HORNBECK OFFSHORE SERVICES INC /LA
Form 10-K
March 01, 2007
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UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D.C. 20549

FORM 10-K

x **ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**
For the Fiscal Year Ended December 31, 2006

OR

¨ **TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**
For the Transition Period from _____ to _____

Commission File Number 333-69826

Hornbeck Offshore Services, Inc.

(Exact Name of Registrant as Specified in Its Charter)

Delaware	**72-1375844**
(State or other jurisdiction of incorporation or organization)	**(I.R.S. Employer Identification Number)**

103 Northpark Boulevard, Suite 300

Covington, Louisiana 70433

(985) 727-2000

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

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

Title of each class	**Name of exchange, on which registered**
Common Stock, $0.01 par value	**New York Stock Exchange**

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

None.

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

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

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

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

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

Large accelerated filer x Accelerated filer ¨ Non-accelerated filer ¨

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

The aggregate market value of the Common Stock held by non-affiliates computed by reference to the price at which the Common Stock was last sold as of the last day of registrant s most recently completed second fiscal quarter is $923,849,590.

The number of outstanding shares of Common Stock as of January 31, 2007 is 25,809,831 shares.

DOCUMENTS INCORPORATED BY REFERENCE

Portions of the Registrant s definitive 2007 proxy statement, anticipated to be filed with the Securities and Exchange Commission within 120 days after the close of the Registrant s fiscal year, are incorporated by reference into Part III of this Annual Report on Form 10-K.

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HORNBECK OFFSHORE SERVICES, INC. AND SUBSIDIARIES

FORM 10-K

FOR THE FISCAL YEAR ENDED DECEMBER 31, 2006

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PART I

ITEMS 1 AND 2. ***Business and Properties.***

Hornbeck Offshore Services, Inc. was incorporated under the laws of the State of Delaware in 1997. In this Annual Report on Form 10-K, references to company, we, us, our or like terms refer to Hornbeck Offshore Services, Inc. and its subsidiaries, except as otherwise indicated. References in this Annual Report on Form 10-K to OSVs mean offshore supply vessels; to MPSVs means multi-purpose supply vessels; to AHTS mean anchor-handling towing supply; to deepwater mean offshore areas, generally 1,000 to 5,000 in depth, and ultra-deepwater areas, generally more than 5,000 in depth; to deep well mean a well drilled to a true vertical depth of 15,000 or greater; and to new generation, when referring to OSVs, mean modern, deepwater-capable vessels subject to the regulations promulgated under the International Convention on Tonnage Measurement of Ships, 1969, which was adopted by the United States and made effective for all U.S.-flagged vessels in 1992 and foreign-flagged equivalent vessels.

BUSINESS

General

We are a leading provider of technologically advanced, new generation OSVs serving the offshore oil and gas industry, primarily in the U.S. Gulf of Mexico, or GoM, and in select international markets. The primary focus of our OSV business is on complex exploration and production activities, which include deepwater, ultra-deepwater, deep well and other logistically demanding projects. Such other projects include, among others, the construction, maintenance and repair of offshore infrastructure. We are also a leading transporter of petroleum products through our tug and tank barge, or TTB, segment serving the energy industry, primarily in the northeastern United States, the GoM and Puerto Rico. Although our vessels operate in domestic and international waters, all but two of our vessels are qualified under Section 27 of the Merchant Marine Act of 1920, also known as the Jones Act, to engage in the U.S. coastwise trade, from which foreign owned, built or crewed vessels are excluded.

In the mid-1990s, oil and gas producers began seeking large hydrocarbon reserves at deeper well depths using new, specialized drilling and production equipment. We recognized that the existing fleet of conventional 180 OSVs operating in the GoM was not designed to support these more complex projects or to operate in the challenging environments in which they were conducted. Therefore, in 1997, we began a program to construct new generation OSVs based upon our proprietary designs. Since that time, we have constructed 17 new generation OSVs using proprietary designs, and have expanded our fleet with the acquisitions of a total of six additional new generation OSVs, one fast supply vessel, two AHTS vessels, and two coastwise sulfur tankers, currently undergoing conversion into MPSVs. We currently have an additional 13 proprietary OSVs under construction. Our OSV fleet is among the youngest in the industry with an average age of approximately six years.

Our OSVs were purposefully designed with the flexibility to meet the diverse needs of our clients in all stages of their exploration and production activities. As a result, all of our OSVs have enhanced capabilities that allow them to more effectively support premium drilling

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equipment required for deep drilling and related specialty services. In contrast to conventional 180 OSVs, our vessels have dynamic positioning capability, as well as greater storage and off-loading capacity. We are capable of providing OSV services to our customers anywhere in the world. While we are committed to maintaining a critical mass of new generation OSVs operating in the GoM, we currently have vessels working offshore Trinidad and Mexico and are actively pursuing additional contracts in these and select other U.S and international markets.

Historically, demand for our OSV services has been primarily driven by the drilling of deep wells, whether in the deepwater, ultra-deepwater or on the U.S. Continental Shelf, and other complex exploration and production projects that require specialized drilling and production equipment. Our new generation OSVs are increasingly in demand by our customers for conventional drilling projects because of the ability of our OSVs to reduce overall offshore logistics costs for the customer through the vessel s greater capacities and operating efficiencies. We have also observed an increased interest in the enhanced capabilities of our OSVs by customers in non-oilfield services such as the U.S. military. Our new generation OSVs are also well suited to support logistically demanding drilling projects in remote frontier areas, where support infrastructure is severely limited.

Our TTB operating fleet consists of 13 ocean-going tugs and 18 ocean-going tank barges. During 2005, we took delivery of five proprietary double-hulled tank barges under our first TTB newbuild program and completed the retrofitting of two 6,100 horsepower tugs. These vessels added 600,000 barrels of new double-hulled capacity, more than replacing the barrel-carrying capacity lost when we retired three of our single-hulled tank barges from service at the end of 2004 as mandated by OPA 90. As part of the first TTB newbuild program, two additional 6,100 horsepower tugs were retrofitted and placed in service during the late first quarter of 2006. In September 2005, we announced our second TTB newbuild program comprised of approximately 400,000 barrels of double-hulled barge capacity and related tugs. We are currently retrofitting four recently acquired 3,000 horsepower tugs and constructing three 60,000-barrel newbuild double-hulled tank barges, which are expected to increase the double-hulled capacity of our TTB fleet by nearly 30% by the end of 2007. The deliveries of these vessels are anticipated on various dates throughout 2007. The retrofit and construction costs for these seven vessels are expected to be $70 million in the aggregate. We continue to explore options with respect to the remaining 220,000 barrels of barge capacity that are contemplated under this program.

We believe that our TTB business complements our OSV business by providing additional revenue and geographic diversification, while allowing us to offer another line of services to integrated oil and gas companies. For example, we have been successful in deploying our TTB equipment to non-traditional markets, such as supporting deepwater well testing and other specialty applications for our upstream customers in the GoM. However, demand for our TTB services has historically been driven by the level of refined petroleum product consumption in the northeastern United States and Puerto Rico, our core operating markets. The Energy Information Administration, or EIA, projects that refined petroleum product consumption in the East Coast region of the United States will increase by an average of 1.1% per year from 2007 to 2011. Demand for refined petroleum products is primarily driven by population growth, the strength of the U.S. economy, seasonal weather patterns, oil prices and competition from alternate energy sources.

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Offshore Supply Vessels

The OSV Industry

OSVs primarily serve exploratory and developmental drilling rigs and production facilities and support offshore construction and subsea maintenance activities. OSVs differ from other types of marine vessels in their cargo carrying flexibility and capacity. In addition to transporting deck cargo, such as pipe or drummed material and equipment, OSVs also transport liquid mud, potable and drilling water, diesel fuel, dry bulk cement and personnel between shore bases and offshore rigs and facilities. In general, demand for OSVs, as evidenced by dayrates and utilization rates, is primarily related to offshore oil and natural gas exploration, development and production activity, which in turn is influenced by a number of factors, including oil and natural gas prices and the drilling budgets of offshore exploration and production companies.

OSVs operate worldwide, but are generally concentrated in relatively few offshore regions with high levels of exploration and development activity such as the GoM, the North Sea, Southeast Asia, West Africa, Latin America and the Middle East. While there is some vessel migration between regions, key factors such as mobilization costs, vessel suitability and government statutes prohibiting foreign-flagged vessels from operating in certain waters generally limit such migration.

The GoM is a critical oil and natural gas supply basin for the United States. Since the late 1990 s, the primary emphasis for the exploratory efforts of offshore operators has increasingly been in the deepwater and ultra-deepwater areas of the GoM rather than the shallow waters of the Continental Shelf. According to the Minerals Management Service, or MMS, from the first major deepwater leasing boom in 1995 to March 2006, oil production grew 525% to 950 thousand barrels per day and natural gas production grew 663% to 3.8 billion cubic feet per day. Recent discoveries of large hydrocarbon reserves in deepwater fields in the GoM and at deeper well depths on the Continental Shelf have resulted in increased developmental and exploratory drilling activities in these areas. The deepwater region of the GoM is an increasingly important source of oil and natural gas production with many unexplored areas of potential oil and natural gas reserves. According to the report, Deepwater Gulf of Mexico 2006: Americas Expanding Frontier, published by the MMS, there have been over 980 exploration wells drilled in the deepwater GoM since 1995 with at least 126 announced deepwater discoveries over the same time period. Twenty two deepwater discoveries have been announced over the last seven years in water depths greater than 7,000 feet. Additionally, the pending expiration of leases with substantial reserve potential is expected to stimulate further exploration and development in the GoM.

While the shallow waters of the Continental Shelf have been actively explored for decades, until recently, relatively few deep wells have been drilled due to the historically high cost associated with such wells. Based on information received from our customers, the dry hole cost of a typical Continental Shelf well drilled from 8,000 to 12,000 generally ranges from $4 million to $8 million, while the dry hole cost for a deep well drilled in a similar location but to 15,000 or more can range from $10 million to $75 million. The higher costs associated with the drilling of deep wells can be attributed to, among other things, the need for specialized, high-end drilling rigs and related equipment, greater volumes of downhole materials such as liquid mud, tubular products and cement, and longer drilling times.

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Despite the higher costs associated with deep well Continental Shelf drilling, operators, especially those in search of natural gas, have continued to demonstrate interest. This interest is driven by, among other things, natural gas prices and the potential for the discovery of significant natural gas reserves. The abundance of existing platforms, production facilities and pipelines on the Continental Shelf allow newly discovered deep gas to flow quickly to market. In addition, MMS data indicates that large new reservoirs potentially offer higher production rates at deep depths than in more mature, shallower well areas. Furthermore, in order to stimulate drilling deeper wells in shallow water depths, the MMS enacted royalty relief in these areas of the Continental Shelf in 2001, expanded the program in August 2003 and again in January 2004. As recently as January 2006, the MMS offered additional relief to lessees or operators that drill wells deeper than 25,000 total vertical depth below the ocean surface. These factors partly compensate for the higher drilling costs of deep wells on the Continental Shelf. While overall natural gas production from the shelf has declined, from 4.8 tcf in 1997 to 3.4 tcf in 2002, leasing activity in water depths less than 500 feet increased from a low of 160 total block leases in 1999 to 580 total block leases in 2005.

In 2006, the MMS estimated that there may be up to 233 tcf of undiscovered, conventionally recoverable, deep well natural gas on the Continental Shelf. This potential reserve base compares favorably to the current total of approximately 28 tcf of proven natural gas reserves in the entire GoM. According to the MMS, in 2005 the deepwater region accounted for 73% of total GoM oil production and 39% of total GoM natural gas production, up substantially from 4% and 1%, respectively, in 1990.

Because oil and natural gas exploration, development and production costs in the shallow well Continental Shelf market are generally lower than those in the deepwater or deep well environments, shallow well drilling activity on the Continental Shelf is typically more sensitive to fluctuations in commodity prices, particularly the price of natural gas. Accordingly, actual or anticipated decreases in oil and natural gas prices generally result in reduced offshore drilling activity and correspondingly lower demand for the conventional 180 OSVs serving the shallow well Continental Shelf market. This causes a corresponding decline in OSV dayrates and utilization rates in that market. In contrast, the relatively larger capital commitments and longer lead times and investment horizons associated with deepwater, particularly ultra-deepwater, and deep well developments make it less likely that an operator will abandon such projects in response to a short-term decline in oil or natural gas prices. We believe that dayrates and utilization rates for new generation OSVs that serve the deepwater and deep well markets generally experience less volatility compared to conventional 180 OSVs and are, therefore, generally less sensitive to short-term commodity price fluctuations.

The Market for New Generation OSVs

Complex exploration and production projects require specialized equipment and higher volumes of supplies to meet the more difficult operating environment associated with such offshore developments. In order to better serve these projects and meet customer demands, new generation OSVs, including our entire OSV fleet, are designed with larger capacities, including greater liquid mud and dry bulk cement capacities, as well as larger areas of open deck space than conventional 180 OSVs. These features are essential to the effective servicing of deepwater drilling projects, which are often distant from shore-based support infrastructure, because they allow a vessel to make fewer trips to supply the liquid mud,

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drilling water, dry bulk cement and other needs of the customer. In addition, OSVs operating in deepwater environments generally require dynamic positioning, or anchorless station-keeping capability, primarily because customers safety procedures preclude OSVs from tying up to deepwater installations, and to enable continued operation in adverse weather conditions. We believe that conventional 180 OSVs, substantially all of which lack dynamic positioning capability and sufficient on-deck or below-deck cargo capacity, are not capable of operating effectively or economically in the deepwater market. In addition, certain ports have draft or other logistical impediments, which limit the pool of new generation vessels capable of servicing such ports. Our proprietary vessels were designed to work under these shallow draft and logistically demanding conditions.

The capabilities and capacities of larger new generation OSVs have resulted in average utilization rates for these OSVs working in the GoM of approximately 95% since their introduction in 1999, which spans two significant market downturns. In contrast, the average utilization rate for the conventional 180 OSV fleet over the same period has been approximately 64%, not taking into account cold-stacked conventional 180 OSVs. Additional utilization for new generation OSVs has come from increasing demand for these vessels in support of conventional shelf drilling projects. Moreover, during the same period, average dayrates for new generation OSVs were generally more than double the average dayrates of conventional 180 OSVs. We believe that demand has outpaced the supply of new generation OSVs in the GoM, a trend we expect to continue. We base our belief on the recent and expected drilling activity in all sectors of the GoM and the observed departure of certain new generation OSVs to domestic non-oilfield and foreign oilfield markets, after taking into account vessels currently available and vessels being constructed under announced construction plans. Furthermore, although U.S.-flagged vessels operating in overseas locations may be remobilized to the GoM, historically such remobilization of such vessels, including those of our competitors and our own has been limited.

According to our analysis of the industry and data compiled from various industry sources, including the U.S. Coast Guard, we recently estimated that as of December 31, 2006, the U.S.-flagged OSV fleet in operation totaled 335 vessels, substantially all of which are located in the GoM. Of this total, approximately 165, or 49%, are conventional 180 OSVs that primarily operate on the Continental Shelf. The remaining 170 vessels are U.S. flagged, new generation OSVs, with 128 currently operating in the GoM. However, during mid-2002 to mid-2004, the most recently experienced soft market in the deepwater, we observed that these modern vessels increasingly migrated, at premium dayrates, to conventional drilling environments, such as the U.S. Continental Shelf, Mexico and Trinidad. Of the conventional OSV fleet, a significant number are currently cold-stacked. Vessels that are cold-stacked have generally been removed from active service by the operator due to lack of demand. In contrast, we believe there are no new generation OSVs currently cold-stacked.

Our OSV Business

We currently own and operate a fleet of 25 new generation OSVs, which includes two foreign-flagged AHTS vessels that primarily operate as supply vessels and for towing jack-up rigs. We also have 13 additional new generation OSVs now under construction. In addition, we own and operate one fast supply vessel and we own two coastwise sulfur tankers that are currently undergoing conversion into MPSVs. Our logistics shore-base in Port Fourchon

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supports logistics requirements of our fleet as well as certain of our customers. In a series of three newbuild programs, we engineered and supervised the construction of 17 of our OSVs expressly to meet the demands of deepwater regions and other complex drilling projects, based on our proprietary designs. Drawing from the vessel operating experience of our in-house engineers, we work closely with potential charterers to design vessels specifically to meet their anticipated needs. This is particularly significant when the charterer will operate a project that could have a duration of more than 20 years and require expenditures exceeding $1 billion. Our 17 proprietary OSVs have up to three times the dry bulk capacity and deck space, two to ten times the liquid mud capacity and two to four times the deck tonnage compared to conventional 180 OSVs. The advanced cargo handling systems of our proprietary OSVs allow for dry bulk and liquid cargos to be loaded and unloaded three times faster than conventional 180 OSVs, while the solid state controls of their engines typically result in a 20% greater fuel efficiency than vessels powered by conventional engines. In addition, our larger classes of proprietary OSV designs, designated by us as our 240 ED and 265 classes, were designed, in part, to supply the substantially greater liquid mud volume and other cargo capacity required for ultra-deepwater drilling. Our newest design, the 250 EDF class, is based on our highly successful 240 ED design modified to lengthen the vessel and expand the propulsion package to achieve faster speeds. We believe that our customers recognition of the superior capabilities of our proprietary OSVs has contributed to our ability to achieve higher dayrates and utilization rates and increased overall operating cost efficiencies compared to our competitors, whether operators of 180 conventional OSVs or new generation vessels.

All of our new generation OSVs are equipped with dynamic positioning systems and controllable pitch thrusters, which allow our vessels to maintain position with minimal variance, and state-of-the-art safety, emergency power, fire alarm and fire suppression systems and systems monitoring equipment. The unique hull design and integrated rudder and thruster system of our proprietary OSVs provide for a more maneuverable vessel. These proprietary vessels also have double-bottomed and double-sided hulls that should minimize environmental impact in the event of vessel collisions or groundings, solid state controls that minimize visible soot and polluting gases and zero discharge sewage and waste systems that minimize the impact on marine environments. In addition, our proprietary OSVs are either fully SOLAS (Safety of Life at Sea) certified or SOLAS ready. SOLAS is the international convention that regulates the technical characteristics of vessels for purposes of ensuring international standards of safety for vessels engaged in commerce between international ports. These features allow us to market our proprietary OSVs for service in international markets.

Our OSVs are capable of providing specialty services in support of certain of our customers, including well stimulation, remotely operated vehicles, or ROVs, used in oilfield subsea construction and maintenance, underwater inspections, marine seismic operations, and certain non-energy applications such as fiber optics cable installation, military work and containerized cargo transportation. Compared to conventional 180 OSVs, our OSVs have more deadweight capacity, deck space, and berthing accommodations, improved maneuverability and greater fuel efficiency. We believe these characteristics strengthen demand for our OSVs in specialty situations. The *HOS Innovator, HOS Dominator,* and *HOS Pioneer* currently provide ROV subsea construction and maintenance support services and the *BJ Blue Ray* provides, and the *HOS Saylor* will soon provide, deepwater well stimulation

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support services. The *BJ Blue Ray* was the first U.S.-flagged well stimulation vessel to receive the American Bureau of Shipping WS and DPS2 class notations. We believe the *BJ Blue Ray* is one of the most technologically sophisticated well stimulation vessels in the world. In addition to the traditional energy-related market for our OSVs, we have also experienced increased demand for specialized non-energy-related uses, which has recently afforded us the opportunity to diversify the market for our vessels and further tighten supply in the GoM.

In mid-2003, we acquired six 220 new generation OSVs from Candy Marine Investment Corporation, or Candy Fleet. These six vessels complement our existing OSV fleet and have allowed us to expand our service offerings to clients, particularly those drilling wells on the Continental Shelf.

In May 2004, we exercised our option to purchase the *HOS Hotshot*, a 165 new generation fast supply vessel, from a domestic shipyard, after having bareboat chartered the vessel for one year. This vessel is currently working under a long-term contract in Mexico and is expected to be sold in 2007.

In January 2005, we acquired a new generation AHTS vessel from a private owner. This vessel, renamed the *HOS Saylor*, was our first foreign-flagged vessel. In March 2005, we acquired the *HOS Navegante*, the sister vessel to the *HOS Saylor*, from an affiliate of the private owner from which the *HOS Saylor* was acquired. The *HOS Navegante*, which is also foreign-flagged, was placed in service in June 2005. These strategic vessel acquisitions complement our growing market presence in international waters. While the *HOS Saylor* and *HOS Navegante* each have anchor-handling capabilities and may be used for that purpose, the vessels are primarily being used as supply vessels and for towing jack-up rigs. The *HOS Saylor* was recently awarded a five-year contract for deepwater well stimulation support services in Mexico and will soon be retrofitted for that purpose.

In November 2001, we purchased a coastwise sulfur tanker, the *Energy Service 9001*, formerly known as the *M/V W.K. McWilliams, Jr.* In the second quarter of 2005, we acquired an identical second coastwise sulfur tanker, the *M/V Benno C. Schmidt*. We are converting these two vessels into 370 class MPSVs. Based on internal estimates, the total project cost to acquire and convert the two vessels, prior to construction period interest, with recent modifications is now expected to be at least $150.0 million in the aggregate. We currently anticipate delivery of the converted vessels during the first half of 2008. We believe that these MPSVs will be the largest OSVs in the world, each with cargo carrying capacities of over 10,000 deadweight tons, including 30,000 barrels of liquid mud. Each MPSV will have nearly three times the deadweight and liquid mud capacity of one of our 265 class new generation OSVs and more than eight times the liquid mud capacity of one of our 200 class new generation OSVs. Our MPSV conversion program is based, in part, on customer feedback and expressed demand for a larger, more versatile, DP-2 vessel capable of meeting the evolving needs of the exploration, development and production life-cycle of an ultra-deepwater field. The hulls of these sister vessels, which were purpose-built for the specific gravity of molten sulfur as a cargo, make them uniquely suited to be converted into large liquid mud carriers. This is especially important given the ever-increasing volumes of liquid mud necessary to spud an ultra-deep well today, with some projects requiring as many as

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100,000 barrels of drilling fluid per spud. These MPSVs will offer our customers multiple capabilities that we believe are well beyond those of any OSV offered or under construction today. With these MPSVs, we will have introduced a single vessel that can uniquely perform a variety of specialty services for which customers must currently use several different types of vessels and/or semi-submersible drilling rigs. In addition to traditional offshore supply vessel capabilities, these MPSVs can be modified to support offshore construction, deepwater well testing, subsea well intervention, ROV operations, pipeline commissioning, pipe-hauling and flotel services, among others.

In September 2005, we announced Phase 1 of our fourth OSV newbuild program under which we initially planned to build an additional 20,000 deadweight tons of new generation OSV vessel capacity at an estimated cost, before capitalized construction period interest, of $170.0 million. However, Phase 1 has been deferred until more favorable shipyard conditions materialize for the construction of the type of vessels contemplated under this phase. In February 2006, we announced Phase 2, which would expand this newbuild program to build a mix of 13 proprietary 240 ED and 250 EDF class vessels. The 250 EDF class adopts our proprietary 240 ED design with modifications that allow for faster transit speeds, a feature that customers have requested, in markets that we serve. Excluding capitalized construction period interest, the current estimated cost of Phase 2 of our fourth OSV newbuild program is approximately $305.0 million, in the aggregate. We are contractually committed with two domestic shipyards for four 240 ED class OSVs and nine 250 EDF class OSVs. The 240 ED and 250 EDF class OSVs to be constructed under Phase 2 of this newbuild program are expected to be delivered by early 2010, with the first vessel due in early 2008.

In December 2005, we acquired for approximately $5.0 million the lease rights for a shore-base facility, formerly known as ASCO Magnolia and renamed HOS Port, located in Port Fourchon, Louisiana. The facility lease has eight years remaining on its initial term, with four additional five-year renewal periods. This acquisition further underscores our long-term commitment to, and continued favorable outlook for the GoM as our primary operating market. HOS Port will not only support our existing OSV fleet and customers logistics requirements, but will also provide a key logistics base for our 370 class MPSVs once they are delivered.

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The following table provides information, as of February 15, 2007, regarding our fleet of vessels that serve our OSV customers.

Offshore Supply Vessels

Name	Class	Current Service Function	Built (Acquired)	Deadweight (long tons)	Brake Horsepower
OSVs:					
BJ Blue Ray	265	Well Stimulation	Nov 2001	3,756	6,700
HOS Brimstone	265	Supply	Jun 2002	3,756	6,700
HOS Stormridge	265	Supply	Aug 2002	3,756	6,700
HOS Sandstorm	265	Supply	Oct 2002	3,756	6,700
HOS Newbuild #1	250 EDF	TBD	TBD (1)	2,950 est.	6,000 est.
HOS Newbuild #2	250 EDF	TBD	TBD (1)	2,950 est.	6,000 est.
HOS Newbuild #3	250 EDF	TBD	TBD (1)	2,950 est.	6,000 est.
HOS Newbuild #4	250 EDF	TBD	TBD (1)	2,950 est.	6,000 est.
HOS Newbuild #5	250 EDF	TBD	TBD (1)	2,950 est.	6,000 est.
HOS Newbuild #6	250 EDF	TBD	TBD (1)	2,950 est.	6,000 est.
HOS Newbuild #7	250 EDF	TBD	TBD (1)	2,950 est.	6,000 est.
HOS Newbuild #8	250 EDF	TBD	TBD (1)	2,950 est.	6,000 est.
HOS Newbuild #9	250 EDF	TBD	TBD (1)	2,950 est.	6,000 est.
HOS Newbuild #10	240 ED	TBD	TBD (1)	2,850 est.	4,000 est.
HOS Newbuild #11	240 ED	TBD	TBD (1)	2,850 est.	4,000 est.
HOS Newbuild #12	240 ED	TBD	TBD (1)	2,850 est.	4,000 est.
HOS Newbuild #13	240 ED	TBD	TBD (1)	2,850 est.	4,000 est.
HOS Bluewater	240 ED	Military	Mar 2003	2,850	4,000
HOS Gemstone	240 ED	Military	Jun 2003	2,850	4,000
HOS Greystone	240 ED	Military	Sep 2003	2,850	4,000
HOS Silverstar	240 ED	Military	Jan 2004	2,850	4,000
HOS Innovator	240 E	ROV Support (2)	Apr 2001	2,380	4,500
HOS Dominator	240 E	ROV Support (2)	Feb 2002	2,380	4,500
HOS Deepwater	240	Supply	Nov 1999	2,250	4,500
HOS Cornerstone	240	Supply	Mar 2000	2,250	4,500
HOS Explorer	220	Supply	Feb 1999 (Jun 2003)	1,607	3,900
HOS Express	220	Supply	Sep 1998 (Jun 2003)	1,607	3,900
HOS Pioneer	220	ROV Support (2)	Jun 2000 (Jun 2003)	1,607	4,200
HOS Trader	220	Supply	Nov 1997 (Jun 2003)	1,607	3,900
HOS Voyager	220	Supply	May 1998 (Jun 2003)	1,607	3,900
HOS Mariner	220	Supply	Sep 1999 (Aug 2003)	1,607	3,900
HOS Crossfire	200	Supply	Nov 1998	1,750	4,000
HOS Super H	200	Supply	Jan 1999	1,750	4,000
HOS Brigadoon	200	Supply	Mar 1999	1,750	4,000
HOS Thunderfoot	200	Supply	May 1999	1,750	4,000
HOS Dakota	200	Supply	Jun 1999	1,750	4,000
MPSVs					
Energy Service 9001	370	Multi-Purpose	TBD (3)	10,300 (est)	TBD
M/V Benno C. Schmidt	370	Multi-Purpose	TBD (3)	10,300 (est)	TBD
AHTS					
HOS Saylor (4)	240	Towing/Supply	Oct 1999 (Jan 2005)	3,322	8,000
HOS Navegante (4)	240	Towing/Supply	Jan 2000 (Mar 2005)	3,322	7,845

Fast Supply Vessel:

HOS Hotshot	165	Fast Supply	Apr 2003 (May 2004)	260	6,200

TBD to be determined

(1) These vessels are currently being constructed under OSV newbuild program #4 with anticipated deliveries ranging from early 2008 through early 2010.
(2) The term ROV means remotely operated vehicle.
(3) These two coastwise sulfur tankers, which will be renamed later, are currently being converted into 370 class MPSVs and are expected to be placed in service during the first half of 2008.
(4) We acquired the *HOS Saylor* and the *HOS Navegante*, each a foreign-flagged AHTS vessel, in the first quarter of 2005. The *HOS Navegante* and *HOS Saylor* are being used primarily for their OSV capabilities and for towing jack-up rigs. The *HOS Saylor* was recently awarded a five-year well stimulation contract. After a retrofit period In a shipyard, the *HOS Saylor* will commence service in Mexico as a well stimulation vessel.

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We have designed and constructed five distinct classes of proprietary OSVs and added a sixth class, through the acquisitions of six OSVs from Candy Fleet, to meet the diverse needs of the offshore oil and gas industry. Upon delivery of our 250 EDF class vessels and our MPSVs, we will have expanded our OSV fleet offering to eight classes of OSVs. The following table provides a comparison of certain specifications and capabilities of our existing new generation OSVs to conventional 180 OSVs

		Our Proprietary Design OSV Classes (1)					Acquired OSVs (3)
	Conventional 180 OSV (2)	200	240	240 E	240 ED	265	220
Size							
Class length overall (ft.)	180	200	240	240	240	265	220
Breadth (ft.)	40	54	54	54	54	60	46
Depth (ft.)	14	18	18	18	20	22	17
Maximum draft (ft.)	12	13	13	13	14.5	16	13.7
Deadweight (long tons)	950	1,750	2,250	2,380	2,850	3,756	1,607
Clear deck area (sq. ft.)	3,450	6,580	8,836	8,100	8,100	9,212	5,472
Capacity							
Fuel capacity (gallons)	79,400	90,000	151,800	135,100	104,210	151,800	114,490
Fuel pumping rate (gallons per minute)	275	550	550	550	550	500	380
Drill water capacity (gallons)	120,000	240,000	240,000	240,000	311,000	413,000	99,000
Dry bulk capacity (cu. ft.)	4,000	7,000	8,400	8,400	6,000	10,800	8,040
Liquid mud capacity (barrels)	1,200	3,640	6,475	6,475	8,300	10,500	2,955
Liquid mud pumping rate (gallons per minute)	250	500	1,000	1,000	1,000	1,000	1,200
Potable water capacity (gallons)	11,500	52,200	52,200	52,200	30,400	20,430	26,800
Machinery							
Main engines (horsepower)	2,250	4,000	4,000	4,000	4,000	6,700	3,900
Auxiliaries (number)	2	3	3	3	3	3	2
Total rating (kw)	200	750	750	750	750	860	250
Bow thruster (horsepower)	325	800	1,600	1,600	1,600	2,400	530
Type of Pitch	Fixed	Controllable	Controllable	Controllable	Controllable	Controllable	Fixed
Stern thruster (horsepower)	None	300	300	800	800	1,600	300
Type of Pitch		Controllable	Controllable	Controllable	Controllable	Controllable	Fixed
Fire fighting (gallons per minute)	None	1,250	2,700	2,700	2,700	2,700	2,600
Dynamic positioning (4)	None	DP0,1	DP1	DP2	DP2	DP2,3	DP0,1
Crew Requirements							
Number of personnel (5)	5	6	6	7	7	8	6

(1) We now have two additional new proprietary classes of new generation vessels, the HOS 250 EDF class OSVs and the HOS 370 class MPSVs, under construction or conversion.

(2) Statistics are for a typical 180 class vessel. Actual specifications and capabilities may vary slightly from vessel to vessel.

(3) Excludes the *HOS Saylor* and the *HOS Navegante*, which are foreign-flagged AHTS vessels, and the *HOS Hotshot*, which is a fast supply vessel.

(4) Dynamic positioning permits a vessel to maintain position without the use of anchors. The numbers 0, 1, 2 and 3 refer to increasing levels of technical sophistication and system redundancy features.

(5) Regulatory manning requirements; depending on the services provided, operators may, and often do, man vessels with more crew than required by regulations.

Additional information with respect to our OSV segment can be found in Note 14 of our consolidated financial statements.

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Tugs and Tank Barges

The Tug and Tank Barge Industry

Introduction. The domestic tank barge industry provides marine transportation of crude oil, petroleum products and petrochemicals by ocean-going tugs and tank barges and is a critical link in the U.S. petroleum distribution chain. Petroleum products are transported in the northeastern United States through a vast network of terminals, tankers and pipelines. According to the EIA, approximately 240 million barrels of petroleum products were transported in 2006 by tankers and tank barges along the East Coast. Additionally, the EIA estimates that Puerto Rico, historically our other core area of TTB operation, consumes 234 thousand barrels of oil daily, or approximately 85 million barrels annually. Since Puerto Rico relies on imports to meet its energy needs, petroleum products are delivered by tank barge for transportation and electric power generation.

Demand for TTB services in the northeastern United States is primarily driven by population growth, the strength of the U.S. economy, seasonal weather patterns, oil prices and competition from alternate energy sources. According to the EIA, demand for petroleum products in the northeastern United States is expected to increase approximately 1.1% annually through 2011, which we believe will generate steadily increasing demand for the tank barge industry.

The largest tank barge market in the northeastern United States is New York Harbor. Imported petroleum products are primarily delivered to New York Harbor as it has the capacity to receive products in cargo lots of 50,000 tons or more per tanker. By contrast, draft limitations in most New England ports and drawbridge limitations in Boston and Portland, Maine limit the average cargo carrying capacity of direct imports into many of the largest New England ports to about 30,000 tons per tanker. As a result, ships importing directly into New England must frequently discharge in multiple ports or terminals or transfer cargos to tank barges. As existing single-hulled tankers are retired due to age or as mandated under OPA 90, they are typically replaced by larger tankers. These larger-sized tankers are being built to facilitate the importation of crude oil and petroleum products into the United States. According to the EIA, over the last 20 years, importation of crude oil to the Northeast has grown at a compounded annual rate of 1.7% while the volume of imported crude oil and petroleum products is expected to grow at a compound annual rate of 1.5% through 2025.

As larger petroleum tankers are being built, we believe that direct delivery into New York Harbor will generate increased tank barge demand for lightering services and further shipment to New England, the Hudson River and Long Island.

Oil Pollution Act of 1990. OPA 90 mandates that all single-hulled tank vessels operating in U.S. waters be removed from petroleum transportation service according to a set time schedule. Data provided by a U.S. Coast Guard report dated September 2001 indicated that 5.5 million barrels of single-hulled tank barge capacity would be retired by 2005 and an additional 3.5 million barrels by 2010, as mandated by OPA 90. According to the report, this represented on a cumulative basis as of each such retirement date, 32% and 52%, respectively, of the total 17.2 million barrel single-hulled tank barge capacity that existed in 2001.The following chart illustrates the capacity of tank vessels that has been or must be removed from service from 2001 through 2015. We believe that, absent a substantial increase

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in the number of double-hulled vessels constructed in the industry or an increase in customer preference for double-hulled vessels, this reduction in capacity, assuming steady demand, may continue to favorably impact dayrates and utilization of the remaining single-hulled tank barges, including our own.

Based on data contained in the United States Coast Guard Report to Congress on the Progress to Replace Single Hull Tank Vessels with Double Hull Tank Vessels, dated September 2001.

Additionally, OPA 90 requires that owners or operators of tankers operating in U.S. waters submit vessel spill response plans to the U.S. Coast Guard for approval and operate according to the plans upon approval. Our vessel response plans have been approved by the U.S. Coast Guard and all of our crew members are trained to comply with these guidelines. For further discussion of OPA 90 see Environmental and Other Governmental Regulation below.

Our Tug and Tank Barge Business

We offer marine transportation, distribution and logistics services primarily in the northeastern United States, the GoM and Puerto Rico with our operating fleet of 13 ocean-going tugs and 18 ocean-going tank barges. In addition, we currently have three more ocean-going tank barges under construction and four recently acquired tugs under retrofit. We provide our services to major oil companies, refineries and oil traders. Generally, a tug and tank barge work together as a tow to transport refined or bunker grade petroleum products. Our tank barges carry petroleum products that are typically characterized as either clean or dirty . Clean products are primarily gasoline, home heating oil, diesel fuel and jet fuel. Dirty products are mainly crude oils, residual crudes and feedstocks, heavy fuel oils and asphalts.

Our tugs and tank barges serve the northeastern U.S. coast, primarily New York Harbor, by transporting both clean and dirty petroleum products to and from refineries and distribution terminals. Our tugs and tank barges also transport both clean and dirty petroleum products

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from refineries and distribution terminals in Puerto Rico to the Puerto Rico Electric Power Authority and to utilities located on other Caribbean islands. In addition, we provide ship lightering, bunkering and docking services in these markets and are well positioned to provide such services to the increasing number of new tankers that are too large to make direct deliveries to distribution terminals and refineries. In addition, during 2005 and 2006, we accessed a new market for our double-hulled barges by performing upstream services for our OSV customers in the deepwater GoM.

In mid-2001, we acquired nine ocean-going tugs and nine ocean-going tank barges from the Spentonbush/Red Star Group, affiliated with Amerada Hess. As part of the acquisition, Amerada Hess entered into a contract of affreightment, or COA, with us for the period from June 1, 2001 through March 31, 2006. We elected not to renew that COA, however, we entered into long-term time charters with Amerada Hess for two tank barges. The time charters were effective upon the expiration of the COA on March 31, 2006. Although we considerably reduced the amount of cargo that we transported on behalf of Amerada Hess, following the expiration of our COA, we were able to successfully redeploy our TTB equipment that was previously dedicated to the Hess COA on time charter agreements with other customers at attractive dayrates. We believe that the tank barge market is currently operating at or near capacity.

During 2005, we completed construction of three 110,000-barrel barges, two 135,000-barrel barges and the retrofit of two 6,100 horsepower tugs. Under our first TTB newbuild program, the *Energy 13501* and *Energy 13502*, 135,000-barrel double-hulled tank barges, were placed in service on March 11, 2005 and December 1, 2005, respectively. The *Energy 11103*, *Energy 11104* and *Energy 11105,* 110,000-barrel double-hulled tank barges, were placed in service on July 10, 2005, October 21, 2005 and December 29, 2005, respectively. Our first TTB newbuild program has added new barrel-carrying capacity of 600,000 barrels in the aggregate, more than replacing the 270,000 barrels of aggregate barrel-carrying capacity lost when we retired three of our single-hulled tank barges from service at the end of 2004, as mandated by OPA 90. Notably, the *Energy 8701*, one of the previously retired tank barges, was reactivated in October 2006 based on Coast Guard approval of an extended OPA 90 retirement date, which added back approximately 86,000 barrels to our capacity. During 2006, we completed the retrofit of two additional 6,100 horsepower tugs under the first TTB newbuild program.

In September 2005, we announced the commencement of our second TTB newbuild program. We have three double-hulled barges with a total of 180,000 barrels of carrying capacity currently under construction at a domestic shipyard and four recently acquired 3,000 horsepower tugs currently being retrofitted at another domestic shipyard. The cost for the construction, acquisition and retrofit of these seven vessels is currently estimated to be approximately $70 million in the aggregate. All of the new vessels currently being constructed or retrofitted under the second TTB newbuild program are expected to be delivered on various dates throughout 2007. We continue to investigate our alternatives with regard to the remaining 220,000 barrels of double-hulled tank barge newbuild capacity originally contemplated to be constructed under this program.

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Currently, six of our tank barges are double-hulled and are not subject to OPA 90 retirement dates. Upon completion of the three tank barges presently under construction under our second TTB newbuild program, 50% of our tank barge fleet barrel-carrying capacity will be double-hulled, up from 44% today and 7% at the end of 2004. Ten of our 12 single-hulled tank barges are not required under OPA 90 to be retired or double-hulled prior to January 1, 2015. The two other single-hulled tank barges are required to be retired from service in 2009. Based on the remaining lives of the majority of our tank barge fleet under OPA 90 and our recent and pending construction programs, we believe we are well positioned to grow our customer base in the northeastern United States, as we believe a large portion of the industry s capacity that was removed from service on January 1, 2005 has not been replaced one-for-one, leaving the market net under-supplied.

The following tables provide information, as of February 15, 2007, regarding the tugs and tank barges that we own, as well as the three double-hulled tank barges now under construction and the four tugs currently being retrofitted.

Ocean-Going Tugs

Name	Gross Tonnage	Length (feet)	Year Built	Brake Horsepower
Freedom Service	180	126	1982	6,140
Liberty Service	180	126	1982	6,140
Patriot Service	198	124	1996	6,140
Eagle Service	198	124	1996	6,140
Caribe Service	194	111	1970	3,900
Atlantic Service	198	105	1978	3,900
Brooklyn Service	198	105	1975	3,900
Gulf Service	198	126	1979	3,900
Erie Service(1)	98	105	1981	3,620
Superior Service(1)	98	105	1981	3,620
Tradewind Service	183	105	1975	3,200
Spartan Service	126	102	1978	3,000
Huron Service(1)	98	105	1981	3,000
Michigan Service(1)	98	105	1981	3,000
Sea Service	173	109	1975	2,820
Bayridge Service	194	100	1981	2,000
Stapleton Service	146	78	1966	1,530

(1) In July 2006, we purchased four tugs from a private owner and renamed them the *Erie Service, Superior Service, Huron Service* and *Michigan Service*. Following a retrofit period in a domestic shipyard, these vessels are expected to be placed in service on various dates throughout 2007.

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Ocean-Going Tank Barges

Name	Barrel Capacity	Length (feet)	Year Built	OPA 90 Date(1)
Ocean-Going Tank Barges:				
Energy 13501	135,380	450	2005	DH
Energy 13502	135,380	450	2005	DH
Energy 11101	111,844	420	1979	2009
Energy 11102	111,844	420	1979	2009
Energy 11103	112,269	390	2005	DH
Energy 11104	112,269	390	2005	DH
Energy 11105	112,269	390	2005	DH
Energy 8701	86,454	360	1976	2015
Energy 8001	81,364	350	1996	DH
Energy 7002	72,693	351	1971	2015
Energy 7001	72,016	300	1977	2015
Energy 6504	66,333	305	1958	2015
Energy 6505	65,710	328	1978	2015
Energy 6503	65,145	327	1988	2015
Energy 6502	64,317	300	1980	2015
Energy 6501	63,875	300	1974	2015
Energy 6506	60,000 est.	360 est.	TBD(2)	DH
Energy 6507	60,000 est.	360 est.	TBD(2)	DH
Energy 6508	60,000 est.	360 est.	TBD(2)	DH
Energy 5501	57,848	341	1969	2015
Energy 2201	22,556	242	1973	2015

TBD: To be determined.
DH: OPA 90 limitations are not applicable to these double-hulled vessels.
(1) Prior to January 1 of the year indicated (except for the *Energy 11101* for which the date is June 1, 2009 and the *Energy 11102* for which the date is December 31, 2009), according to OPA 90, the vessel must be refurbished as a double hull or be retired from petroleum transportation service in U.S. waters. For a discussion of OPA 90 see Environmental and Other Governmental Regulation below.
(2) The *Energy 6506*, *Energy 6507* and *Energy 6508* are 60,000-barrel double-hulled tank barges currently under construction with anticipated delivery on various dates throughout 2007.

Additional information with respect to our TTB segment can be found in Note 14 of our consolidated financial statements.

Our Competitive Strengths

Technologically Advanced Fleet of New Generation OSVs. Our technologically advanced, new generation OSVs were designed with the specifications necessary for operations in complex and challenging drilling environments, including deepwater, deep well and other logistically demanding projects. Such other projects include, among other things, the construction, maintenance and repair of offshore infrastructure. Our new generation OSVs have significantly more capacity and operate more efficiently than conventional 180 OSVs. While operators are especially concerned with a vessel s ability to avoid collisions with multi-million dollar drilling rigs or production platforms during adverse weather conditions, they are hesitant to stop operations under such conditions due to the high daily cost of halting such complex operations. Our proprietary vessels, including the MPSVs to be converted, incorporate sophisticated technologies and are designed specifically to operate safely in complex exploration and production

environments. These technologies include dynamic positioning, roll reduction systems and controllable pitch thrusters, which allow our vessels to

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maintain position with minimal variance, and our unique cargo handling systems, which permit high volume transfer rates of liquid mud and dry bulk. We believe that we earn higher average dayrates and maintain higher utilization rates than our competitors due to the superior capabilities of our OSVs, our eight-year track record of safe and reliable performance and the collaborative efforts of our in-house engineering team in providing marine engineering solutions to our customers.

Jones Act Qualified Fleet. All but two of our vessels are Jones Act qualified. The Jones Act prohibits vessels that are foreign built, foreign owned, foreign crewed or foreign flagged from participating in the U.S. coastwise trade. Nearly all of the services provided by our vessels, in both of our fleets, constitute coastwise trade as defined by the Jones Act. Consequently, competition for our services is largely restricted to other U.S. vessel owners and operators.

Young OSV Fleet with Lower Cost of Ownership. We believe that we operate one of the youngest fleets of U.S.-flagged OSVs. While the average age of the conventional 180 U.S.-flagged OSV fleet is approximately 27 years, the average age of our existing OSV fleet is approximately six years. Based on our current fleet complement, once our 15 new vessels now under construction or conversion are delivered, our average fleet age will be even lower. Newer vessels generally experience less downtime and require significantly less maintenance and scheduled drydocking costs compared to older vessels. In addition, we believe that our operation of new, technologically advanced OSVs gives us a competitive advantage in obtaining long-term contracts for our vessels and in attracting and retaining crews. Since we accepted delivery of our first OSV in November 1998, the average utilization rate for our OSVs has been approximately 93% based on a 365-day denominator. According to WorkBoat magazine, the GoM industry average for conventional 180 OSVs was approximately 85% over the same time period, based on vessel days available for service. We expect that our newer, larger, faster and more cost-efficient vessels will remain in high demand as deepwater, ultra-deepwater and other complex and challenging exploration, development and production activities continue to increase globally and as opportunities for military and other specialty service contracts continue to present themselves.

Commitment to Quality, Health, Safety and the Environment. As part of our commitment to Quality, Health, Safety and the Environment, we have voluntarily pursued and received certifications that are not generally held by other companies in our industry. We are one of the few OSV companies operating in the GoM and internationally that is approved under the U.S. Coast Guard s Streamlined Inspection Program in which we and the Coast Guard cooperate to develop training, inspection and compliance processes, with our personnel conducting periodic examinations of vessel systems to the requirements of the vessels Coast Guard certifications, and taking corrective actions where necessary. Both of our principal office locations in Covington, Louisiana and Brooklyn, New York and our field office in Trinidad, as well as all of our vessels in the OSV fleet and a majority of our vessels in the TTB fleet, are certified under the International Safety Management Code, or ISM Code, developed by the International Maritime Organization to provide internationally recognized standards for the safe management and operation of ships and for pollution prevention. We received ISO 14001:2004 certification for our environmental management system in 2006. Quality, Health, Safety and Environmental Certifications are an increasingly important consideration for both our OSV and TTB customers due to the environmental and regulatory sensitivity associated

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with offshore drilling and production activity and waterborne transportation of petroleum products, respectively. We believe that customers recognize our commitment to safety and that our strong reputation and performance history provide us with a competitive advantage.

Leading Market Presence in Core Target Markets. Our 23 U.S.-flagged OSVs comprise the second largest fleet of technologically advanced, new generation OSVs qualified for work in the GoM. Currently, 16 of our 23 U.S.-flagged OSVs operate in that area. We also operate three U.S.-flagged OSVs and one foreign-flagged AHTS offshore Trinidad, which currently represents the largest market share in that region. We believe that we are the fourth largest tank barge transporter of petroleum products in New York Harbor, a market that has a fairly even distribution among the top five operators and we operate one of the largest fleets of tugs and tank barges for the transportation of petroleum products in Puerto Rico. We believe that having scale in our selected markets benefits our customers and provides us with operating efficiencies.

Successful Track Record of Vessel Construction and Acquisitions. Our management has significant naval architecture, marine engineering and shipyard experience. We believe we are unique in the role we play in the design of our vessels and the manner in which we work closely with our contracted shipyards in their construction. We typically source and supply many of the manufactured components (owner-furnished equipment), comprising a large portion of the aggregate cost of a vessel, directly from vendors rather than through the shipyard. In addition to substantial cost savings, we believe our approach enables us to better control the construction process, resulting in a higher quality vessel and an enhanced level of service from these vendors during the applicable warranty periods. Our company has designed its operations and management systems in contemplation of additional growth through new vessel construction and acquisitions. To date, we have successfully completed three proprietary OSV newbuild programs involving 17 new generation OSVs and one proprietary TTB newbuild program involving five ocean-going double-hulled tank barges. In addition, our MPSV conversion program, our fourth OSV newbuild program, and our second TTB newbuild program are currently underway. To date, we have also successfully completed and integrated multiple acquisitions involving 17 ocean-going tugs and 13 ocean-going tank barges, two coastwise tankers, six 220 new generation OSVs, one 165 fast supply vessel, and two foreign-flagged AHTS vessels.

Experienced Management Team with Proven Track Record. Our executive management team has an average of 22 years of domestic and international marine transportation industry-related experience. We believe that our team has successfully demonstrated its ability to grow our fleet through new construction and strategic acquisitions and to secure profitable contracts for our vessels in both favorable and unfavorable market conditions. Moreover, our in-house engineering team has significant operating experience that enables us to more effectively design and manage our new vessel construction programs, adapt our vessels for specialized purposes, oversee and manage the drydocking process and provide custom marine engineering solutions to our customers. We believe this will continue to result in a lower overall cost of ownership over the life of our vessels compared to our competitors, as well as a competitive advantage in securing contracts for our vessels as the benefits of our proprietary designs and in-house engineering capabilities are recognized by our customers.

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Our Strat egy

Apply Existing and Develop New Technologies to Meet our Customers Vessel Needs. Our new generation OSVs and MPSVs, including those planned or under construction or conversion, are designed to meet the higher capacity and performance needs of our clients increasingly more complex drilling and production programs. In addition, our recently delivered proprietary double-hulled tank barges, including those planned or under construction, are designed to maximize transit speed, improve cargo through-put rates and enhance crew safety features. Our new generation OSVs are equipped with sophisticated propulsion and cargo handling systems, dynamic positioning capabilities and have larger capacities than conventional 180 OSVs. We are committed to applying existing and developing new technologies to maintain a technologically advanced fleet that will enable us to continue to provide a high level of customer service and meet the developing needs of our customers for OSVs and ocean-going tugs and tank barges, as well as other types of vessels that complement our two business segments. Improvements in exploration and production technologies have enabled operators to pursue larger scale, more complex drilling programs in remote locations and under more challenging operating conditions. We believe that the trend toward increasingly more complex projects will increase the demand for our technologically advanced fleet of new generation OSVs. Oil and natural gas exploration and development activity in these regions has increased recently as a result of several factors, including world-class exploration potential, improvements in exploration and production technologies for deepwater projects, and slowing or declining production from onshore and shallow water fields. We believe that deepwater regions worldwide and deep well drilling on the Continental Shelf will continue to be active areas for exploration and development in the foreseeable future, and that demand for our OSVs, which are uniquely equipped to serve the current and planned drilling programs in these markets, will continue to be strong. We also believe that some non-energy related uses for our OSVs, including military applications and other specialty services, may allow us to further diversify in additional markets.

Expand Fleet Through Newbuilds and Strategic Acquisitions. We plan to expand our fleet through construction of new vessels, including construction of new generation OSVs and double-hulled tank barges, as market conditions warrant, through conversion and retrofitting of existing vessels and through strategic acquisitions. Our current fleet expansion initiatives include our MPSV conversion program, our second TTB newbuild program, and our fourth OSV newbuild program. The main determinants of the level and timing of incremental newbuild programs initiated by us in the future will be our assessment of the visible supply and visible demand for our vessels and our receiving acceptable shipyard terms and conditions. We intend to use our expertise and experience to evaluate the economics of, and where appropriate, execute strategic acquisitions where the opportunity exists to expand our service offerings in our core markets and create or enhance long-term customer relationships. As of December 31, 2006, we have completed multiple acquisitions involving 45 vessels, and constructed 17 proprietary OSVs and five proprietary double-hulled tank barges with 13 OSVs, three tank barges, two MPSVs and four ocean-going tugs currently under construction, conversion or retrofit.

Pursue Optimal Mix of Long-Term and Short-Term Contracts. We seek to balance our portfolio of customer contracts by entering into both long-term and short-term charters. Long- term charters, which contribute to higher utilization rates, provide us with more predictable

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cash flow. Some of our long-term charters contain annual dayrate escalation provisions. Short-term charters provide the opportunity to benefit from increasing dayrates in favorable market cycles, but are also subject to the negative effect of declining market cycles. We plan our mix of long-term and short-term, or spot, market contracts with respect to our OSVs based on anticipated market conditions. Our COA with Amerada Hess for the services of tugs and tank barges in the northeastern United States expired on March 31, 2006. Although we considerably reduced the amount of cargo transported for Amerada Hess since the expiration of the COA, we have successfully redeployed the barrel-carrying capacity previously required to serve the COA through other customers. We believe that the tank barge market in the northeastern United States is currently operating at or near full practical capacity. This has allowed us to diversify our TTB customer base and geographic markets by exposing a greater portion of our fleet to currently favorable market conditions. Other than the Amerada Hess COA, our other TTB contracts typically have been renewed annually over the last several years.

Build Upon Existing Customer Relationships. We intend to build upon existing customer relationships by expanding the services we offer to those customers with diversified marine transportation needs. Many integrated oil and gas companies require OSVs to support their exploration and production activities and ocean-going tugs and tank barges to support their refining, trading and retail distribution activities. During 2005 and 2006, we were able to access a new market application for our double-hulled tank barges by using them to support existing OSV customers for upstream services such as deepwater well testing in the GoM. Moreover, many of our customers that conduct operations internationally have expressed interest in chartering our OSVs in such markets. We now have roughly 20% of our supply vessel fleet chartered for use in international markets, with four OSVs operating offshore Trinidad and one OSV and one fast supply vessel offshore Mexico. Our management team has significant international experience and will continue to evaluate such opportunities.

Optimize Tug and Tank Barge Operations. Due to OPA 90 phase-out requirements of single-hulled barges, the total barrel-carrying capacity of existing tank vessels transporting petroleum products domestically is projected to decline from its current level without a commensurate increase in newbuildings and retrofittings. In addition, the energy industry is increasingly outsourcing its marine transportation requirements and focusing on safety and reliability as a key determinant in awarding new business. We believe that these trends are improving the balance of supply and demand, resulting in improved tank barge utilization and dayrates. Notwithstanding the recent deployment of our TTB equipment to upstream customers, these trends have recently allowed us to roughly double our operating margin for downstream work in this segment over year-ago levels to a higher new level that we believe is sustainable for the foreseeable future.

Custome rs and Charter Terms

Major oil companies, large independent oil and gas exploration, development and production companies and large oil service companies constitute the majority of our customers for our OSV services, while refining, marketing and trading companies constitute the majority of our customers for our TTB services. The percentage of revenues attributable to a customer in any particular year depends on the level of oil and natural gas exploration,

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development and production activities undertaken or refined petroleum products or crude oil transported by a particular customer, the availability and suitability of our vessels for the customer s projects or products and other factors, many of which are beyond our control. We enter into a variety of contract arrangements with our customers, including spot and time charters, COAs, consecutive voyage contracts and, occasionally, bareboat charters. Our contracts are obtained through competitive bidding or, with established customers, through negotiation. For the year ended December 31, 2006, Amerada Hess Corporation and Military Sealift Command each accounted for more than 10% of our total revenues. For a discussion of significant customers in prior periods, see Note 13 of the notes to our consolidated financial statements.

Most of the contracts for our OSVs contain early termination options in favor of the customer; however, some have early termination penalties designed to discourage the customers from exercising such options. Our tank barges have historically operated under time charters or COAs commensurate with market conditions. However, since the non-renewal of our five-year COA with Amerada Hess, which expired March 31, 2006, we have been successful in shifting our entire TTB fleet to time charters. Since we commenced operations, our OSVs have performed services for more than 90 different customers, and our tugs and tank barges have performed services for more than 250 different customers. Because of the variety and number of customers historically using the services of our fleet, and the approximate balance between supply and demand in both the OSV and TTB markets, we believe that the loss of any one customer would not have a material adverse effect on our business.

Because of our successful proprietary newbuild designs, charterers have contacted us in certain circumstances to construct vessels to meet their needs. In such circumstances, we have generally contracted these specially designed vessels for three to five years, with renewal options, before construction is completed. Although we will design vessels to meet the specific needs of a charterer, we ensure in our design that customization does not preclude efficient operation of these vessels for other customers, for other purposes or in other situations.

Co mpetition

We operate in a highly competitive industry including competitors with conventional 180 OSVs, competitors with new generation OSVs and competitors in the TTB business with both single-hullled and double-hulled tank barges. Competition in the OSV and domestic ocean-going TTB segments of the marine transportation industry primarily involves factors such as:

- quality and capability of the vessels and crew members;
- ability to meet the customer s schedule;
- safety record;
- reputation;
- price; and

experience.

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All but two of our 60 vessels are U.S.-flagged and are qualified under the Jones Act to engage in domestic coastwise trade. The terms of the Jones Act restrict the ability of vessels that are not built in the United States, documented under the laws of the United States and controlled by U.S. citizens to engage in the coastwise trade in the United States and Puerto Rico. See Environmental and Other Governmental Regulation for a more detailed discussion of the Jones Act.

We believe that only about 30% of the new generation OSVs currently operating in the GoM are owned by publicly-traded companies. We believe we operate the second largest fleet of new generation OSVs in the GoM, and are the only publicly traded company with a significant fleet of U.S.-flagged, new generation OSVs. In contrast, approximately 54% of the conventional 180 OSVs operating on the Continental Shelf of the GoM are owned by publicly-traded companies. We operate one of the largest tank barge fleets in Puerto Rico and believe that we are the fourth largest transporter by tank barge of petroleum products in New York Harbor, a market that has a fairly even distribution among the top five competitors. All but one of our direct competitors in our segment of the TTB industry are privately held.

We do not anticipate significant competition in the near term from pipelines as an alternative method of petroleum product delivery in the northeastern United States or Puerto Rico. No pipelines are currently under construction that could provide significant competition to tank barges in the northeastern United States or Puerto Rico, nor are any new pipelines likely to be built in the near future due to cost constraints and logistical and environmental requirements.

Although some of our principal competitors are larger and have greater financial resources and, with respect to OSVs, extensive international operations, we believe that our operating capabilities and reputation enable us to compete effectively with other fleets in the market areas in which we operate. In particular, we believe that the relatively young age and advanced features of our OSVs provide us with a competitive advantage. The ages of our OSVs range from three years to nine years, while the average age of the industry s conventional 180 U.S.-flagged OSV fleet is approximately 26 years. Retirement of older vessels has already commenced and we believe that many more of these older vessels will be retired in the next few years. The young age of our fleet, together with the advanced capabilities of our vessels, position us to take advantage of the expanding deepwater, deep well and other logistically demanding exploration and production projects in the GoM and around the world. In addition, our new generation OSVs are also increasingly in demand by our customers for conventional shallow-water drilling projects because of the ability of our OSVs to reduce overall offshore logistics costs for the customer through the vessels greater capacities and operating efficiencies. We also compete with other operators of new generation OSVs

Environmental and Other Governmental Regulation

Our operations are significantly affected by a variety of federal, state, local and international laws and regulations governing worker health and safety and the manning, construction and operation of vessels. Certain U.S. governmental agencies, including the Department of Homeland Security and agencies under its auspices (such as the U.S. Coast Guard and the U.S. Customs and Border Protection), the National Transportation Safety Board, and the Maritime Administration of the U.S. Department of Transportation, have

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jurisdiction over our operations. In addition, private industry organizations such as the American Bureau of Shipping oversee aspects of our business. The U.S. Coast Guard and the National Transportation Safety Board establish safety criteria and are authorized to investigate vessel accidents and recommend improved safety standards, requirements, tonnage requirements and restrictions, hull and shafting requirements and vessel documentation. Coast Guard regulations require that each of our vessels be drydocked for inspection at least twice within a five-year period.

Under the Jones Act, the privilege of transporting merchandise or passengers for hire in the coastwise trade in U.S. domestic waters is restricted to only those vessels that are controlled by U.S. citizens and are built in and documented under the laws of the United States. To engage in coastwise trade, a corporation is not considered a U.S. citizen unless, among other things:

- the corporation is organized under the laws of the United States or of a state, territory or possession of the United States;
- at least 75% of the ownership of voting interests with respect to its capital stock is held by U.S. citizens;
- the corporation s chief executive officer, president and chairman of the board are U.S. citizens; and
- no more than a minority of the number of directors necessary to constitute a quorum for the transaction of business are non-U.S. citizens.

We meet all of the foregoing requirements. If we should fail to comply with these requirements, our vessels would lose their eligibility to engage in coastwise trade within U.S. domestic waters. To facilitate compliance, our certificate of incorporation:

- limits ownership by non-U.S. citizens of any class of our capital stock (including our common stock) to 20%, so that foreign ownership will not exceed the 25% permitted;
- permits withholding of dividends and suspension of voting rights with respect to any shares held by non-U.S.citizens that exceed 20%;
- permits a stock certification system with two types of certificates to aid tracking of ownership;
- permits our board of directors to redeem any shares held by non-U.S. citizens that exceed 20%; and
- permits our board of directors to make such determinations to ascertain ownership and implement such measures as reasonably may be necessary.

Jones Act restrictions have been challenged by interests seeking to facilitate foreign competition for coastwise trade. Historically, their efforts have been defeated by large margins when considered by the U.S. Congress. Industry associations and participants actively responded to and successfully defeated certain recent challenges involving the nature, extent and availability of

lease-finance alternatives permitted by a 1996 amendment of the Jones Act. Under the provisions of that amendment, certain foreign interests operated and proposed to operate in the U.S. coastwise trade. In addition, in the interest of national defense, the Secretary of Homeland Security may suspend the citizen requirements of the Jones Act.

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Should foreign competition be permitted to enter the U.S. coastwise market to any significant extent, it could have an adverse effect on the U.S. marine industry and on us.

Our operations are also subject to a variety of federal, state, local and international laws and regulations regarding the discharge of materials into the environment or otherwise relating to environmental protection. The requirements of these laws and regulations have become more complex and stringent in recent years and may, in certain circumstances, impose strict liability, rendering a company liable for environmental damages and remediation costs without regard to negligence or fault on the part of such party. Aside from possible liability for damages and costs including natural resource damages associated with releases of oil or hazardous materials into the environment, such laws and regulations may expose us to liability for the conditions caused by others or even acts of ours that were in compliance with all applicable laws and regulations at the time such acts were performed. Failure to comply with applicable laws and regulations may result in the imposition of administrative, civil and criminal penalties, revocation of permits, issuance of corrective action orders and suspension or termination of our operations. Moreover, it is possible that changes in the environmental laws, regulations or enforcement policies that impose additional or more restrictive requirements or claims for damages to persons, property, natural resources or the environment could result in substantial costs and liabilities to us. We believe that we are in substantial compliance with currently applicable environmental laws and regulations.

OPA 90 and regulations promulgated pursuant thereto impose a variety of regulations on responsible parties related to the prevention and/or reporting of oil spills and liability for damages resulting from such spills. A responsible party includes the owner or operator of an onshore facility, pipeline or vessel or the lessee or permittee of the area in which an offshore facility is located. OPA 90 assigns liability to each responsible party for oil removal costs and a variety of public and private damages. Under OPA 90, tank vessels of over 3,000 gross tons that carry oil or other hazardous materials in bulk as cargo, a term, which includes our tank barges, are subject to liability limits of the greater of $1,200 per gross ton or $10 million. For any vessels, other than tank vessels, that are subject to OPA 90, the liability limits are the greater of $600 per gross ton or $500,000. A party cannot take advantage of liability limits if the spill was caused by gross negligence or willful misconduct or resulted from violation of a federal safety, construction or operating regulation. In addition, there are no liability limits for vessels carrying crude oil from a well situated on the Continental Shelf. If the party fails to report a spill or to cooperate fully in the cleanup, the liability limits likewise do not apply and certain defenses may not be available. Moreover, OPA 90 imposes on responsible parties the need for proof of financial responsibility to cover at least some costs in a potential spill. As required, we have provided satisfactory evidence of financial responsibility to the U.S. Coast Guard for all of our vessels over 300 tons.

OPA 90 also imposes ongoing requirements on a responsible party, including preparedness and prevention of oil spills, preparation of an oil spill response plan and proof of financial responsibility (to cover at least some costs in a potential spill) for vessels in excess of 300 gross tons. We have engaged the National Response Corporation to serve as our independent contractor for purposes of providing stand-by oil spill response services in all geographical areas of our fleet operations. In addition, our Oil Spill Response Plan has been approved by the U.S. Coast Guard.

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OPA 90 requires that all newly-built tank vessels used in the transportation of petroleum products be built with double hulls and provides for a phase-out period for existing single hull vessels. We previously retired from service three single-hulled tank barges at the end of 2004 pursuant to OPA 90. One of the three single-hulled barges, the *Energy 8701*, returned to service during 2006 after a re-measurement conducted by the U.S. Coast Guard and recertification extending its retirement date to 2015. Modifying or replacing existing vessels to provide for double hulls will be required of all tank barges and tankers in the industry by the year 2015. We are in a favorable position concerning this provision because a significant number of vessels in our fleet of tank barges measure less than 5,000 gross tons. Vessels of such tonnage may continue to operate without double hulls through the year 2015. Under existing legal requirements, therefore, we will be required to modify or retire from service only two of our existing single-hulled tank barges before 2015. However, if there are changes in the law that accelerate the time frame for retirement of such vessels, or if customer policies or preferences that mandate the use of double-hulled vessels become significantly more prevalent, absent our implementation of a more aggressive replacement or newbuild program, such changes in law or in customer mandates could adversely affect our results of operations and financial condition.

The Clean Water Act imposes strict controls on the discharge of pollutants into the navigable waters of the United States. The Clean Water Act also provides for civil, criminal and administrative penalties for any unauthorized discharge of oil or other hazardous substances in reportable quantities and imposes substantial liability for the costs of removal and remediation of an unauthorized discharge. Many states have laws that are analogous to the Clean Water Act and also require remediation of accidental releases of petroleum in reportable quantities. Our OSVs routinely transport diesel fuel to offshore rigs and platforms and also carry diesel fuel for their own use. Our OSVs also transport bulk chemical materials used in drilling activities and liquid mud, which contain oil and oil by-products. In addition, our tank barges are specifically engaged to transport a variety of petroleum products. We maintain vessel response plans as required by the Clean Water Act to address potential oil and fuel spills.

The Comprehensive Environmental Response, Compensation, and Liability Act of 1980, also known as CERCLA or Superfund, and similar laws impose liability for releases of hazardous substances into the environment. CERCLA currently exempts crude oil from the definition of hazardous substances for purposes of the statute, but our operations may involve the use or handling of other materials that may be classified as hazardous substances. CERCLA assigns strict liability to each responsible party for all response and remediation costs, as well as natural resource damages and thus we could be held liable for releases of hazardous substances that resulted from operations by third parties not under our control or for releases associated with practices performed by us or others that were standard in the industry at the time.

The Resource Conservation and Recovery Act regulates the generation, transportation, storage, treatment and disposal of onshore hazardous and non-hazardous wastes and requires states to develop programs to ensure the safe disposal of wastes. We generate non-hazardous wastes and small quantities of hazardous wastes in connection with routine operations. We believe that all of the wastes that we generate are handled in all material respects in compliance with the Resource Conservation and Recovery Act and analogous state statutes.

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In addition to laws and regulations affecting us directly, our operations are also influenced by laws, regulations and policies which affect our customers drilling programs and the oil and natural gas industry as a whole.

The Outer Continental Shelf Lands Act gives the federal government broad discretion to regulate the release of offshore resources of oil and natural gas. Because our operations rely primarily on offshore oil and natural gas exploration, development and production, if the government were to exercise its authority under the Outer Continental Shelf Lands Act to restrict the availability of offshore oil and natural gas leases, such an action would have a material adverse effect on our financial condition and results of operations.

We currently have in place protection and indemnity insurance that includes coverage for pollution incidents. Our OSVs have $5 million in primary insurance coverage for such offshore pollution incidents, with an additional $100 million in excess umbrella coverage. In addition, our tugs and tank barges have insurance coverage for oil spills with a coverage limit of $1 billion.

Both of our principal office locations in Covington, Louisiana and Brooklyn, New York, our field office in Trinidad, as well as all of the vessels in our OSV fleet and a majority of our vessels in our TTB fleet, are certified to the standards of the ISM Code for the safe management and operation of ships and for pollution prevention. In addition, our OSVs, domestically and internationally, participate in the U.S. Coast Guard s Streamlined Inspection Program (SIP), which ensures the overall readiness level of our vessel lifesaving and other critical safety and emergency systems. We believe that our voluntary attainment and maintenance of these certifications and participation in these programs provides evidence of our commitment to operate in a manner that minimizes any impact on the environment from our fleet operations.

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RISK FACTORS

Our results of operations and financial condition can be adversely affected by numerous risks. You should carefully consider the risks described below as well as the other information we have provided in this Annual Report on Form 10-K. The risks described below are not the only ones we face. Additional risks not presently known to us or that we currently deem immaterial may also impair our business operations.

Demand for our OSV services substantially depends on the level of activity in offshore oil and gas exploration, development and production.

The level of offshore oil and gas exploration, development and production activity has historically been volatile and is likely to continue to be so in the future. The level of activity is subject to large fluctuations in response to relatively minor changes in a variety of factors that are beyond our control, including:

- prevailing oil and natural gas prices and expectations about future prices and price volatility;
- the cost of offshore exploration for, and production and transportation of, oil and natural gas;
- worldwide demand for oil and natural gas;
- consolidation of oil and gas and oil service companies operating offshore;
- availability and rate of discovery of new oil and natural gas reserves in offshore areas;
- local and international political and economic conditions and policies;
- technological advances affecting energy production and consumption;
- weather conditions;
- environmental regulation; and
- the ability of oil and gas companies to generate or otherwise obtain funds for exploration and production.

We expect levels of oil and gas exploration, development and production activity to continue to be volatile and affect the demand for our OSVs.

A prolonged, material downturn in oil and natural gas prices is likely to cause a substantial decline in expenditures for exploration, development and production activity, which would likely result in a corresponding decline in the demand for OSVs and thus decrease the utilization and dayrates of our OSVs. Such decreases could have a material adverse effect on our financial condition and results of operations. Moreover, increases in oil and natural gas prices and higher levels of expenditure by oil and gas companies for exploration, development and production may not necessarily result in increased demand for our OSVs.

Increases in the supply of vessels could decrease dayrates.

Certain of our competitors have announced plans to construct new OSVs to be deployed in domestic and foreign locations. A remobilization to the GoM oilfield of U.S.-flagged OSVs

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currently operating in other regions or in non-oilfield applications would result in an increase in OSV capacity in our primary market. Additionally, construction of double-hulled, ocean-going tank barges in sufficient size and number to exceed the replacement of the single-hulled tank barges that have been or still need to be retired under OPA 90 would create an increase in ocean-going tank barge capacity. Further, a repeal, suspension or significant modification of the Jones Act, or the administrative erosion of its benefits, permitting OSVs or tank barges that are either foreign-flagged, foreign-built, foreign-owned, foreign-controlled or foreign-operated to engage in the U.S. coastwise trade, would also result in an increase in capacity. Any increase in the supply of OSVs, whether through new construction, refurbishment or conversion of vessels from other uses, remobilization or changes in law or its application, could not only increase competition for charters and lower utilization and dayrates, which would adversely affect our revenues and profitability, but could also worsen the impact of any downturn in oil and natural gas prices on our results of operations and financial condition. Similarly, any increase in the supply of ocean-going tank barges, could not only increase competition for charters and lower utilization and dayrates, which could negatively affect our revenues and profitability, but could also worsen the impact of any reduction in domestic consumption of refined petroleum products or crude oil on our results of operations and financial condition.

Intense competition in our industry could reduce our profitability and market share.

Contracts for our OSVs and tank barges are generally awarded on an intensely competitive basis. The most important factors determining whether a contract will be awarded include:

- quality and capability of the vessels and crew members;
- ability to meet the customer s schedule;
- safety record;
- reputation;
- price; and
- experience.

Some of our competitors, including diversified multinational companies in the OSV segment, have substantially greater financial resources and larger operating staffs than we do. They may be better able to compete in making vessels available more quickly and efficiently, meeting the customer s schedule and withstanding the effect of declines in dayrates and utilization rates. They may also be better able to weather a downturn in the oil and gas industry. As a result, we could lose customers and market share to these competitors. Some of our competitors may also be willing to accept lower dayrates in order to maintain utilization, which can have a negative impact upon dayrates and utilization in both of our market segments.

The failure to successfully complete construction or conversion of our vessels or repairs, maintenance and routine drydockings on schedule and on budget and to

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utilize such vessels and the other vessels in our fleet at profitable levels could adversely affect our financial condition and results of operations.

We have 13 new generation OSVs and three double-hulled, ocean-going tank barges currently under construction, four ocean-going tugs being retrofitted and two coastwise sulfur tankers currently undergoing conversion into MPSVs. We have also announced plans to construct additional double-hulled tank barges and may plan to construct other such vessels as market conditions warrant. We also routinely engage shipyards to drydock our vessels for regulatory compliance and to provide repair and maintenance. Our construction projects and drydockings are subject to the risks of delay and cost overruns inherent in any large construction project, including shortages of equipment, lack of shipyard availability, unforeseen engineering problems, work stoppages, weather interference, unanticipated cost increases, inability to obtain necessary certifications and approvals and shortages of materials or skilled labor. Significant delays could have a material adverse effect on anticipated contract commitments or anticipated revenues with respect to vessels under construction, conversion or for other drydockings. Further, significant cost overruns or delays for vessels under construction, conversion or retrofit not adequately protected by liquidated damages provisions, in general could adversely affect our financial condition and results of operations. Moreover, customer demand for vessels currently under construction or conversion may not be as strong as we presently anticipate, and our inability to obtain contracts on anticipated terms or at all may have a material adverse effect on our revenues and profitability. In addition, our OSVs are typically chartered or hired to provide services to a specified drilling rig. A delay in the availability of the drilling rig to our customer may have an adverse impact on our utilization of the contracted vessel and thus on our financial condition and results of operations. Likewise, there are several deepwater-capable drilling rigs under construction that, if delayed or cancelled, could adversely impact us.

If we are unable to acquire additional vessels or businesses and successfully integrate them into our operations, our ability to grow may be limited.

We regularly consider possible acquisitions of single vessels, vessel fleets and businesses that complement our existing operations to enable us to grow our business. We can give no assurance that we will be able to identify desirable acquisition candidates or that we will be successful in entering into definitive agreements or closing such acquisitions on satisfactory terms. An inability to acquire additional vessels or businesses may limit our growth potential. Even if we consummate an acquisition, we may be unable to integrate it into our existing operations successfully or realize the anticipated benefits of the acquisition. The process of integrating acquired operations into our own may result in unforeseen operating difficulties, may require significant management attention and financial resources.

Revenues from our TTB business could be adversely affected by a decline in demand for domestic refined petroleum products and crude oil or a change in existing methods of delivery in response to insufficient availability of TTB services and other conditions.

A reduction in domestic consumption of refined petroleum products or crude oil may adversely affect the revenues of our TTB business and, therefore, our financial condition and results of operation. Weather conditions also affect demand for our TTB services. For example, a mild winter may reduce demand for heating oil in the northeastern United States.

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Moreover, alternative methods of delivery of refined petroleum products or crude oil may develop as a result of insufficient availability of TTB services, the cost of compliance with homeland security, environmental regulations or increased liabilities connected with the transportation of refined petroleum products and crude oil. For example, long-haul transportation of refined petroleum products and crude oil is generally less costly by pipeline than by tank barge. While there are significant impediments to building new pipelines, such as high capital costs and environmental concerns, entities may propose new pipeline construction to meet demand for petroleum products. To the extent new pipeline segments are built or existing pipelines converted to carry petroleum products, such activity could have an adverse effect on our ability to compete in particular markets.

The early termination of contracts on our vessels could have an adverse effect on our operations.

Most of the long-term contracts for our vessels contain early termination options in favor of the customer; however, some have early termination penalties or other provisions designed to discourage the customers from exercising such options. We cannot assure that our customers would not choose to exercise their termination rights in spite of such penalties or the threat of litigation with us. Until replacement of such business with other customers, any termination could temporarily disrupt our business or otherwise adversely affect our financial condition and results of operations. We might not be able to replace such business on economically equivalent terms.

We are subject to complex laws and regulations, including environmental regulations, that can adversely affect the cost, manner or feasibility of doing business.

Increasingly stringent federal, state, local and foreign laws and regulations governing worker health and safety and the manning, construction and operation of vessels significantly affect our operations. Many aspects of the marine industry are subject to extensive governmental regulation by the United States Coast Guard, the National Transportation Safety Board and the United States Customs Service, and their foreign equivalents, and to regulation by private industry organizations such as the American Bureau of Shipping. The Coast Guard and the National Transportation Safety Board set safety standards and are authorized to investigate vessel accidents and recommend improved safety standards, while the Customs Service is authorized to inspect vessels at will. Our operations are also subject to federal, state, local and international laws and regulations that control the discharge of pollutants into the environment or otherwise relate to environmental protection. Compliance with such laws, regulations and standards may require installation of costly equipment, increased manning, or operational changes. While we endeavor to comply with all applicable laws, we might not and our failure to comply with applicable laws and regulations may result in administrative and civil penalties, criminal sanctions, imposition of remedial obligations or the suspension or termination of our operations. Some environmental laws impose strict liability for remediation of spills and releases of oil and hazardous substances, which could subject us to liability without regard to whether we were negligent or at fault. These laws and regulations may expose us to liability for the conduct of, or conditions caused by, others, including charterers. Moreover, these laws and regulations could change in ways that substantially increase costs that we may not be able to pass along to our customers. Any changes in laws, regulations or standards that would impose additional requirements or restrictions could adversely affect our financial condition and results of operations.

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We are also subject to the Merchant Marine Act of 1936, which provides that, upon proclamation by the President of a national emergency or a threat to the security of the national defense, the Secretary of Transportation may requisition or purchase any vessel or other watercraft owned by United States citizens (which includes United States corporations), including vessels under construction in the United States. If one of our OSVs, tugs or tank barges were purchased or requisitioned by the federal government under this law, we would be entitled to be paid the fair market value of the vessel in the case of a purchase or, in the case of a requisition, the fair market value of charter hire. However, if one of our tugs is requisitioned or purchased and its associated tank barge is left idle, we would not be entitled to receive any compensation for the lost revenues resulting from the idled barge. We would also not be entitled to be compensated for any consequential damages we suffer as a result of the requisition or purchase of any of our OSVs, tugs or tank barges. The purchase or the requisition for an extended period of time of one or more of our OSVs, tugs or tank barges could adversely affect our results of operations and financial condition.

Finally, we are subject to the Merchant Marine Act of 1920, commonly referred to as the Jones Act, which requires that vessels engaged in coastwise trade to carry cargo between U.S. ports be documented under the laws of the United States and be controlled by U.S. citizens. To ensure that we are determined to be a U.S. citizen as defined under these laws, our certificate of incorporation contains certain restrictions on the ownership of our capital stock by non-U.S. citizens and establishes certain mechanisms to maintain compliance with these laws. If we are determined at any time not to be in compliance with these citizenship requirements, our vessels would become ineligible to engage in the coastwise trade in U.S. domestic waters, and our business and operating results would be adversely affected. The Jones Act s provisions restricting coastwise trade to vessels controlled by U.S. citizens have recently been circumvented by foreign interests that seek to engage in trade reserved for vessels controlled by U.S. citizens and otherwise qualifying for coastwise trade. Legal challenges against such actions are difficult, costly to pursue and are of uncertain outcome. To the extent such efforts are successful and foreign competition is permitted, such competition could have a material adverse effect on domestic companies in the offshore service vessel industry and on our financial condition and results of operations. In addition, in the interest of national defense, the Secretary of Homeland Security is authorized to suspend the coastwise trading restrictions imposed by the Jones Act on vessels not controlled by U.S. citizens. Such a waiver was issued following Hurricane Katrina and was in effect on a temporary basis for tank vessels that carried petroleum products. A more limited waiver continues in existence for vessels that carry petroleum cargoes from the Strategic Petroleum Reserve.

Our business involves many operating risks that may disrupt our business or otherwise result in substantial losses, and insurance may be unavailable or inadequate to protect us against these risks.

Our vessels are subject to operating risks such as:

- catastrophic marine disaster;
- adverse weather and sea conditions;
- mechanical failure;
- collisions or allisions;

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oil and hazardous substance spills;

navigation errors;

acts of God; and

war and terrorism.

The occurrence of any of these events may result in damage to or loss of our vessels and their tow or cargo or other property and injury to passengers and personnel. If any of these events were to occur, we could be exposed to liability for resulting damages and possible penalties, that pursuant to typical marine indemnity policies, we must pay and then seek reimbursement from our insurer. Affected vessels may also be removed from service and thus be unavailable for income-generating activity. While we believe our insurance coverage is at adequate levels and insures us against risks that are customary in the industry, we may be unable to renew such coverage in the future at commercially reasonable rates. Moreover, existing or future coverage may not be sufficient to cover claims that may arise. Finally, we do not maintain insurance for loss of income resulting from a marine casualty

Our expansion into international markets subjects us to risks inherent in conducting business internationally.

Over the past several years we have derived an increasing portion of our revenues from foreign sources. We therefore face risks inherent in conducting business internationally, such as legal and governmental regulatory requirements, potential vessel seizure or nationalization of assets, import-export quotas or other trade barriers, difficulties in collecting accounts receivable and longer collection periods, political and economic instability, kidnapping of or assault on personnel, adverse tax consequences, difficulties and costs of staffing international operations, currency exchange rate fluctuations and language and cultural differences. All of these risks are beyond our control and difficult to insure against. We cannot predict the nature and the likelihood of any such events. If such an event should occur, however, it could have a material adverse effect on our financial condition and results of operations.

Future results of operations depend on the long-term financial stability of our customers.

Many of the contracts we enter into for our vessels are full utilization contracts with initial terms ranging from one to five years. We enter into these long-term contracts with our customers based on a credit assessment at the time of execution. Our financial condition in any period may therefore depend on the long-term stability and creditworthiness of our customers. We can provide no assurance that our customers will fulfill their obligations under our long-term contracts and the insolvency or other failure of a customer to fulfill its obligations under such contract could adversely affect our financial condition and results of operations.

We may be unable to attract and retain qualified, skilled employees necessary to operate our business.

Our success depends in large part on our ability to attract and retain highly skilled and qualified personnel. Our inability to hire, train and retain a sufficient number of qualified employees could impair our ability to manage, maintain and grow our business.

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In crewing our vessels, we require skilled employees who can perform physically demanding work. As a result of the volatility of the oil and gas industry and the demanding nature of the work, potential vessel employees may choose to pursue employment in fields that offer a more desirable work environment at wage rates that are competitive with ours. With a reduced pool of workers, it is possible that we will have to raise wage rates to attract workers and to retain our current employees such as occurred in 2006. If we are not able to increase our service rates to our customers to compensate for wage-rate increases, our financial condition and results of operations may be adversely affected. If we are unable to recruit qualified personnel we may not be able to operate our vessels at full utilization, which would adversely affect our results of operations.

Our employees are covered by federal laws that may subject us to job-related claims in addition to those provided by state laws.

Some of our employees are covered by provisions of the Jones Act, the Death on the High Seas Act and general maritime law. These laws preempt state workers compensation laws and permit these employees and their representatives to pursue actions against employers for job-related incidents in federal courts based on tort theories. Because we are not generally protected by the damage limits imposed by state workers compensation statutes, we may have greater exposure for any claims made by these employees.

Our success depends on key members of our management, the loss of whom could disrupt our business operations.

We depend to a large extent on the efforts and continued employment of our executive officers and key management personnel. We do not maintain key-man insurance. The loss of services of one or more of our executive officers or key management personnel could have a negative impact on our financial condition and results of operations.

Restrictions contained in the indenture governing our 6.125% Senior Notes due 2014 and in the agreement governing our revolving credit facility may limit our ability to obtain additional financing and to pursue other business opportunities.

Covenants contained in the indenture governing our 6.125% Senior Notes due 2014 and in the agreement governing our revolving credit facility require us to meet certain financial tests, which may limit or otherwise restrict:

- our flexibility in operating, planning for, and reacting to changes, in our business;
- our ability to dispose of assets, withstand current or future economic or industry downturns and compete with others in our industry for strategic opportunities; and
- our ability to obtain additional financing for working capital, capital expenditures, including our newbuild programs, acquisitions, general corporate and other purposes.

We have high levels of fixed costs that will be incurred regardless of our level of business activity.

Our business has high fixed costs, and downtime or low productivity due to reduced demand, weather interruptions or other causes can have a significant negative effect on our operating results and financial condition.

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If we are required to retire our existing single-hulled tank barges earlier than anticipated due to either regulatory or other requirements, it could adversely affect our business.

OPA 90 requires that all newly-built tank vessels used in the transportation of petroleum products be built with double hulls and provides for a phase-out period for existing single-hulled vessels. Modifying or replacing existing vessels to provide for double hulls will be required for all tank barges and tankers in the industry by the year 2015. A significant number of vessels in our tank barge fleet measure less than 5,000 gross tons. Under current law, certain of our vessels may continue to operate without double hulls through 2014. However, if there are changes in the law that accelerate the time frame for retirement of such vessels, or if customer policies or preferences that mandate the use of double-hulled vessels become significantly more prevalent, absent our implementation of a more aggressive replacement or newbuild program, such changes in law or in customer mandates could adversely affect our results of operations and financial condition.

We may not have the ability to raise the funds necessary to settle conversion of the 1.625% convertible senior notes or to purchase such notes upon a fundamental change or on other purchase dates as defined in the agreement, and our future debt may contain limitations on our ability to pay cash upon conversion or repurchase of shares.

Upon conversion of the 1.625% convertible senior notes, we may pay a settlement amount in cash and shares of our common stock, if any, based upon a 25 trading-day observation period. In addition, on November 15, 2013, November 15, 2016 and November 15, 2021, holders of the 1.625% convertible senior notes may require us to purchase their notes for cash. We cannot assure you that we will have sufficient financial resources, or would be able to arrange financing, to pay the settlement amount in cash, or the purchase price or fundamental change purchase price for the 1.625% convertible senior notes tendered by the holders in cash. Further, our ability to pay the settlement amount in cash, or the purchase price or fundamental change purchase price for the 1.625% convertible senior notes in cash may be subject to limitations in our revolving credit facility or any other indebtedness we may have in the future. If the holders of the 1.625% convertible senior notes convert such notes or require us to repurchase them, we may seek the consent of our lenders or attempt to refinance the debt, but there can be no assurance that we will be able to do so. Failure by us to pay the settlement amount upon conversion or purchase the notes when required will result in an event of default with respect to the notes, which may also result in the acceleration of our other indebtedness.

Our revenues and operating results may vary significantly from quarter to quarter due to a number of factors such as volatility in our vessel dayrates, changes in utilization, vessel incidents and other unforeseen matters. Many of these factors that may cause our actual financial results to vary from our publicly disclosed earnings guidance and forecasts are outside of our control.

Our actual financial results might vary from those anticipated by us or by securities analysts and investors, and these variations could be material. From time to time we publicly provide earnings or other forms of guidance, which reflect our predictions about future dayrates, utilization, operating costs and capital structure, among other factors. These

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numerous assumptions may be impacted by factors that are beyond our control and might not turn out to be correct.

We are susceptible to unexpected increases in operating expenses such as materials and supplies, crew wages, maintenance and repairs, and insurance costs.

Many of our operating costs are unpredictable and vary based on events beyond our control. Our gross margins will vary based on fluctuations in our operating costs. If our costs increase or we encounter unforeseen costs, we may not be able to recover such costs from our customers, which could adversely affect our financial position, results of operations and cash flows.

The convertible note hedge and warrant transactions may affect the value of our common stock.

In connection with the original issuance of the 1.625% convertible senior notes, we entered into convertible note hedge and warrant transactions with counterparties that include affiliates of the initial purchasers of the convertible senior notes. The convertible note hedge transactions are expected to reduce the potential dilution upon conversion of such notes. However, if the warrants are exercised, such exercise would mitigate some of that reduction. In connection with these hedging and warrant transactions, such counterparties or their affiliates may enter into, or may unwind, various derivatives and/or purchase or sell our common stock in secondary market transactions (and are likely to do so during any observation period related to a conversion of notes).

The effect, if any, of these convertible note hedge and warrant transactions or any of these hedging activities on the market price of our common stock or the convertible senior notes will depend in part on market conditions and cannot be ascertained at this time, but any of these activities could materially and adversely affect the value of our common stock.

The fundamental change purchase feature of the 1.625% convertible senior notes and provisions of our certificate of incorporation, bylaws, stockholder rights plan and Delaware law may delay or prevent an otherwise beneficial takeover attempt of our company.

The terms of the notes require us to purchase the notes for cash in the event of a fundamental change. A takeover of our company would trigger the requirement that we purchase the notes. Furthermore, our certificate of incorporation and bylaws, Delaware corporations law, and our stockholder rights plan contain provisions that could have the effect of making it more difficult for a third party to acquire, or discourage a third party from attempting to acquire, control of us. These provisions could limit the price that investors might be willing to pay in the future for shares of our common stock and may have the effect of delaying or preventing a takeover of our company that would otherwise be beneficial to investors.

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Conversion of the 1.625% convertible senior notes or exercise of the warrants issued in the warrant transactions may dilute the ownership interest of existing stockholders.

The conversion of the 1.625% convertible senior notes or exercise of some or all of the warrants we issued in the warrant transactions may dilute the ownership interests of existing stockholders. Although the convertible note hedge transactions are expected to reduce potential dilution upon conversion of the 1.625% convertible senior notes, the warrant transactions could have a dilutive effect on our earnings per share to the extent that the price of our common stock exceeds the strike price of the warrants. Any sales in the public market of our common stock issuable upon such conversion of the 1.625% convertible senior notes could adversely affect prevailing market prices of our common stock. In addition, the anticipated exercise of the warrants for shares of our common stock could depress the price of our common stock.

Operating Hazards and Insurance

The operation of our vessels is subject to various risks, such as catastrophic marine disaster, adverse weather conditions, mechanical failure, collision and navigation errors, all of which represent a threat to personnel safety and to our vessels and cargo. We maintain insurance coverage that we consider customary in the industry against certain of these risks, including, as discussed above, $1 billion in pollution insurance for the TTB fleet and $105 million of pollution coverage for the OSVs. We believe that our current level of insurance is adequate for our business and consistent with industry practice, and we have not experienced a loss in excess of our policy limits. We may not be able to obtain insurance coverage in the future to cover all risks inherent in our business, or insurance, if available, may be at rates that we do not consider to be commercially reasonable. In addition, as single-hulled tank barges increase in age, insurers may be less willing to insure and customers less willing to hire single-hulled vessels. The terms of our entry into a mutual protection and indemnity association covering marine risks relating to our TTB business allows additional premiums to be called for from time to time, and paid by association members in respect of unanticipated reserve requirements of the association.

Employees

On December 31, 2006, we had 742 employees, including 583 operating personnel and 159 corporate, administrative and management personnel. None of our employees are represented by a union or employed pursuant to a collective bargaining agreement or similar arrangement. We have not experienced any strikes or work stoppages, and our management believes that we continue to enjoy good relations with our employees.

Properties

Our corporate headquarters are located in Covington, Louisiana. Our primary office lease covers 23,756 square feet and has an initial term of five years, which commenced in September 2003, with two additional five-year renewal periods. In August 2005 and December 2005, we entered into agreements that increased our total office space by an additional 5,500 square feet and 4,700 square feet, respectively. We also hold a one-year lease on 4,500-square-feet in a warehouse near our corporate headquarters to maintain

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spare parts inventory. To support our OSV operations in the GoM, we lease a shore base facility in Port Fourchon, Louisiana operated under the name HOS Port. Our facility lease for HOS Port, which commenced in December 2005, has an initial term of eight years with four additional five-year renewal periods. The base facility covers approximately 24 acres of land and includes approximately 1,850 linear feet of dock space and 13,125 square feet of warehouse and office space. For local support in Puerto Rico, we lease an office consisting of approximately 1,900 square feet. To support our operations in the northeastern United States, we lease office space and warehouse space in Brooklyn, New York, consisting of approximately 66,760 square feet. We also lease dock space, consisting of approximately 36,000 square feet, in Brooklyn, New York. We operate our TTB fleet from these New York facilities. The lease on our Brooklyn facilities is currently scheduled to expire in March 2007 and we intend to renew our lease for that facility prior to expiration. We believe that our facilities, including waterfront locations used for vessel dockage and certain vessel repair work, provide an adequate base of operations for the foreseeable future. Information regarding our fleet is set forth above in Offshore Supply Vessels Our OSV Business and Tugs and Tank Barges Our Tug and Tank Barge Business .

Seasonality of Business

Demand for our OSV services is directly affected by the levels of offshore drilling activity. Budgets of many of our customers are based upon a calendar year, and demand for our services has historically been stronger in the third and fourth calendar quarters when allocated budgets are expended by our customers and weather conditions are more favorable for offshore activities. Many other factors, such as the expiration of drilling leases and the supply of and demand for oil and natural gas, may affect this general trend in any particular year. In addition, we typically have an increase in demand for our OSVs to survey and repair offshore infrastructure immediately following major hurricanes in the GoM.

Tank barge services are significantly affected by the strength of the U.S. economy, changes in weather patterns and population growth that affect the consumption of and the demand for refined petroleum products and crude oil. The TTB market, in general, is marked by steady demand over time, although such demand is seasonal and often dependent on weather conditions. Unseasonably mild winters result in significantly lower demand for heating oil in the northeastern United States, which is a significant market for our TTB services. Conversely, the summer driving season can increase demand for automobile fuel and, accordingly, the demand for our services.

Availability of Reports, Certain Committee Charters and Other Information

Our website address is http://www.hornbeckoffshore.com/. We make available on this website, free of charge, access to our Annual Reports on Form 10-K, Quarterly Reports on Form 10-Q, Current Reports on Form 8-K and amendments to those reports, as well as other documents that we file with, or furnish to, the Commission pursuant to Sections 13(a) or 15(d) of the Exchange Act, as soon as reasonably practicable after such documents are filed with, or furnished to, the Commission. You may read and copy any materials we file with the Commission at the Commission s Public Reference Room at 100 F Street, N.E., Washington, DC 20549. You can obtain information on the operation of the Public Reference Room by calling the Commission at 1-800-732-0330. The SEC maintains an Internet site that contains

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reports, proxy and information statements, and other information regarding issuers that file electronically with the Commission at http://www.sec.gov

Our Corporate Governance Guidelines, Employee Code of Business Conduct and Ethics (which applies to all employees, including our Chief Executive Officer and certain Financial and Accounting Officers), Board of Directors Code of Business Conduct and Ethics, and the charters for our Audit, Nominating/Corporate Governance and Compensation Committees, can all be found on the Investor Relations page of our website (http://www.hornbeckoffshore.com/) under Corporate Governance . We intend to disclose any changes to or waivers from the Employee Code of Business Conduct and Ethics that would otherwise be required to be disclosed under Item 5.05 of Form 8-K on our website. We will also provide printed copies of these materials to any stockholder upon request to Hornbeck Offshore Services Inc., Attn: Chief Compliance Officer, 103 Northpark Boulevard, Suite 300, Covington, Louisiana 70433. The information on our website is not, and shall not be deemed to be, a part of this report or incorporated into any other filings we make with the Commission.

Item 3 ***Legal Proceedings***

On January 18, 2007, Anthony Caiafa filed an action in the United States District Court for the Eastern District of Louisiana against Hornbeck Offshore Services, Inc. and Todd M. Hornbeck, our Chairman of the Board, President, and Chief Executive Officer. On January 24, 2007, Thomas Schedler filed a similar action in the United States District Court for the Eastern District of Louisiana against Hornbeck Offshore Services, Inc., Todd M. Hornbeck and James O. Harp, Jr., our Executive Vice President and Chief Financial Officer. On January 26, 2007, Michael D. Fontenelle filed another similar action in the United States District Court for the Eastern District of Louisiana against Hornbeck Offshore Services, Inc. and Todd M. Hornbeck. On February 8, 2007, Oakmont Capital Management, LLC filed a similar action in the United States District Court for the Eastern District of Louisiana against Hornbeck Offshore Services, Inc., Todd M. Hornbeck, James O. Harp, Jr. and Carl G. Annessa, our Executive Vice President and Chief Operating Officer. These lawsuits purport to be filed as a class action on behalf of the plaintiffs and other similarly situated purchasers of our securities from November 1, 2006 to January 10, 2007. In their complaints, the plaintiffs allege that Hornbeck Offshore Services, Inc. and the other defendants violated Section 10(b) of the Securities Exchange Act of 1934, as amended, and Rule 10b-5 thereunder, by allegedly making false and misleading statements, and/or by omitting to state material facts necessary to make the statements not misleading, in connection with its forward earnings guidance and its January 10, 2007 announcement of preliminary financial results for the fourth quarter of 2006 and the full year of 2006 that fell short of such guidance and indicated an anticipated reduction in 2007 guidance. The Company and such officers deny these allegations and believe that these actions are without merit. We intend to defend these actions vigorously. However, we cannot predict whether we will prevail in the actions or estimate the amount of damages that we might incur. We are also unable to estimate any reimbursement that we may receive from insurance policies in the event that we incur any damages or costs in connection with these actions.

Item 4 ***Submission of Matters to a Vote of Security Holders***

None.

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PART II

Item 5 ***Market for the Registrant s Common Stock and Related Stockholder Matters***

Our common stock, $0.01 par value, trades on the New York Stock Exchange, or NYSE, under the trading symbol HOS . The following table sets forth, for the quarterly period indicated, the high and low sale prices for our common stock as reported by the NYSE during 2006 and 2005.

	2006		2005	
	High	Low	High	Low
First Quarter	$ 40.73	$ 29.66	$ 26.14	$ 18.10
Second Quarter	$ 40.96	$ 29.44	$ 27.73	$ 20.10
Third Quarter	$ 36.74	$ 29.62	$ 37.49	$ 26.81
Fourth Quarter	$ 38.72	$ 30.47	$ 36.89	$ 27.81

On January 31, 2007, we had 174 holders of record of our common stock.

We have not previously declared or paid, and we do not plan to declare or pay in the foreseeable future, any cash dividends on our common stock. We presently intend to retain all of the cash our business generates to meet our working capital requirements and fund future growth. Any future payment of cash dividends will depend upon the financial condition, capital requirements and earnings of our Company, as well as other factors that our Board of Directors may deem relevant. In addition, the indenture governing our 6.125% senior notes and our revolving credit facility include restrictions on our ability to pay cash dividends on our common stock. See Item 7 Management s Discussion and Analysis of Financial Condition and Results of Operations and Note 6 of the notes to our consolidated financial statements for further discussion.

On November 13, 2006, we completed a private offering of $250.0 million of our 1.625% convertible senior unsecured notes due 2026, or the convertible notes, to qualified institutional buyers pursuant to Rule 144A under the Securities Act. In connection with the sale of the convertible notes, we entered into convertible note hedge transactions with respect to our common stock with Jefferies International Limited, Bear, Stearns International Limited and AIG-FP Structured Finance (Cayman) Limited, or the dealers. Each of the convertible note hedge transactions involves the purchase of call options, or the call options, with exercise prices equal to the conversion price of the convertible notes, and is intended to limit exposure to dilution to the Company s stockholders upon the potential future conversion of the convertible notes. The convertible note hedge transactions cover approximately the same number of shares of the Company s common stock underlying the convertible notes, subject to customary anti-dilution adjustments, at a strike price of approximately $48.48 per share of common stock.

We also entered into separate warrant transactions, or warrants, whereby we sold to the counterparties warrants to acquire approximately the same number of shares of our common stock underlying the convertible notes, subject to customary anti-dilution adjustments, at a strike price of $62.59 per share of common stock. On exercise of the warrants, we have the option to deliver cash

or shares of our common stock equal to the difference between the then market price and strike price. The issuance of the warrants and the underlying shares of

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our common stock issuable upon exercise of the warrants was not registered under the Securities Act, and the warrants and common stock issuable upon exercise of the warrants cannot be offered or sold in the United States absent registration under the Securities Act or an applicable exemption from such registration requirements. For more information regarding this convertible note offering and convertible note hedge and warrant transactions, please refer to the Liquidity and Capital Resources section of Management s Discussion and Analysis of Financial Condition and Results of Operations or Note 6 within the consolidated financial statements contained within this Annual Report on Form 10-K.

In connection with the issuance of the convertible senior notes, in November 2006 our Board of Directors authorized us to use up to 30% of the net proceeds from the convertible senior note offering to repurchase shares of the Company s common stock.

Period	Total Number of Shares Repurchased	Average Price Paid per Share	Total Number of Shares Purchased as Part of Publicly Announced Plans or Programs	Maximum number of Shares that May Yet be Purchased Under the Plans or Programs
October 1-31, 2006		$		
November 1-30, 2006	1,795,100	$ 35.26	1,795,100	
December 1-31, 2006		$		
Total Shares Repurchased	1,795,100	$ 35.26	1,795,100	

See Item 12 Security Ownership of Certain Beneficial Owners and Management and Related Stockholder Matters for information regarding shares of common stock authorized for issuance under our equity compensation plans.

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Item 6 ***Selected Financial Data***

SELECTED HISTORICAL CONSOLIDATED FINANCIAL INFORMATION

(In thousands, except operating and per share data)

Our selected historical consolidated financial information as of and for the periods ended December 31, 2006, 2005, 2004, 2003 and 2002 was derived from our audited historical consolidated financial statements prepared in accordance with generally accepted accounting principles, or GAAP. The data should be read in conjunction with and is qualified in its entirety by reference to Management s Discussion and Analysis of Financial Condition and Results of Operations and our historical consolidated financial statements and the notes to those statements included elsewhere in this Annual Report on Form 10-K.

	Year Ended December 31,				
	2006	2005	2004	2003	2002
Statements of Operations Data:					
Revenues	$ 274,551	$ 182,586	$ 132,261	$ 110,813	$ 92,585
Operating expenses	95,591	66,910	58,520	46,805	36,337
Depreciation and amortization	32,021	27,270	23,135	17,590	12,296
General and administrative expenses	28,388	20,327	14,759	10,731	9,681
Gain on sale of assets	1,854	1,893	65	713	32
Operating income	120,405	69,972	35,912	36,400	34,303
Loss on early extinguishment of debt		1,698	22,443		
Interest income	16,074	3,178	356	178	667
Interest expense	17,675	12,558	17,698	18,523	16,207
Other income (loss) (1)	70	87	70	(7)	23
Income (loss) before income taxes	118,874	58,981	(3,803)	18,048	18,786
Income tax expense (benefit)	43,159	21,538	(1,320)	6,858	7,139
Net income (loss)	75,715	37,443	(2,483)	11,190	11,647
Per Share Data:					
Basic net income (loss)	$ 2.81	$ 1.67	$ (0.13)	$ 0.84	$ 0.96
Diluted net income (loss)	$ 2.76	$ 1.64	$ (0.13)	$ 0.82	$ 0.94
Weighted average basic shares outstanding	26,966	22,369	19,330	13,397	12,098
Weighted average diluted shares outstanding(2)	27,461	22,837	19,330	13,604	12,428
Balance Sheet Data (at period end):					
Cash and cash equivalents	$ 474,261	$ 271,739	$ 54,301	$ 12,899	$ 22,228
Working capital	489,261	290,471	52,556	17,698	22,265
Property, plant, and equipment, net	531,951	462,041	361,219	316,715	226,232
Total assets	1,098,380	796,675	460,571	365,242	278,290
Total short-term debt (3)			15,449		
Total long-term debt (4)	549,497	299,449	225,000	212,677	172,306
Total stockholders equity	454,873	429,495	182,904	112,395	71,876
Statement of Cash Flows Data:					