

HERCULES OFFSHORE, INC.
Form 10-Q
April 23, 2014
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UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549
FORM 10-Q
 QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the quarterly period ended March 31, 2014
or
 TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
Commission file number: 0-51582

HERCULES OFFSHORE, INC.
(Exact name of registrant as specified in its charter)

Delaware
(State or other jurisdiction of incorporation or organization)

56-2542838
(I.R.S. Employer Identification No.)

9 Greenway Plaza, Suite 2200
Houston, Texas
(Address of principal executive offices)
(713) 350-5100
(Registrant's telephone number, including area code)

77046
(Zip Code)

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

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§ 232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes No

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

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

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

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Indicate the number of shares outstanding of each of the issuer's classes of common stock, as of the latest practicable date.

Common Stock, par value \$0.01 per share

Outstanding as of April 17, 2014

160,643,649

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PART I. FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS

HERCULES OFFSHORE, INC. AND SUBSIDIARIES

CONSOLIDATED BALANCE SHEETS

(In thousands, except par value)

	March 31, 2014 (Unaudited)	December 31, 2013
ASSETS		
Current Assets:		
Cash and Cash Equivalents	\$197,212	\$198,406
Accounts Receivable, Net of Allowance for Doubtful Accounts of \$357 and \$891 as of March 31, 2014 and December 31, 2013, Respectively	224,199	220,139
Prepays	10,031	20,395
Current Deferred Tax Asset	10,876	10,876
Other	17,708	17,363
	460,026	467,179
Property and Equipment, Net	1,807,343	1,808,526
Cash Designated for Debt Retirement	79,928	—
Other Assets, Net	28,142	25,743
	\$2,375,439	\$2,301,448
LIABILITIES AND STOCKHOLDERS' EQUITY		
Current Liabilities:		
Accounts Payable	\$83,031	\$80,018
Accrued Liabilities	70,919	81,500
Interest Payable	32,142	33,067
Insurance Notes Payable	—	9,568
Other Current Liabilities	29,093	35,735
	215,185	239,888
Long-term Debt	1,290,664	1,210,676
Deferred Income Taxes	14,788	14,452
Other Liabilities	10,230	12,732
Commitments and Contingencies		
Stockholders' Equity:		
Common Stock, \$0.01 Par Value; 300,000 Shares Authorized; 163,348 and 162,144 Shares Issued, Respectively; 160,640 and 159,761 Shares Outstanding, Respectively	1,633	1,621
Capital in Excess of Par Value	2,173,307	2,170,811
Treasury Stock, at Cost, 2,708 and 2,383 Shares, Respectively	(56,717)	(55,165)
Retained Deficit	(1,273,651)	(1,293,567)
	844,572	823,700
	\$2,375,439	\$2,301,448

The accompanying notes are an integral part of these financial statements.

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CONSOLIDATED STATEMENTS OF OPERATIONS

(In thousands, except per share data)

(Unaudited)

	Three Months Ended March	
	31,	
	2014	2013
Revenue	\$256,734	\$186,195
Costs and Expenses:		
Operating Expenses	140,752	113,954
Depreciation and Amortization	40,083	34,938
General and Administrative	18,227	19,116
	199,062	168,008
Operating Income	57,672	18,187
Other Income (Expense):		
Interest Expense	(22,901)	(17,095)
Loss on Extinguishment of Debt	(15,158)	—
Other, Net	150	196
Income Before Income Taxes	19,763	1,288
Income Tax Benefit	153	39,010
Income from Continuing Operations	19,916	40,298
Loss from Discontinued Operations, Net of Taxes	—	(5,136)
Net Income	\$19,916	\$35,162
Earnings (Loss) Per Share:		
Basic:		
Income from Continuing Operations	\$0.12	\$0.25
Loss from Discontinued Operations	—	(0.03)
Net Income	\$0.12	\$0.22
Diluted:		
Income from Continuing Operations	\$0.12	\$0.25
Loss from Discontinued Operations	—	(0.03)
Net Income	\$0.12	\$0.22
Weighted Average Shares Outstanding:		
Basic	160,070	158,931
Diluted	161,883	161,125

The accompanying notes are an integral part of these financial statements.

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CONSOLIDATED STATEMENTS OF CASH FLOWS

(In thousands)

(Unaudited)

	Three Months Ended March 31,	
	2014	2013
Cash Flows from Operating Activities:		
Net Income	\$ 19,916	\$ 35,162
Adjustments to Reconcile Net Income to Net Cash Provided by Operating Activities:		
Depreciation and Amortization	40,083	40,815
Stock-Based Compensation Expense	2,400	2,737
Deferred Income Taxes	(4,616)	) (36,616)
Other	3,089	1,947
(Increase) Decrease in Operating Assets -		
Accounts Receivable	(3,834)	) 8,607
Prepaid Expenses and Other	9,879	(3,293)
Increase (Decrease) in Operating Liabilities -		
Accounts Payable	1,887	13,751
Insurance Notes Payable	(9,568)	) (9,123)
Other Current Liabilities	(16,119)	) (3,325)
Other Liabilities	(2,472)	) (1,983)
Net Cash Provided by Operating Activities	40,645	48,679
Cash Flows from Investing Activities:		
Acquisition of Assets	—	(97,000)
Capital Expenditures	(40,665)	) (44,973)
Proceeds from Sale of Assets, Net	1,679	2,748
Net Cash Used in Investing Activities	(38,986)	) (139,225)
Cash Flows from Financing Activities:		
Long-term Debt Borrowings	300,000	—
Redemption of 7.125% Senior Secured Notes	(220,072)) —
Cash Designated for Debt Retirement	(79,928)) —
Payment of Debt Issuance Costs	(2,961)) —
Other	108	768
Net Cash Provided by (Used In) Financing Activities	(2,853)	) 768
Net Decrease in Cash and Cash Equivalents	(1,194)	) (89,778)
Cash and Cash Equivalents at Beginning of Period	198,406	259,193
Cash and Cash Equivalents at End of Period	\$ 197,212	\$ 169,415

The accompanying notes are an integral part of these financial statements.

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HERCULES OFFSHORE, INC. AND SUBSIDIARIES
 NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
 UNAUDITED

1. General

Hercules Offshore, Inc., a Delaware corporation, and its majority owned subsidiaries (the “Company”) provide shallow-water drilling and marine services to the oil and natural gas exploration and production industry globally through its Domestic Offshore, International Offshore and International Liftboats segments (See Note 10). At March 31, 2014, the Company owned a fleet of 38 jackup rigs, 19 liftboat vessels as well as operated an additional five liftboat vessels owned by a third party. The Company’s diverse fleet is capable of providing services such as oil and gas exploration and development drilling, well service, platform inspection, maintenance and decommissioning operations in several key shallow-water provinces around the world.

The consolidated financial statements of the Company are unaudited; however, they include all adjustments of a normal recurring nature which, in the opinion of management, are necessary for a fair presentation. Certain information relating to the Company’s organization and footnote disclosures normally included in financial statements prepared in accordance with U.S. generally accepted accounting principles have been condensed or omitted in this Form 10-Q pursuant to Securities and Exchange Commission rules and regulations. These financial statements should be read in conjunction with the audited consolidated financial statements for the year ended December 31, 2013 and the notes thereto included in the Company’s Annual Report on Form 10-K. The results of operations for the three months ended March 31, 2014 are not necessarily indicative of the results expected for the full year.

2. Supplemental Financial Information

Consolidated Balance Sheet Information

Other current liabilities consisted of the following:

	March 31, 2014	December 31, 2013
	(in thousands)	
Other Current Liabilities:		
Deferred Revenue - Current Portion	\$19,154	\$21,480
Other	9,939	14,255
	\$29,093	\$35,735

3. Earnings Per Share

The reconciliation of the numerators and denominators used for the computation of basic and diluted earnings per share is as follows:

	Three Months Ended March 31,	
	2014	2013
	(in thousands)	
Numerator:		
Income from continuing operations	\$19,916	\$40,298
Loss from discontinued operations, net of taxes	—	(5,136)
Net income	\$19,916	\$35,162
Denominator:		
Weighted average basic shares	160,070	158,931
Add effect of stock equivalents	1,813	2,194
Weighted average diluted shares	161,883	161,125

The Company calculates basic earnings per share by dividing net income by the weighted average number of shares outstanding. Diluted earnings per share is computed by dividing net income by the weighted average number of shares outstanding during the period as adjusted for the dilutive effect of the Company’s stock option, time-based restricted stock and performance-based restricted stock awards. The effect of stock option and restricted stock awards is not

included in the computation for periods in which a net loss occurs, because to do so would be anti-dilutive. The Company's diluted earnings per

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HERCULES OFFSHORE, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

UNAUDITED

share calculation excludes 1.2 million and 1.1 million stock equivalents for the three months ended March 31, 2014 and 2013, respectively, due to their anti-dilutive effect.

4. Business Combination and Asset Acquisitions

Prior to June 24, 2013, the Company held a 32% equity investment in Discovery Offshore S.A. ("Discovery"). On June 24, 2013 (the "Acquisition Date"), the Company acquired an additional 52% interest to bring the total interest held to 84% ("Discovery Transaction") and began consolidating Discovery's results of operations from that date. As of December 31, 2013, the Company held a 100% interest in Discovery as a result of additional purchases of shares of Discovery common stock subsequent to the Acquisition Date.

The unaudited pro forma financial information set forth below has been compiled from historical financial statements as recast for the Company's discontinued operations and other information, but is not necessarily indicative of the results that actually would have been achieved had the transaction occurred at the date indicated or that may be achieved in the future:

	Three Months Ended March 31, 2013 (in millions, except per share data)
Revenue	\$ 184.0
Income from Continuing Operations	39.4
Loss from Discontinued Operations, Net of Taxes	(5.1)
Net Income	\$ 34.3
Net Income Per Share:	
Basic:	
Income from Continuing Operations	\$ 0.25
Loss from Discontinued Operations	(0.03)
Net Income	\$ 0.22
Diluted:	
Income from Continuing Operations	\$ 0.24
Loss from Discontinued Operations	(0.03)
Net Income	\$ 0.21

In March 2013, the Company acquired the offshore drilling rig Hercules 267 for \$55.0 million and the liftboat Bull Ray for \$42.0 million.

5. Dispositions and Discontinued Operations

In 2013, the Company sold its U.S. Gulf of Mexico Liftboats and related assets and additionally sold twelve of its inland barge rigs and related assets, comprising the majority of the Inland segment fleet. The results of operations of the former Domestic Liftboat and Inland segments are reflected in the Consolidated Statements of Operations for the three months ended March 31, 2013 as discontinued operations.

Interest charges of \$0.8 million and \$0.6 million have been allocated, based on a pro rata calculation of the net assets sold as compared to the Company's consolidated net assets, to the Inland and Domestic Liftboats segments, respectively, for the three months ended March 31, 2013.

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HERCULES OFFSHORE, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

UNAUDITED

Operating results included in discontinued operations were as follows:

	Three Months Ended March 31, 2013 (in thousands)
Inland:	
Revenue	\$4,348
Loss Before Income Taxes	\$(4,785)
Income Tax Benefit	350
Loss from Discontinued Operations, Net of Taxes	\$(4,435)
Domestic Liftboats:	
Revenue	\$14,784
Loss Before Income Taxes	\$(701)
Income Tax Benefit	—
Loss from Discontinued Operations, Net of Taxes	\$(701)
Total:	
Revenue	\$19,132
Loss Before Income Taxes	\$(5,486)
Income Tax Benefit	350
Loss from Discontinued Operations, Net of Taxes	\$(5,136)

6. Debt

Senior Secured Credit Agreement

On April 3, 2012, the Company entered into a credit agreement which as amended on July 8, 2013 (the "Credit Agreement") governs its senior secured revolving credit facility (the "Credit Facility"). The Credit Agreement provides for a \$150.0 million senior secured revolving credit facility. As of March 31, 2014, no amounts were outstanding and \$10.5 million in letters of credit had been issued under the Credit Facility, therefore the remaining availability under this facility was \$139.5 million. During any period of time that outstanding letters of credit under the Credit Facility exceed \$10 million or there are any revolving borrowings outstanding under the Credit Facility, the Company will have to maintain compliance with a maximum secured leverage ratio (as defined in the Credit Agreement, being generally computed as the ratio of secured indebtedness to consolidated cash flow). The maximum secured leverage ratio is 3.50 to 1.00. As of March 31, 2014, the Company was in compliance with all covenants under its revolving credit facility.

The Company's obligations under the Credit Agreement are guaranteed by substantially all of the Company's current domestic subsidiaries (collectively, the "Guarantors"), and the obligations of the Company and the Guarantors are secured by liens on substantially all of the vessels owned by the Company and the Guarantors, together with certain accounts receivable, equity of subsidiaries, equipment and other assets.

6.75% Senior Notes due 2022

On March 26, 2014, the Company completed the issuance and sale of \$300.0 million aggregate principal amount of senior notes at a coupon rate of 6.75% ("6.75% Senior Notes") with maturity in April 2022. These notes were sold at par and the Company received net proceeds from the offering of the notes of approximately \$294.8 million after deducting bank fees and estimated offering expenses. Interest on the notes will accrue from and including March 26, 2014 at a rate of 6.75% per year and is payable semi-annually in arrears on April 1 and October 1 of each year, beginning October 1, 2014. These notes are guaranteed by each of the Guarantors that guarantee the Company's obligations under its Credit Agreement.

Prior to April 1, 2017, the Company may redeem the notes with the net cash proceeds of certain equity offerings, at a redemption price equal to 106.75% of the aggregate principal amount plus accrued and unpaid interest; provided, that (i) after giving effect to any such redemptions, at least 65% of the notes originally issued would remain outstanding immediately after such redemption and (ii) the Company makes such redemption not more than 180 days after consummation of such equity offering. In addition, prior to April 1, 2017, the Company may redeem all or part of the notes at a price equal to 100% of the

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HERCULES OFFSHORE, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

UNAUDITED

aggregate principal amount of the notes to be redeemed, plus the applicable premium, as defined in the indenture, and accrued and unpaid interest.

On or after April 1, 2017, the Company may redeem all or part of the notes at the redemption prices set forth below, together with accrued and unpaid interest, if any, to the redemption date, if redeemed during the 12-month period beginning April 1 of the years indicated:

Year	Optional Redemption Price	
2017	105.063	%
2018	103.375	%
2019	101.688	%
2020 and thereafter	100.000	%

If the Company experiences certain kinds of changes of control, holders of the notes will be entitled to require the Company to purchase all or any portion of the notes for a cash price equal to 101.0% of the principal amount of the applicable notes, plus accrued and unpaid interest, if any, to the date of purchase. Furthermore, in certain circumstances following an asset sale (as defined in the indenture), the Company may be required to use the excess proceeds to offer to repurchase the notes at an offer price in cash equal to 100% of their principal amount, plus accrued and unpaid interest.

Retirement of 7.125% Senior Secured Notes

In 2012, the Company issued \$300.0 million of senior secured notes at a coupon rate of 7.125% ("7.125% Senior Secured Notes") with maturity in April 2017. On March 12, 2014 the Company commenced a cash tender offer (the "Tender offer") for any and all of the \$300.0 million outstanding aggregate principal amount of its 7.125% Senior Secured Notes. Senior secured notes totaling approximately \$220.1 million were settled on March 26, 2014 for \$232.7 million using a portion of the proceeds from the issuance of the 6.75% Senior Notes. Liens securing the Company's obligations and certain other restrictions under the 7.125% Senior Secured Notes were released pursuant to the supplemental indenture which became effective on March 26, 2014. The Company expects to use the remaining net proceeds from the 6.75% Senior Notes due 2022 offering, together with cash on hand, to complete the redemption of the remaining \$79.9 million aggregate principal amount of the 7.125% Senior Secured Notes on April 29, 2014 for approximately \$84.2 million. As such, the Company has classified approximately \$79.9 million of its cash on hand as Cash Designated for Debt Retirement on the Balance Sheet as of March 31, 2014.

Other Indenture Provisions

The Credit Agreement as well as the indentures governing the 8.75% Senior Notes, 7.5% Senior Notes, 6.75% Senior Notes, 7.125% Senior Secured Notes, 10.25% Senior Notes and 3.375% Convertible Senior Notes contain customary events of default. In addition, the Credit Agreement as well as the indentures governing the 8.75% Senior Notes, 7.5% Senior Notes, 6.75% Senior Notes, 10.25% Senior Notes and 3.375% Convertible Senior Notes also contain a provision under which an event of default by the Company or by any restricted subsidiary on any other indebtedness exceeding \$25.0 million would be considered an event of default under the Credit Agreement and indentures if such default: a) is caused by failure to pay the principal at final maturity, or b) results in the acceleration of such indebtedness prior to maturity.

The Credit Agreement as well as the indentures governing the 8.75% Senior Notes, 7.5% Senior Notes, 6.75% Senior Notes, and 10.25% Senior Notes contain covenants that, among other things, limit the Company's ability and the ability of its restricted subsidiaries to:

- incur additional indebtedness or issue certain preferred stock;
- pay dividends or make other distributions;
- make other restricted payments or investments;
- sell assets;

- create liens;
- enter into agreements that restrict dividends and other payments by restricted subsidiaries;
- engage in transactions with affiliates; and
- consolidate, merge or transfer all or substantially all of its assets.

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HERCULES OFFSHORE, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

UNAUDITED

Substantially all of the Company's domestic subsidiaries guarantee the obligations under the Credit Agreement, the 8.75% Senior Notes, 7.5% Senior Notes, 6.75% Senior Notes, 7.125% Senior Secured Notes and 10.25% Senior Notes.

Loss on Extinguishment of Debt

During the three months ended March 31, 2014, the Company incurred the following charges which are included in Loss on Extinguishment of Debt in the Consolidated Statement of Operations:

In March 2014, the Company incurred a pretax charge of \$15.2 million, \$15.2 million net of tax, consisting of a \$12.6 million call premium and \$1.4 million of unamortized debt issuance costs related to the redemption of the 7.125% Senior Secured Notes, as well as \$1.1 million of bank fees related to the issuance of the 6.75% Senior Notes.

7. Fair Value Measurements

Fair value measurements are generally based upon observable and unobservable inputs. Observable inputs reflect market data obtained from independent sources, while unobservable inputs reflect the Company's view of market assumptions in the absence of observable market information. The Company utilizes valuation techniques that maximize the use of observable inputs and minimize the use of unobservable inputs. The Company uses the fair value hierarchy included in Financial Accounting Standards Board ("FASB") Accounting Standards Codification ("ASC") Topic 820-10, Fair Value Measurements and Disclosure ("ASC 820-10"), which is intended to increase consistency and comparability in fair value measurements and related disclosures. The fair value hierarchy consists of the following three levels:

Level 1 — Inputs are quoted prices in active markets for identical assets or liabilities.

Level 2 — Inputs are quoted prices for similar assets or liabilities in an active market, quoted prices for identical or similar assets or liabilities in markets that are not active, inputs other than quoted prices that are observable and market-corroborated inputs which are derived principally from or corroborated by observable market data.

Level 3 — Inputs are derived from valuation techniques in which one or more significant inputs or value drivers are unobservable.

Fair Value of Financial Instruments

The carrying amounts of the Company's financial instruments, which include cash and cash equivalents, accounts receivable, accounts payable, accrued liabilities and other current liabilities, approximate fair values because of the short-term nature of the instruments. The fair value of the Company's cash equivalents are Level 1.

The fair value of the Company's 3.375% Convertible Senior Notes, 8.75% Senior Notes, 7.5% Senior Notes, 6.75% Senior Notes, 10.25% Senior Notes and 7.125% Senior Secured Notes is estimated based on quoted prices in active markets. The fair value of the Company's 7.375% Senior Notes is estimated based on discounted cash flows using inputs from quoted prices in active markets for similar debt instruments. The inputs used to determine fair value are considered Level 2 inputs.

The following table provides the carrying value and fair value of the Company's long-term debt instruments:

	March 31, 2014		December 31, 2013	
	Carrying Value	Fair Value	Carrying Value	Fair Value
	(in millions)			
8.75% Senior Notes, due July 2021	\$400.0	\$444.6	\$400.0	\$447.5
7.5% Senior Notes, due October 2021	300.0	304.9	300.0	317.3
6.75% Senior Notes, due April 2022	300.0	295.3	—	—
7.125% Senior Secured Notes, due April 2017	79.9	84.4	300.0	320.1
10.25% Senior Notes, due April 2019	200.0	225.2	200.0	226.8
3.375% Convertible Senior Notes, due June 2038	7.2	6.8	7.2	7.1
7.375% Senior Notes, due April 2018	3.5	3.4	3.5	3.5

8. Long-Term Incentive Awards
Stock-based Compensation

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HERCULES OFFSHORE, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

UNAUDITED

The Company's 2004 Amended and Restated Long-Term Incentive Plan (the "2004 Plan") provides for the granting of stock options, restricted stock, phantom stock, performance stock awards and other stock-based awards to selected employees and non-employee directors of the Company. At March 31, 2014, approximately 2.1 million shares were available for grant or award under the 2004 Plan.

During the three months ended March 31, 2014, the Company granted the following equity awards:

Time-based awards The Company granted 1.2 million time-based restricted stock awards to employees which vest 1/3 per year. The grant-date fair value per share for these time-based restricted stock awards is equal to the closing price of the Company's stock on the grant date, which was a weighted-average grant date fair value of \$4.72 for the awards granted in the three months ended March 31, 2014.

Objective-based awards The Company granted additional compensation awards to employees that are based on the Company's achievement of certain Company-based performance objectives as well as the Company's achievement of certain market-based objectives. These awards, which cliff vest on the third anniversary of the grant date, are payable in shares at target levels when combined and in cash for the amount above target up to maximum, as defined by the agreements. For the CEO's portion of these awards, the portion payable in cash is based on the achievement of certain market-based and Company-based performance objectives being met at threshold levels when combined. The fair value of all awards requiring share settlement is measured at the fair value on the grant date, while those requiring cash settlement are remeasured at the end of each reporting period.

The Company accounts for awards, or the portion of the awards, requiring cash settlement under stock-compensation principles of accounting as liability instruments. The fair value of all liability instruments are being remeasured based on the awards' estimated fair value at the end of each reporting period and are being recorded to expense over the vesting period.

The awards that are based on the Company's achievement of market-based objectives related to the Company's stock price are valued using a Monte Carlo simulation. The Company uses various assumptions to estimate the fair value of the Company's objective-based awards. The Company uses the historical volatility of its common stock to estimate volatility while the dividend yield assumptions are based on historical and anticipated dividend payouts. The risk-free interest rate assumptions are based on observed interest rates consistent with the approximate vesting periods and the stock price used represents the closing price of the Company's common stock at the valuation date.

9. Income Taxes

The Company, directly or through its subsidiaries, files income tax returns in the United States, and multiple state and foreign jurisdictions. The Company's tax returns for 2007 through 2013 remain open for examination by the taxing authorities in the respective jurisdictions where those returns were filed. Although the Company believes that its estimates are reasonable, the final outcome in the event that the Company is subjected to an audit could be different from that which is reflected in its historical income tax provision and accruals. Such differences could have a material effect on the Company's income tax provision and net income in the period in which such determination is made. In addition, TODCO tax obligations from periods prior to its initial public offering in 2004 are indemnified by Transocean, the former owner of TODCO, under the tax sharing agreement, except for the Trinidad and Tobago jurisdiction. The Company's Trinidadian and Tobago tax returns are open for examination for the years 2007 through 2013.

Effective April 27, 2011, the Company completed the Seahawk Transaction. For tax purposes this was characterized as a reorganization pursuant to IRC §368(a)(1)(G). Therefore, the Company recorded deferred tax assets, net of a valuation allowance, of approximately \$37.7 million in the first quarter 2013. There can be no assurance that these deferred tax assets will be realized.

From time to time, the Company's tax returns are subject to review and examination by various tax authorities within the jurisdictions in which the Company operates or has operated. The Company is currently contesting tax assessments in Venezuela, and may contest future assessments where the Company believes the assessments are

meritless.

In June 2013, the U.S. Internal Revenue Service commenced an audit of the U.S. Corporate Income Tax Return for the 2010 calendar year. The audit was completed during March 2014 and the Company received notification from the Internal Revenue Service that the audit resulted in no change to the Company's reported tax. In January 2014, the Federal Inland Revenue Service of Nigeria notified the Company that it will initiate an audit including calendar years 2007 through 2011. While the Company cannot predict or provide assurance regarding the outcome of these proceedings, the Company does not expect the ultimate liability to have a material effect on its consolidated financial statements.

During the three months ended March 31, 2014, the Company recognized \$4.8 million of tax benefit as a result of the tolling of a statute of limitations in a foreign jurisdiction.

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HERCULES OFFSHORE, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

UNAUDITED

10. Segments

The Company currently reports its business activities in three business segments: (1) Domestic Offshore, (2) International Offshore and (3) International Liftboats. The Company eliminates inter-segment revenue and expenses, if any.

The results of operations of the former Domestic Liftboats and Inland segments are reflected in the Consolidated Statements of Operations for the three months ended March 31, 2013 as discontinued operations. The financial information of the Company's discontinued operations is not included in the results of operations presented for the Company's reporting segments (See Note 5). The remaining assets of the former Inland segment, which included spare equipment, one cold stacked barge and a barge that will be used as a training rig, have been transferred to the Domestic Offshore segment and the historical results of Domestic Offshore have been recast to include the operating results of these assets.

The Company's jackup rigs are used primarily for exploration and development drilling in shallow waters. The Company's liftboats are self-propelled, self-elevating vessels with a large open deck space, which provides a versatile, mobile and stable platform to support a broad range of offshore maintenance and construction services throughout the life of an oil or natural gas well.

Information regarding the Company's reportable segments is as follows:

	Three Months Ended March 31, 2014			Three Months Ended March 31, 2013		
	Revenue	Income (Loss) from Operations	Depreciation and Amortization	Revenue	Income (Loss) from Operations	Depreciation and Amortization
	(in thousands)			(in thousands)		
Domestic Offshore	\$143,265	\$51,546	\$17,371	\$121,115	\$39,955	\$19,844
International Offshore	80,938	14,642	16,626	31,774	(12,169)	10,020
International Liftboats	32,531	5,564	5,126	33,306	5,152	4,352
	\$256,734	\$71,752	\$39,123	\$186,195	\$32,938	\$34,216
Corporate	—	(14,080)	960	—	(14,751)	722
Total Company	\$256,734	\$57,672	\$40,083	\$186,195	\$18,187	\$34,938

	Total Assets	
	March 31, 2014	December 31, 2013
	(in thousands)	
Domestic Offshore	\$815,510	\$783,652
International Offshore	1,310,433	1,290,122
International Liftboats	201,218	180,356
Corporate	48,278	47,318
Total Company	\$2,375,439	\$2,301,448

11. Commitments and Contingencies

Legal Proceedings

The Company is involved in various claims and lawsuits in the normal course of business. As of March 31, 2014, management did not believe any accruals were necessary in accordance with FASB ASC 450-20, Contingencies — Loss Contingencies.

Shareholder Derivative Suits

Say-on-Pay Litigation

In June 2011, two separate shareholder derivative actions were filed purportedly on the Company's behalf in response to its failure to receive a majority advisory "say-on-pay" vote in favor of the Company's 2010 executive compensation. On June 8,

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HERCULES OFFSHORE, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

UNAUDITED

2011, the first action was filed in the District Court of Harris County, Texas, and on June 23, 2011, the second action was filed in the United States Court for the District of Delaware. Subsequently, on July 21, 2011, the plaintiff in the Harris County action filed a concurrent action in the United States District Court for the Southern District of Texas. Each action named the Company as a nominal defendant and certain of its officers and directors, as well as the Company's Compensation Committee's consultant, as defendants. Plaintiffs allege that the Company's directors breached their fiduciary duty by approving excessive executive compensation for 2010, that the Compensation Committee consultant aided and abetted that breach of fiduciary duty, that the officer defendants were unjustly enriched by receiving the allegedly excessive compensation, and that the directors violated the federal securities laws by disseminating a materially false and misleading proxy. The plaintiffs seek damages in an unspecified amount on the Company's behalf from the officer and director defendants, certain corporate governance actions, and an award of their costs and attorney's fees. The Company and the other defendants have filed motions to dismiss these cases for failure to make demand upon the Company's board and for failing to state a claim. On June 11, 2012, the plaintiff in the Harris County action voluntarily dismissed his action. On March 14, 2013, the Company's and the other defendants' motions to dismiss the Delaware federal action were granted. The motions to dismiss the Texas federal action are pending.

The Company does not expect the ultimate outcome of the shareholder derivative lawsuit to have a material adverse effect on its consolidated results of operations, financial position or cash flows.

The Company and its subsidiaries are involved in a number of other lawsuits, all of which have arisen in the ordinary course of business. The Company does not believe that the ultimate liability, if any, resulting from any such other pending litigation will have a material adverse effect on its business or consolidated financial statements.

The Company cannot predict with certainty the outcome or effect of any of the litigation matters specifically described above or of any other pending litigation. There can be no assurance that the Company's belief or expectations as to the outcome or effect of any lawsuit or other litigation matter will prove correct, and the eventual outcome of these matters could materially differ from management's current estimates.

Insurance and Indemnity

The Company is self-insured for the deductible portion of its insurance coverage. Management believes adequate accruals have been made on known and estimated exposures up to the deductible portion of the Company's insurance coverage. Management believes that claims and liabilities in excess of the amounts accrued are adequately insured. However, the Company's insurance is subject to exclusions and limitations, and there is no assurance that such coverage will adequately protect the Company against liability from all potential consequences. In addition, there is no assurance of renewal or the ability to obtain coverage acceptable to the Company. The Company maintains insurance coverage that includes coverage for physical damage, third party liability, workers' compensation and employer's liability, general liability, vessel pollution and other coverages.

Effective May 1, 2013, the Company completed the annual renewal of all of its key insurance policies. The Company's primary marine package provides for hull and machinery coverage for substantially all of the Company's rigs and liftboats up to a scheduled value of each asset. The total maximum amount of coverage for these assets is \$1.7 billion. The marine package includes protection and indemnity and maritime employer's liability coverage for marine crew personal injury and death and certain operational liabilities, with primary coverage (or self-insured retention for maritime employer's liability coverage) of \$5.0 million per occurrence with excess liability coverage up to \$200.0 million. The marine package policy also includes coverage for personal injury and death of third parties with primary and excess coverage of \$25.0 million per occurrence with additional excess liability coverage up to \$200.0 million, subject to a \$250,000 per-occurrence deductible. The marine package also provides coverage for cargo and charterer's legal liability. The marine package includes limitations for coverage for losses caused in U.S. Gulf of Mexico named windstorms, including an annual aggregate limit of liability of \$75.0 million for property damage and removal of wreck liability coverage. The Company also procured an additional \$75.0 million excess policy for removal of wreck

and certain third-party liabilities incurred in U.S. Gulf of Mexico named windstorms. Deductibles for events that are not caused by a U.S. Gulf of Mexico named windstorm are 12.5% of the insured drilling rig values per occurrence, subject to a minimum of \$1.0 million, and \$1.0 million per occurrence for liftboats. The deductible for drilling rigs in a U.S. Gulf of Mexico named windstorm event is \$25.0 million. Vessel pollution is covered under a Water Quality Insurance Syndicate policy ("WQIS Policy") providing limits as required by applicable law, including the Oil Pollution Act of 1990. The WQIS Policy covers pollution emanating from the Company's vessels and drilling rigs, with primary limits of \$5.0 million (inclusive of a \$3.0 million per-occurrence deductible) and excess liability coverage up to \$200.0 million.

Control-of-well events generally include an unintended flow from the well that cannot be contained by equipment on site (e.g., a blow-out preventer), by increasing the weight of the drilling fluid, or that does not naturally close itself off through what is typically described as "bridging over". The Company carries a contractor's extra expense policy with \$25.0 million primary

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HERCULES OFFSHORE, INC. AND SUBSIDIARIES

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liability coverage for well control costs, pollution and expenses incurred to redrill wild or lost wells, with excess liability coverage up to \$200.0 million for pollution liability that is covered in the primary policy. The policies are subject to exclusions, limitations, deductibles, self-insured retention and other conditions. In addition to the marine package, the Company has separate policies providing coverage for onshore foreign and domestic general liability, employer's liability, auto liability and non-owned aircraft liability, with customary deductibles and coverage. The Company's drilling contracts provide for varying levels of indemnification from its customers and in most cases, may require the Company to indemnify its customers for certain liabilities. Under the Company's drilling contracts, liability with respect to personnel and property is customarily assigned on a "knock-for-knock" basis, which means that the Company and its customers assume liability for their respective personnel and property, regardless of how the loss or damage to the personnel and property may be caused, and even if the Company is grossly negligent. However, since the Macondo blowout and resulting litigation, some of the Company's customers have been reluctant to extend their indemnity obligations in instances where the Company is grossly negligent. The Company's customers typically assume responsibility for and agree to indemnify the Company from any loss or liability resulting from pollution or contamination, including clean-up and removal and third-party damages arising from operations under the contract and originating below the surface of the water, including as a result of blowouts or cratering of the well ("Blowout Liability"). The customer's assumption for Blowout Liability may, in certain circumstances, be contractually limited or could be determined to be unenforceable in the event of the Company's gross negligence, willful misconduct or other egregious conduct. In addition, the Company may not be indemnified for statutory penalties and punitive damages relating to such pollution or contamination events. The Company generally indemnifies the customer for the consequences of spills of industrial waste or other liquids originating solely above the surface of the water and emanating from its rigs or vessels.

The Company has separate primary marine packages for Hercules Triumph and Hercules Resilience that each provide hull and machinery coverage up to \$250.0 million, subject to a \$2.5 million per-occurrence deductible, which increases to \$5.0 million for losses incurred during delivery voyages. Each marine package also provides coverage for cargo, contractor's extra expense and loss of hire coverage. The Company also has operational protection and indemnity coverage up to \$500.0 million per rig, subject to a \$50,000 per-occurrence deductible for claims originating outside the U.S. and a \$250,000 per-occurrence deductible for claims originating in the U.S. Additionally, the Company has coverage for extended contractual liability that includes subsea activities, property and personnel, and clean-up costs up to \$25.0 million per rig and pollution-by-blowout coverage up to \$10.0 million per rig, all subject to certain contractual assumptions and limitations. The Company does not have coverage inclusive of U.S. Gulf of Mexico named windstorms for the Hercules Triumph and Hercules Resilience.

In 2013, in connection with the renewal of certain of its insurance policies, the Company entered into an agreement to finance a portion of its annual insurance premiums. Approximately \$30.7 million was financed through this arrangement with an interest rate of 3.24%. Additionally, \$1.3 million of insurance premiums for the Hercules Triumph were financed at an interest rate of 3.24%. There was \$9.6 million outstanding in insurance notes payable at December 31, 2013 which were fully paid by their maturity date of March 2014.

Hercules 265 Incident and Settlement of Property Damage Insurance Claim

In July 2013, the Company's jackup drilling rig Hercules 265, a 250' mat-supported cantilevered unit operating in the U.S. Gulf of Mexico Outer Continental Shelf lease block South Timbalier 220, experienced a well control incident. The rig sustained substantial damage in the incident and the Company's insurance underwriters determined that the rig was a constructive total loss. The cause of the incident is unknown but is under investigation. The Company also has removal of wreck coverage up to a total amount of \$110.0 million. In the event any pollution emanated from the Company's rig or equipment as a result of the incident, the Company's vessel pollution policy provides coverage, subject to deductibles and limitations. The Company and its insurance underwriters continue to negotiate the insurance recovery amounts for costs related to the salvage of the rig and certain other insured losses.

Sales and Use Tax Audits

Certain of the Company's legal entities are under audit by various taxing authorities for several prior-year periods. These audits are ongoing and the Company is working to resolve all relevant issues. The Company has an accrual of \$6.8 million and \$9.1 million related to these sales and use tax matters, which is included in Accrued Liabilities on the Consolidated Balance Sheets as of March 31, 2014 and December 31, 2013, respectively.

12. Accounting Pronouncements

In July 2013, the FASB issued Accounting Standards Update ("ASU") No. 2013-11, Presentation of an Unrecognized Tax Benefit When a Net Operating Loss Carryforward, a Similar Tax Loss, or a Tax Credit Carryforward Exists ("ASU 2013-11").

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HERCULES OFFSHORE, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

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The amendments in this ASU provides guidance on presentation of unrecognized tax benefits and is expected to reduce diversity in practice and better reflect the manner in which an entity would settle at the reporting date any additional income taxes that would result from the disallowance of a tax position when net operating loss carryforwards, similar tax losses, or tax credit carryforwards exist. The amendments in this ASU were effective prospectively for interim and annual periods beginning after December 15, 2013, with early adoption and retrospective application permitted. The Company adopted ASU 2013-11 as of January 1, 2014 with no material impact on its consolidated financial statements.

In April 2014, the FASB issued ASU No. 2014-08, Presentation of Financial Statements and Property, Plant, and Equipment: Reporting Discontinued Operations and Disclosures of Disposals of Components of an Entity ("ASU 2014-08"). The amendments in this ASU require that a disposal representing a strategic shift that has (or will have) a major effect on an entity's operations and financial results should be reported as discontinued operations. The amendments also expand the disclosure requirements for discontinued operations and add new disclosures for disposals of a significant part of an organization that does not qualify as discontinued operations. The amendments in this ASU are effective prospectively for annual periods beginning on or after December 15, 2014, and interim periods within those years. Early adoption is permitted for disposals that have not been previously reported. The Company does not expect the adoption of this standard to have a material impact on its consolidated financial statements.

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

The following discussion and analysis of our financial condition and results of operations should be read in conjunction with the accompanying unaudited consolidated financial statements as of March 31, 2014 and for the three months ended March 31, 2014 and March 31, 2013, included elsewhere herein, and with our Annual Report on Form 10-K for the year ended December 31, 2013. The following discussion and analysis contains forward-looking statements that involve risks and uncertainties. Please read "Forward-Looking Statements" below for a discussion of certain limitations inherent in such statements. Our actual results may differ materially from those anticipated in these forward-looking statements as a result of certain factors. Please also read "Risk Factors" in Item 1A of our Annual Report on Form 10-K for the year ended December 31, 2013 and Item 1A of Part II of this quarterly report for a discussion of certain risks facing our company.

OVERVIEW

We are a leading provider of shallow-water drilling and marine services to the oil and natural gas exploration and production industry globally. We provide these services to national oil and gas companies, major integrated energy companies and independent oil and natural gas operators. As of April 22, 2014, we owned a fleet of 38 jackup rigs, 19 liftboat vessels as well as operated an additional five liftboat vessels owned by a third party. Our diverse fleet is capable of providing services such as oil and gas exploration and development drilling, well service, platform inspection, maintenance and decommissioning operations in several key shallow-water provinces around the world. Our drilling rigs are used primarily for exploration and development drilling in shallow waters. Under most of our contracts, we are paid a fixed daily rental rate called a "dayrate," and we are required to pay all costs associated with our own crews as well as the upkeep and insurance of the rig and equipment.

Our liftboats are self-propelled, self-elevating vessels with a large open deck space, which provides a versatile, mobile and stable platform to support a broad range of offshore maintenance and construction services throughout the life of an oil or natural gas well. Under most of our liftboat contracts, we are paid a fixed dayrate for the rental of the vessel, which typically includes the costs of a small crew of five to ten employees, and we also receive a variable rate for reimbursement of other operating costs such as catering, fuel, oil, rental equipment, crane overtime and other items. Our backlog at April 22, 2014, totaled approximately \$1.0 billion for our executed contracts. Approximately \$424.0 million of this backlog is expected to be realized during the remainder of 2014. We calculate our contract revenue backlog, or future contracted revenue, as the contract dayrate multiplied by the number of days remaining on the contract, assuming full utilization, less any penalties or reductions in dayrate for late delivery or non-compliance with contractual obligations. Backlog excludes revenue for management agreements, mobilization, demobilization, contract preparation and customer reimbursables. The amount of actual revenue earned and the actual periods during which revenue is earned will be different than the backlog disclosed or expected due to various factors. Downtime due to various operational factors, including unscheduled repairs, maintenance, operational delays, health, safety and environmental incidents, weather events in the Gulf of Mexico and elsewhere and other factors (some of which are beyond our control), may result in lower dayrates than the full contractual operating dayrate. In some of the contracts, our customer has the right to terminate the contract without penalty and in certain instances, with little or no notice.

Regulation

The Coast Guard issued a Policy Letter in July 2011 that provides for more frequent inspections of foreign flagged Mobile Offshore Drilling Units ("MODUs") that operate on the U.S. Outer Continental Shelf ("OCS"). The Coast Guard will make determinations to conduct more frequent inspections of foreign flagged MODUs in accordance with its Mobile Offshore Drilling Unit Safety and Environmental Protection Compliance Targeting Matrix. We may be subject to increased costs and potential downtime for certain of our rigs operating on the OCS if such rigs are determined by the Coast Guard to need additional oversight and inspection under this Policy Letter.

In addition to this Coast Guard Policy Letter, in November 2011, the Bureau of Safety and Environmental Enforcement ("BSEE") announced a change in its enforcement policies in the aftermath of the Macondo well blowout in April 2010, pursuant to which the agency has extended its regulatory enforcement reach to include contractors as well as offshore lease operators. Consequently, the BSEE may elect to hold contractors, including drilling contractors, liable for alleged violations of law arising in the BSEE's jurisdictional area. In August 2012, the BSEE issued an

Interim Policy Letter that established the parameters by which BSEE will issue incidents of noncompliance to drilling contractors for serious violations of BSEE regulations. Implementation of this change in enforcement policy by the BSEE could subject us to added liabilities, including sanctions and penalties, as well as increased costs arising from contractual arrangements in master services agreements that failed to take into account such change in enforcement policy with respect to our operations in the U.S. Gulf of Mexico, which may have an adverse effect on our business and results of operations.

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RESULTS OF OPERATIONS

The following table sets forth financial information by operating segment and other selected information for the periods indicated:

	Three Months Ended March 31,		Change	% Change	
	2014	2013			
	(Dollars in thousands)				
Domestic Offshore:					
Number of rigs (as of end of period)	28	29			
Revenue	\$143,265	\$121,115	\$22,150	18.3	%
Operating expenses	72,800	59,751	13,049	21.8	%
Depreciation and amortization expense	17,371	19,844	(2,473)	(12.5))%
General and administrative expenses	1,548	1,565	(17)	(1.1))%
Operating income	\$51,546	\$39,955	\$11,591	29.0	%
International Offshore:					
Number of rigs (as of end of period)	10	9			
Revenue	\$80,938	\$31,774	\$49,164	154.7	%
Operating expenses	47,538	31,911	15,627	49.0	%
Depreciation and amortization expense	16,626	10,020	6,606	65.9	%
General and administrative expenses	2,132	2,012	120	6.0	%
Operating income (loss)	\$14,642	\$(12,169)	) \$26,811	n/m	
International Liftboats:					
Number of liftboats (as of end of period)	24	25			
Revenue	\$32,531	\$33,306	\$(775)	(2.3))%
Operating expenses	20,414	22,292	(1,878)	(8.4))%
Depreciation and amortization expense	5,126	4,352	774	17.8	%
General and administrative expenses	1,427	1,510	(83)	(5.5))%
Operating income	\$5,564	\$5,152	\$412	8.0	%
Total Company:					
Revenue	\$256,734	\$186,195	\$70,539	37.9	%
Operating expenses	140,752	113,954	26,798	23.5	%
Depreciation and amortization expense	40,083	34,938	5,145	14.7	%
General and administrative expenses	18,227	19,116	(889)	(4.7))%
Operating income	57,672	18,187	39,485	217.1	%
Interest expense	(22,901)	) (17,095)	) (5,806)	) 34.0	%
Loss on extinguishment of debt	(15,158)	) —	(15,158)	) n/m	
Other, net	150	196	(46)	(23.5))%
Income before income taxes	19,763	1,288	18,475	n/m	
Income tax benefit	153	39,010	(38,857)	(99.6))%
Income from continuing operations	19,916	40,298	(20,382)	(50.6))%
Loss from discontinued operations, net of taxes	—	(5,136)) 5,136	n/m	
Net income	\$19,916	\$35,162	\$(15,246)	(43.4))%

"n/m" means not meaningful.

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The following table sets forth selected operational data by operating segment for the periods indicated:

Three Months Ended March 31, 2014

	Operating Days	Available Days	Utilization(1)	Average Revenue per Day(2)	Average Operating Expense per Day(3)
Domestic Offshore	1,344	1,620	83.0	% \$106,596	\$44,938
International Offshore	595	675	88.1	% 136,030	70,427
International Liftboats	1,199	2,070	57.9	% 27,132	9,862

Three Months Ended March 31, 2013

	Operating Days	Available Days	Utilization(1)	Average Revenue per Day(2)	Average Operating Expense per Day(3)
Domestic Offshore	1,548	1,620	95.6	% \$78,240	\$36,883
International Offshore	269	450	59.8	% 118,119	70,913
International Liftboats	1,450	2,011	72.1	% 22,970	11,085

Utilization is defined as the total number of days our rigs or liftboats, as applicable, were under contract, known as operating days, in the period as a percentage of the total number of available days in the period. Days during which our rigs and liftboats were undergoing major refurbishments, upgrades or construction, and days during which our rigs and liftboats are cold stacked, are not counted as available days. Days during which our liftboats are in the shipyard undergoing drydocking or inspection are considered available days for the purposes of calculating utilization.

(1) Average revenue per rig or liftboat per day is defined as revenue earned by our rigs or liftboats, as applicable, in the period divided by the total number of operating days for our rigs or liftboats, as applicable, in the period. Average operating expense per rig or liftboat per day is defined as operating expenses, excluding depreciation and amortization, incurred by our rigs or liftboats, as applicable, in the period divided by the total number of available days in the period. We use available days to calculate average operating expense per rig or liftboat per day rather than operating days, which are used to calculate average revenue per rig or liftboat per day, because we incur operating expenses on our rigs and liftboats even when they are not under contract and earning a dayrate.

For the Three Months Ended March 31, 2014 and 2013

Revenue

Consolidated. The increase in consolidated revenue is described below.

Domestic Offshore. Revenue increased for our Domestic Offshore segment due to higher average dayrates in the Current Quarter as compared to the Comparable Quarter, which contributed to an increase of approximately \$44 million. Partially offsetting this increase, operating days declined in the Current Quarter as compared to the Comparable Quarter, which contributed to a decrease in revenue of approximately \$22 million, primarily due to two rigs being in the shipyard a significant portion of the Current Quarter for special surveys and the Hercules 265 being out of service.

International Offshore. Revenue for our International Offshore segment increased due to the following:

- \$20.7 million increase from Hercules Triumph primarily due to the rig commencing work in November 2013;
- \$12.9 million increase from Hercules 266 as the rig commenced work in April 2013;
- \$9.7 million increase from Hercules 267 as the rig commenced work in November 2013; and
- \$5.7 million increase from Hercules Resilience primarily due to the rig commencing work in February 2014;

International Liftboats. The decrease in revenue from our International Liftboats segment resulted largely from a decrease in utilization of the majority of our vessels in West Africa. This decrease was partially offset by a \$5.2 million increase from the Bull Ray, which was purchased in March 2013.

Operating Expenses

Consolidated. The increase in consolidated operating expenses is described below.

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Domestic Offshore. The increase in operating expenses for our Domestic Offshore segment is primarily due to the following:

- \$2.9 million increase in labor costs in the Current Quarter as compared to the Comparable Quarter;
- \$2.9 million increase to state sales and use taxes in the Current Quarter;
- \$1.5 million of asset sale gains in the Comparable Quarter; and
- \$3.3 million increase due to the reactivation of Hercules 209 in May 2013.

International Offshore. The increase in operating expenses for our International Offshore segment is primarily due to the following:

- \$6.9 million increase from Hercules Triumph primarily due to the rig commencing operations in November 2013;
- \$7.0 million increase from Hercules 267 as it commenced work in November 2013;
- \$4.5 million increase from Hercules 266 as the rig began working in April 2013;
- \$3.7 million increase from Hercules Resilience primarily due to the rig commencing operations in February 2014; and
- \$5.4 million decrease from Hercules 260 in the Current Quarter as compared to the Comparable Quarter primarily due to repair costs in the Comparable Quarter related to the rig's spud can damage.

International Liftboats. The decrease in operating expenses for our International Liftboats segment is primarily due to the \$2.6 million write down of a cold stacked vessel in West Africa to fair market value in the Comparable Quarter.

Depreciation and Amortization

The increase in depreciation and amortization is largely due to the additional depreciation for the Hercules 266, Hercules Triumph, Hercules 267 and other capital projects, which contributed to increases of \$2.7 million, \$2.0 million, \$1.6 million and \$4.1 million, respectively. These increases are partially offset by a reduction in depreciation of \$3.4 million due to rigs impaired in 2013.

Interest Expense

The increase in interest expense for the Current Quarter is primarily due to \$8.7 million in interest on our 8.75% Senior Notes due 2021 which were issued in July 2013, partially offset by a \$2.4 million reduction in interest expense associated with the redemption of our 10.5% Senior Notes and refinancing these notes with the issuance of our 7.5% Senior Notes in the fourth quarter of 2013. Additionally, we redeemed a portion of our 3.375% Convertible Senior Notes in the second quarter of 2013 which contributed to a \$1.3 million reduction in interest expense in the Current Quarter as compared to the Comparable Quarter.

Loss on Extinguishment of Debt

During the Current Quarter, we redeemed \$220.1 million aggregate principal amount of our 7.125% Senior Secured Notes and expensed \$12.6 million for the call premium and wrote off \$1.4 million in unamortized debt issuance costs associated with these notes. In addition, we expensed \$1.1 million in bank fees related to the issuance of the 6.75% Senior Notes.

Income Tax Benefit

During the Current Quarter we generated an income tax benefit from continuing operations of \$0.2 million compared to \$39.0 million in the Comparable Quarter. The change is primarily related to the \$37.7 million tax benefit recorded in the Comparable Quarter related to the tax attributes received from the Seahawk Transaction. Additionally, the variation is due to the tax effect of the mix of earnings (losses) from different jurisdictions partially offset by the impact of discrete items.

Discontinued Operations

We had a loss from our former Inland and Domestic Liftboat operations of \$4.4 million, net of taxes, and \$0.7 million, net of taxes, respectively, in the comparable quarter. The sale of the Inland assets and domestic liftboats assets was completed in the third quarter of 2013.

Non-GAAP Financial Measures

Regulation G, General Rules Regarding Disclosure of Non-GAAP Financial Measures and other SEC regulations define and prescribe the conditions for use of certain Non-Generally Accepted Accounting Principles ("Non-GAAP") financial measures. We use various Non-GAAP financial measures such as adjusted operating income, adjusted income from continuing operations, adjusted diluted earnings per share from continuing operations, EBITDA and Adjusted EBITDA. EBITDA is defined as net income plus interest expense, income taxes, depreciation and

amortization. We believe that in addition to GAAP based financial information, Non-GAAP amounts are meaningful disclosures for the following reasons: i) each are components of the measures used by our board of directors and management team to evaluate and analyze our operating performance and

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historical trends, ii) each are components of the measures used by our management team to make day-to-day operating decisions, iii) under certain scenarios the Credit Agreement requires us to maintain compliance with a maximum secured leverage ratio, which contains Non-GAAP adjustments as components, iv) each are components of the measures used by our management to facilitate internal comparisons to competitors' results and the shallow-water drilling and marine services industry in general, v) results excluding certain costs and expenses provide useful information for the understanding of the ongoing operations without the impact of significant special items, and vi) the payment of certain bonuses to members of our management is contingent upon, among other things, the satisfaction by the Company of financial targets, which may contain Non-GAAP measures as components. We acknowledge that there are limitations when using Non-GAAP measures. The measures below are not recognized terms under GAAP and do not purport to be an alternative to net income as a measure of operating performance or to cash flows from operating activities as a measure of liquidity. EBITDA and Adjusted EBITDA are not intended to be a measure of free cash flow for management's discretionary use, as it does not consider certain cash requirements such as tax payments and debt service requirements. Because all companies do not use identical calculations, the amounts below may not be comparable to other similarly titled measures of other companies.

The following tables present a reconciliation of the GAAP financial measures to the corresponding adjusted financial measures (in thousands, except per share amounts):

	Three Months Ended March 31,	
	2014	2013
Income from Continuing Operations	\$19,916	\$40,298
Adjustments:		
Loss on extinguishment of debt	15,158	—
Tax benefit (a)	—	(37,729)
Total adjustments	15,158	(37,729)
Adjusted Income from Continuing Operations	\$35,074	\$2,569
Diluted Earnings per Share from Continuing Operations	\$0.12	\$0.25
Adjustments:		
Loss on extinguishment of debt	0.10	—
Tax benefit (a)	—	(0.23)
Total adjustments	0.10	(0.23)
Adjusted Diluted Earnings per Share from Continuing Operations	\$0.22	\$0.02
Income from Continuing Operations	\$19,916	\$40,298
Interest expense	22,901	17,095
Income tax benefit	(153)	(39,010)
Depreciation and amortization	40,083	34,938
EBITDA	82,747	53,321
Adjustments:		
Loss on extinguishment of debt	15,158	—
Total adjustments	15,158	—
Adjusted EBITDA	\$97,905	\$53,321

(a) Tax benefit recognized of \$37.7 million related to the change in characterization of the Seahawk acquisition for tax purposes from a purchase of assets to a reorganization.

CRITICAL ACCOUNTING POLICIES

We believe that our more critical accounting policies include those related to property and equipment, revenue recognition, income taxes, stock-based compensation and accrued self-insurance reserves. Inherent in such policies are certain key assumptions and estimates. For additional information regarding our critical accounting policies, please read "Management's Discussion and Analysis of Financial Condition and Results of Operations - Critical Accounting

Policies” in Item 7 of our Annual Report on Form 10-K for the year ended December 31, 2013.

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OUTLOOK

Offshore

Demand for our oilfield services is driven by our exploration and production customers' capital spending, which can experience significant fluctuations depending on current commodity prices and their expectations of future price levels, among other factors.

Drilling activity levels in the shallow-water U.S. Gulf of Mexico are dependent on crude oil and natural gas prices, prospectivity of hydrocarbons, capital budgets of our customers as well as their ability to obtain necessary drilling permits to operate in the region. Although natural gas has historically accounted for a greater percentage of hydrocarbon production in the U.S. Gulf of Mexico, our domestic offshore customers are now largely focused on drilling activities that contain higher concentrations of crude oil and condensates. We expect this condition to persist, given the disparity between the price of crude oil and natural gas.

The supply of marketed jackup rigs in the U.S. Gulf of Mexico has declined significantly since the financial crisis starting in 2008 and again with the imposition of new regulations during 2010. Drilling contractors have elected to cold stack, or no longer actively market, a number of rigs in the region, and in other instances have mobilized rigs out of the U.S. Gulf of Mexico. As a result, the number of existing, actively marketed jackup rigs in the U.S. Gulf of Mexico, has declined from approximately 63 rigs in late 2008 to 37 rigs as of April 21, 2014, of which we estimate that 32 rigs are contracted.

Discussions with our domestic customers suggest an extensive inventory of oil and liquids rich directed drilling opportunities exists in the U.S. Gulf of Mexico Shelf. Relatively high crude oil prices and our customers' emphasis on drilling oil and liquids rich prospects could support a relatively stable base of jackup rig demand over the long term. Tempering this long term demand outlook for oil drilling is the market expectation for a prolonged period of low natural gas prices. Although natural gas prices have improved over the past six months, customer discussions do not currently indicate incremental demand for gas-directed drilling activity. In addition, slower contracting activity since late 2013 has led to a decline in Domestic Offshore backlog. Over the next several years, we estimate approximately 17 jackup rigs owned by international drilling contractors working in Mexico are scheduled to end their current contracts with PEMEX. It is uncertain whether PEMEX will re-contract these rigs, and if not, where these rigs will migrate to. With regard to our cost structure, we expect to experience some inflationary pressures, particularly in labor, as strong drilling activity worldwide has led to a tightening of skilled labor across the oilfield service industry. Demand for rigs in our International Offshore segment is primarily dependent on crude oil prices. Relatively high crude oil prices and capital budget announcements by National and International Oil Companies, leads us to believe that international capital spending and demand for jackup rigs overseas will increase in 2014. Our expectation for greater international rig demand is tempered by the anticipated growth in supply from newly constructed rigs. As of April 21, 2014, there were approximately 447 existing, actively marketed jackup rigs outside of the U.S. Gulf of Mexico, excluding cold stacked rigs, of which only 19 rigs were uncontracted. In addition, globally, there are an estimated 144 new jackup rigs either under construction, on order, or planned for delivery from 2014 to 2017, of which 127 are without contracts. With the exception of the rigs we acquired from Discovery, all of the jackup rigs under construction have higher specifications than the rigs in our existing fleet.

Demand for rigs of similar class to the rigs acquired from Discovery, and the premium dayrates that such rigs historically command, is dependent on the need by oil and gas companies to utilize high specification and harsh environment ("HS/HE") jackup rigs with capabilities that exceed many of the standard rigs currently in existence, and availability of these HS/HE rigs. We believe that demand for HS/HE jackup rigs has grown, driven by harsher environmental conditions, greater well depths and increased complexities of the offshore wells drilled by oil and gas companies. We expect this trend to continue through the foreseeable future, as oil and gas companies further expand their exploration efforts into frontier areas that are often characterized by these greater challenges. Tempering our near term expectations for HS/HE jackup rig demand is the growth in new rig supply that is previously referenced, several of which are competitive with the rigs acquired from Discovery.

Liftboats

Demand for liftboats is typically a function of our customers' demand for offshore infrastructure construction, inspection and maintenance, well maintenance, well plugging and abandonment, and other related activities. Although

activity levels for liftboats are not as closely correlated to commodity prices as our drilling segments, commodity prices are still a key driver of liftboat demand. Demand for liftboat services in West Africa was fairly weak in the beginning months of 2014 and we could see continued volatility in utilization through the rest of the year.

Additionally, expected mobilization of additional vessels to the region could potentially impact the utilization and pricing for our liftboat fleet. Utilization can and has been negatively impacted by local labor disputes and regional conflicts, particularly in West Africa. In the Middle East, we expect healthy multi-year demand for liftboats to support increases in construction and well servicing activity levels.

Over the long term, we believe that international liftboat demand will benefit from: (i) the aging offshore infrastructure

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and maturing offshore basins, (ii) desire by our international customers to economically produce from these mature basins and service their infrastructure and (iii) the cost advantages of liftboats to perform these services relative to alternatives. Tempering this demand outlook is (i) our expectation of increased competition from newly constructed liftboats and mobilizations of existing liftboats primarily from the U.S. Gulf of Mexico to international markets, (ii) the risk of recurring political, social and union unrest, principally in West Africa and (iii) increased pressure to have local ownership of assets, principally in Nigeria.

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LIQUIDITY AND CAPITAL RESOURCES

Sources and Uses of Cash

Sources and uses of cash for the three months ended March 31, 2014 are as follows (in millions):

Net Cash Provided by Operating Activities	\$40.6	
Net Cash Provided by (Used in) Investing Activities:		
Capital Expenditures	(40.7)
Proceeds from Sale of Assets, Net	1.7	
Total	(39.0)
Net Cash Provided by (Used in) Financing Activities:		
Long-term Debt Borrowings	300.0	
Redemption of 7.125% Senior Secured Notes	(220.1)
Cash Designated for Debt Retirement	(79.9)
Payment of Debt Issuance Costs	(2.9)
Other	0.1	
Total	(2.8)
Net Decrease in Cash and Cash Equivalents	\$(1.2)

Sources of Liquidity and Financing Arrangements

Our liquidity is comprised of cash on hand, cash from operations and availability under our revolving credit facility. We also maintain a shelf registration statement covering the future issuance from time to time of various types of securities, including debt and equity securities. Additional debt issuances are subject to certain restrictions in our Credit Agreement and indentures. We currently believe we will have adequate liquidity to fund our operations. However, to the extent we do not generate sufficient cash from operations we may need to raise additional funds through debt, equity offerings or the sale of assets. Furthermore, we may need to raise additional funds through debt or equity offerings or asset sales to refinance existing debt, to fund capital expenditures or for general corporate purposes.

Cash Requirements and Contractual Obligations

Our current debt structure is used to fund our business operations.

Senior Secured Credit Agreement

On April 3, 2012 we entered into a credit agreement which as amended on July 8, 2013 (the "Credit Agreement") governs our senior secured revolving credit facility (the "Credit Facility"). The Credit Agreement provides for a \$150.0 million senior secured revolving credit facility. As of March 31, 2014, no amounts were outstanding and \$10.5 million in letters of credit had been issued under the Credit Facility, therefore, the remaining availability under this facility was \$139.5 million. During any period of time that outstanding letters of credit under the Credit Facility exceed \$10 million or there are any revolving borrowings outstanding under the Credit Facility, we will have to maintain compliance with a maximum secured leverage ratio (as defined in the Credit Agreement, being generally computed as the ratio of secured indebtedness to consolidated cash flow). The maximum secured leverage ratio is 3.50 to 1.00. As of March 31, 2014, we were in compliance with all covenants under our revolving credit facility.

Our obligations under the Credit Agreement are guaranteed by substantially all of our current domestic subsidiaries (collectively, the "Guarantors"), and the obligations of the Company and the Guarantors are secured by liens on substantially all of the vessels owned by the Company and the Guarantors, together with certain accounts receivable, equity of subsidiaries, equipment and other assets.

6.75% Senior Notes

On March 26, 2014, we completed the issuance and sale of \$300.0 million aggregate principal amount of senior notes at a coupon rate of 6.75% ("6.75% Senior Notes") with maturity in April 2022. These notes were sold at par and we received net proceeds from the offering of the notes of approximately \$294.8 million after deducting bank fees and estimated offering expenses. Interest on the notes will accrue from and including March 26, 2014 at a rate of 6.75% per year and is payable semi-annually in arrears on April 1 and October 1 of each year, beginning October 1, 2014. These notes are guaranteed by each of the Guarantors that guarantee our obligations under our Credit Agreement.

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Prior to April 1, 2017, we may redeem the notes with the net cash proceeds of certain equity offerings, at a redemption price equal to 106.75% of the aggregate principal amount plus accrued and unpaid interest; provided, that (i) after giving effect to any such redemptions, at least 65% of the notes originally issued would remain outstanding immediately after such redemption and (ii) we make such redemption not more than 180 days after consummation of such equity offering. In addition, prior to April 1, 2017, we may redeem all or part of the notes at a price equal to 100% of the aggregate principal amount of the notes to be redeemed, plus the applicable premium, as defined in the indenture, and accrued and unpaid interest.

On or after April 1, 2017, we may redeem all or part of the notes at the redemption prices set forth below, together with accrued and unpaid interest, if any, to the redemption date, if redeemed during the 12-month period beginning April 1 of the years indicated:

Year	Optional Redemption Price	
2017	105.063	%
2018	103.375	%
2019	101.688	%
2020 and thereafter	100.000	%

If we experience certain kinds of changes of control, holders of the notes will be entitled to require us to purchase all or any portion of the notes for a cash price equal to 101.0% of the principal amount of the applicable notes, plus accrued and unpaid interest, if any, to the date of purchase. Furthermore, in certain circumstances following an asset sale (as defined in the indenture), we may be required to use the excess proceeds to offer to repurchase the notes at an offer price in cash equal to 100% of their principal amount, plus accrued and unpaid interest.

Retirement of 7.125% Senior Secured Notes

In 2012, we issued \$300.0 million of senior secured notes at a coupon rate of 7.125% ("7.125% Senior Secured Notes") with maturity in April 2017. On March 12, 2014, we commenced a cash tender offer (the "Tender offer") for any and all of the \$300.0 million outstanding aggregate principal amount of our 7.125% Senior Secured Notes. Senior secured notes totaling approximately \$220.1 million were settled on March 26, 2014 for \$232.7 million using a portion of the proceeds from the issuance of the 6.75% Senior Notes. Liens securing our obligations and certain other restrictions under the 7.125% Senior Secured Notes were released pursuant to the supplemental indenture which became effective on March 26, 2014. We expect to use the remaining net proceeds from the 6.75% Senior Notes offering, together with cash on hand, to complete the redemption of the remaining \$79.9 million aggregate principal amount of the 7.125% Senior Secured Notes on April 29, 2014 for approximately \$84.2 million. As such, we have classified approximately \$79.9 million of our cash on hand as Cash Designated for Debt Retirement on the Balance Sheet as of March 31, 2014.

Other Indenture Provisions

The Credit Agreement as well as the indentures governing the 8.75% Senior Notes, 7.5% Senior Notes, 6.75% Senior Notes, 7.125% Senior Secured Notes, 10.25% Senior Notes and 3.375% Convertible Senior Notes contain customary events of default. In addition, the Credit Agreement as well as the indentures governing the 8.75% Senior Notes, 7.5% Senior Notes, 6.75% Senior Notes, 10.25% Senior Notes and 3.375% Convertible Senior Notes also contain a provision under which an event of default by the Company or by any restricted subsidiary on any other indebtedness exceeding \$25.0 million would be considered an event of default under the Credit Agreement and indentures if such default: a) is caused by failure to pay the principal at final maturity, or b) results in the acceleration of such indebtedness prior to maturity.

The Credit Agreement as well as the indentures governing the 8.75% Senior Notes, 7.5% Senior Notes, 6.75% Senior Notes, and 10.25% Senior Notes contain covenants that, among other things, limit our ability and the ability of our restricted subsidiaries to:

- incur additional indebtedness or issue certain preferred stock;
- pay dividends or make other distributions;
- make other restricted payments or investments;
- sell assets;

- create liens;
- enter into agreements that restrict dividends and other payments by restricted subsidiaries;
- engage in transactions with affiliates; and
- consolidate, merge or transfer all or substantially all of our assets.

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Substantially all of our domestic subsidiaries guarantee the obligations under the Credit Agreement, the 8.75% Senior Notes, 7.5% Senior Notes, 6.75% Senior Notes, 7.125% Senior Secured Notes and 10.25% Senior Notes.

Loss on Extinguishment of Debt

During the three months ended March 31, 2014, we incurred the following charges which are included in Loss on Extinguishment of Debt in the Consolidated Statement of Operations:

In March 2014, we incurred a pretax charge of \$15.2 million, \$15.2 million net of tax, consisting of a \$12.6 million call premium and \$1.4 million of unamortized debt issuance costs related to the redemption of the 7.125% Senior Secured Notes, as well as \$1.1 million of bank fees related to the issuance of the 6.75% Senior Notes.

Insurance and Indemnity

We maintain insurance coverage that includes coverage for physical damage, third party liability, workers' compensation and employer's liability, general liability, vessel pollution and other coverages.

Effective May 1, 2013, we completed the annual renewal of all of our key insurance policies. Our primary marine package provides for hull and machinery coverage for substantially all of our rigs and liftboats up to a scheduled value of each asset. The total maximum amount of coverage for these assets is \$1.7 billion. The marine package includes protection and indemnity and maritime employer's liability coverage for marine crew personal injury and death and certain operational liabilities, with primary coverage (or self-insured retention for maritime employer's liability coverage) of \$5.0 million per occurrence with excess liability coverage up to \$200.0 million. The marine package policy also includes coverage for personal injury and death of third parties with primary and excess coverage of \$25.0 million per occurrence with additional excess liability coverage up to \$200.0 million, subject to a \$250,000 per-occurrence deductible. The marine package also provides coverage for cargo and charterer's legal liability. The marine package includes limitations for coverage for losses caused in U.S. Gulf of Mexico named windstorms, including an annual aggregate limit of liability of \$75.0 million for property damage and removal of wreck liability coverage. We also procured an additional \$75.0 million excess policy for removal of wreck and certain third-party liabilities incurred in U.S. Gulf of Mexico named windstorms. Deductibles for events that are not caused by a U.S. Gulf of Mexico named windstorm are 12.5% of the insured drilling rig values per occurrence, subject to a minimum of \$1.0 million, and \$1.0 million per occurrence for liftboats. The deductible for drilling rigs in a U.S. Gulf of Mexico named windstorm event is \$25.0 million. Vessel pollution is covered under a Water Quality Insurance Syndicate policy ("WQIS Policy") providing limits as required by applicable law, including the Oil Pollution Act of 1990. The WQIS Policy covers pollution emanating from our vessels and drilling rigs, with primary limits of \$5.0 million (inclusive of a \$3.0 million per-occurrence deductible) and excess liability coverage up to \$200.0 million.

Control-of-well events generally include an unintended flow from the well that cannot be contained by equipment on site (e.g., a blow-out preventer), by increasing the weight of the drilling fluid, or that does not naturally close itself off through what is typically described as "bridging over". We carry a contractor's extra expense policy with \$25.0 million primary liability coverage for well control costs, pollution and expenses incurred to redrill wild or lost wells, with excess liability coverage up to \$200.0 million for pollution liability that is covered in the primary policy. The policies are subject to exclusions, limitations, deductibles, self-insured retention and other conditions. In addition to the marine package, we have separate policies providing coverage for onshore foreign and domestic general liability, employer's liability, auto liability and non-owned aircraft liability, with customary deductibles and coverage.

Our drilling contracts provide for varying levels of indemnification from our customers and in most cases, may require us to indemnify our customers for certain liabilities. Under our drilling contracts, liability with respect to personnel and property is customarily assigned on a "knock-for-knock" basis, which means that we and our customers assume liability for our respective personnel and property, regardless of how the loss or damage to the personnel and property may be caused, and even if we are grossly negligent. However, since the Macondo blowout and resulting litigation, some of our customers have been reluctant to extend their indemnity obligations in instances where we are grossly negligent. Our customers typically assume responsibility for and agree to indemnify us from any loss or liability resulting from pollution or contamination, including clean-up and removal and third-party damages arising from operations under the contract and originating below the surface of the water, including as a result of blowouts or cratering of the well ("Blowout Liability"). The customer's assumption for Blowout Liability may, in certain circumstances, be contractually limited or could be determined to be unenforceable in the event of our gross

negligence, willful misconduct or other egregious conduct. In addition, we may not be indemnified for statutory penalties and punitive damages relating to such pollution or contamination events. We generally indemnify the customer for the consequences of spills of industrial waste or other liquids originating solely above the surface of the water and emanating from our rigs or vessels.

We have separate primary marine packages for Hercules Triumph and Hercules Resilience that each provide hull and machinery coverage up to \$250.0 million, subject to a \$2.5 million per-occurrence deductible, which increases to \$5.0 million for losses incurred during delivery voyages. Each marine package also provides coverage for cargo, contractor's extra expense and loss of hire coverage. We also have operational protection and indemnity coverage up to \$500.0 million per rig, subject to a

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\$50,000 per-occurrence deductible for claims originating outside the U.S. and a \$250,000 per-occurrence deductible for claims originating in the U.S. Additionally, we have coverage for extended contractual liability that includes subsea activities, property and personnel, and clean-up costs up to \$25.0 million per rig and pollution-by-blowout coverage up to \$10.0 million per rig, all subject to certain contractual assumptions and limitations. We do not have coverage inclusive of U.S. Gulf of Mexico named windstorms for the Hercules Triumph and Hercules Resilience. We are self-insured for the deductible portion of our insurance coverage. Management believes adequate accruals have been made on known and estimated exposures up to the deductible portion of our insurance coverage. Management believes that claims and liabilities in excess of the amounts accrued are adequately insured. However, our insurance is subject to exclusions and limitations, and there is no assurance that such coverage will adequately protect us against liability from all potential consequences. In addition, there is no assurance of renewal or the ability to obtain coverage acceptable to us.

In 2013, in connection with the renewal of certain of our insurance policies, we entered into an agreement to finance a portion of our annual insurance premiums. Approximately \$30.7 million was financed through this arrangement with an interest rate of 3.24%. Additionally, \$1.3 million of insurance premiums for the Hercules Triumph were financed at an interest rate of 3.24%. There was \$9.6 million outstanding in insurance notes payable at December 31, 2013 which were fully paid by their maturity date of March 2014.

Hercules 265 Incident and Settlement of Property Damage Insurance Claim

In July 2013, our jackup drilling rig Hercules 265, a 250' mat-supported cantilevered unit operating in the U.S. Gulf of Mexico Outer Continental Shelf lease block South Timbalier 220, experienced a well control incident. The rig sustained substantial damage in the incident and our insurance underwriters determined that the rig was a constructive total loss. The cause of the incident is unknown but is under investigation. We also have removal of wreck coverage up to a total amount of \$110.0 million. In the event any pollution emanated from our rig or equipment as a result of the incident, our vessel pollution policy provides coverage, subject to deductibles and limitations. We and our insurance underwriters continue to negotiate the insurance recovery amounts for costs related to the salvage of the rig and certain other insured losses.

Capital Expenditures

We currently expect total capital expenditures during the remainder of 2014 to approximate \$85 million to \$100 million. Planned capital expenditures include items related to general maintenance, regulatory, refurbishment, upgrades and contract specific modifications to our rigs and liftboats. Changes in timing of certain planned capital expenditure projects may result in a shift of spending levels beyond 2014.

From time to time, we may review possible acquisitions of rigs, liftboats or businesses, joint ventures, mergers or other business combinations, and we may have outstanding from time to time bids to acquire certain assets from other companies. We may not, however, be successful in our acquisition efforts. If we acquire additional assets, we would expect that our ongoing capital expenditures as a whole would increase in order to maintain our equipment in a competitive condition.

Our ability to fund capital expenditures would be adversely affected if conditions deteriorate in our business.

Contractual Obligations

Our contractual obligations and commitments principally include obligations associated with our outstanding indebtedness, certain income tax liabilities, bank guarantees, letters of credit, future minimum operating lease obligations, purchase commitments and management compensation obligations. Except for the following, during the first three months of 2014, there were no material changes outside the ordinary course of business in the specified contractual obligations.

- Settled \$9.6 million of insurance notes payable outstanding at December 31, 2013;
- Retired \$220.1 million aggregate principal amount of the 7.125% Senior Secured Notes and expect to retire the remaining \$79.9 million aggregate principal amount of these notes in the second quarter of 2014 (See Item 2. "Management's Discussion and Analysis of Financial Condition and Results of Operations-Liquidity and Capital Resources-Cash Requirements and Contractual Obligations") and
- Issued \$300.0 million aggregate principal amount of 6.75% Senior Notes due 2022 (See Item 2. "Management's Discussion and Analysis of Financial Condition and Results of Operations-Liquidity and Capital Resources-Cash

Requirements and Contractual Obligations").

For additional information about our contractual obligations as of December 31, 2013, see "Management's Discussion and Analysis of Financial Condition and Results of Operations-Liquidity and Capital Resources-Contractual Obligations" in Item 7 of our Annual Report on Form 10-K for the year ended December 31, 2013.

Accounting Pronouncements

See Note 12 to our condensed consolidated financial statements included elsewhere in this report.

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FORWARD-LOOKING STATEMENTS

This Quarterly Report on Form 10-Q includes “forward-looking statements” within the meaning of Section 27A of the Securities Act of 1933, as amended (“the Securities Act”), and Section 21E of the Exchange Act that are applicable to us and our business. All statements, other than statements of historical fact, included in this quarterly report, including statements that address outlook, activities, events or developments that we intend, contemplate, estimate, expect, project, believe or anticipate will or may occur in the future are forward-looking statements. These include such matters as:

- our levels of indebtedness, covenant compliance and access to capital under current market conditions;
 - our ability to enter into new contracts for our rigs and liftboats, including our two ultra-high specification rigs, and future utilization rates and dayrates for the units;
 - our ability to renew or extend our contracts, or enter into new contracts, when such contracts expire;
 - demand for our rigs and our liftboats;
 - activity levels of our customers and their expectations of future energy prices and ability to obtain drilling permits in an efficient manner or at all;
 - sufficiency and availability of funds for required capital expenditures, working capital and debt service;
 - our ability to close the sale and purchase of assets on time;
 - expected completion times for our repair, refurbishment and upgrade projects;
 - our ability to complete our shipyard projects incident free;
 - our ability to complete our shipyard projects on time to avoid cost overruns and contract penalties;
 - our ability to effectively reactivate rigs that we have stacked;
 - the timing and cost of shipyard projects and refurbishments and the return of idle rigs to work;
 - our plans to increase international operations;
 - expected useful lives of our rigs and liftboats;
 - future capital expenditures and refurbishment, reactivation, transportation, repair and upgrade costs;
 - liabilities and restrictions under applicable laws of the jurisdictions in which we operate and regulations protecting the environment;
 - expected outcomes of litigation, investigations, claims, disputes and tax audits and their expected effects on our financial condition and results of operations;
 - the existence of insurance coverage and the extent of recovery from our insurance underwriters for claims made under our insurance policies; and
 - expectations regarding offshore drilling and liftboat activity and dayrates, market conditions, demand for our rigs and liftboats, operating revenue, operating and maintenance expense, insurance coverage, insurance expense and deductibles, interest expense, debt levels and other matters with regard to outlook and future earnings.
- We have based these statements on our assumptions and analyses in light of our experience and perception of historical trends, current conditions, expected future developments and other factors we believe are appropriate in the circumstances. Forward-looking statements by their nature involve substantial risks and uncertainties that could significantly affect expected results, and actual future results could differ materially from those described in such statements. Although it is not possible to identify all factors, we continue to face many risks and uncertainties. Among the factors that could cause actual future results to differ materially are the risks and uncertainties described under “Risk Factors” in Item 1A of our Annual Report on Form 10-K for the year ended December 31, 2013 and Item 1A of Part II of this quarterly report and the following:
- oil and natural gas prices and industry expectations about future prices;
 - levels of oil and gas exploration and production spending;
 - demand for and supply of offshore drilling rigs and liftboats;
 - our ability to enter into and the terms of future contracts;
 - the adequacy and costs of sources of credit and liquidity;
 - our ability to collect receivables due from our customers;
 -

the worldwide military and political environment, uncertainty or instability resulting from an escalation or additional outbreak of armed hostilities or other crises in the Middle East, North Africa, West Africa, Asia, Eastern Europe and other oil and natural gas producing regions or acts of terrorism or piracy;
the ability of our customers in the U.S. Gulf of Mexico to obtain drilling permits in an efficient manner or at all;

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the impact of governmental laws and regulations, including laws and regulations in the U.S. Gulf of Mexico following the Macondo well incident;

- our ability to obtain in a timely manner visas and work permits for our employees working in international jurisdictions, particularly in Angola;

the impact of local content and cabotage laws and regulations in international jurisdictions in which we operate, particularly Nigeria;

the impact of tax laws, regulations, interpretations and audits in jurisdictions where we conduct business;

uncertainties relating to the level of activity in offshore oil and natural gas exploration, development and production;

competition and market conditions in the contract drilling and liftboat industries;

the availability of skilled personnel and the rising cost of labor;

labor relations and work stoppages, particularly in the Nigerian labor environment;

operating hazards such as hurricanes, severe weather and seas, fires, cratering, blowouts and other well control

incidents, war, terrorism and cancellation or unavailability of insurance coverage or insufficient insurance coverage;

the enforceability and interpretations of indemnity and liability provisions contained in our drilling contracts, particularly in the U.S. Gulf of Mexico;

the effect of litigation, investigations, audits and contingencies; and

our inability to achieve our plans or carry out our strategy.

Many of these factors are beyond our ability to control or predict. Any of these factors, or a combination of these factors, could materially affect our future financial condition or results of operations and the ultimate accuracy of the forward-looking statements. These forward-looking statements are not guarantees of our future performance, and our actual results and future developments may differ materially from those projected in the forward-looking statements. Management cautions against putting undue reliance on forward-looking statements or projecting any future results based on such statements or present or prior earnings levels. In addition, each forward-looking statement speaks only as of the date of the particular statement, and we undertake no obligation to publicly update or revise any forward-looking statements except as required by applicable law.

ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

We believe our exposure to market risk has not changed materially from that disclosed in our Annual Report on Form 10-K for the year ended December 31, 2013. For quantitative and qualitative disclosures about market risk, see Item 7A, "Quantitative and Qualitative Disclosures About Market Risk", of such report.

ITEM 4. CONTROLS AND PROCEDURES

Evaluation of Disclosure Controls and Procedures

Our management, with the participation of our chief executive officer and our chief financial officer, evaluated the effectiveness of our disclosure controls and procedures as of the end of the period covered by this report. Our chief executive officer and chief financial officer evaluated whether our disclosure controls and procedures as of the end of the period covered by this report were designed to ensure that information required to be disclosed by us in the reports that we file or submit under the Securities Exchange Act of 1934 is (1) recorded, processed, summarized and reported within the time periods specified in the SEC's rules and forms and (2) accumulated and communicated to our management, including our chief executive officer and our chief financial officer, as appropriate to allow timely decisions regarding required disclosure. Based on their evaluation, our chief executive officer and chief financial officer concluded that our disclosure controls and procedures were effective to achieve the foregoing objectives as of the end of the period covered by this report.

There were no changes in our internal control over financial reporting that occurred during the most recent fiscal quarter that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

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PART II. OTHER INFORMATION

ITEM 1. LEGAL PROCEEDINGS

The information set forth under the caption "Legal Proceedings" in Note 11 of the Notes to the Unaudited Consolidated Financial Statements in Item 1 of Part 1 of this report is incorporated by reference in response to this item.

ITEM 1A. RISK FACTORS

For additional information about our risk factors, see Item 1A of our Annual Report on Form 10-K for the year ended December 31, 2013.

ITEM 2. UNREGISTERED SALES OF EQUITY SECURITIES AND USE OF PROCEEDS

The following table sets forth for the periods indicated certain information with respect to our purchases of our common stock:

Period	Total Number of Shares Purchased (1)	Average Price Paid per Share	Total Number of Shares Purchased as Part of a Publicly Announced Plan (2)	Maximum Number of Shares That May Yet Be Purchased Under the Plan (2)
January 1-31, 2014	218	\$5.80	N/A	N/A
February 1-28, 2014	225,808	4.74	N/A	N/A
March 1-31, 2014	99,419	4.82	N/A	N/A
Total	325,445	4.77	N/A	N/A

(1) Represents the surrender of shares of our common stock to satisfy tax withholding obligations in connection with the vesting of restricted stock issued to employees under our stockholder-approved long-term incentive plan.

(2) We did not have at any time during the quarter, and currently do not have, a share repurchase program in place.

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ITEM 6. EXHIBITS

- 4.1 — First Supplemental Indenture dated as of March 26, 2014 to Indenture dated as of April 3, 2012, by and among Hercules Offshore, Inc., the Guarantors named therein and U.S. Bank National Association as Trustee (incorporated by reference to Exhibit 4.1 to the Current Report on Form 8-K filed March 31, 2014 (the "March 2014 8-K")).
- 4.2 — Indenture dated as of March 26, 2014, by and among Hercules Offshore, Inc., the Guarantors named therein and U.S. Bank National Association as Trustee (incorporated by reference to Exhibit 4.2 to the March 2014 8-K).
- 4.3 — Form of 6.750% Senior Note Due 2022 (included as Exhibit A to Exhibit 4.2 of the March 2014 8-K). Purchase Agreement, dated March 12, 2014, by and among Hercules Offshore, Inc., the guarantors party thereto, Deutsche Bank Securities Inc., Credit Suisse Securities (USA) LLC, Goldman, Sachs & Co., UBS Securities LLC and Capital One Securities, Inc., as representatives of the initial purchasers named in Schedule I thereto (incorporated by reference to Exhibit 10.1 to the Current Report on Form 8-K filed March 18, 2014).
- 10.1 —
- *10.2 — Form of 2014 Phantom Stock Agreement and Cash Award Agreement for Chief Executive Officer.
- *10.3 — Form of 2014 Phantom Stock Agreement for Employees.
- *31.1 — Certification of Chief Executive Officer of Hercules pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
- *31.2 — Certification of Chief Financial Officer of Hercules pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
- *32.1 — Certification of the Chief Executive Officer and the Chief Financial Officer of Hercules pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
- *101.INS — XBRL Instance Document
- *101.SCH — XBRL Schema Document
- *101.CAL — XBRL Calculation Linkbase Document
- *101.DEF — XBRL Definition Linkbase Document
- *101.LAB — XBRL Label Linkbase Document
- *101.PRE — XBRL Presentation Linkbase Document

* Filed herewith.

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SIGNATURES

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

HERCULES OFFSHORE, INC.

By: /S/ John T. Rynd
John T. Rynd
Chief Executive Officer and President
(Principal Executive Officer)

By: /S/ Stephen M. Butz
Stephen M. Butz
Executive Vice President and Chief Financial Officer
(Principal Financial Officer)

By: /S/ Troy L. Carson
Troy L. Carson
Senior Vice President and Chief Accounting Officer
(Principal Accounting Officer)

Date: April 23, 2014