HELIX ENERGY SOLUTIONS GROUP INC
Form 10-Q
July 30, 2010

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549

Form 10-Q

[X] Quarterly report pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934
For the quarterly period ended June 30, 2010

or

[ ] Transition report pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934
For the transition period from__________ to__________

Commission File Number 001-32936

HELIX ENERGY SOLUTIONS GROUP, INC.
(Exact name of registrant as specified in its charter)

Minnesota (State or other jurisdiction of incorporation or organization)	95–3409686 (I.R.S. Employer Identification No.)
400 North Sam Houston Parkway East Suite 400 Houston, Texas (Address of principal executive offices)	77060 (Zip Code)

(281) 618–0400
(Registrant's telephone number, including area code)

NOT APPLICABLE
(Former name, former address and former fiscal year, if changed since last report)

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or 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, or a non-accelerated filer. See definition of "accelerated filer and large accelerated filer" in Rule 12b-2 of the Exchange Act. (Check one):

Large accelerated filer	[√]	Accelerated filer	[ ]	Non-accelerated filer	[ ]

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).

Yes [ ] No [√]

As of July 27, 2010, 105,443,450 shares of common stock were outstanding.

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PART I. FINANCIAL INFORMATION
Item 1. Financial Statements.

HELIX ENERGY SOLUTIONS GROUP, INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATED BALANCE SHEETS
(in thousands)

	June 30, 2010 (Unaudited)	December 31, 2009
ASSETS		
Current assets:		
Cash and cash equivalents	$ 270,001	$ 270,673
Accounts receivable —		
Trade, net of allowance for uncollectible accounts of $419 and $5,172, respectively	175,240	145,519
Unbilled revenue	17,308	17,854
Costs in excess of billing	11,829	9,305
Other current assets	120,670	122,209
Total current assets	595,048	565,560
Property and equipment	4,454,976	4,352,109
Less — accumulated depreciation	(1,789,416)	(1,488,403)
	2,665,560	2,863,706
Other assets:		
Equity investments	187,694	189,411
Goodwill	76,134	78,643
Other assets, net	82,137	82,213
	$ 3,606,573	$ 3,779,533
LIABILITIES AND SHAREHOLDERS' EQUITY		
Current liabilities:		
Accounts payable	$ 163,975	$ 155,457
Accrued liabilities	202,154	200,607
Current maturities of long-term debt	11,396	12,424
Total current liabilities	377,525	368,488
Long-term debt	1,347,994	1,348,315
Deferred income taxes	383,652	442,607
Asset retirement obligations	165,799	182,399
Other long-term liabilities	5,109	4,262
Total liabilities	2,280,079	2,346,071
Convertible preferred stock	1,000	6,000
Commitments and contingencies		
Shareholders' equity:		
Common stock, no par, 240,000 shares authorized, 105,681and 104,281 shares issued, respectively	906,153	907,691
Retained earnings	416,365	519,807

Accumulated other comprehensive loss	(20,502)	(22,241)
Total controlling interest shareholders’ equity	1,302,016	1,405,257
Noncontrolling interests	23,478	22,205
Total equity	1,325,494	1,427,462
	$ 3,606,573	$ 3,779,533

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

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HELIX ENERGY SOLUTIONS GROUP, INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS (UNAUDITED)
(in thousands, except per share amounts)

	Three Months Ended June 30, 2010	Three Months Ended June 30, 2009
Net revenues:		
Contracting services	$ 196,676	$ 404,647
Oil and gas	102,586	89,992
	299,262	494,639
Cost of sales:		
Contracting services	140,126	312,502
Oil and gas	94,092	(16,692)
Oil and gas property impairments	159,862	63,073
	394,080	358,883
Gross profit (loss)	(94,818)	135,756
Gain on oil and gas derivative contracts	2,482	4,121
Gain (loss) on sale or acquisition of assets, net	(14)	1,319
Selling and administrative expenses	(24,546)	(39,372)
Income (loss) from operations	(116,896)	101,824
Equity in earnings of investments	1,656	6,264
Gain on sale of Cal Dive common stock	—	59,442
Net interest expense	(20,523)	(15,644)
Other income (expense)	(1,659)	8,176
Income (loss) before income taxes	(137,422)	160,062
Provision (benefit) for income taxes	(52,366)	56,809
Income (loss) from continuing operations	(85,056)	103,253
Discontinued operations, net of tax	(17)	9,836
Net income (loss), including noncontrolling interests	(85,073)	113,089
Less: net income applicable to noncontrolling interests….	(444)	(12,620)
Net income (loss) applicable to Helix	(85,517)	100,469
Preferred stock dividends	(34)	(250)
Net income (loss) applicable to Helix common shareholders	$ (85,551)	$ 100,219
Basic earnings (loss) per share of common stock:		
Continuing operations	$ (0.82)	$ 0.92
Discontinued operations	—	0.10
Net income (loss) per common share	$ (0.82)	$ 1.02
Diluted earnings (loss) per share of common stock:		
Continuing operations	$ (0.82)	$ 0.85
Discontinued operations	—	0.09
Net income (loss) per common share	$ (0.82)	$ 0.94

Weighted average common shares outstanding:		
Basic	104,125	96,936
Diluted	104,125	105,995

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

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HELIX ENERGY SOLUTIONS GROUP, INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS (UNAUDITED)
(in thousands, except per share amounts)

	Six Months Ended June 30, 2010	Six Months Ended June 30, 2009
Net revenues:		
Contracting services	$ 307,531	$ 815,441
Oil and gas	193,301	250,173
	500,832	1,065,614
Cost of sales:		
Contracting services	226,374	638,200
Oil and gas	172,446	67,375
Oil and gas property impairments	170,974	63,073
	569,794	768,648
Gross profit (loss)	(68,962)	296,966
Gain on oil and gas derivative contracts	2,482	78,730
Gain on sale or acquisition of assets, net	6,233	1,773
Selling and administrative expenses	(65,047)	(80,725)
Income (loss) from operations	(125,294)	296,744
Equity in earnings of investments	6,711	13,767
Gain on sale of Cal Dive common stock	—	59,442
Net interest expense	(36,158)	(37,611)
Other income (expense)	(7,217)	7,948
Income (loss) before income taxes	(161,958)	340,290
Provision (benefit) for income taxes	(59,927)	121,728
Income (loss) from continuing operations	(102,031)	218,562
Discontinued operations, net of tax	(44)	7,282
Net income (loss), including noncontrolling interests	(102,075)	225,844
Less: net income applicable to noncontrolling interests…	(1,273)	(18,173)
Net income (loss) applicable to Helix	(103,348)	207,671
Preferred stock dividends	(94)	(563)
Preferred stock beneficial conversion charges	—	(53,439)
Net income (loss) applicable to Helix common shareholders	$ (103,442)	$ 153,669
Basic earnings (loss) per share of common stock:		
Continuing operations	$ (1.00)	$ 1.50
Discontinued operations	—	0.08
Net income (loss) per common share	$ (1.00)	$ 1.58
Diluted earnings (loss) per share of common stock:		
Continuing operations	$ (1.00)	$ 1.37
Discontinued operations	—	0.07

Net income (loss) per common share	$ (1.00)	$ 1.44
Weighted average common shares outstanding:		
Basic	103,610	96,077
Diluted	103,610	106,000

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

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HELIX ENERGY SOLUTIONS GROUP, INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS (UNAUDITED)
(in thousands)

	Six Months Ended June 30, 2010	Six Months Ended June 30, 2009
Cash flows from operating activities:		
Net income (loss), including noncontrolling interests	$ (102,075)	$ 225,844
Adjustments to reconcile net income (loss), including noncontrolling interests to net cash provided by operating activities		
Depreciation and amortization	146,268	157,289
Asset impairment charge and dry hole expense	170,784	63,499
Equity in earnings of investments, net of distributions	—	(3,697)
Amortization of deferred financing costs	3,768	2,903
Loss (income) from discontinued operations	44	(7,282)
Stock compensation expense	4,589	7,188
Amortization of debt discount	4,136	3,876
Deferred income taxes	(54,749)	19,917
Excess tax benefit from stock-based compensation	2,163	754
Gain on sale or acquisition of assets	(6,233)	(1,773)
Unrealized (gain) loss on derivative contracts	2,813	(24,667)
Gain on sale of investment in Cal Dive common stock	—	(59,442)
Changes in operating assets and liabilities:		
Accounts receivable, net	(30,591)	(14,231)
Other current assets	16,477	15,704
Income tax payable	(10,811)	124,531
Accounts payable and accrued liabilities	28,027	9,220
Asset retirement obligation costs	(28,727)	(11,775)
Other noncurrent, net	(9,439)	(78,865)
Cash provided by operating activities	136,444	428,993
Cash used in discontinued operations	(44)	(6,121)
Net cash provided by operating activities	136,400	422,872
Cash flows from investing activities:		
Capital expenditures	(135,612)	(238,402)
Investments in equity investments	(6,307)	(454)
Distributions from equity investments, net	8,132	3,253
Insurance recovery for capital items	16,106	—
Proceeds from sale of Cal Dive common stock	—	196,656
Reduction in cash from deconsolidation of Cal Dive	—	(112,995)
Proceeds from sales of property	—	23,238

Other	109	(15)
Net cash used in investing activities	(117,572)	(128,719)
Cash provided by discontinued operations	—	20,874
Net cash used in investing activities	(117,572)	(107,845)

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HELIX ENERGY SOLUTIONS GROUP, INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS (UNAUDITED)
(Continued)
(in thousands)

	Six Months Ended June 30,	
	2010	2009
Cash flows from financing activities:		
Repayment of Helix Term Loan	(2,163)	(2,163)
Repayments on Helix Revolver	—	(349,500)
Repayment of MARAD borrowings	(2,403)	(2,081)
Borrowings on CDI Revolver	—	100,000
Repayments on CDI Term Note	—	(20,000)
Deferred financing costs	(2,792)	(28)
Repurchases of common stock	(9,127)	(753)
Excess tax benefit from stock-based compensation	(2,163)	(754)
Loan note repayment, preferred stock dividends paid and other	(1,098)	(500)
Net cash used in financing activities	(19,746)	(275,779)
Effect of exchange rate changes on cash and cash equivalents	246	(931)
Net (decrease) increase in cash and cash equivalents	(672)	38,317
Cash and cash equivalents:		
Balance, beginning of year	270,673	223,613
Balance, end of period	$ 270,001	$ 261,930

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

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HELIX ENERGY SOLUTIONS GROUP, INC. AND SUBSIDIARIES
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

Note 1 – Basis of Presentation

The accompanying condensed consolidated financial statements include the accounts of Helix Energy Solutions Group, Inc. and its majority-owned subsidiaries (collectively, "Helix" or the "Company"). Unless the context indicates otherwise, the terms "we," "us" and "our" in this report refer collectively to Helix and its majority-owned subsidiaries.   Until June 2009, Cal Dive International, Inc. (collectively with its subsidiaries referred to as “Cal Dive” or “CDI”) was a majority-owned subsidiary of Helix. Helix sold substantially all its ownership interest in Cal Dive during 2009 (see Note 4 below and Note 3 of our Annual Report on Form 10-K for the year ended December 31, 2009 (“2009 Form 10-K”)).   All material intercompany accounts and transactions have been eliminated. These unaudited condensed consolidated financial statements have been prepared pursuant to instructions for the Quarterly Report on Form 10-Q required to be filed with the Securities and Exchange Commission (“SEC”), and do not include all information and footnotes normally included in annual financial statements prepared in accordance with U.S. generally accepted accounting principles.

The accompanying condensed consolidated financial statements have been prepared in conformity with U.S. generally accepted accounting principles and are consistent in all material respects with those applied in our 2009 Form 10-K. The preparation of these financial statements requires us to make estimates and judgments that affect the amounts reported in the financial statements and the related disclosures. Actual results may differ from our estimates. Management has reflected all adjustments (which were normal recurring adjustments unless otherwise disclosed herein) that it believes are necessary for a fair presentation of the condensed consolidated balance sheets, results of operations, and cash flows, as applicable. The operating results for the periods ended June 30, 2010 are not necessarily indicative of the results that may be expected for the year ending December 31, 2010. Our balance sheet as of December 31, 2009 included herein has been derived from the audited balance sheet as of December 31, 2009 included in our 2009 Form 10-K. These unaudited condensed consolidated financial statements should be read in conjunction with the annual audited consolidated financial statements and notes thereto included in our 2009 Form 10-K.

Certain reclassifications were made to previously reported amounts in the condensed consolidated financial statements and notes thereto to make them consistent with the current presentation format.

Note 2 – Company Overview

We are an international offshore energy company that provides reservoir development solutions and other contracting services to the energy market as well as our own oil and gas properties. Our Contracting Services segment utilizes our vessels, offshore equipment and methodologies to deliver services that encompass the complete lifecycle of an offshore oil and gas field and that may reduce finding and development costs. Our Contracting Services operations are located primarily in the Gulf of Mexico, North Sea, Asia Pacific and West Africa regions. Our Oil and Gas segment engages in exploration, development and production activities. Our oil and gas operations are almost exclusively located in the Gulf of Mexico.

Contracting Services Operations
We seek to provide services and methodologies that we believe are critical to finding and developing offshore reservoirs and maximizing production economics. Our “life of field” services are segregated into three disciplines: subsea construction, well operations and production facilities. We have disaggregated our contracting services operations into two continuing reportable segments: Contracting Services and Production Facilities. Our Contracting

Services business primarily consists of deepwater construction and well operation activities. Formerly, we had a third Contracting Services segment, Shelf Contracting, which represented the assets of CDI. We sold substantially all of our ownership of CDI through various transactions in 2009 (Note 4). Our Production Facilities business includes our investments in Deepwater Gateway, L.L.C. ("Deepwater Gateway"), Independence Hub, LLC ("Independence Hub") and the Helix Producer I ("HP I") vessel.

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Oil and Gas Operations

We began our oil and gas operations to provide a more efficient solution to offshore abandonment, to expand our off-season asset utilization of our contracting services business and to generate incremental returns. Over time, we evolved this business model to include not only mature oil and gas properties but also proved and unproved reserves yet to be developed and explored. This has led to the assembly of services that allows us to create value at key points in the life of a reservoir from exploration through development, life of field management and operating through abandonment.

Discontinued Operations

In April 2009, we sold Helix Energy Limited ("HEL"), our former reservoir technology consulting business, to a subsidiary of Baker Hughes Incorporated for $25 million. As a result of the sale of HEL, which entity's operations were conducted by its wholly owned subsidiary, Helix RDS Limited ("Helix RDS"), we have presented the results of Helix RDS as discontinued operations in the accompanying condensed consolidated financial statements (Note 3). HEL and Helix RDS were previously included in our Contracting Services segment.

Business Strategy

During 2009, we focused on improving our balance sheet by increasing our liquidity through reductions in planned capital spending and potential additional dispositions of our non-core business assets. During 2009, we completed the following dispositions of non-core business assets:

- Sold five oil and gas properties for approximately $24 million;
- Sold a total of 15.2 million shares of CDI common stock held by us to CDI for $100 million in separate transactions in January and June 2009;
- Sold a total of 45.8 million shares of CDI common stock held by us to third parties in two separate public secondary offerings for approximately $404.4 million, net of underwriting fees in June 2009 and September 2009. For additional information regarding the sales of CDI common shares by us see Note 4; and
- Sold Helix RDS Limited, our subsurface reservoir consulting business for $25 million in April 2009.

In March 2010, we announced that we had engaged advisors to assist us with evaluating potential alternatives for the disposition of our oil and gas business. At the time of the filing of this Current Report on Form 10-Q we do not have an approved or definitive plan for such disposition of our oil and gas business.

Recent Events in Gulf of Mexico

Oil Spill

On April 20, 2010, an explosion occurred on the Deepwater Horizon drilling rig located on the site of the Macondo well at Mississippi Canyon Block 252. The resulting events included loss of life, the complete destruction of the drilling rig and an oil spill, the magnitude of which is unprecedented in U.S territorial waters. The operator of the Macondo project, BP PLC ("BP") has recently controlled the flow of the oil from the well and ultimately plans to plug the well. Simultaneously, efforts to contain and ultimately remediate the environmental impacts caused by the oil spill are ongoing. We have contracted three of our vessels, the Q4000, the Express and the HP I to participate in the coordinated containment response to the oil spill in the Gulf of Mexico.

Drilling Moratorium

On May 12, 2010, the U.S. Department of Interior ("DOI") announced a total moratorium on new drilling in the Gulf of Mexico. This moratorium also affected 33 in progress wells in the deepwater. On May 28, 2010 the moratorium on drilling in the shallow water of the Gulf, as defined as water depths less than 500 feet, was lifted. However, the DOI extended the drilling moratorium on deepwater wells through November 2010. This drilling moratorium was challenged in court and the court enjoined its enforcement. However, the DOI has recently amended its drilling moratorium which remains in effect at the time of this filing despite additional potential legal challenges.

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Note 3 – Details of Certain Accounts

Other current assets consisted of the following as of June 30, 2010 and December 31, 2009:

	June 30, 2010	December 31, 2009
	(in thousands)	
Other receivables	$ 3,851	$ 7,990
Prepaid insurance	12,901	11,105
Other prepaids	16,545	21,819
Inventory	25,808	25,755
Current deferred tax assets	15,057	24,517
Hedging assets	15,306	6,214
Gas imbalance	6,774	7,655
Income tax receivable	18,139	8,492
Assets of discontinued operations	825	878
Other	5,464	7,784
	$ 120,670	$ 122,209

Other assets, net, consisted of the following as of June 30, 2010 and December 31, 2009:

	June 30, 2010	December 31, 2009
	(in thousands)	
Restricted cash	$ 35,519	$ 35,409
Deferred drydock expenses, net	14,238	12,030
Deferred financing costs	29,284	30,061
Intangible assets with finite lives, net	713	768
Other	2,383	3,945
	$ 82,137	$ 82,213

Accrued liabilities consisted of the following as of June 30, 2010 and December 31, 2009:

	June 30, 2010	December 31, 2009
	(in thousands)	
Accrued payroll and related benefits	$ 25,976	$ 30,513
Royalties payable	11,146	5,717
Asset retirement obligation	76,708	65,729
Unearned revenue	9,188	3,672
Accrued interest	27,826	27,830
Billing in excess of cost	6,814	—
Deposit	25,542	25,542
Hedge liability	5,108	19,536

Liabilities of discontinued operations	13	451
Other	13,833	21,617
	$ 202,154	$ 200,607

Note 4 — Ownership of Cal Dive International, Inc.

In January 2009, we sold approximately 13.6 million shares of Cal Dive common stock to Cal Dive for $86 million. This transaction constituted a single transaction and was not part of any planned set of transactions that would have resulted in us having a noncontrolling interest in Cal Dive, and reduced our ownership in Cal Dive to approximately 51%. Because we retained control of CDI immediately after the transaction, the loss of approximately $2.9 million on this sale was treated as a reduction of our equity.

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In June 2009, we sold 22.6 million shares of Cal Dive common stock held by us pursuant to a secondary public offering ("Offering") and Cal Dive repurchased an additional 1.6 million shares of its common stock from us. Following the closing of these two transactions, our ownership of Cal Dive common stock was reduced to approximately 26%. Since we no longer held a controlling interest in Cal Dive, we ceased consolidating Cal Dive effective June 10, 2009, and subsequently accounted for our remaining ownership interest in Cal Dive under the equity method of accounting until September 2009, when we sold substantially all of our remaining interest in Cal Dive.

We continue to own 0.5 million shares of Cal Dive common stock, representing less than 1% of the total outstanding shares of Cal Dive. Accordingly, we now classify our remaining interest in Cal Dive as an investment available for sale pursuant to ASC Topic No. 320 "Investment - Debt and Equity Securities." As an investment available for sale, the value of our remaining interest will be marked-to-market at each period end with the corresponding change in value being reported as a component of other accumulated comprehensive income (loss) in the accompanying condensed consolidated balance sheets (Note 11). The pre-tax value of our remaining investment in Cal Dive as of June 30, 2010 has decreased $0.9 million since December 31, 2009 and $2.2 million since our Cal Dive sales transaction in September 2009. We consider our unrealized losses on our remaining Cal Dive investment to be temporary. We will continue to monitor our investment and should we determine that these losses are not temporary we will remove the unrealized amounts from our accumulated comprehensive loss by recording the difference between our original investment and the then expected realizable value as a non operating expense charge in our consolidated statement of operations.

See Note 3 of our 2009 Form 10-K for additional information regarding our sale transactions involving Cal Dive common stock in 2009.

Note 5 – Convertible Preferred Stock

In January 2009, Fletcher International, Ltd. ("Fletcher") issued a redemption notice with respect to its $30 million of Series A-2 Cumulative Convertible Preferred Stock, and, pursuant to the resulting redemption, we issued and delivered 5,938,776 shares of our common stock to Fletcher. Accordingly, in the first quarter of 2009 we recognized a $29.3 million charge to reflect the terms of this redemption, which was recorded as a reduction in our net income applicable to common shareholders. This beneficial conversion charge reflected the value associated with the additional 3,974,718 shares delivered over the original 1,964,058 shares that would have been contractually required to be issued upon a conversion but was limited to the $29.3 million of net proceeds we received from the issuance of the Series A-2 Cumulative Convertible Preferred Stock in June 2004.

In February 2009, the price of our common stock fell below $2.767 per share. Under terms of the agreement governing the issuance of the cumulative convertible preferred stock, we provided notice to Fletcher that with respect to the $25 million of Series A-1 Cumulative Convertible Preferred Stock the conversion price was reset to $2.767, the established minimum price per the agreement, and that Fletcher shall have no further rights to redeem the shares, and we have no further right to pay dividends in common stock. As a result of the reset of the conversion price, Fletcher would receive an aggregate of 9,035,056 shares in future conversion(s) into our common stock. In the event we elect to settle any future conversion in cash, Fletcher would receive cash in an amount approximately equal to the value of the shares it would receive upon a conversion, which could be substantially greater than the original face amount of the Series A-1 Cumulative Convertible Preferred Stock, and which would result in additional beneficial conversion charges in our statement of operations. Under the existing terms of our Senior Credit Facilities (Note 9) we are not permitted to deliver cash upon a conversion of the Convertible Preferred Stock.

In connection with the reset of the conversion price of the Series A-1 Cumulative Convertible Preferred Stock to $2.767, we were required to recognize a $24.1 million charge to reflect the value associated with the additional 7,368,388 shares that will be required to be delivered upon any future conversion(s) over the 1,666,668 shares that were to be delivered under the original contractual terms. This $24.1 million charge was recorded as a beneficial conversion charge reducing our net income applicable to common shareholders. The beneficial conversion charge for the Series A-1 Cumulative Convertible Preferred Stock is limited to the $24.1 million of net proceeds received upon its issuance in January 2003.

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In May 2010, Fletcher converted $5 million of its Series A-1 Cumulative Convertible Preferred Stock into 1,807,011 shares of our common stock. In the third quarter of 2009, Fletcher converted $19 million of its Series A-1 Cumulative Convertible Preferred Stock into 6,866,641 shares of our common stock. The remaining $1 million of the Series A-1 Cumulative Convertible Preferred Stock, which is convertible into 361,402 shares of our common stock, maintains its mezzanine presentation below liabilities but is not included as a component of shareholders' equity, because we may, under certain instances be required to settle any future conversions in cash. Prior to any future conversion(s), the common shares issuable will be assessed for inclusion in our diluted earnings per share computations using the if converted method based on the applicable conversion price of $2.767 per share, meaning that for all periods in which we have positive earnings from continuing operations and our average stock price exceeds $2.767 per share we will have an assumed conversion of convertible preferred stock and the 361,402 shares will be included in our diluted shares outstanding amount.

Note 6 – Oil and Gas Properties

In March 2010, we announced that we engaged advisors to assist us with evaluating potential alternatives for the disposition of our oil and gas business. At the time of the filing of this Quarterly Report on Form 10-Q we do not have an approved or definitive plan for such disposition of our oil and gas business.

We follow the successful efforts method of accounting for our interests in oil and gas properties. Under the successful efforts method, the costs of successful wells and leases containing productive reserves are capitalized. Costs incurred to drill and equip development wells, including unsuccessful development wells, are capitalized. Costs incurred relating to unsuccessful exploratory wells are charged to expense in the period in which the drilling is determined to be unsuccessful.

Depletion expense is determined on a field-by-field basis using the units-of-production method, with depletion rates for leasehold acquisition costs based on estimated total remaining proved reserves. Depletion rates for well and related facility costs are based on estimated total remaining proved developed reserves associated with each individual field. The depletion rates are changed whenever there is an indication of the need for a revision but, at a minimum, are evaluated annually. Any such revisions are accounted for prospectively as a change in accounting estimate.

Mid Year Reserve Assessment

In connection with our regular mid-year review as well as our efforts to pursue potential divestment alternatives for our oil and gas business, we engaged an independent petroleum reservoir engineering firm to update our estimates of proved reserves for our domestic oil and gas properties as of June 30, 2010. The resulting independent petroleum engineer reserve report indicated the we had a significant reduction in proved reserves resulting from a combination of factors including well performance issues at certain of our producing fields, most notably our Bushwood field at Garden Banks Blocks 462/463/506/507, as well as changes in the field economics of some of our other oil and gas properties. The changes in field economics primarily affected properties that were either close to the end of their production life or in which we had proved undeveloped reserves, which would have been required to be developed in the near term. The decision not to develop these properties in light of these economic changes was also driven by our desire to pursue potential alternatives to divest our oil and gas business and the increasing uncertainties about future oil and gas operations in the Gulf of Mexico as a result of the oil spill from the Macondo well. As a result of the reduction in estimated reserves we were required to record oil and gas property impairment charges of $159.9 million at June 30, 2010.

Impairments

Following the determination of a significant reduction in our estimates of proved reserves at June 30, 2010, we recorded oil and gas property impairment charges totaling $159.9 million which affected the carrying value of 15 of our Gulf of Mexico oil and gas properties.

In the first quarter of 2010, we recorded $7.0 million of impairment charges primarily resulting from natural gas price declines since year end 2009. The three properties subject to these impairment

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charges produce natural gas almost entirely. Separately, we also recorded a $4.1 million impairment charge for our only non-domestic oil and gas property (see "United Kingdom Property" below).

In the second quarter of 2009, we recorded an aggregate of approximately $63.1 million of impairment charges. These charges primarily reflected the approximate $51.5 million of impairment-related charges recorded to properties that were severely damaged by Hurricane Ike (as discussed below in Insurance). Separately, we also recorded $11.5 million of impairment charges to reduce the asset carrying value of four fields following reductions in their estimated proved reserves as evaluated at June 30, 2009.

Exploration and Other

As of June 30, 2010, we capitalized approximately $3.2 million of costs associated with ongoing exploration and/or appraisal activities. Such capitalized costs may be charged against earnings in future periods if management determines that commercial quantities of hydrocarbons have not been discovered or that future appraisal drilling or development activities are not likely to occur.

The following table details the components of exploration expense for the three and six month periods ended June 30, 2010 and 2009 (in thousands):

	Three Months Ended June 30,		Six Months Ended June 30,	
	2010	2009	2010	2009
Delay rental and geological and geophysical costs	$ 1,182	$ 1,061	$ 1,528	$ 1,533
Dry hole expense	(10)	422	(190)	426
Total exploration expense	$ 1,172	$ 1,483		