TIDEWATER INC
Form 10-Q
July 27, 2006

# UNITED STATES

# SECURITIES AND EXCHANGE COMMISSION

**Washington, D.C. 20549**

# FORM 10-Q

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

**For the Quarterly Period Ended June 30, 2006**

**OR**

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

**For the transition period from to .**

**Commission file number: 1-6311**

# Tidewater Inc.

**(Exact name of registrant as specified in its charter)**

| | |
|---|---|
| **Delaware** | **72-0487776** |
| **(State or other jurisdiction of incorporation or organization)** | **(I.R.S. employer identification no.)** |

**601 Poydras St., Suite 1900**

**New Orleans, Louisiana 70130**

**(Address of principal executive offices, including zip code)**

**(504) 568-1010**

**(Registrant s telephone number, including area code)**

**N/A**

***(Former name or former address, if changed since last report)***

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 of such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes x No ¨

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

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

56,323,299 shares of Tidewater Inc. common stock $.10 par value per share were outstanding on July 7, 2006. Excluded from the calculation of shares outstanding at July 7, 2006 are 2,025,125 shares held by the Registrant s Grantor Stock Ownership Trust. Registrant has no other class of common stock outstanding.

## PART I. FINANCIAL INFORMATION

**ITEM 1. FINANCIAL STATEMENTS**

**TIDEWATER INC.**

**UNAUDITED CONDENSED CONSOLIDATED BALANCE SHEETS**

| (In thousands, except share and par value data) | June 30, 2006 | March 31, 2006 |
|---|---|---|
| ASSETS | | |
| Current assets: | | |
| Cash and cash equivalents | $ 224,298 | 246,109 |
| Trade and other receivables, net | 258,654 | 237,428 |
| Marine operating supplies | 42,295 | 41,181 |
| Other current assets | 9,959 | 4,325 |
| Total current assets | 535,206 | 529,043 |
| Investments in, at equity, and advances to unconsolidated companies | 24,025 | 34,308 |
| Properties and equipment: | | |
| Vessels and related equipment | 2,480,799 | 2,457,947 |
| Other properties and equipment | 50,177 | 50,205 |
| | 2,530,976 | 2,508,152 |
| Less accumulated depreciation and amortization | 1,149,400 | 1,134,425 |
| Net properties and equipment | 1,381,576 | 1,373,727 |
| Goodwill | 328,754 | 328,754 |
| Other assets | 79,668 | 98,708 |
| Total assets | $ 2,349,229 | 2,364,540 |
| LIABILITIES AND STOCKHOLDERS EQUITY | | |
| Current liabilities: | | |
| Accounts payable and accrued expenses | 94,470 | 97,265 |
| Accrued property and liability losses | 7,111 | 7,223 |
| Other current liabilities | 18,214 | 11,266 |
| Total current liabilities | 119,795 | 115,754 |
| Long-term debt | 300,000 | 300,000 |
| Deferred income taxes | 177,177 | 175,267 |
| Accrued property and liability losses | 20,376 | 21,732 |
| Other liabilities and deferred credits | 94,083 | 92,666 |
| Stockholders equity: | | |
| Common stock of $.10 par value, 125,000,000 shares authorized, issued 58,348,424 shares at June and 60,310,164 shares at March | 5,835 | 6,031 |
| Other stockholders equity | 1,631,963 | 1,653,090 |
| Total stockholders equity | 1,637,798 | 1,659,121 |

| | | |
|---|---|---|
| Total liabilities and stockholders equity | $ 2,349,229 | 2,364,540 |

See Notes to Unaudited Condensed Consolidated Financial Statements.

**TIDEWATER INC.**

**UNAUDITED CONDENSED CONSOLIDATED STATEMENTS OF EARNINGS**

| (In thousands, except share and per share data) | | Three Months Ended June 30, 2006 | 2005 |
|---|---|---|---|
| Revenues: | | | |
| Vessel revenues | $ | 258,685 | 185,392 |
| Other marine revenues | | 11,135 | 6,775 |
| | | 269,820 | 192,167 |
| Costs and expenses: | | | |
| Vessel operating costs | | 119,762 | 106,210 |
| Costs of other marine revenues | | 9,914 | 4,590 |
| Depreciation and amortization | | 27,797 | 26,337 |
| General and administrative | | 23,692 | 19,259 |
| Gain on sales of assets | | (2,713) | (1,634) |
| | | 178,452 | 154,762 |
| | | 91,368 | 37,405 |
| Other income (expenses): | | | |
| Foreign exchange gain (loss) | | (769) | 608 |
| Equity in net earnings of unconsolidated companies | | 2,449 | 2,167 |
| Minority interests | | 20 | (23) |
| Interest and miscellaneous income | | 4,777 | 1,205 |
| Interest and other debt costs | | (2,580) | (2,362) |
| | | 3,897 | 1,595 |
| Earnings before income taxes | | 95,265 | 39,000 |
| Income taxes | | 23,816 | 10,140 |
| Net earnings | $ | 71,449 | 28,860 |
| Basic earnings per common share | $ | 1.25 | .50 |
| Diluted earnings per common share | $ | 1.23 | .50 |
| Weighted average common shares outstanding | | 57,296,433 | 57,230,937 |
| Incremental common shares from stock options | | 711,830 | 351,098 |
| Adjusted weighted average common shares | | 58,008,263 | 57,582,035 |
| Cash dividends declared per common share | $ | .15 | .15 |

See Notes to Unaudited Condensed Consolidated Financial Statements.

**TIDEWATER INC.**

**UNAUDITED CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS**

| | Three Months Ended June 30, | |
|---|---|---|
| **(In thousands)** | **2006** | **2005** |
| Net cash provided by operating activities | $ 98,337 | 34,308 |
| Cash flows from investing activities: | | |
| Proceeds from sales of assets | 7,021 | 3,210 |
| Additions to properties and equipment | (40,108) | (43,874) |
| Repayments of advances to unconsolidated companies | 9,496 | |
| Other | 259 | |
| Net cash (used in) investing activities | (23,332) | (40,664) |
| Cash flows from financing activities: | | |
| Debt borrowings | 5,000 | 30,000 |
| Principal payments on debt | (5,000) | (15,000) |
| Proceeds from issuance of stock options | 3,263 | 116 |
| Cash dividends | (8,728) | (8,629) |
| Stock repurchases | (91,351) | |
| Other | | (364) |
| Net cash (used in) provided by financing activities | (96,816) | 6,123 |
| Net change in cash and cash equivalents | (21,811) | (233) |
| Cash and cash equivalents at beginning of period | 246,109 | 15,376 |
| Cash and cash equivalents at end of period | $ 224,298 | 15,143 |
| Supplemental disclosure of cash flow information: | | |
| Cash paid during the period for: | | |
| Interest | $ 125 | 889 |
| Income taxes | $ 7,404 | 5,662 |

See Notes to Unaudited Condensed Consolidated Financial Statements.

**TIDEWATER INC.**

**NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**

**(1) Interim Financial Statements**

The unaudited condensed consolidated financial statements for the interim periods presented herein have been prepared in conformity with United States generally accepted accounting principles and, in the opinion of management, include all adjustments (consisting only of normal recurring adjustments) necessary for a fair presentation of the condensed consolidated balance sheets and the condensed consolidated statements of earnings and cash flows at the dates and for the periods indicated as required by Rule 10-01 of Regulation S-X of the Securities and Exchange Commission (SEC). Results of operations for interim periods are not necessarily indicative of results of operations for the respective full years. These unaudited condensed consolidated financial statements should be read in conjunction with the consolidated financial statements and notes thereto in the company s Annual Report on Form 10-K for the year ended March 31, 2006, filed with the SEC on May 30, 2006.

**(2) Stockholders Equity**

At June 30, 2006 and March 31, 2006, 2,026,397 and 2,167,021 shares, respectively, of common stock were held in a grantor stock ownership plan trust for the benefit of stock-based employee benefits programs. These shares are not included in common shares outstanding for earnings per share calculations and transactions between the company and the trust, including dividends paid on the company s common stock, are eliminated in consolidating the accounts of the trust and the company.

**(3) Common Stock Repurchase Program**

In July 2005, the company s Board of Directors authorized the company to spend up to $120.0 million to repurchase shares of its common stock. Repurchases are made through open market or privately-negotiated transactions. The company used its available cash and, when considered advantageous, borrowings under its revolving credit facility to fund the share repurchases. The Board of Directors authorization for this repurchase program expired on June 30, 2006. For the three-month period ended June 30, 2006, the company spent $91.4 million for the repurchase and cancellation of 1,941,100 common shares, or an average price paid per common share of $47.06. From inception of the repurchase program through its conclusion on June 30, 2006, the company spent $112.1 million for the repurchase and cancellation of 2,396,100 common shares, or an average price paid per common share of $46.79.

On July 20, 2006, the company s Board of Directors authorized a new program for the company to spend up to $157.9 million to repurchase shares of its common stock in open-market or privately-negotiated transactions. The company intends to use its available cash and, when considered advantageous, borrowings under its revolving credit facility, to fund the share repurchases. The repurchase program will end when all the authorized funds have been expended or June 30, 2007, unless extended by the Board of Directors.

**(4) Stock-Based Compensation**

On April 1, 2006, the company adopted Statement of Financial Accounting Standards (SFAS) No. 123 (Revised 2004), *Share-Based Payment* (SFAS 123R). This standard requires expensing of stock options and other share-based payments and supersedes SFAS No. 123, *Accounting for Stock-Based Compensation* and Accounting Principles Board (APB) Opinion No. 25, *Accounting for Stock Issued to Employees*, and its related implementation guidance that had allowed companies to choose between expensing stock options or showing pro-forma disclosure only. SFAS 123R eliminates the ability to account for stock-based compensation transactions using the intrinsic value method under APB Opinion No. 25 and instead requires that such transactions be accounted for using a fair-value-based method. In addition, the SEC issued Staff Accounting Bulletin 107 in April 2005, which provides supplemental implementation guidance for SFAS 123R.

Prior to adoption of SFAS 123R, the company measured compensation expense for its stock-based compensation plan using the intrinsic value recognition and measurement principles as prescribed by APB Opinion No. 25 and related interpretations. The company also used the disclosure provision of SFAS No. 148, *Accounting for Stock-Based Compensation Transition and Disclosure,* which amended the disclosure provision of SFAS No. 123. The following table illustrates the effect on net earnings and earnings per share for the three months ended June 30, 2005 had the company determined compensation cost based on the fair value at the grant date for its stock options under SFAS No. 123.

| **(In thousands, except share data)** | **Quarter Ended June 30, 2005** |
|---|---|
| Net earnings as reported | $ 28,860 |
| Add stock-based employee compensation expense included in reported net earnings, net of tax | 586 |
| Less total stock-based employee compensation expense, under fair value method for all awards, net of tax | (1,199) |
| Pro forma net earnings | $ 28,247 |
| Basic earnings per common share: | |
| As reported | $ .50 |
| Pro forma | $ .49 |
| Diluted earnings per common share: | |
| As reported | $ .50 |
| Pro forma | $ .49 |

***General***

The company s employee stock option and restricted stock plans are long-term retention plans that are intended to attract, retain and provide incentives for talented employees, including officers and non-employee directors, and to align stockholder and employee interests. The company believes its employee stock option plans are critical to its operation and productivity. The employee stock option plans allow the company to grant, on a discretionary basis, both incentive stock options and non-qualified stock options, as well as restricted stock.

***Stock Option Plans***

The company grants stock options to its employees, including officers, under the 1997 and 2001 Stock Incentive Plans. Under the 2001 Stock Incentive Plan, the company can grant options to non-employee directors on a non-discretionary basis up to 5,000 shares per director per year. Generally, options have been granted that vest annually over a three-year vesting period from the date of grant. Options expire at the earlier of either three months after termination of the grantee s employment or ten years after the date of grant.

The company uses the Black-Scholes option-pricing model to determine the fair-value of stock-based awards under SFAS 123R, consistent with that used for pro forma disclosures under SFAS No. 123. The company elected to use the modified prospective transition method as permitted by SFAS 123R and, accordingly, prior periods have not been restated to reflect the impact of SFAS 123R. Effective in fiscal 2007, the modified prospective transition method requires that stock-based compensation expense be recorded for all new and unvested stock options and restricted stock grants that are ultimately expected to vest as the requisite service is rendered.

The company recorded $1.0 million of stock-option compensation expense during the quarter ended June 30, 2006 as a result of the adoption of SFAS 123R, which had the effect of reducing earnings per share by $0.01. No stock-option compensation costs were capitalized as part of the cost of an asset as of June 30, 2006. Stock-based compensation expense for awards granted prior to April 1, 2006 is based on the grant date fair-value as determined under the pro forma provisions of SFAS No. 123.

As of June 30, 2006, total unrecognized stock-option compensation costs amounted to $5.0 million. Unvested stock-option compensation costs will be recognized as the underlying stock options vest over a period of up to 3 years. The amount of unrecognized stock-option compensation will be affected by any future stock option grants and by the termination of any employee that has received stock options that are unvested as of their termination date.

The company did not grant stock options during the quarter ended June 30, 2006. The following table sets forth a summary of option activity under our stock option program for the three months ended June 30, 2006:

| | Weighted-average Exercise Price | Number Of Options Outstanding |
|---|---|---|
| Balance at March 31, 2006 | $ 38.57 | 3,662,875 |
| Granted | | |
| Exercised | 31.15 | (134,583) |
| Expired or cancelled/forfeited | 33.77 | (7,000) |
| Balance at June 30, 2006 | $ 38.87 | 3,521,292 |

The intrinsic value of options exercised during the quarter ended June 30, 2006 was $3.1 million. No stock options vested during the current period. The company does not have share-based liabilities.

Information regarding the 3,521,292 options outstanding at June 30, 2006 can be grouped into three general exercise-price ranges as follows:

| | Exercise Price Range | | |
|---|---|---|---|
| At June 30, 2006 | $ 22.75 -$29.44 | $ 32.25 -$40.28 | $ 42.19-$59.00 |
| Options outstanding | 1,102,312 | 946,730 | 1,472,250 |
| Weighted average exercise price | $ 27.02 | $ 36.46 | $ 49.28 |
| Weighted average remaining contractual life | 5.9 years | 5.4 years | 4.6 years |
| Options exercisable | 1,005,461 | 946,730 | 1,192,739 |
| Weighted average exercise price of options exercisable | $ 26.92 | $ 36.46 | $ 47.76 |
| Weighted average remaining contractual life of exercisable shares | 5.8 years | 5.4 years | 3.4 years |

The aggregate intrinsic value of the options outstanding and the options exercisable at June 30, 2006 was $41.0 million and $38.9 million, respectively.

***Restricted Stock***

The company grants restricted shares to key employees, including officers, under the company s Employee Restricted Stock Plan and the 1997 and 2001 Stock Incentive Plans. These plans provide for the granting of restricted stock and/or performance awards to officers and key employees. The company awards both time-based shares and performance-based shares of restricted stock. Time-based restricted stock vests over a four year period and requires no goals to be accomplished other than the passage of time and continued employment. Performance-based restricted stock vests at the end of a four year period and can be accelerated if the company meets specific annual targets. During the restricted period, the restricted shares may not be transferred or encumbered, but the recipient has the right to vote and receive dividends on the restricted shares.

The company did not grant restricted stock during the quarter ended June 30, 2006. The following table sets forth a summary of restricted stock activity of the company for the three months ended June 30, 2006:

| | Weighted-average Grant-Date Fair Value | Time Based Shares | Performance Based Shares |
|---|---|---|---|
| Non-vested balance at March 31, 2006 | $ 45.58 | 137,571 | 320,550 |
| Granted | | | |
| Vested | 37.55 | | (39,863) |
| Cancelled/forfeited | 40.84 | (6,480) | (4,125) |
| Non-vested balance at June 30, 2006 | $ 46.49 | 131,091 | 276,562 |

The compensation expense related to non-vested restricted stock totaled $1.2 million and $0.8 million for the quarter ended June 30, 2006 and 2005, respectively. No restricted stock compensation costs were capitalized as part of the cost of an asset as of June 30, 2006. The deferred amount is being amortized by equal monthly charges to earnings over the respective four-year vesting periods. As of June 30, 2006, total unrecognized restricted stock compensation costs amounted to $16.7 million. The amount of unrecognized restricted stock compensation will be affected by any future restricted stock grants and by the separation of an employee from the company who has received restricted stock grants that are unvested as of their separation date.

The Employee Restricted Stock Plan is the only equity compensation plan that has not been approved by shareholders. The 1997 and 2001 Stock Incentive Plans are approved by shareholders.

**(5) Income Taxes**

Income tax expense for interim periods is based on estimates of the effective tax rate for the entire fiscal year. The effective tax rate applicable to pre-tax earnings for the quarters ended June 30, 2006 and 2005 was 25% and 26%, respectively.

**(6) Employee Benefit Plans**

A defined benefit pension plan covers certain U.S. citizen employees and employees who are permanent residents of the United States. Benefits are based on years of service and employee compensation. In addition, the company also offers a supplemental retirement plan (supplemental plan) that provides pension benefits to certain employees in excess of those allowed under the company s tax-qualified pension plan. The company contributed $0.3 million to the defined benefit pension plan during the quarter ended June 30, 2006 and expects to contribute an additional $0.9 million to the plan during the remainder of the current fiscal year.

Qualified retired employees currently are covered by a program which provides limited health care and life insurance benefits. Costs of the program are based on actuarially determined amounts and are accrued over the period from the date of hire to the full eligibility date of employees who are expected to qualify for these benefits.

The net periodic benefit cost for the company s U.S. defined benefit pension plan and the supplemental plan (referred to collectively as Pension Benefits ) and the postretirement health care and life insurance plan (referred to collectively as Other Benefits ) is comprised of the following components:

| (In thousands) | Quarter Ended June 30, 2006 | 2005 |
|---|---|---|
| **Pension Benefits:** | | |
| Service cost | $ 232 | 190 |
| Interest cost | 918 | 882 |
| Expected return on plan assets | (628) | (613) |
| Amortization of prior service cost | 15 | 22 |
| Recognized actuarial loss | 331 | 237 |
| Net periodic benefit cost | $ 868 | 718 |
| **Other Benefits:** | | |
| Service cost | $ 323 | 503 |
| Interest cost | 413 | 591 |
| Amortization of prior service cost | (550) | (4) |
| Recognized actuarial loss | 387 | 127 |
| Net periodic benefit cost | $ 573 | 1,217 |

**(7) Contingencies**

At the conclusion of its examination of the company s income tax returns covering fiscal years 2001 and 2002, the Internal Revenue Service (IRS) proposed changes to taxable income which, if sustained, would result in additional income tax of $12.8 million. The proposed increase in taxable income results primarily from the IRS disallowance of all claimed deductions from taxable income related to the company s foreign sales corporation (FSC) as well as all deductions claimed under the Extraterritorial Income Exclusion (ETI). The company has filed a formal protest with the IRS seeking a reconsideration of their position taken. The company has also received a final assessment of additional income tax of $1.75 million resulting from the IRS s earlier examination of the company s income tax returns for fiscal years 1999 and 2000. Such assessment is also due to the IRS disallowance of essentially all deductions related to FSC activity during that period. The company has paid the 1999 and 2000 assessment and has begun the process of seeking a refund of the taxes paid through the initiation of legal proceedings. The IRS has begun an examination of the company s 2003 and 2004 federal income tax returns. The company also has additional ongoing examinations by various state and foreign tax authorities. The company does not believe that the results of these examinations will have a material adverse effect on the company s financial position or results of operations.

Certain current and former subsidiaries of the company are, or have been, participating employers in an industry-wide multi-employer retirement fund in the United Kingdom, the Merchant Navy Officers Pension Fund (MNOPF.) The company has been informed of an estimated 234 million sterling, or approximately $433 million, total fund deficit as estimated by the MNOPF actuary, that will require contributions from the participating employers. Substantially all of the fund s deficit allocable to the company relates to current operating subsidiaries as the company does not believe, on the advice of counsel, that it is liable for any additional portion of the fund s deficit that relates to subsidiaries that have either been sold or dissolved in prior years. The amount of the company s share of the fund s deficit will depend ultimately on a number of factors including an updated calculation of the total fund deficit, the number of participating employers, and the final method used in allocating the required contribution among participating employers.

In August 2005, the company received an invoice from the fund in the amount of $3.8 million for what the trustees calculated to be the company s current share of the fund deficit. Accordingly, the company recorded this amount in full as crew cost expense during the second quarter of fiscal 2006. As allowed by the terms of the assessment, approximately $0.7 million of the invoiced amount was paid during fiscal 2006 with the remainder, including interest charges, to be paid in annual installments over nine years. The annual installment payments are paid in the fourth quarter of each fiscal year and, as such, no amounts were paid during the quarter ended June 30, 2006.

It is possible that in the future the fund s trustee may claim that the company owes additional amounts for various reasons, including the results of future fund valuation reports and whether other assessed parties have the financial capability to contribute their respective allocations.

The company has previously disclosed that it is the subject of an informal inquiry by the Securities and Exchange Commission (SEC) related to the $26.5 million impairment charge that it recorded in its fiscal year ended March 31, 2004 that was related to 83 stacked vessels that had been used in the Gulf of Mexico. The company is in discussions with the SEC in an effort to resolve the matters raised by the inquiry. At this time, the company is unable to predict the timing or ultimate outcome of these discussions.

Various legal proceedings and claims are outstanding which arose in the ordinary course of business. In the opinion of management, the amount of ultimate liability, if any, with respect to these actions will not have a material adverse effect on the company s financial position, results of operations, or cash flows.

**(8) New Accounting Pronouncements**

In May 2005 the Financial Accounting Standards Board (FASB) issued SFAS No. 154, *Accounting Changes and Error Corrections*, which replaces APB No. 20, *Accounting Changes*, and SFAS No. 3, Reporting *Accounting Changes in Interim Financial Statements*. SFAS No. 154 applies to all voluntary changes in accounting principle, and changes the requirements for accounting for and reporting of a change in accounting principle. SFAS No. 154 requires retrospective application to prior periods financial statements of a voluntary change in accounting principle unless it is impracticable. APB No. 20 previously required that most voluntary changes in accounting principle be recognized with a cumulative effect adjustment in net income of the period of the change. SFAS No. 154 is effective for accounting changes made in annual periods beginning after December 15, 2005.

In July 2006, the FASB issued FASB Interpretation No. 48, *Accounting for Uncertainty in Income Taxes an interpretation of FASB Statement No. 109* (FIN 48), which clarifies the accounting and disclosure for uncertain tax positions, as defined. FIN 48 seeks to reduce the diversity in practice associated with certain aspects of the recognition and measurement related to accounting for income taxes. This interpretation is effective for fiscal years beginning after December 15, 2006. The company is assessing FIN 48 and has not determined yet the impact that the adoption of FIN 48 will have on its result of operations or financial position.

From time to time, new accounting pronouncements are issued by the FASB that are adopted by the company as of the specified effective date. Unless otherwise discussed, management believes that the impact of recently issued standards, which are not yet effective, will not have a material impact on the company s consolidated financial statements upon adoption.

**(9) Segment and Geographic Distribution of Operations**

The company follows SFAS No. 131, *Disclosures about Segments of an Enterprise and Related Information* and operates in two business segments: United States and International. The following table provides a comparison of revenues, operating profit, depreciation and amortization, and additions to properties and equipment for the quarters ended June 30, 2006 and 2005. Vessel revenues and operating costs relate to vessels owned and operated by the company while other marine services relate to the activities of the company s shipyards, brokered vessels and other miscellaneous marine-related businesses.

| (In thousands) | Quarter Ended June 30, 2006 | 2005 |
|---|---|---|
| Revenues: | | |
| Vessel revenues: | | |
| United States | $ 61,808 | 35,282 |
| International | 196,877 | 150,110 |
| | 258,685 | 185,392 |
| Other marine revenues | 11,135 | 6,775 |
| | $269,820 | 192,167 |
| Marine operating profit: | | |
| Vessel activity: | | |
| United States | $ 25,924 | 6,853 |
| International | 68,116 | 32,779 |
| | 94,040 | 39,632 |
| Gain on sales of assets | 2,713 | 1,634 |
| Other marine services | 1,100 | 2,064 |
| Operating profit | $ 97,853 | 43,330 |
| Equity in net earnings of unconsolidated companies | 2,449 | 2,167 |
| Interest and other debt costs | (2,580) | (2,362) |
| Corporate general and administrative | (6,295) | (4,534) |
| Other income | 3,838 | 399 |
| Earnings before income taxes | $ 95,265 | 39,000 |
| Depreciation and amortization: | | |
| Marine equipment operations | | |
| United States | $ 6,089 | 5,045 |
| International | 21,550 | 21,133 |
| General corporate depreciation | 158 | 159 |
| | $ 27,797 | 26,337 |
| Additions to properties and equipment: | | |
| Marine equipment operations | | |
| United States | $ 15,368 | 10,859 |
| International | 19,695 | 32,965 |
| General corporate | 5,045 | 50 |
| | $ 40,108 | 43,874 |

**REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM**

To the Board of Directors and Stockholders of Tidewater Inc.:

We have reviewed the accompanying condensed consolidated balance sheet of Tidewater Inc. and subsidiaries (the Company ) as of June 30, 2006, and the related condensed consolidated statements of earnings and cash flows for the three-month periods ended June 30, 2006 and 2005. These interim financial statements are the responsibility of the Company s management.

We conducted our reviews in accordance with the standards of the Public Company Accounting Oversight Board (United States). A review of interim financial information consists principally of applying analytical procedures and making inquiries of persons responsible for financial and accounting matters. It is substantially less in scope than an audit conducted in accordance with the standards of the Public Company Accounting Oversight Board (United States), the objective of which is the expression of an opinion regarding the financial statements taken as a whole. Accordingly, we do not express such an opinion.

Based on our reviews, we are not aware of any material modifications that should be made to such condensed consolidated interim financial statements for them to be in conformity with accounting principles generally accepted in the United States of America.

We have previously audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the consolidated balance sheet of Tidewater Inc. and subsidiaries as of March 31, 2006, and the related consolidated statements of earnings, stockholders equity and other comprehensive income, and cash flows for the year then ended (not presented herein); and in our report dated May 25, 2006 we expressed an unqualified opinion on those consolidated financial statements. In our opinion, the information set forth in the accompanying condensed consolidated balance sheet as of March 31, 2006, is fairly stated, in all material respects, in relation to the consolidated balance sheet from which it has been derived.

/s/ DELOITTE & TOUCHE LLP

New Orleans, Louisiana
July 25, 2006

**ITEM 2. MANAGEMENT S DISCUSSION AND ANALYSIS**

**Forward Looking Information and Cautionary Statement**

*In accordance with the safe harbor provisions of the Private Securities Litigation Reform Act of 1995, the company notes that this Quarterly Report on Form 10-Q and the information incorporated herein by reference contain certain forward-looking statements which reflect the company s current view with respect to future events and financial performance. Any such forward-looking statements are subject to risks and uncertainties and the company s future results of operations could differ materially from historical results or current expectations. Some of these risks are discussed in this report, and include, without limitation, fluctuations in oil and gas prices; level of fleet additions by competitors and industry overcapacity; changes in capital spending by customers in the energy industry for exploration, development and production; changing customer demands for different vessel specifications which may make some of our vessels technologically obsolete for certain customer projects or in certain markets; acts of terrorism; significant weather conditions; unsettled political conditions, war, civil unrest and governmental actions, especially in higher risk countries of operations; foreign currency fluctuations; and environmental and labor laws.*

*Forward-looking statements, which can generally be identified by the use of such terminology as may, expect, anticipate, estimate, forecast, believe, think, can, could, will, continue, intend, seek, plan, should, would and similar expressions contained i report, are predictions and not guarantees of future performance or events. Any forward-looking statements are based on current industry, financial and economic information, which the company has assessed but which by its nature is dynamic and subject to rapid and possibly abrupt changes. The company s actual results could differ materially from those stated or implied by such forward-looking statements due to risks and uncertainties associated with our business. The forward-looking statements should be considered in the context of the risk factors listed above and discussed in Items 1, 1A, 2 and 7 included in the company s Annual Report on Form 10-K for the year ended March 31, 2006, filed with the Securities and Exchange Commission (SEC) on May 30, 2006 and elsewhere in this Form 10-Q. Investors and prospective investors are cautioned not to place undue reliance on such forward-looking statements. Management disclaims any obligation to update or revise the forward-looking statements contained herein to reflect new information, future events or developments.*

**Overview**

The company provides services to the global offshore energy industry through the operation of a diversified fleet of marine service vessels. Revenues, net earnings and cash flows from operations are dependent upon the activity level of the vessel fleet. Vessel fleet activity levels are dependent upon oil and natural gas prices, which, in turn, are determined by the supply/demand relationship for crude oil and natural gas. The following information contained in this Form 10-Q should be read in conjunction with the unaudited condensed consolidated financial statements and notes thereto included in Item 1 of this Quarterly Report and related disclosures and the company s Annual Report on Form 10-K for the year ended March 31, 2006, filed with the SEC on May 30, 2006.

**General Market Conditions and Results of Operations**

Offshore service vessels provide a diverse range of services and equipment to the energy industry. The company s revenues and operating profit are primarily driven by fleet size, vessel utilization and day rates because operating costs and depreciation do not change proportionally when revenue changes. Operating costs primarily consist of crew costs, repair and maintenance, insurance, fuel, lube oil and supplies. Fleet size and utilization are the major factors which affect crew costs. The timing and amount of repair and maintenance costs are influenced by customer demands, vessel age and scheduled drydockings to satisfy safety and inspection requirements mandated by regulatory agencies. Drydocking costs are only incurred if economically justified, taking into consideration the vessel s age, physical condition and future marketability. The following table compares revenues and operating expenses (excluding general and administrative expense, depreciation expense and gain on sales of assets) for the quarters ended June 30, 2006 and 2005 and for the quarter ended March 31, 2006. Vessel revenues and operating costs relate to vessels owned and operated by the company while other marine revenues relate to third-party activities of the company s shipyards, brokered vessels and other miscellaneous marine-related activities.

| (In thousands) | Quarter Ended June 30, 2006 | Quarter Ended June 30, 2005 | Quarter Ended March 31, 2006 |
|---|---|---|---|
| Revenues: | | | |
| Vessel revenues: | | | |
| United States | $ 61,808 | 35,282 | 53,664 |
| International | 196,877 | 150,110 | 181,610 |
| | 258,685 | 185,392 | 235,274 |
| Other marine revenues | 11,135 | 6,775 | 11,266 |
| | $ 269,820 | 192,167 | 246,540 |
| Operating costs: | | | |
| Vessel operating costs: | | | |
| Crew costs | $ 63,409 | 58,957 | 62,252 |
| Repair and maintenance | 24,989 | 19,796 | 22,659 |
| Insurance and loss reserves | 4,548 | 5,524 | 4,624 |
| Fuel, lube and supplies | 11,365 | 9,433 | 10,770 |
| Vessel operating leases | 254 | | 23 |
| Other | 15,197 | 12,500 | 15,524 |
| | 119,762 | 106,210 | 115,852 |
| Costs of other marine revenues | 9,914 | 4,590 | 9,086 |
| | $ 129,676 | 110,800 | 124,938 |

The following table subdivides vessel operating costs presented above by the company s United States and International segments for the quarters ended June 30, 2006 and 2005 and for the quarter ended March 31, 2006.

| (In thousands) | Quarter Ended June 30, 2006 | Quarter Ended June 30, 2005 | Quarter Ended March 31, 2006 |
|---|---|---|---|
| Operating costs: | | | |
| United States vessel operating costs: | | | |
| Crew costs | $ 15,795 | 12,795 | 15,912 |
| Repair and maintenance | 5,049 | 3,852 | 4,252 |
| Insurance and loss reserves | 2,729 | 2,404 | 1,387 |
| Fuel, lube and supplies | 1,731 | 1,346 | 1,133 |
| Vessel operating leases | 254 | | 23 |
| Other | 1,765 | 962 | 1,320 |
| | 27,323 | 21,359 | 24,027 |
| International vessel operating costs: | | | |
| Crew costs | $ 47,614 | 46,162 | 46,340 |
| Repair and maintenance | 19,940 | 15,944 | 18,407 |
| Insurance and loss reserves | 1,819 | 3,120 | 3,237 |
| Fuel, lube and supplies | 9,634 | 8,087 | 9,637 |
| Vessel operating leases | | | |
| Other | 13,432 | 11,538 | 14,204 |

| | | | |
|---|---|---|---|
| | 92,439 | 84,851 | 91,825 |
| Total operating costs | $ 119,762 | 106,210 | 115,852 |

Marine support services are conducted worldwide with highly mobile assets. Revenues are principally derived from offshore service vessels, which regularly and routinely move from one operating area to another, often to and from offshore operating areas of different continents. Because of this asset mobility, revenues and long-lived assets attributable to the company s international marine operations in any one country are not material as that term is defined by SFAS No. 131.

As a result of the uncertainty of a certain customer to make payment of vessel charter hire, the company has deferred the recognition of approximately $4.7 million of billings as of June 30, 2006 ($6.1 million of billings as of March 31, 2006), which would otherwise have been recognized as revenue. The company will recognize the amounts as revenue as cash is collected or at such time as the uncertainty has been significantly reduced.

Strong industry fundamentals coupled with disciplined spending resulted in an improved first quarter for Tidewater. The company s net earnings in the first quarter of fiscal 2007 grew approximately 148% over net earnings achieved during the first quarter of fiscal 2006. The company s domestic revenues increased approximately 75%, or $26.5 million, during the current quarter as compared to the same period in fiscal 2006 while the company s international revenues increased $46.8 million, or approximately 31% during the same comparative period.

Higher average day rates and utilization are at the root of the company s domestic results of operations for the first quarter of fiscal 2007. Average day rates for the total domestic-based fleet increased approximately 69% during the first quarter of fiscal 2007 as compared to the first quarter of fiscal 2006 while utilization for the entire domestic-based fleet increased approximately 11% during the same comparative periods. The strong first quarter of fiscal 2007 is a result of several significant improvements in the market for offshore support vessels which began last calendar year. In the first half of calendar year 2005, the market for offshore support vessels tightened as drilling operators discovered that offshore vessels that were in service were in short supply due to high demand associated with the continuation of repair work to the offshore energy infrastructure that was damaged by Hurricane Ivan in calendar year 2004. Hurricanes Katrina and Rita, which caused extensive damage to the energy industry infrastructure in the oil producing areas of the U.S. Gulf Coast in late August and September 2005, respectively, further tightened the offshore vessel market as exploration and production (E&P) companies scrambled to find available vessels for the necessary repair work resulting from the damage caused by the two storms. Demand for the company s vessels was strong before the two storms and business has been brisk since the storms propelling charter rates past levels achieved in the 1997 and 2001 industry upturns. The Gulf of Mexico supply boat market still has a significant number of vessels stacked and withdrawn from service that could resume active status, but only after significant expenditures to drydock and re-certify the vessels. The company sold, to third party operators or to scrap dealers, 18 of its stacked vessels and vessels withdrawn from service during the current quarter. Upon completion of the needed repair work in the U.S. Gulf of Mexico, and assuming no significant damage from any hurricanes during 2006, the number of available drilling rigs in the U.S. market should be the primary driver of the company s future profitability in the domestic market and, at present time, the offshore rig count in the Gulf of Mexico remains relatively depressed as compared to past up cycles. The strength of the international drilling market has attracted offshore rigs from the U.S. market over the past few years and this trend is expected to continue in the upcoming quarters. Over the longer term, the company s domestic-based fleet should be influenced more by the active offshore rig count than by any other single outside influence. Certain sell-side analysts reports indicate that over the next 4 years the offshore drilling rig count will increase as newbuild orders for jackup rigs currently stand at approximately 91 rigs.

For two years in a row, certain sell-side analysts have reported in their mid-year E&P capital spending reports that worldwide E&P expenditures are exceeding original estimates. These analysts are currently reporting that calendar year 2006 worldwide E&P capital expenditures are forecast to grow approximately 21% over calendar year 2005 spending as compared to spending estimate increases reported in December 2005 of approximately 15%. Domestic E&P expenditures for calendar year 2006 are now forecast to be at approximately 28% over calendar year 2005 spending as compared to a 15% increase for 2006 that was originally forecast in December 2005. On the international front, it is now estimated that international E&P spending will rise approximately 20% over calendar year 2005 budgets with significant increases by the European and U.S. major oil companies, U.S. independent oil companies and the national E&P companies. These analysts also report that many of the corporations surveyed for the report indicated higher E&P spending in calendar year 2007.

Commodity prices for crude oil and natural gas are critical factors in E&P companies development of capital spending budgets. In May 2006, commodity prices for natural gas decreased below the $6.00 per Mcf level for the first time in over a year on the news that inventory levels for the resource exceeded five-year inventory averages due to warmer than normal winter weather this past winter season in the Northern Hemisphere, and despite shut-ins in natural gas production caused by the damage sustained from the two hurricanes. By the end of June 2006, natural gas inventories exceeded the five-year average by approximately 32% as reported by the Department of Energy. Domestic results of operations are primarily driven by natural gas exploration and production and, given these inventory levels, it is possible the recent level of drilling activity will somewhat abate. Nevertheless, the company has reaped the benefits of the current strength in the offshore drilling market.

Higher average day rates and utilization are also at the root of the strength of the company s international-based results of operations for the first quarter of fiscal 2007. Average day rates for the total international-based fleet increased approximately 18% during the first quarter of fiscal 2007 as compared to the first quarter of fiscal 2006 while utilization for the entire international-based fleet increased approximately 11% during the same comparative periods. The company s international results of operations have been primarily dependent on the supply and demand relationship for crude oil and, at present, crude oil prices are at historically high levels. Sell-side analysts forecast that demand for crude oil will likely remain strong throughout calendar year 2006 and expect future crude oil commodity prices to remain at attractive levels due to high consumer demand, tight crude oil inventory supplies coupled with chronically low excess Organization of Petroleum Exporting Countries (OPEC) production capacity and continued concerns over possible supply interruptions caused by geopolitical risk in certain countries that are members of OPEC. Management anticipates international vessel demand will remain strong along with these market conditions.

Marine operating profit and other components of earnings before income taxes for the quarters ended June 30 and March 31 consists of the following:

| | Quarter Ended June 30, | | Quarter Ended March 31, |
|---|---|---|---|
| **(In thousands)** | **2006** | **2005** | **2006** |
| Vessel activity: | | | |
| United States | $ 25,924 | 6,853 | 21,253 |
| International | 68,116 | 32,779 | 53,209 |
| | 94,040 | 39,632 | 74,462 |
| Gain on sales of assets | 2,713 | 1,634 | 10,875 |
| Other marine services | 1,100 | 2,064 | 2,060 |
| Operating profit | $ 97,853 | 43,330 | 87,397 |
| Equity in net earnings of unconsolidated companies | 2,449 | 2,167 | 2,925 |
| Interest and other debt costs | (2,580) | (2,362) | (2,444) |
| Corporate general and administrative | (6,295) | (4,534) | (6,722) |
| Other income | 3,838 | 399 | 3,728 |
| Earnings before income taxes | $ 95,265 | 39,000 | 84,884 |

***United States-based Operations***

U.S.-based vessel revenues for the first quarter of fiscal 2007 increased approximately 75% and 15%, or $26.5 million and $8.1 million, as compared to the first and fourth quarters of fiscal 2006, respectively, due to an increase in average day rates on all vessel classes operating in the domestic market and due to an increase in utilization on the company s towing supply/supply, crew/utility and offshore tug class of vessels.

The active towing supply/supply vessels, the company s major income producing vessel class in the domestic market, were responsible for generating approximately 56% and 63% of the revenue growth during the first quarter of fiscal 2007 as compared to the first and fourth quarters of fiscal 2006, respectively, while the company s deepwater class of vessels contributed approximately 22% and 11% of revenue growth during the same comparative periods, respectively. Utilization rates on the towing supply/supply vessels during the first quarter of fiscal 2007 increased approximately 3% and 4% as compared to the first and fourth quarters of fiscal 2006, respectively, while average day rates on this same class of vessel increased

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approximately 62% and 10% during the same comparative periods, respectively. Average day rates for the company s deepwater class of vessels increased approximately 42% and 7% during first quarter of fiscal 2007 as compared to the first and fourth quarters of fiscal 2006, respectively. Utilization rates on the deepwater class slipped approximately 6% and 6% during the first quarter of fiscal 2007 as compared to the first and fourth quarters of fiscal 2006, respectively.

The company s crew/utility class and offshore tugs class of vessels also had impressive results. During the first quarter of fiscal 2007 as compared to the first and fourth quarters of fiscal 2006, the crew/utility class of vessels experienced an increase in average day rates of approximately 68% and 18%, respectively, while its utilization rates increased approximately 20% and 11%, respectively. The company s offshore tugs experienced an increase in average day rates during the first quarter of fiscal 2007 of approximately 73% and 64% as compared to the first and fourth quarters of fiscal 2006, respectively, while its utilization rates increased approximately 52% and 29% during the same periods, respectively.

During the first quarter of fiscal 2007, operating profit for the U.S.-based vessels increased $19.1 million and $4.7 million, or approximately 278% and 22%, as compared to the first and fourth quarters of fiscal 2006, respectively, due to higher revenues from increased demand, translating into higher utilization and average day rates. Higher revenues were somewhat offset by increases in domestic vessel operating costs.

***International-based Operations***

International-based vessel revenues during the first quarter of fiscal 2007 increased approximately 31% and 8%, or $46.8 million and $15.3 million, as compared to the first and fourth quarters of fiscal 2006, respectively, due to higher average day rates and utilization on the total international fleet. For the first quarter of fiscal 2007 as compared to same period in fiscal 2006, the company s international deepwater, towing supply/supply, crew/utility and offshore tug classes of vessels generated approximately 16%, 62%, 12% and 9%, respectively, of the revenue growth during the comparative periods. The company s international deepwater, towing supply/supply, crew/utility and offshore tug classes of vessels generated approximately 13%, 48%, 24% and 14%, respectively, of the revenue growth during the first quarter of fiscal 2007 as compared to the fourth quarter of fiscal 2006, respectively.

International-based vessel operating profit for the first quarter of fiscal 2007 increased $35.3 million and $14.9 million, or approximately 108% and 28%, as compared to the first quarter and fourth quarters of fiscal 2006, respectively, due to higher revenues. Higher international-based revenues earned during the current quarter were partially offset by increases in vessel operating costs primarily repair and maintenance, fuel, lube and supplies and other vessel costs.

***Other Items***

Gain on sales of assets for the first quarter of fiscal 2007 were approximately 66% higher than the same period in fiscal 2006 due to receiving higher sales prices on the mix of vessels sold. Gain on sales of assets were significantly lower during the first quarter of fiscal 2007 as compared to the fourth quarter of fiscal 2006 because of a higher number of vessel sales during the previous quarter.

**Vessel Class Statistics**

Vessel utilization is determined primarily by market conditions and to a lesser extent by drydocking requirements. Vessel day rates are determined by the demand created through the level of offshore exploration, development and production spending by energy companies relative to the supply of offshore service vessels. Suitability of equipment and the degree of service provided also influence vessel day rates. Vessel utilization rates are calculated by dividing the number of days a vessel works during a reporting period by the number of days the vessel is available to work in the reporting period. Average day rates are calculated by dividing the revenue a vessel earns during a reporting period by the number of days the vessel worked in the reporting period. Vessel utilization and average day rates are calculated on active vessels only and as such, do not include vessels withdrawn from active service or joint venture vessels. The following tables compare day-based utilization percentages and average day rates by vessel class and in total for the quarter periods ended June 30, 2006 and 2005 and for the quarter ended March 31, 2006:

| | Quarter Ended June 30, 2006 | 2005 | Quarter Ended March 31, 2006 |
|---|---|---|---|
| **UTILIZATION:** | | | |
| United States-based fleet: | | | |
| Deepwater vessels | 93.8% | 100.0 | 99.7 |
| Towing-supply/supply | 64.2 | 62.4 | 62.0 |
| Crew/utility | 96.4 | 80.6 | 86.6 |
| Offshore tugs | 39.8 | 26.2 | 30.8 |
| Total | 68.0% | 61.5 | 64.5 |
| International-based fleet: | | | |
| Deepwater vessels | 89.3% | 85.5 | 89.9 |
| Towing-supply/supply | 77.4 | 71.5 | 76.8 |
| Crew/utility | 83.8 | 75.2 | 76.2 |
| Offshore tugs | 72.1 | 57.5 | 63.3 |
| Other | 45.8 | 34.6 | 28.8 |
| Total | 78.4% | 70.9 | 75.2 |
| Worldwide fleet: | | | |
| Deepwater vessels | 90.2% | 87.4 | 91.7 |
| Towing-supply/supply | 74.8 | 69.7 | 74.0 |
| Crew/utility | 85.8 | 76.5 | 78.5 |
| Offshore tugs | 63.9 | 48.4 | 53.7 |
| Other | 45.8 | 34.6 | 28.8 |
| Total | 76.4% | 69.0 | 72.9 |
| | | | |
| **AVERAGE VESSEL DAY RATES:** | | | |
| United States-based fleet: | | | |
| Deepwater vessels | $ 21,380 | 15,041 | 20,006 |
| Towing-supply/supply | 11,645 | 7,169 | 10,545 |
| Crew/utility | | | |