</i>	
	<i>(In thousands)</i>	
Revenues	\$ 355,859	\$ 272,567
	-----	-----
Costs and Expenses:		
Cost of operations	301,789	226,653
Selling, general and administrative expenses	28,601	27,055
Equity in income of investees	(367)	(1,433)
Reorganization charges	4,943	3,922
	-----	-----
Total Costs and Expenses	334,966	256,197
	-----	-----
Operating Income	20,893	16,370
	-----	-----
Other Income (Expense):		
Interest income	2,364	963
Interest expense	(1,475)	(174)
Other-net	(3,248)	(894)
	-----	-----
Total Other Income (Expense)	(2,359)	(105)
	-----	-----
Income before Provision for Income Taxes	18,534	16,265
	-----	-----
Provision for Income Taxes	7,869	6,630
	-----	-----
Net Income	\$ 10,665	\$ 9,635
	=====	=====

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THE BABCOCK & WILCOX COMPANY
DEBTOR-IN-POSSESSION
CONDENSED CONSOLIDATED BALANCE SHEET

[\[Enlarge/Download Table\]](#)

	<i>March 31, 2001</i>	<i>December 31, 2000</i>
	-----	-----
	<i>(Unaudited)</i>	
	<i>(In thousands)</i>	
Assets:		
Current Assets	\$ 532,922	\$ 553,937
Property, Plant and Equipment	77,969	80,459
Products Liabilities Recoverable	1,152,489	1,153,761
Goodwill	75,901	77,093
Prepaid Pension Costs	21,096	20,369
Other Assets	158,571	128,043
	-----	-----
Total Assets	\$ 2,018,948	\$ 2,013,662
	-----	-----
Liabilities:		
Current Liabilities	\$ 372,750	\$ 364,977
Liabilities Subject to Compromise(A)	1,450,822	1,456,313
Accrued Postretirement Benefit Obligation	594	566
Other long-term liabilities	16,162	18,589
Stockholder's Equity:		
Common Stock	1,001	1,001
Capital in Excess of Par Value	134,733	134,733
Retained Earnings	71,489	60,824
Accumulated Other Comprehensive Loss	(28,603)	(23,341)
	-----	-----
Total Liabilities and Stockholder's Equity	\$ 2,018,948	\$ 2,013,662
	-----	-----
(A) Liabilities subject to compromise consist of the following:		
Accounts payable	\$ 3,011	\$ 3,113
Provision for warranty	19,986	21,742
Other current liabilities	24,238	25,302
Products liabilities	1,307,725	1,307,725
Accumulated postretirement benefit obligation	74,215	75,910
Other long-term liabilities	21,647	22,521
	-----	-----
	\$ 1,450,822	\$ 1,456,313
	=====	=====

B&W and its [subsidiaries](#) routinely engage in intercompany transactions with other entities within the McDermott group of companies in the ordinary course of business. These transactions include services received by B&W and its [subsidiaries](#) from MII and MI under a support services agreement. These services include the following: accounting, treasury, tax administration, and other financial services; human relations; public relations; corporate secretarial; and corporate officer services. In addition, B&W is responsible for its share of federal income taxes included in MI's federal tax return under a tax-sharing arrangement. As a result of its bankruptcy filing, B&W and its filing [subsidiaries](#) are precluded from paying dividends to shareholders and making payments on any pre-bankruptcy filing accounts or notes

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payable that are due and owing to any other entity within the McDermott group of companies (the "Pre-Petition Inter-company Payables") and other creditors during the pendency of the bankruptcy case, without the Bankruptcy Court's approval. Moreover, no assurances can be given that any of the Pre-Petition Inter-company Payables will be paid or otherwise satisfied in connection with the confirmation of a B&W [plan of reorganization](#). As of [February 21, 2000](#), the day prior to the bankruptcy filing, B&W and its filing [subsidiaries](#) had Pre-Petition Inter-company Payables of approximately \$51,350,000 and pre-petition inter-company receivables from other entities within the McDermott group of companies (other than [subsidiaries](#) of B&W) of approximately \$58,143,000. In the course of the conduct of B&W's and its [subsidiaries](#)' business, MII and MI have agreed to indemnify two surety companies for B&W's and its [subsidiaries](#)' obligations under surety bonds issued in connection with their customer [contracts](#). In addition to this indemnity, these two surety companies requested and, in June 2000, obtained from the Bankruptcy Court, subject to DIP Credit Facility and certain professional fees, super-priority administrative expense status in bankruptcy for their claims against B&W and its filing [subsidiaries](#) resulting from their exposure under any bond issued post-bankruptcy filing for B&W's and its [subsidiaries](#)' businesses. At [March 31, 2001](#), the total value of B&W's and its [subsidiaries](#)' customer [contracts](#) yet to be completed covered by such indemnity arrangements was approximately \$235,756,000 of which approximately \$140,305,000 relates to bonds issued after [February 21, 2000](#).

B&W's financial results are included in our consolidated results through [February 21, 2000](#), the day prior to B&W's Chapter 11 filing. However, generally accepted accounting principles specifically require that any entity whose financial statements were previously consolidated with those of its parent (as B&W's were with ours) that files for protection under the U.S. Bankruptcy Code, whether solvent or insolvent, must be prospectively deconsolidated from the parent and presented on the cost method. The cost method requires us to present the net assets of B&W at [February 22, 2000](#) as an investment and not recognize any income or loss from B&W in our results of operations during the reorganization period. This investment of \$166,234,000, as of [February 21, 2000](#), increased to \$186,966,000 due to post-bankruptcy filing adjustments to the net assets of B&W and is subject to periodic reviews for recoverability. When B&W emerges from the jurisdiction of the Bankruptcy Court, the subsequent accounting will be determined based upon the applicable circumstances and facts at such time, including the terms of any [plan of reorganization](#).

We have assessed B&W's liquidity position as a result of the bankruptcy filing and believe that B&W can continue to fund its and its [subsidiaries](#)' operating activities and meet its debt and capital requirements for the foreseeable future. However, the ability of B&W to continue as a going concern is dependent upon its ability to settle its ultimate asbestos liability from its net assets, future profits and cash flow and available

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insurance proceeds, whether through the confirmation of a [plan of reorganization](#) or otherwise. The B&W condensed consolidated financial information set forth above has been prepared on a going concern basis which contemplates continuity of operations, realization of assets, and liquidation of liabilities in the ordinary course of business. As a result of the bankruptcy filing and related events, there is no assurance that the carrying amounts of assets will be realized or that liabilities will be liquidated or settled for the amounts recorded. In addition, a rejection of our [plan of reorganization](#) could change the amounts reported in the B&W financial statements and cause a material decrease in the carrying amount of our investment. The independent accountant's report on the separate consolidated financial statements of B&W for the periods ended [December 31, 2000](#) and [1999](#) includes an explanatory paragraph indicating that these issues raise substantial doubt about B&W's ability to continue as a going concern.

Following is our condensed Pro Forma consolidated Statements of Income, assuming the deconsolidation of B&W, for the three months ended [March 31, 2000](#):

Assumes deconsolidation as of the beginning of the period presented:

[\[Download Table\]](#)

	<i>(Unaudited)</i> <i>(In thousands)</i>
Revenues	\$435,996
Operating Income	\$ 1,039
Income before Benefit from Income Taxes	\$ 1,890
Net Income	\$ 2,362
Earnings per Common Share:	
Basic	\$ 0.04
Diluted	\$ 0.04

We believe that the bankruptcy filing and the weak Marine Construction Services markets have contributed to the reduction in our credit rating from BA1 to BA3 by Moody's Investor Service and BB to B by Standard & Poors and, consequently, could adversely impact our access to capital. In addition, MI and JRM and their respective [subsidiaries](#) are limited, as a result of covenants in debt instruments, in their ability to transfer funds to MII and its other [subsidiaries](#) through cash dividends or through unsecured loans or investments. As a result, we have assessed our ability to continue as a going concern and have concluded that we can continue to fund our operating activities and capital requirements for the foreseeable future. In this regard, management will be required to address several significant issues:

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- o Negative cash flows. We expect to incur negative cash flows in the next quarter, with a return to a positive cash flow position in the third and fourth quarters of the year. We expect to satisfy our working capital needs and fund negative cash flows in the first two quarters of 2001 through increased borrowings on our existing credit facilities. We expect to return to positive cash flows through a combination of improved market conditions, as well as a reduction in general and administrative costs.
- o Reduction in surety bond capacity. We have been notified by our two surety companies that they are no longer willing to issue bonds on our behalf. We obtain surety bonds in the ordinary course of business of several of our operations to secure [contract](#) bids and to meet the bonding requirements of various construction and other [contracts](#) with customers. We expect to obtain the coverage we require through other surety companies as well as using our existing credit facilities for [contract](#)-related performance guarantees. We do not expect this situation to impact MII's liquidity negatively for the foreseeable future.
- o Upcoming maturity of MI's 9.375% notes. MI's 9.375% notes, which have an aggregate outstanding principal amount of \$225,000,000, are scheduled to mature on [March 15, 2002](#). MI currently has insufficient cash and other liquid resources on hand to fund the repayment of its 9.375% notes. We are currently exploring various alternatives relative to extending the maturity of these notes, as well as other potential refinancing alternatives. We expect these efforts will be successful. In addition, for the 2001 year, MI would be entitled to \$249,637,000 on the exercise of all of its rights under the Intercompany Agreement, which would generate tax of \$87,338,000. MI does not currently intend to exercise its right to sell under the Intercompany Agreement (although it may in the future elect to do so). There is no assurance, however, that MI's efforts to extend the maturity of or refinance these notes will be successful. In that case MI will have to consider exercising its rights under the Intercompany Agreement, selling all or a part of one or more of its operating [subsidiaries](#), or some combination of these and other alternatives. MI's level of indebtedness and its lack of liquidity pose substantial risks to MI and the holders of its debt securities. The inability to refinance the notes successfully could have a material adverse impact on MII's liquidity, financial position and results of operations.

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

CAUTIONARY STATEMENT CONCERNING FORWARD-LOOKING STATEMENTS

We are including the following discussion to inform our existing and potential security holders generally of some of the risks and uncertainties that can affect [our company](#) and to take advantage of the "safe harbor" protection for forward-looking statements that applicable federal securities law affords.

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From time to time, our management or persons acting on our behalf make forward-looking statements to inform existing and potential security holders about [our company](#). These statements may include projections and estimates concerning the timing and success of specific projects and our future backlog, revenues, income and capital spending. Forward-looking statements are generally accompanied by words such as "estimate," "project," "predict," "believe," "expect," "anticipate," "plan," "goal" or other words that convey the uncertainty of future events or outcomes. In addition, sometimes we will specifically describe a statement as being a forward-looking statement and refer to this cautionary statement.

In addition, various statements this Quarterly Report on Form 10-Q contains, including those that express a belief, expectation or intention, as well as those that are not statements of historical fact, are forward-looking statements. These forward-looking statements speak only as of the date of this report, we disclaim any obligation to update these statements, and we caution you not to rely on them unduly. We have based these forward-looking statements on our current expectations and assumptions about future events. While our management considers these expectations and assumptions to be reasonable, they are inherently subject to significant business, economic, competitive, regulatory and other risks, contingencies and uncertainties, most of which are difficult to predict and many of which are beyond our control. These risks, contingencies and uncertainties relate to, among other matters, the following:

- o general economic and business conditions and industry trends;
- o the continued strength of the industries in which we are involved;
- o decisions about offshore developments to be made by oil and gas companies;
- o the deregulation of the U.S. electric power market;
- o the highly competitive nature of our businesses;
- o our future financial performance, including availability, terms and deployment of capital;
- o the continued availability of qualified personnel;
- o changes in, or our failure or inability to comply with, government regulations and adverse outcomes from legal and regulatory proceedings, including the results of ongoing governmental investigations and related civil lawsuits involving alleged anticompetitive practices in our marine construction business;
- o estimates for pending and future nonemployee asbestos claims against B&W and potential adverse developments that may occur in the Chapter 11 reorganization proceedings involving B&W and certain of its [subsidiaries](#);
- o changes in existing environmental regulatory matters;
- o rapid technological changes;
- o difficulties we may encounter in obtaining regulatory or other necessary approvals of any strategic transactions;

- o social, political and economic situations in foreign countries where we do business;

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- o effects of asserted and unasserted claims; and
- o our ability to obtain surety bonds and letters of credit.

We believe the items we have outlined above are important factors that could cause our actual results to differ materially from those expressed in a forward-looking statement made in this report or elsewhere by us or on our behalf. We have discussed many of these factors in more detail elsewhere in this report. These factors are not necessarily all the important factors that could affect us. Unpredictable or unknown factors we have not discussed in this report could also have material adverse effects on actual results of matters that are the subject of our forward-looking statements. We do not intend to update our description of important factors each time a potential important factor arises. We advise our security holders that they should (1) be aware that important factors not referred to above could affect the accuracy of our forward-looking statements and (2) use caution and common sense when considering our forward-looking statements.

GENERAL

The amount of revenues we generate from our Marine Construction Services segment largely depends on the level of oil and gas development activity in the world's major hydrocarbon producing regions. Our revenues from this segment reflect the variability associated with the timing of significant development projects. Although oil and gas prices have increased over the past year, this is not expected to have a significant impact on our Marine Construction Services' customers' exploration and production spending for the first half of 2001. Consequently, we do not expect our Marine Construction Services segment's revenues to increase significantly until the second half of 2001. During 2001, we should begin to see modest benefits from stronger marine construction results, followed by more substantial improvements in 2002. Although the timing of the award of many marine construction projects remains uncertain, we believe this segment's backlog should continue to increase for the foreseeable future.

The revenues of our Government Operations segment are largely a function of capital spending by the U.S. Government. As a result of reductions in the defense budget over the past several years, we do not expect this segment to experience any significant growth in the next three years. We expect this segment's backlog to remain relatively constant since it is the sole supplier to the U.S. Navy of nuclear fuel assemblies and major nuclear reactor components for the Naval Reactors Program. We currently expect the 2001 operating activity of this segment will be about the same as in 2000.

The revenues of our Industrial Operations segment are affected by variations in the business cycles in its customers' industries and the overall economy. Legislative and regulatory issues such as environmental regulations and fluctuations in U.S. Government funding patterns also affect this segment. We currently expect the 2001 operating activity of this segment will be about the same as in 2000.

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After net interest expense, other expenses and taxes, we expect net results to be positive in the next quarter. We expect profitability to improve in each of the final three quarters of 2001 as JRM markets recover and as the Y-12 and Pantex [contracts](#) recently awarded to BWXT increase income from investees in Government Operations during the second half of the year.

Effective [February 22, 2000](#) and until B&W and its filing [subsidiaries](#) emerge from the Chapter 11 reorganization proceedings and the subsequent accounting is determined, we no longer consolidate B&W's and its [subsidiaries](#)' results of operations in our condensed consolidated financial statements and our investment in B&W is presented on the cost method. Through [February 21, 2000](#), B&W's and its [subsidiaries](#)' results are included in our segment results under Power Generation Systems - B&W (see Note 5 to the condensed consolidated financial statements). B&W and its consolidated [subsidiaries](#)' pre-bankruptcy filing revenues of \$155,774,000 and operating income of \$9,410,000 are included in our consolidated financial results for the three months ended [March 31, 2000](#).

In general, each of our business segments is composed of capital-intensive businesses that rely on large [contracts](#) for a substantial amount of their revenues.

We evaluate the realizability of our long-lived assets, including property, plant and equipment and goodwill, whenever events or changes in circumstances indicate that we may not be able to recover the carrying amounts of those assets. We carry our property, plant and equipment at cost, reduced by provisions to recognize economic impairment when we determine impairment has occurred.

We derive a significant portion of our revenues from foreign operations. As a result, international factors, including variations in local economies and changes in foreign currency exchange rates affect our revenues and operating results. We use derivative financial instruments, primarily forward [contracts](#), to reduce the impact of changes in foreign exchange rates on operating results. We use these instruments primarily to hedge our exposure associated with revenues or costs on our long-term [contracts](#) which are denominated in currencies other than our operating entities' functional currencies. Because we generally do not hedge beyond our exposure, we believe this practice minimizes the impact of foreign exchange rate movements on our operating results.

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RESULTS OF OPERATIONS - THREE MONTHS ENDED MARCH 31, 2001 VS. THREE MONTHS ENDED MARCH 31, 2000

Marine Construction Services

Revenues decreased \$71,955,000 to \$134,680,000 due to lower volume in offshore activities in the Far East relating to the West Natuna project. Higher volumes from engineering and North American activities partially offset this decrease.

Segment operating loss increased \$4,629,000 to \$10,416,000, primarily due to lower volume in offshore activities in the Far East relating to the West Natuna project. Higher volumes and margins in North American activities and lower general and administrative expenses partially offset these decreases.

Loss from investees decreased \$7,500,000 to \$46,000, primarily due to higher operating results in our Mexican and SPARS joint ventures. The prior year included higher losses associated with our U.K. fabrication joint venture.

Government Operations

Revenues increased \$6,143,000 to \$120,863,000, primarily due to higher volumes from nuclear fuel assemblies and reactor components for the U.S. Government and commercial work. Lower volumes from other government operations and management and operating [contracts](#) for U.S. Government-owned facilities partially offset these increases.

Segment operating income decreased \$2,296,000 to \$11,047,000, primarily due to lower margins from management and operating [contracts](#) for U.S. Government-owned facilities and lower volumes and margins from other government operations. Higher volumes and margins from commercial work and lower general and administrative expenses partially offset these decreases.

Income from investees increased \$3,350,000 to \$4,702,000, primarily due to higher operating results from a joint venture in Idaho and the start-up of our Pantex and Y-12 joint ventures.

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Industrial Operations

Revenues increased \$53,686,000 to \$168,928,000, primarily due to higher volumes from engineering and plant maintenance activities in Canadian operations and from air-cooled heat exchangers.

Power Generation Systems

Revenues increased \$8,352,000 to \$8,434,000, primarily due to the acquisition of various business units of the Ansaldo Volund Group, an international power generation operation.

Income (loss) from investees increased \$1,100,000 from a loss of \$865,000 to income of \$235,000, primarily due to the operating loss of a certain foreign joint venture exited in the prior year.

Other Income Statement Items

Interest income decreased \$1,297,000 to \$5,848,000, primarily due to a decrease in investments.

Interest expense increased \$1,308,000 to \$10,131,000, primarily due to changes in prevailing interest rates.

Other-net decreased \$4,585,000 from income of \$2,413,000 to a loss of \$2,172,000. The three months ended [March 31, 2001](#) includes an impairment loss of approximately \$2,800,000 relating to available-for-sale securities whose decline in value has been judged to be other than temporary.

The provision for income taxes increased \$618,000 to \$3,935,000, while the income (loss) before provision for income taxes decreased \$11,682,000 from income of \$11,184,000 to a loss of \$498,000. The change in the relationship of pretax income to the provision for income taxes primarily resulted from earnings decreasing in non-taxable jurisdictions. The provision for the three months ended [March 31, 2001](#) and [2000](#) reflect non-deductible amortization of goodwill of \$4,502,000. The goodwill was created by the premium we paid on the acquisition of the minority interest in JRM in June 1999. Income taxes in the three months ended [March 31, 2000](#) also include a provision of \$3,800,000 for B&W for the pre-filing period. Also included are tax benefits relating to favorable tax settlements in foreign jurisdictions totaling approximately \$2,300,000 and \$5,500,000 at [March 31, 2001](#) and [2000](#), respectively. We operate in many different tax jurisdictions. Within these jurisdictions, tax provisions vary because of nominal rates, allowability of deductions, credits and other benefits and tax bases (for example, revenue versus income). These variances, along with variances in our mix of income from these jurisdictions, are responsible for shifts in our effective tax rate.

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Backlog

[\[Download Table\]](#)

	<u>3/31/01</u>	<u>12/31/00</u>
	<i>(Unaudited)</i>	
	<i>(In thousands)</i>	
Marine Construction Services	\$ 807,241	\$ 541,647
Government Operations	972,819	1,078,803
Industrial Operations	475,393	396,429
Power Generation Systems	43,790	48,631
	-----	-----
TOTAL BACKLOG	\$2,299,243	\$2,065,510
	=====	=====

Backlog for the Marine Construction Services segment increased primarily because of recent awards of new offshore construction programs.

At [March 31, 2001](#), Government Operations' backlog with the U. S. Government was \$926,078,000 (of which \$9,835,000 had not been funded). This segment's backlog is not expected to experience significant growth as a result of reductions in defense budgets. However, management expects this segment's backlog to remain relatively constant since it is the sole source provider of nuclear fuel assemblies and nuclear reactor components for the U. S. Government.

Liquidity and Capital Resources

During the three months ended [March 31, 2001](#), our cash and cash equivalents decreased \$27,583,000 to \$57,037,000 and total debt decreased \$49,796,000 to \$369,707,000, primarily due to a decrease in short-term borrowings of \$48,838,000. During this period, we received cash of \$388,901,000 from sales and maturities of investments and \$543,000 from the sale of assets. We used cash of \$348,883,000 for the purchase of investments, \$12,813,000 in operating activities and \$7,764,000 for additions to property, plant and equipment.

At [March 31, 2001](#) and [December 31, 2000](#), we had available various uncommitted short-term lines of credit from banks totaling \$12,439,000 and \$12,819,000, respectively. There were no borrowings against these lines at [March 31, 2001](#) or [December 31, 2000](#).

On [February 21, 2000](#), B&W and certain of its [subsidiaries](#) entered into the DIP Credit Facility to satisfy their working capital and letter of credit needs during the pendency of their bankruptcy case. As a condition to borrowing or obtaining letters of credit under the DIP Credit Facility, B&W must comply with certain financial covenants. There were no borrowings under this facility at [March 31, 2001](#) or

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[December 31, 2000](#). See Note 8 to the condensed consolidated financial statements for further information on the DIP Credit Facility.

On [February 21, 2000](#), we also entered into other financing arrangements providing financing to the balance of our operations. This financing, as amended on [April 24, 2000](#), consists of a \$200,000,000 credit facility for MII, BWXT and Hudson Products Corporation (the "[MII Credit Facility](#)") and a \$200,000,000 credit facility for JRM and its [subsidiaries](#) (the "[JRM Credit Facility](#)"). Each facility is with a group of lenders, for which Citibank, N.A. is acting as the administrative agent.

The MII Credit Facility consists of two tranches, each of which has a three-year term. One is a revolving credit facility that provides for up to \$100,000,000 to the borrowers. Borrowings under this facility may be used for working capital and general corporate purposes. The second tranche provides for up to \$200,000,000 of letters of credit and may be used to reimburse issuers for drawings under certain outstanding letters of credit totaling \$31,519,000 issued for the benefit of B&W and its [subsidiaries](#). The aggregate amount of loans and amounts available for drawing under letters of credit outstanding under the MII Credit Facility may not exceed \$200,000,000. This facility is secured by a collateral account funded with various U.S. government securities with a marked-to-market value equal to 105% of the aggregate amount available for drawing under letters of credit and revolving credit borrowings then outstanding. Borrowings against this facility at [March 31, 2001](#) and [December 31, 2000](#) were \$20,000,000 and \$10,000,000, respectively. Borrowings increased to \$40,000,000 as of [May 8, 2001](#). Letters of credit against this facility outstanding at [March 31, 2001](#) totaled approximately \$51,000,000.

The JRM Credit Facility also consists of two tranches. One is a revolving credit facility that provides for up to \$100,000,000 for advances to borrowers. Borrowings under this facility may be used for working capital and general corporate purposes. The second tranche provides for up to \$200,000,000 of letters of credit. The aggregate amount of loans and amounts available for drawing under letters of credit outstanding under the JRM Credit Facility may not exceed \$200,000,000. The facility is subject to certain financial and non-financial covenants. Borrowings against this facility at [March 31, 2001](#) and [December 31, 2000](#) were \$25,000,000 and \$50,000,000, respectively. Borrowings increased to \$30,000,000 as of [May 8, 2001](#). Letters of credit outstanding against this facility at [March 31, 2001](#) totaled approximately \$68,000,000.

At [March 31, 2001](#), we had total cash, cash equivalents and investments of \$380,014,000. Our investment portfolio consists primarily of government obligations and other investments in debt

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securities. The fair value of our investments at [March 31, 2001](#) was \$322,977,000. As of [March 31, 2001](#), we had pledged approximately \$44,742,000 fair value of these investments to secure a letter of credit in connection with certain reinsurance agreements. In addition, approximately \$206,159,000 fair value of these investments were pledged to secure the MII Credit Facility. We had free cash available totaling approximately \$46,000,000 at [March 31, 2001](#).

In connection with B&W's bankruptcy filing, MII entered into a support agreement pursuant to which it agreed to provide MI with standby financial support on its interest payments on its (i) \$225,000,000 in aggregate principal amount of 9.375% Notes due 2002, (ii) \$9,500,000 in aggregate principal amount of Series A Medium Term Notes due 2003, (iii) \$64,000,000 in aggregate principal amount of Series B Medium Term Notes due 2005, 2008 and 2023, and (iv) \$17,000,000 in principal amount under a Pollution Control Note due 2009. MI is required to pay MII \$5,000 per month under the support agreement which expires on [March 15, 2002](#).

MI's 9.375% notes with an aggregate principal amount of \$225,000,000 are scheduled to mature on [March 15, 2002](#). MI currently has insufficient cash and other liquid resources on hand to fund the repayment of its 9.375% notes. However, MI owns substantial [subsidiaries](#) outside the B&W Chapter 11 filing, including BWXT which comprises our Government Operations segment and Hudson Products Corporation which operates our heat exchanger business. In addition, MI has a financial asset pursuant to a stock purchase and sale agreement with MII (the "*Intercompany Agreement*"). For the 2001 year, MI would be entitled to \$249,637,000 on the exercise of all of its rights under that agreement, which would generate tax of \$87,338,000.

We are currently exploring various alternatives relative to extending the maturity of these notes, as well as other potential refinancing alternatives. We expect these efforts will be successful. MI does not currently intend to exercise its right to sell under the Intercompany Agreement (although it may in the future elect to do so). There is no assurance, however, that MI's efforts to extend the maturity of or refinance these notes will be successful. In that case MI will have to consider exercising its rights under

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the Intercompany Agreement, selling all or a part of one or more of its operating [subsidiaries](#), or some combination of these and other alternatives. MI's level of indebtedness and its lack of liquidity pose substantial risks to MI and the holders of its debt securities. The inability to refinance the notes successfully could have a material adverse impact on the MII's liquidity, financial position and results of operations.

MI and JRM and their respective [subsidiaries](#) are restricted, as a result of covenants in debt instruments, in their ability to transfer funds to MII and its other [subsidiaries](#) through cash dividends or through unsecured loans or investments. At [March 31, 2001](#), substantially all the net assets of MI were subject to those restrictions. At [March 31, 2001](#), JRM and its [subsidiaries](#) could make unsecured loans to or investments in MII and its other [subsidiaries](#) of approximately \$72,000,000.

Our two surety companies have notified us that they are no longer willing to issue bonds on our behalf. We obtain surety bonds in the ordinary course of business of several of our operations to secure [contract](#) bids and to meet the bonding requirements of various construction and other [contracts](#) with customers. We are currently negotiating with other surety companies. We expect to obtain the coverage we require through other surety companies as well as using our existing credit facilities for [contract](#)-related performance guarantees. This issue primarily affects B&W and its [subsidiaries](#). We do not expect this situation to impact MII's liquidity negatively for the foreseeable future.

We expect to incur negative cash flows in the next quarter of 2001, with the third and fourth quarters returning to a positive cash flow position. We expect to meet capital expenditure, working capital and debt maturity requirements from cash and cash equivalents and short-term borrowings.

MI and its [subsidiaries](#) are unable to incur additional long-term debt obligations under one of MI's public debt [indentures](#), other than in connection with certain extension, renewal or refunding transactions (including an extension or refinancing of MI's 9.375% notes).

As a result of its bankruptcy filing, B&W and its filing [subsidiaries](#) are precluded from paying dividends to shareholders and making payments on any pre-bankruptcy filing accounts or notes payable that are due and owing to any other entity within the McDermott group of companies (the "*Pre-Petition Inter-company Payables*") and other creditors during the pendency of the bankruptcy case, without the Bankruptcy Court's approval.

We believe that the bankruptcy filing and the weak Marine Construction Services markets contributed to the reduction in our credit rating in June 2000 from BA1 to BA3 by Moody's Investor

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Service and from BB+ to B in December 2000 by Standard & Poors and, consequently, could adversely impact our access to capital. As a result, we have assessed our ability to continue as a going concern and have concluded that we can continue to fund our operating activities and capital requirements for the foreseeable future.

At [March 31, 2001](#), we had a valuation allowance for deferred tax assets of \$15,959,000, which cannot be realized through carrybacks and future reversals of existing taxable temporary differences. We believe that our remaining deferred tax assets are realizable through carrybacks and future reversals of existing taxable temporary differences, future taxable income and, if necessary, the implementation of tax planning strategies involving sales of appreciated assets. Uncertainties that affect the ultimate realization of our deferred tax assets include the risk of incurring losses in the future and the possibility of declines in value of appreciated assets involved in the tax planning strategies we have identified. We have considered these factors in determining our valuation allowance. We will continue to assess the adequacy of our valuation allowance on a quarterly basis.

We have evaluated and expect to continue evaluating possible strategic acquisitions, some of which may be material. At any given time we may be engaged in discussions or negotiations or enter into agreements relating to potential acquisition transactions.

The Babcock & Wilcox Company

B&W and its [subsidiaries](#) conduct substantially all of the operations of our Power Generation Systems segment. The amount of revenues we generate from our Power Generation Systems segment primarily depends on capital spending by customers in the electric power generation industry. In that industry, persistent economic growth in the United States has brought the supply of electricity into approximate balance with energy demand, except during periods of peak demand. Electric power producers have generally been meeting these peaks with new combustion turbines rather than new base-load capacity. In January, 2001, the state of California experienced shortages of electricity during periods of peak demand. This has caused many power companies to re-examine their needs for new power plants and for improvements at existing power plants. Depending on the outcome of these studies, power companies may order new plants and may improve their existing plants. New U.S. emissions requirements have also prompted some customers to place orders for environmental equipment. Domestic demand for electrical power generation industry services and replacement nuclear steam generators continues at strong levels. The international markets remain unsettled.

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We currently expect the 2001 operating activity of this segment will be about the same as in 2000.

B&W's financial results are included in our consolidated results through [February 21, 2000](#), the day prior to B&W's Chapter 11 filing. However, generally accepted accounting principles specifically require that any entity whose financial statements were previously consolidated with those of its parent (as B&W's were with ours) that files for protection under the U.S. Bankruptcy Code, whether solvent or insolvent, must be prospectively deconsolidated from the parent and presented on the cost method. The cost method requires us to present the net assets of B&W at [February 22, 2000](#) as an investment and not recognize any income or loss from B&W in our results of operations during the reorganization period. This investment of \$186,966,000 as of [March 31, 2001](#) is subject to periodic reviews for recoverability. When B&W emerges from the jurisdiction of the Bankruptcy Court, the subsequent accounting will be determined based upon the applicable circumstances and facts at such time, including the terms of any [plan of reorganization](#). See Note 8 to the condensed consolidated financial statements for B&W's financial information at [March 31, 2001](#).

In the three months ended [March 31, 2001](#):

B&W's revenues increased \$83,292,000 to \$355,859,000, primarily due to higher volumes from the fabrication and erection of fossil fuel steam and environmental control systems, fabrication, repair and retrofit of existing facilities, replacement parts and nuclear services;

B&W's operating income increased \$4,523,000 to \$20,893,000, primarily due to higher volumes from fabrication and erection of fossil fuel steam and environmental control systems and replacement parts and higher volumes and margins from the fabrication, repair and retrofit of existing facilities and nuclear services. In addition, B&W experienced lower sales and marketing expenses. Lower margins from replacement nuclear steam generators, higher reorganization expenses associated with the Chapter 11 filing and lower operating results from a joint venture located in Canada partially offset these increases. In addition, B&W experienced favorable employee benefit adjustments in the prior year, primarily due to income from over-funded pension plans;

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Other net expense for the three months ended [March 31, 2001](#) includes an impairment loss of \$3,000,000 relating to available-for-sale securities whose decline in value had been judged to be other than temporary.

B&W's backlog at [March 31, 2001](#) and [December 31, 2000](#) was \$1,343,879,000 and \$1,030,628,000, respectively.

In connection with the bankruptcy filing, B&W and its filing [subsidiaries](#) entered into the DIP Credit Facility with a group of lenders, with Citibank, N.A. as administrative agent, for a three-year term. The facility is subject to certain financial and non-financial covenants. See Note 8 to the condensed consolidated financial statements for further information on the DIP Credit Facility.

We have assessed B&W's liquidity position as a result of the bankruptcy filing and believe that B&W can continue to fund its and its [subsidiaries'](#) operating activities and meet its debt and capital requirements for the foreseeable future. However, the ability of B&W to continue as a going concern is dependent upon its ability to settle its ultimate asbestos liability from its net assets, future profits and cash flow and available insurance proceeds, whether through the confirmation of a [plan of reorganization](#) or otherwise. As a result of the bankruptcy filing and related events, there is no assurance that the carrying amounts of assets will be realized or that liabilities will be liquidated or settled for the amounts recorded. In addition, a rejection of our plan of reorganization could change the amounts reported in the B&W financial statements and cause a material decrease in the carrying amount of our investment in B&W. See Note 8 to the condensed consolidated financial statements for more information.

PART II

McDERMOTT INTERNATIONAL, INC.

OTHER INFORMATION

Item 1. [LEGAL PROCEEDINGS](#)

In March 1997, we, with the help of outside counsel, began an investigation into allegations of wrongdoing by a limited number of former employees of MII and JRM and others. The allegations concerned the heavy-lift business of JRM's HeereMac joint venture ("HeereMac") with Heerema Offshore Construction Group, Inc. ("Heerema") and the heavy-lift business of JRM. Upon becoming aware of these allegations, we notified authorities, including the Antitrust Division of the Department of Justice ("DOJ"), the Securities and Exchange Commission ("SEC") and the European Commission. As a result of our prompt disclosure of the allegations, MII and JRM and their officers, directors and employees at the time of the disclosure were granted immunity from criminal prosecution by the DOJ for any anti-

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competitive acts involving worldwide heavy-lift activities. In June 1999, the DOJ agreed to our request to expand the scope of the immunity to include a broader range of our marine construction activities and affiliates. We have cooperated fully with the investigations of the DOJ and the SEC into these matters. In February 2001, we were advised that the SEC has terminated its investigation and no enforcement action has been recommended.

On becoming aware of the allegations involving HeereMac, we initiated action to terminate JRM's interest in HeereMac, and, on [December 19, 1997](#), Heerema acquired JRM's interest in exchange for cash and title to several pieces of equipment. On [December 21, 1997](#), HeereMac and one of its employees pled guilty to criminal charges by the DOJ that they and others had participated in a conspiracy to rig bids in connection with the heavy-lift business of HeereMac in the Gulf of Mexico, the North Sea and the Far East. HeereMac and the HeereMac employee were fined \$49,000,000 and \$100,000, respectively. As part of the plea, both HeereMac and certain employees of HeereMac agreed to cooperate fully with the DOJ investigation. Neither MII, JRM nor any of their officers, directors or employees was a party to those proceedings.

In July 1999, a former JRM officer pled guilty to charges brought by the DOJ that he participated in a bid-rigging conspiracy for the sale of marine construction services in the U.S. Gulf of Mexico and elsewhere. In May 2000, another former JRM officer was indicted by the DOJ for participating in a bid-rigging conspiracy for the sale of marine construction services in the Gulf of Mexico. His trial was held in February 2001 and at the conclusion of the Government's case, the presiding Judge directed a judgment of acquittal. Also in February 2001, we were advised that the SEC has terminated its investigation and no enforcement action has been recommended.

We have cooperated with the DOJ in its investigation. The DOJ also has requested additional information from us relating to possible anti-competitive activity in the marine construction business of McDermott-ETPM East, Inc., one of the operating companies within JRM's former McDermott-ETPM joint venture with ETPM S.A., a French company. In connection with the termination of the McDermott-ETPM joint venture on [April 3, 1998](#), JRM assumed 100% ownership of McDermott-ETPM East, Inc., which was renamed J. Ray McDermott Middle East, Inc.

In June 1998, Phillips Petroleum Company (individually and on behalf of certain co-venturers) and several related entities (the "*Phillips Plaintiffs*") filed a lawsuit in the United States District Court for the Southern District of Texas against MII, JRM, MI, McDermott-ETPM, Inc., certain JRM [subsidiaries](#), HeereMac, Heerema, certain Heerema affiliates and others, alleging that the defendants engaged in anti-

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competitive acts in violation of Sections 1 and 2 of the Sherman Act and Sections 15.05 (a) and (b) of the Texas Business and Commerce Code, engaged in fraudulent activity and tortiously interfered with the plaintiffs' businesses in connection with certain offshore transportation and installation projects in the Gulf of Mexico, the North Sea and the Far East (the "*Phillips Litigation*"). In December 1998, Den norske stats oljeselskap a.s., individually and on behalf of certain of its ventures and its participants (collectively "*Statoil*"), filed a similar lawsuit in the same court (the "*Statoil Litigation*"). In addition to seeking injunctive relief, actual damages and attorneys' fees, the plaintiffs in the Phillips Litigation and Statoil Litigation have requested punitive as well as treble damages. In January 1999, the court dismissed without prejudice, due to the court's lack of subject matter jurisdiction, the claims of the Phillips Plaintiffs relating to alleged injuries sustained on any foreign projects. In July 1999, the court also dismissed the Statoil Litigation for lack of subject matter jurisdiction. Statoil appealed this dismissal to the Fifth Circuit Court of Appeals. The Fifth Circuit affirmed the district court decision in February 2000. Statoil filed a motion for rehearing en banc which was denied on [March 12, 2001](#). In September 1999, the Phillips Plaintiffs filed notice of their request to dismiss their remaining domestic claims in the lawsuit in order to seek an appeal of the dismissal of their claims on foreign projects, which request was subsequently denied.

In June 1998, Shell Offshore, Inc. and several related entities also filed a lawsuit in the United States District Court for the Southern District of Texas against MII, JRM, MI, McDermott-ETPM, Inc., certain JRM [subsidiaries](#), HeereMac, Heerema and others, alleging that the defendants engaged in anti-competitive acts in violation of Sections 1 and 2 of the Sherman Act (the "*Shell Litigation*"). Subsequently, the following parties (acting for themselves and, in certain cases, on behalf of their respective co-venturers and for whom they operate) intervened as plaintiffs in the Shell Litigation: Amoco Production Company and B.P. Exploration & Oil, Inc.; Amerada Hess Corporation; Conoco Inc. and certain of its affiliates; Texaco Exploration and Production Inc. and certain of its affiliates; Elf Exploration UK PLC and Elf Norge a.s.; Burlington Resources Offshore, Inc.; The Louisiana Land & Exploration Company; Marathon Oil Company and certain of its affiliates; VK-Main Pass Gathering Company, L.L.C., Green Canyon Pipeline Company, L.L.C.; Delos Gathering Company, L.L.C.; Chevron U.S.A. Inc. and Chevron Overseas Petroleum Inc.; Shell U.K. Limited and certain of its affiliates; Woodside Energy, Ltd; and Saga Petroleum, S.A.. Also, in December 1998, Total Oil Marine p.l.c. and Norsk Hydro Produksjon a.s., individually and on behalf of their respective co-venturers, filed similar lawsuits in the same court, which lawsuits were consolidated with the Shell Litigation. In addition to seeking injunctive relief, actual damages and attorneys' fees, the plaintiffs in the Shell Litigation request treble damages. In February 1999, we filed a motion to dismiss the foreign project claims of the

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plaintiffs in the Shell Litigation due to the Texas district court's lack of subject matter jurisdiction, which motion is pending before the court. Subsequently, the Shell Litigation plaintiffs were allowed to amend their complaint to include non-heavy lift marine construction activity claims against the defendants. Currently, we are awaiting the court's decision on our motion to dismiss the foreign claims. In the meantime, the Court has allowed limited discovery.

We recently learned that on [December 15, 2000](#), lawsuits were filed by a number of Norwegian oil companies against MII, Heeremac, Heerema and Saipem S.p.A. for violations of the Norwegian Pricing Act of 1953 in connection with projects in Norway. Plaintiffs include Norwegian affiliates of various of the plaintiffs in the Shell civil case pending in Houston. Most of the projects were performed by Saipem S.p.A. or its affiliates, with some by Heerema/HeereMac and none by MII. We understand that the conduct alleged by plaintiffs is the same conduct which plaintiffs allege in the U.S. civil cases. The first appearance is scheduled for [October 4, 2001](#) in Oslo.

As a result of the initial allegations of wrongdoing in March 1997, we formed and have continued to maintain a special committee of our Board of Directors to monitor and oversee our investigation into all of these matters.

It is not possible to predict the ultimate outcome of the DOJ investigation, our internal investigation, the above-referenced lawsuits or any actions that may be taken by others as a result of HeereMac's guilty plea or otherwise. These matters could result in civil and criminal liability and have a material adverse effect on our consolidated financial position and results of operations.

B&W and Atlantic Richfield Company ("[ARCO](#)") are defendants in a lawsuit filed by Donald F. Hall, Mary Ann Hall and others in the United States District Court for the Western District of Pennsylvania. The suit involves approximately 300 separate claims for compensatory and punitive damages relating to the operation of two former nuclear fuel processing facilities located in Pennsylvania (the "[Hall Litigation](#)"). The plaintiffs in the Hall Litigation allege, among other things, that they suffered personal injury, property damage and other damages as a result of radioactive emissions from these facilities. In September 1998, a jury found B&W and ARCO liable to eight plaintiffs in the first cases brought to trial, awarding \$36,700,000 in compensatory damages. In June 1999, the district court set aside the \$36,700,000 judgment and ordered a new trial on all issues. In November 1999, the district court allowed an interlocutory appeal by the plaintiffs of certain issues, including the granting of the new trial and the court's rulings on certain evidentiary matters, which, following B&W's bankruptcy filing, the Third Circuit Court of Appeals declined to accept for review. The plaintiffs' claims against B&W in the Hall

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Litigation have been automatically stayed as a result of the B&W bankruptcy filing. B&W has also filed a complaint for declaratory and injunctive relief with the Bankruptcy Court seeking to stay the pursuit of the Hall Litigation against ARCO during the pendency of B&W's bankruptcy proceeding due to common insurance coverage and the risk to B&W of issue or claim preclusion, which stay the Bankruptcy Court denied in October 2000. B&W has appealed this decision.

In 1998, B&W settled all pending and future punitive damage claims in the Hall Litigation for \$8,000,000 for which it seeks reimbursement from other parties. There is a controversy between B&W and its insurers as to the amount of coverage available under the liability insurance policies covering the facilities. B&W filed a declaratory judgment action in a Pennsylvania State Court seeking a judicial determination as to the amount of coverage available under the policies. On [April 28, 2001](#), in response to cross-motions for partial summary judgment, the Pennsylvania State Court issued its ruling regarding: (i) the applicable trigger of coverage under the Nuclear Energy Liability Policies issued by B&W's nuclear insurers; and (ii) the scope of the nuclear insurers' defense obligations to B&W under these policies. With respect to the trigger of coverage, the Pennsylvania State Court held that a "*manifestation*" trigger applied to the underlying claims at issue. Although the Court did not make any determination of coverage with respect to any of the underlying claims, we believe the effect of its ruling is to increase the amount of coverage potentially available to B&W under the policies at issue to \$320,000,000. With respect to the nuclear insurers' duty to defend B&W, the Court held that B&W is entitled to separate and independent counsel funded by the nuclear insurers. We believe that all claims under the Hall Litigation will be resolved within the limits of coverage of our insurance policies; but our insurance coverage may not be adequate and we may be materially adversely impacted if our liabilities exceed our coverage. B&W transferred the two facilities subject to the Hall Litigation to BWXT in June 1997 in connection with BWXT's formation and an overall corporate restructuring.

In December 1999 and early 2000, several persons who allegedly purchased shares of our common stock during the period from [May 21, 1999](#) through [November 11, 1999](#) filed four purported class action complaints against MII and two of its executive officers, Roger E. Tetrault and Daniel R. Gaubert, in the United States District Court for the Eastern District of Louisiana. Each of the complaints alleged that the defendants violated federal securities laws by disseminating materially false and misleading information and/or concealing material adverse information relating to our estimated liability for asbestos-related claims. Each complaint sought relief, including unspecified compensatory damages and an award for costs and expenses. The four cases were subsequently consolidated. In June 2000, the plaintiffs filed a consolidated amended complaint, and in July 2000, we filed a motion to dismiss all claims asserted in that complaint. In September 2000, the District Court dismissed with prejudice the plaintiffs' consolidated

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amended complaint for failure to state a claim upon which relief can be granted, which dismissal the plaintiffs appealed to the U.S. Fifth Circuit Court of Appeals in October 2000. On [April 25, 2001](#), the plaintiffs-appellants filed a motion to voluntarily dismiss their appeal and the appeal was dismissed by the U.S. Fifth Circuit Court on [April 26, 2001](#).

In December 1998, JRM was in the process of installing a deck module on a compliant tower in the Gulf of Mexico for Texaco Exploration and Production, Inc. ("*Texaco*") when the main hoist load line failed, resulting in the loss of the module. As a result, Texaco has withheld payment to JRM of \$23,000,000 due under the installation [contract](#), and, in January 2000, JRM instituted an arbitration proceeding against Texaco seeking the amount owed. Texaco has countered in the arbitration, claiming consequential damages for delays resulting from the incident, as well as costs incurred to complete the project with another contractor. Texaco has also filed a lawsuit against a number of other parties, claiming that they are responsible for the incident. It is our position that the [contract](#) between the parties prohibits Texaco's claims against JRM and JRM is entitled to the amount withheld.

In early April 2001, a group of insurance underwriters who have previously provided insurance to B&W under our excess liability policies filed (1) a complaint for declaratory judgment and damages against MII in the U.S. District Court for the Eastern District of Louisiana and (2) a declaratory judgment complaint against B&W in the U.S. Bankruptcy Court for the Eastern District of Louisiana. The insurance policies at issue in this litigation provide a significant portion of B&W's excess liability coverage available for the resolution of the asbestos-related claims that are the subject of the B&W Chapter 11 proceeding. The complaints contain substantially identical factual allegations. These include allegations that, in the course of settlement discussions with the representatives of the asbestos claimants in the B&W bankruptcy proceeding, MII and B&W breached the confidentiality provisions of an agreement they entered into with these insurers relating to insurance payments of the insurers as a result of asbestos claims. They also allege that MII and B&W have wrongfully attempted to expand the underwriters' obligations under that agreement and the applicable policies through the filing of a plan of reorganization in the B&W bankruptcy proceeding that contemplates the transfer of rights under that agreement and those policies to a trust that will manage the pending and future asbestos-related claims against B&W and certain of its affiliates. The complaints seek declarations that, among other things, the defendants are in material breach of the agreement with the insurers and that the plaintiff underwriters owe no further obligations to MII and B&W under that agreement. With respect to the insurance policies, if the insurers should succeed in terminating the agreement, they seek to litigate issues under the policies in order to reduce their coverage obligations. The complaint in the District Court case also seeks a recovery of unspecified compensatory damages. Management believes these complaints and the substantive allegations they

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contain are without merit. Management intends to contest and defend against these actions vigorously. In management's opinion, these complaints will not have a material adverse effect on our consolidated financial position or results of operations.

On [April 30, 2001](#), B&W filed a declaratory judgment action in its Chapter 11 proceeding against MI, BWICO, BWXT, Hudson Products Corporation and McDermott Technologies, Inc. seeking a judgment, among other things, that B&W was not insolvent at the time of, or rendered insolvent as a result of, a corporate reorganization that we completed in the fiscal year ended [March 31, 1999](#), which involved B&W's cancellation of a \$313,000,000 note receivable and B&W's transfer of all the capital stock of Hudson Products Corporation, Tracy Power, BWXT and McDermott Technologies, Inc. to BWICO, and that the transfers are not voidable. As an alternative, and only in the event that the Bankruptcy Court finds B&W insolvent at a pertinent time, the action preserves B&W's claims against the defendants. We believe that B&W was solvent at the time of the transfers and that the transfers are not voidable. However, if the declaratory judgment were adversely decided by the Bankruptcy Court, it could have a material adverse effect on our consolidated financial position and results of operations.

See Note 8 to the condensed consolidated financial statements regarding B&W's potential liability for non-employee asbestos claims and the Chapter 11 reorganization proceedings commenced by B&W and certain of its [subsidiaries](#) on [February 22, 2000](#).

Item 6. EXHIBITS AND REPORTS ON FORM 8-K

- (a) Exhibit 3.1 - McDermott International, Inc.'s Articles of Incorporation, as amended ([incorporated by reference](#) to Exhibit 3.1 of McDermott International, Inc.'s Form 10-K for the fiscal year ended [March 31, 1996](#)).

[Exhibit 3.2](#) - Amended and Restated [By-Laws](#) of McDermott International, Inc.

- (b) Reports on Form 8-K

There were no reports on Form 8-K filed during the three months ended [March 31, 2001](#).

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SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

McDERMOTT INTERNATIONAL, INC.

/s/ [Bruce F. Longaker](#)

By: [Bruce F. Longaker](#)
Executive Vice President and Chief
Financial Officer (Principal Financial
and Accounting Officer and Duly
Authorized Representative)

[May 11, 2001](#)

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EXHIBIT INDEX

[\[Download Table\]](#)

<u>Exhibit</u> -----	<u>Description</u> -----
3.1	McDermott International, Inc.'s Articles of Incorporation , as amended (incorporated by reference to Exhibit 3.1 of McDermott International, Inc.'s Form 10-K for the fiscal year ended March 31, 1996).
3.2	Amended and Restated By-laws of McDermott International, Inc.

Dates Referenced Herein and Documents Incorporated By Reference

<u><i>This 10-Q Filing</i></u>	<u><i>Date</i></u>	<u><i>Referenced-On Page</i></u>		<u><i>Other Filings</i></u>
		<u><i>First</i></u>	<u><i>Last</i></u>	
	3/31/96	<u>52</u>	<u>54</u>	10-K405, 10-K/A, 10-K405/A
	12/19/97	<u>12</u>	<u>47</u>	
	12/21/97	<u>12</u>	<u>47</u>	
	4/3/98	<u>13</u>	<u>47</u>	
	3/31/99	<u>17</u>	<u>52</u>	10-K, 10-K/A
	5/21/99	<u>16</u>	<u>50</u>	
	11/11/99	<u>16</u>	<u>50</u>	
	12/31/99	<u>33</u>		10-KT/A, 10-KT
	2/21/00	<u>19</u>	<u>45</u>	
	2/22/00	<u>10</u>	<u>52</u>	8-K
	3/31/00	<u>2</u>	<u>39</u>	10-Q
	4/24/00	<u>41</u>		
	12/15/00	<u>14</u>	<u>49</u>	
	12/31/00	<u>5</u>	<u>46</u>	10-K405, 10-K405/A
	1/1/01	<u>11</u>	<u>22</u>	
	2/20/01	<u>24</u>		
	2/22/01	<u>24</u>		
	3/12/01	<u>14</u>	<u>48</u>	
	3/29/01	<u>26</u>		
For The Period Ended	3/31/01	<u>1</u>	<u>52</u>	
	4/25/01	<u>16</u>	<u>51</u>	
	4/26/01	<u>16</u>	<u>51</u>	10-K405/A
	4/28/01	<u>15</u>	<u>50</u>	
	4/30/01	<u>1</u>	<u>52</u>	
	5/8/01	<u>41</u>		
	5/11/01	<u>53</u>		
Filed On / Filed As Of	5/15/01			
	5/23/01	<u>24</u>		
	7/17/01	<u>24</u>		
	7/30/01	<u>26</u>		
	10/4/01	<u>15</u>	<u>49</u>	
	12/31/01	<u>10</u>		10-K405
	3/15/02	<u>34</u>	<u>42</u>	

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