

Refocused Restructured Reinforced Refinancing

Stolt Offshore S.A.
Annual Report and Accounts 2003



Corporate and financial highlights

For the year ended 30 November (in millions, except per share data)	2003 \$	2002 \$	2001 \$
Net operating revenue	1,482.3	1,437.5	1,255.9
(Loss) income from operations	(380.5)	(123.6)	36.4
Net loss	(418.1)	(151.9)	(14.2)
Cash flows from operating activities	(27.5)	84.7	16.7
Loss per share:			
Basic	(4.51)	(1.79)	(0.16)
Diluted	(4.51)	(1.79)	(0.16)
Weighted average number of economically equivalent shares outstanding:			
Basic	92.6	85.0	87.2
Diluted	92.6	85.0	87.2

As at 30 November (in millions, except per share data)	2003 \$	2002 \$	2001 \$
Long-term debt and capital lease obligations	385.0	335.0	358.7
Shareholders' equity	107.3	517.1	660.0
Book value per Common Share and Common Share equivalent	1.16	5.54	7.57

2003 Operating revenue by region (in \$ millions)

Africa, the Mediterranean and Caspian Sea region (AFMED)	673.8
Northern Europe and Canada region (NEC)	387.6
North America and Mexico region (NAMEX)	200.6
South America region (SAM)	56.0
Asia and Middle East region (AME)	26.8
Corporate	137.5
Total	1,482.3



1 AFMED 45%	4 SAM 4%
2 NEC 26%	5 AME 2%
3 NAMEX 14%	4 Corporate 9%

Fixed assets as at 30 November 2003 (in \$ thousands)

Construction support ships	618.6
Operating equipment	277.3
Land and buildings	24.2
Other assets	13.2
Less accumulated depreciation and amortisation (418.7)	
Total	514.6



1 Construction support ships 66%
2 Operating equipment 30%
3 Land and buildings 3%
4 Other assets 1%

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We are rebuilding our Company. With a refocused business, a new organisation, a strengthened management team and a rigorous adherence to procedures, we are on track to return to profitability.

So far we have:

- ▶ **Refocused** our chosen market segments to concentrate on our main strengths and we are selling assets and businesses that no longer fit our core activities.
- ▶ **Restructured** our organisation with new Regional Businesses fully accountable for all project work in their geographical area. We have changed more than half of our senior management team.
- ▶ **Reinforced** consistent, coherent operating procedures world-wide with global direction and control provided by the corporate team.
- ▶ **Refinanced** by raising equity to strengthen our balance sheet, negotiating a new bonding line and changing the covenants on existing credit facilities to better suit our financial position.

To find out more turn to pages 12–15.

Chairman's statement

Message from the Chairman

2003 was a brutal year for Stolt Offshore. The challenges and costs of turning the Company around have far exceeded the expectations of all those close to the process. At year-end, we reported a net loss of \$418 million, after minority interests, which included \$177 million of asset impairments. The good news is that we consider most of the restructuring programme is now behind us and there is genuine cause for optimism as we move into 2004.

While our strategy for the development of this business over recent years may have been good, with the benefit of hindsight we now see that mistakes were made which stretched our financial capabilities. The former management team did an outstanding job when the Company was a niche subsea contractor, but were not able to handle the multiple acquisitions and the integrations needed to make Stolt Offshore a profitable EPIC (Engineering, Procurement, Installation and Commissioning) contractor.

In March 2003 Tom Ehret joined us as Chief Executive Officer to lead the Stolt Offshore turnaround process. In April 2003 Stuart Jackson joined us as Chief Financial Officer. Tom's first action was to develop his 'Blueprint for financial recovery' which has refocused our approach to our markets and restructured our organisation. Under this plan Tom quickly led an exhaustive top-to-bottom strategic analysis and review of the Company.

As a result of this rigorous process, substantial changes were made to refocus the business on what it does best. Stolt Offshore is now refocused on the three core markets where it can generate the greatest value: SURF (subsea, umbilicals, risers, flowlines), which has always been the key capability of the Company; conventional construction of platforms and pipelines in areas adjacent to

The good news is that we consider most of the restructuring programme is now behind us and there is genuine cause for optimism as we move into 2004.

deepwater basins; and subsea inspection, maintenance and repair. The other activities, such as the provision of third party engineering, welding technology and ROV (Remotely Operated Vehicle) drill support have been or are in the process of being sold. This will enable management to give all of its attention to the three core markets where it can generate the best value. An internal and geographic restructuring has taken place and a programme of disposals of the assets that we no longer require is now under way.

Project control processes have been reinforced through new tendering and contracting procedures, global supply chain management and project management procedures. The discipline that Tom is imposing to ensure that these processes are rigorously adhered to will prevent us from taking on the contract risks and the onerous contract terms that have hurt Stolt Offshore so badly over the last four years.

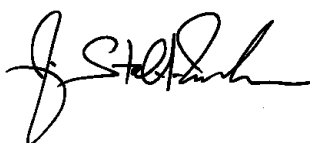
As the year progressed, the losses on a small number of major projects in West Africa and the Mediterranean put the Company in breach of the financial covenants on our major credit agreements. We then spent many months negotiating covenant waivers with our lenders in order to gain time to plan and put into place a major financial restructuring.

In mid-February 2004, Stolt Offshore raised \$100 million in a private placement with European investors and we intend to raise approximately \$50 million more in a subsequent issue. A new bonding facility of \$100 million was put in place with a number of existing lenders and our banks agreed new covenants on our credit lines that were more appropriate to our financial situation. The Stolt-Nielsen Transportation Group also agreed to convert \$50 million of subordinated debt into Stolt Offshore Common Shares.

In addition, we issued 17 million new Common Shares to the Stolt-Nielsen Transportation Group on conversion of all of the Stolt Offshore Class B Shares to Common Shares. These actions, when they are all complete, will result in a \$200 million strengthening of Stolt Offshore's balance sheet and provide enough cash and performance bonds for the Company to compete as an independent competitive offshore contractor.

We have a strong and talented new management team. We have aggressively refocused the Company on the markets where we have the most to offer, restructured the business so that it can more efficiently address these markets and reinforced the procedures that will deliver quality project management. We have also refinanced the Company so that it can play a leading role in the offshore construction industry.

Stolt Offshore is not yet out of the woods, but the future now looks far better than it did a few months ago. Our customers have continued to value our abilities through the difficult months. We won the \$250 million Langed pipelay project in November and our largest ever contract, the \$550 million Greater Plutonio project from BP, in February 2004. The activity level industry-wide is slow this year but is shaping up for a stronger year in 2005.



Jacob Stolt-Nielsen
Chairman



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Chief Executive's statement

We are putting Stolt Offshore back on track.

The Blueprint – a clear strategy for financial recovery

- ▶ We have identified past problems and defined our new strategy.
- ▶ Our new focus is on fewer market segments where we can create the greatest value.
- ▶ We are disposing of non-essential ships and businesses.
- ▶ A new global organisation is now in place which has clear lines of responsibility.
- ▶ 30 out of 40 senior managers are newly appointed.
- ▶ We have reinforced our approach to project risk assessment and management.
- ▶ We have refinanced our debt, strengthening the balance sheet and securing new bonding facilities.
- ▶ Our customers continue to support us. Recent major project wins are evidence of this.
- ▶ The full benefits of our reorganisation will not be clear until the latter part of 2004.

2003 was a year dominated by a small number of large loss-making projects, tough decisions and extraordinary change within Stolt Offshore. Our financial performance reflects the measures we took to transform the Company. They were costly, but they have removed systemic failings from the organisation.

The dynamics of this industry demand close focus on the market segments where we can create the greatest value, superior project management founded on sound procedures governing all aspects of the project from targeting to delivery, a consistent response to our customers world-wide and the necessary corporate discipline to ensure that standards are maintained and procedures followed. These principles governed the comprehensive 'Blueprint' strategic review which redefined our market focus and led to the restructuring of the Company initiated in 2003.

We are now refocused on our core markets of SURF, Conventional and IMR which together are expected to represent industry-wide revenues of some \$38 billion from 2004 to 2007.

To address these markets in the most efficient way possible, we have put in place a new Group-wide organisation in which our Regional Businesses have profit and loss responsibility for everything that happens in their sphere of influence, with the definition of operating procedures and the provision of support and control coming from a significantly strengthened corporate team. In this way we are imposing a consistency of conduct throughout our operations which is founded on positive teamwork and a culture of open communication.

'...The measures we took to transform the Company... were costly, but they have removed systemic failings from the organisation.'

'The process of turning Stolt Offshore around still has a long way to go... I am however happy with the quality of the backlog that we are now building up for 2005 and beyond, a time when we see stronger markets in which we will play our full part.'



The management team has changed to support the new strategy. We are all part of a senior management team at Stolt Offshore where 30 out of 40 senior positions were new appointments by the end of 2003. On completion of our change programme, we expect to have reduced the workforce by 21%, reduced our annual SG&A costs by 15% and through write-downs and disposals, brought our asset base closer to both our commercial strategy and our income. These disposals are expected to raise \$100–\$150 million by the end of 2004.

We have also reinforced our approach to project risk assessment and management. We are strengthening the quality of our project management through training and strict process control and we are now managing the supply chain globally to maximise our purchasing power. In this way we will have enhanced control of our future projects and developed a much improved ability to forecast our financial position. We will also be able to avoid the incidences of poor tendering and project management that have so damaged the Company in recent years.

A great deal of my time and that of our CFO Stuart Jackson has been absorbed this year in the lengthy process of refinancing the Company. Now that this process is reaching a conclusion, both Stuart and I will be able to direct more of our efforts to the day-to-day management of the Company, to facilitating the ongoing change process that will be with us for some time yet, and to ensuring that we deliver a strong financial performance.

The process of turning Stolt Offshore around still has a long way to go. The award of the Norsk Hydro Ormen Lange trunkline project, now known as Langeled, and the BP Greater Plutonio project, which at \$550 million is our largest to date, demonstrates that our customers recognise that our ongoing restructuring will make us a stronger company. I am, however, happy with the quality of the backlog that we are now building up for 2005 and beyond, a time when we see stronger markets in which we will play our full part and a time when I am confident that we will once again deliver the returns that our shareholders can rightly expect.

Tom Ehret
Chief Executive Officer

Who we are and what we do

Stolt Offshore's mission is to design, procure, fabricate, install and maintain complete subsea pipeline and riser systems for the global offshore oil and gas industry.

We specialise in harsh marine environments where natural conditions demand first-rate experience, first-rate know-how and first-rate resources. We also deliver our products and services in more conventional waters adjacent to deepwater oil and gas provinces.

Our business is conducted through projects. We invest in people and applied technology to enhance our performance and respond to new challenges. We operate as an integrated group of companies.

Where we have come from

Our roots go back to the early 1960s and the earlier days of offshore exploration and production in the harsh environment of the seas of Northern Europe. Starting life as a company operating divers and remotely operated vehicles on the construction projects that brought the first of the North Sea oil fields on stream, we have grown our abilities over the years by developing the first specialist subsea construction ships and then by adding pipelay capabilities.

With the growth in the offshore construction market from a business primarily located in the North Sea in the late 1990s to one which is now truly world-wide, the Company has grown rapidly. During the period 1998 to 2000 we acquired companies that added the market positioning, assets and the technologies that we needed to be a global contractor. Following a period of consolidation in our market sector Stolt Offshore is now one of only four offshore construction contractors that work world-wide.

Whereas the growth by acquisition strategy was sound, with hindsight we paid too much for our acquisitions and failed to adequately integrate the companies and cultures into a single entity. During this time a small number of major African EPIC projects were badly bid and managed. While the greater part of our global business remained solid, losses incurred on these contracts in Africa have impacted our financial results over the last three years.

Where we are today

A new CEO and CFO joined the Company in early 2003 and a 'Blueprint for financial recovery' was launched in July. Under this plan, the market focus has been narrowed to only those segments where we have real strengths. These are subsea umbilicals, risers and flowlines (SURF), the conventional installation of platforms and pipelines and the inspection, maintenance and repair market (IMR). Assets and businesses now surplus to our core activities are being sold. A new global organisation has been put in place with clear lines of responsibility and accountability. 30 out of 40 senior managers were newly appointed by December 2003. The Company has been refinanced and its capital structure simplified early in 2004. Most of the provisions of the Blueprint were in place by financial year-end 2003.

Where we are going

The core market segments for the Company are forecast to generate \$38 billion of revenues in our industry over the period 2004-07. This is a 30% increase in these markets over the previous four-year period. Stolt Offshore is the only pure play offshore construction contractor among its major competitors. We intend to maintain this position as we use our established strengths to deliver value from this growing market.

Where we operate

Stolt Offshore operates in most parts of the world where there is offshore oil and gas exploration and production in deep water. The business is managed through regional offices each with profit and loss responsibility for their region.



North America & Mexico (NAMEX)

This region contributes some 14% of total revenues in 2003 from Conventional and SURF projects as well as day rate diving and IMR work. Trunkline projects such as the Duke/Williams Gulfstream project are also typical of this region.



Africa & the Mediterranean (AFMED)

The AFMED region accounted for 45% of total revenues in 2003. Large SURF projects such as ExxonMobil Erha and BP Greater Plutonio are typical of this region with Conventional projects and a limited number of IMR projects.



South America (SAM)

The majority of our operations in this region are in Brazil for Petrobras in what is essentially a single customer market. 4% of total revenue for 2003 came from this region. We have a four-year contract for one ship with an optional four-year extension and a second ship on a four-year contract.



Northern Europe & Canada (NEC)

SURF, IMR and trunkline projects account for most of our business in this region which contributed 26% of total revenues in 2003. Both small marginal fields and new deep water developments such as the Ormen Lange field in Norway are typical of this region. There is an active IMR market.



Asia & the Middle East (AME)

The Asia & Middle East region accounted for some 2% of revenue in 2003. We are active in the Conventional and IMR markets in this region. Following the expansion of the area of responsibility for this region in the second half of 2003, a strategy is being developed to grow our share of this market.

Our key products and services

Stolt Offshore specialises in subsea construction work providing services that add value for our customers throughout the entire life cycle of an offshore oil or gas field. This includes engineering, flowline and pipeline lay, construction, inspection, maintenance and repair services much of which is conducted in deepwater and harsh environments.



Above, top
The *Seaway Polaris* installing an offshore platform in West Africa.

Above, bottom
Design drawing showing part of Stolt Offshore's latest generation of ultra-deepwater Remotely Operated Vehicles (ROVs).

Our key customers

Our key customers are the multinational, national and independent oil and gas companies around the world. 82% of 2003 revenue was from large national and multinational companies.

Stolt Offshore worked for 99 separate customers during 2003, five of which accounted for 68% of revenue. These were Shell, Total, Chevron Texaco, Norsk Hydro and Project Consulting Services. The second five largest were Petrobras, BP, NAM, Amerada Hess and ExxonMobil who together accounted for 16% of revenues.



Our competitors

The offshore oil and gas business is highly competitive. Consolidation in recent years has resulted in fewer but more substantial competitors. There are five main competitors for the SURF market with a larger number, on a regional basis, in our other market segments.

Operating review

Disappointing results but significant restructuring undertaken.

A refocused company moving back on track

While the loss for the year of \$418 million was very poor, the progress that Stolt Offshore has made with the reconstruction of our business provides a solid platform for growth. Market orientation and discipline are now transformed and the Company is starting to see the benefits of the restructuring. The targeted reduction of costs and reconfiguration of the asset base progress according to plan.

Financial restructuring enables us to play a leading role in the offshore industry

Efforts to turn the Company around are being recognised by shareholders who have contributed a capital injection of \$100 million by way of a private placement. Our largest major shareholder, Stolt-Nielsen S.A., made a \$50 million debt for equity swap. Concurrently our lenders have provided a \$100 million performance bonding facility. In addition we intend to raise approximately \$50 million by way of a subsequent share issue in May 2004. All of these actions after year-end are the measures of our achievement in 2003.

Our future strategy is to rebalance the business

Our strategy going forward is to continue with the process of reorganising the Company, to manage the completion of the last of the loss-making legacy contracts to contain ongoing losses as we go through 2004 and to continue to build our backlog, for 2005 and beyond, with new projects which have acceptable contract terms and margins as we move back to profitability.

Africa & the Mediterranean (AFMED)

Continuing losses on the legacy contracts, Bonga, Burullus and OGGs masked the good quality of deepwater work on other projects such as Girassol 2 and Ceiba. A major restructuring of this region is in progress and will run throughout 2004.

Financial result

	\$m
Net operating revenue	673.8
Net loss before tax	(285.2)
Fixed asset write-offs	65.1



The OGGs platform topsides fabricated at the Stolt Offshore fabrication yard in Warri, Nigeria.

Major projects

- ▶ Shell OGGs
- ▶ British Gas/Burullus Scarab & Saffron
- ▶ Shell Bonga
- ▶ Shell Forcados/Yokri
- ▶ ChevronTexaco Sanha Bomboco
- ▶ ExxonMobil Erha
- ▶ Amerada Hess Ceiba

Recent contract awards

BP Greater Plutonio \$550 million.
Total Amenam II.

2004 outlook

Lower revenues than 2003 due to some major projects completing and other large contracts being in an early stage.

Northern Europe & Canada (NEC)

2003 saw a high level of activity in Norway in the SURF market as well as the Dutch sector of the North Sea. The IMR market was also busy with the BP IMR contract and through the Stolt/Subsea 7 joint venture.

Financial result

	\$m
Net operating revenue	387.6
Net income before tax	23.1
Fixed asset write-offs	0.1



On deck on the pipelay ship, Seaway Falcon.

Major projects

- ▶ Norsk Hydro Vigdis
- ▶ Total Skirne Byggve
- ▶ NAM K7 & K15
- ▶ Lyse Rogass
- ▶ Stolt/Subsea 7 joint venture
- ▶ Shell Cleaver Bank

Recent contract awards

Langed trunkline pipelay \$250 million.
ExxonMobil Arthur, Paladin Montrose
Arbroath and BP Endeavour Hot-tap.

2004 outlook

The North Sea market is similar to 2003 with some projects delayed to 2005.

North America & Mexico (NAMEX)

The major projects for the year were the Duke Hubline pipelay, a mainly reimbursable contract and the BHP Angostura pipelay in Trinidad. With no dedicated SURF ship in the region this market sector was quiet. The IMR performance was stronger than usual, much of it related to repairing hurricane damage.

Financial result

	\$m
Net operating revenue	200.6
Net loss before tax	(32.3)
Fixed asset write-offs	12.4



Extreme weather conditions early in 2003 hampered progress on the Hubline project.

Major projects

- ▶ Duke Energy/AGT Hubline pipelay
- ▶ BHP Billiton Angostura
- ▶ IMR projects

Recent contract awards

British Gas Dolphin and NGC Bud Developments, Trinidad and Tobago.

2004 outlook

The Angostura pipelay work continues into 2004 and results will improve due to significant write-offs taken in 2003.

South America (SAM)

A very good year of operating two ships on charter to Petrobras in Brazil. Both ships saw very high levels of utilisation. Drill support and survey ROV operations also performed well.

Financial result

	\$m
Net operating revenue	56.0
Net income before tax	18.2
Fixed asset write-offs	0.0



Brazil is the only market that takes construction ships on long-term charter.

Major projects

- ▶ Petrobras charter *Seaway Condor*
- ▶ Petrobras charter *Seaway Harrier*

2004 outlook

Both of the ship charters with Petrobras continue in 2004 however revenue may be marginally lower.

Asia & Middle East (AME)

The majority of revenue came from shallow water IMR projects as well as some conventional and survey projects.

Financial result

	\$m
Net operating revenue	26.8
Net loss before tax	(6.6)
Fixed asset write-offs	0.0



Divers continue to play an important part in subsea construction.

Major projects

- ▶ Total UHB repairs
- ▶ PNG Panarang Penping
- ▶ Survey projects
- ▶ Panyu diving

2004 outlook

Higher activity levels are anticipated in 2004 with a specialist SURF ship being allocated to the region later in the year and the disposal of some under-performing assets in Q1 2004.

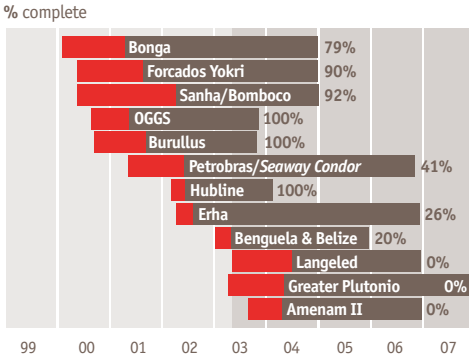
Major projects at a glance

Major loss-making projects tendered in 2000 impacted 2003 results.

Major contracts over \$100 million

The chart below shows projects of over \$100 million in value which are still in progress or completed in 2003. Those which are typically loss-making or at very low margins are those that started the tender process in 2000. This was before we put into place stronger procedures governing risk assessment and acceptable contract terms, were enforced.

Projects tendered in 2002 for execution through to 2005 and beyond largely carry far less risk and more acceptable margins. These two pages show a selection of well tendered and managed projects from around the world as well as some of the legacy projects.



Major projects over \$100 million % complete as at 31 March 2004

Introduction of new management team
 Contract tender period
 Project execution period

ExxonMobil Erha project – Nigeria

Overview

A deepwater development off Nigeria where Stolt Offshore is installing 26 km of flowlines and steel catenary risers as well as the offshore loading buoy and its mooring system. Much of the fabrication work is at the Stolt Offshore yard at Warri in Nigeria.

- ▶ Contract value on award \$275 million
- ▶ Award date September 2002
- ▶ Completion at year-end 15%
- ▶ Offshore installation in 2006



The early months of a major offshore development are devoted to detailed engineering.

Total Girassol phase 2 – Angola

Overview

The second phase of this major deepwater development with the tie-back of additional wells to the riser towers on the main Girassol development by installation and tie-in of insulated towed pipeline bundles. Pipe connections made by MATIS™, a Stolt Offshore engineered connection system.

- ▶ Contract value on award \$89 million
- ▶ Award date March 2001
- ▶ Completion at year-end 100%



The MATIS™ remotely operated tie-in system used for all subsea pipe connections on this project.

Petrobras ship charters – Brazil

Overview

Two long-term day rate ship charters to Petrobras. *Seaway Condor* undertakes deepwater flexible flowline installation. *Seaway Harrier* provides diver and ROV field maintenance services.

- ▶ *Seaway Condor*: four-year charter from August 2002 for approximately \$30 million per year
- ▶ *Seaway Harrier*: four-year charter from July 2001 for approximately \$16 million per year



The *Seaway Condor* lays flexible pipelines in deep water in Brazil.

Total Skirne Byggve project – Norway

Overview

A two well subsea tie-back to the Heimdal platform, typical of the type of work undertaken in the North Sea to tie back new small reservoirs to existing process platforms.

- ▶ Contract value on award \$48.5 million
- ▶ Award date October 2002
- ▶ Completion at year-end 99%



Typical wellhead protection structures for a subsea field development.

ChevronTexaco Sanha Bomboco – Angola

Overview

A project to fabricate and install five platforms offshore Angola which has seen some delays and cost overruns in the engineering, fabrication and installation programme and recently in the hook-up to live producing platforms.

- ▶ Contract value on award \$240 million
- ▶ Awarded May 2002
- ▶ Completion at year-end 71%



Installation of the offshore platform deck on the Sanha Bomboco project

Shell Nigeria Offshore Gas Gathering System (OGGS) – Nigeria

Overview

A large trunkline installation project for the *LB 200* and other assets to link several offshore gas fields to a processing site.

- ▶ Contract value on award \$135 million
- ▶ Award date July 2001
- ▶ Completion at year-end 100%

Local community unrest, strikes, piracy and delays in pipe supply disrupted the project causing long delays for the *LB 200* and *Seaway Orion* pipelay barges. A loss of \$29.3 million was recorded, some of which was recovered from the customer.

Shell Bonga development – Nigeria

Overview

The installation of steel catenary risers, export pipelines and production and water injection flowlines for the first major deepwater FPSO development in Nigeria.

- ▶ Contract value on award \$200 million
- ▶ Award date March 2001
- ▶ Completion at year-end 71%

The project has incurred losses from delays in engineering and on the installation programme which was moved into a poor weather season by late availability of the *Seaway Polaris*, as well as delays on the installation programme. Losses of \$6.2 million were booked in 2002 with additional losses of \$67.8 million in 2003.

Amerada Hess Ceiba project – Equatorial Guinea

Overview

The installation of risers and flowlines and subsea structures on the three phases of the Ceiba development in deep water off Equatorial Guinea and the provision of assistance with changing the FPSO.

- ▶ Contract value on award \$126 million over three phases, \$24.6 million for final phase in 2003
- ▶ First phase awarded 2001
- ▶ Completion at year-end 100%



The *Seaway Polaris* holding production risers during an FPSO change out.

Duke/AGT Hubline project – North America

Overview

A pipelay project for the *DLB801* and other subcontracted ships and barges in Massachusetts partly on a combined day rate and lump sum contract.

- ▶ Contract value on award \$84 million
- ▶ Award date July 2002
- ▶ Completion at year-end 100%

Project delays from extreme weather conditions in the winter of 2002, seabed conditions and other factors caused the project to exceed budget, leading to a dispute over the cost plus element of the contract. A loss of \$16.1 million was recorded, at year-end 2003, and the dispute was resolved in March 2004.

Burullus Scarab & Saffron – Egypt

Overview

The first deepwater development in the Eastern Mediterranean. Installation of gas export pipelines from shore to offshore fields where flowlines, service lines, manifolds and well control umbilicals are installed.

- ▶ Contract value on award \$145 million
- ▶ Award date May 2001
- ▶ Completion at year-end 100%

Following a \$35.2 million downgrade recorded in 2002, a further \$51.7 million downgrade in 2003 resulted from some 100 additional ship days devoted to meeting first gas target date and rectifying installation problems. Some of the extra costs were recovered from the customer.

Refocused. Our chosen market segments position us well for future earnings growth.

Historically, Stolt Offshore has provided a full range of engineering, subsea construction and inspection, repair and maintenance (IMR) services in both deep and shallow water environments. In July 2003 we initiated a comprehensive review of our strategy, capabilities and operations. The resulting 'Blueprint' plan set out a new strategy that emphasises our deep water strengths and reduces our target markets to three primary segments plus the trunkline business. Our core markets are now:

SURF

The design, installation and maintenance of subsea construction, umbilical, riser and flowline systems (SURF) in deep water and harsh environments.

Conventional

The provision of conventional construction services in shallow water environments where this is complementary to our deep water SURF business.

IMR

Subsea inspection, maintenance and repair services on producing oil and gas fields to maintain an ongoing market presence in key deep water areas and adjacent shallow water environments.

Disposal of businesses and assets

With our new focus on fewer market segments, a number of assets and businesses are no longer essential to serve our core markets. We expect cash receipts of \$100-150 million from this disposal programme by the end of 2004.

Progress on disposals

As this disposal process has progressed, we and our joint venture partners have sold the ROV drill support business, which includes 44 ROVs and 200 people and ongoing contracts in the North Sea, Angola and Brazil to Oceaneering International in February 2004 for approximately \$48 million. The *Seaway Kingfisher*, in which Stolt Offshore has a 50% interest, has been placed on a 12 month charter, and the *Annette*, *American Eagle*, *Seaway Rover*, *Seaway Invincible* and the *Seaway Pioneer* have been sold.

Businesses offered for sale are as follows:

- ▶ The Paragon Companies: Engineering businesses located in Houston and Paris.
- ▶ Serimer Dasa: A specialised welding technology company located in Paris.



SURF market by region 2004-07 \$15.2b

The SURF market is expected to total some \$15.2 billion or 40% of our core market in the 2004-07 period, a share increase of 6% on the previous four years.

- 1 SAM 11%
- 2 NEC 25%
- 3 NAMEX 15%
- 4 AME 12%
- 5 AFMED 37%



Conventional market by region 2004-07 \$13.7b

The Conventional market is expected to grow by 13% from the 2000-03 period to some \$13.7 billion during the 2004-07 period and to make up 36% of our core market.

- 1 NAMEX 54%
- 2 AFMED 46%



IMR market by region 2004-07 \$9.3b

The IMR market being essentially a spot market appears at short notice and is difficult to forecast. However our expectations are for market growth of 24% to some \$9.3 billion in the 2004-07 period over 2000-03 \$7.5 billion.

- 1 SAM 6%
- 2 NEC 28%
- 3 NAMEX 20%
- 4 AME 29%
- 5 AFMED 17%

+30%

These markets are expected to total some \$38 billion in the four-year period 2004-07, a 30% increase over the previous four-year period.



SURF market growth +53% 2000-07 \$25.1b



Conventional market growth +13% 2000-07 \$25.8b



IMR market growth +24% 2000-07 \$16.8b



Jean-Luc Laloë
Corporate Vice President
Strategic Planning

Restructured. Our new project-driven organisation and regional accountability is now in place.

Our business is the efficient delivery of offshore construction projects. To do this we have to deliver the same quality of response to our customers wherever they may be in the world. We need highly disciplined control of our tendering and project management procedures and we need clear lines of responsibility and accountability.

A new corporate organisation was put in place in the second half of 2003 which realigned the previous structure from a product line focus to a regional structure with five operating regions:

- ▶ Africa & Mediterranean (AFMED)
- ▶ Northern Europe & Canada (NEC)
- ▶ North America & Mexico (NAMEX)
- ▶ South America (SAM)
- ▶ Asia & the Middle East (AME)

Each region is headed by a Vice President with profit and loss responsibility for all business activities in their region. The regional organisation is supported by the corporate team who define operating procedures and provide the support and control necessary to ensure that these are followed or adapted to specific circumstances.

Thirty of forty senior management were newly appointed to their positions by the end of 2003. Other structural changes include a reduction in the workforce by 21% and a reduction of our annual SG&A costs by 15%. Through write-downs and disposals our asset base has been brought in line with both our commercial strategy and our income expectations.

Managing skilled resources

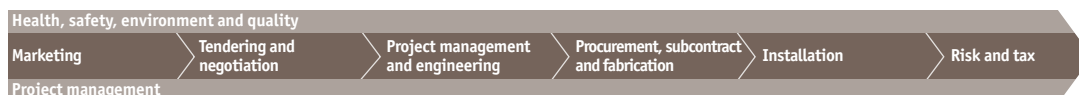
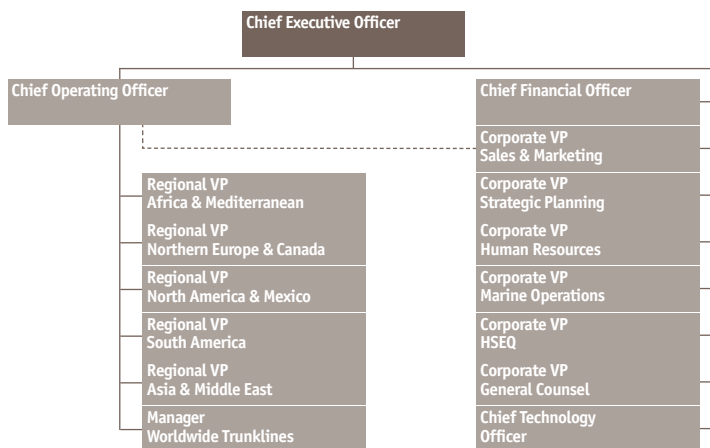
As we see growth in our market segments in the years ahead, our forward planning of essential project management and engineering resources, an industry wide concern, is now being conducted at a global as well as a regional level.

In parallel with this initiative, we are now working to improve Group efficiency by ensuring that all of our marketing and tendering, project management and control, technical and installation engineering processes, are common world-wide. In this way we will be able to transfer human resources and projects or parts of project work scopes between regions, to optimise the utilisation of skilled resources wherever they may be.

We also have a proactive training programme that addresses both the core processes for current employees as well as for new recruits. In this way we will ensure that we not only anticipate our future requirements for skilled manpower but that we meet these needs with the appropriate numbers of skilled personnel.



Bruno Chabas
Chief Operating Officer



Reinforced. Strict adherence to the procedures which govern all aspects of project delivery will ensure success.

The exercise of efficient and adequate control over how we manage our projects from tendering through to delivery is an essential if we are to ensure that our operations are not only properly controlled but have good predictability in terms of financial results. To this end, a number of new project management and tendering procedures have been implemented resulting in a change in the way in which we evaluate new business opportunities.

Project management

The business of Stolt Offshore is the efficient delivery of offshore construction projects. Our project managers are responsible for maximising the project contribution to earnings while ensuring that our customers get a quality of service that both meets our contractual obligations and adds value to the project. New project management procedures have been implemented and a project manager training programme covering all aspects of their role has been instituted.

Formal tender review process

The information contained in tender review packages is now uniform across our organisation allowing us to weigh the risks and benefits of tendering for various projects. A larger proportion of tenders are being reviewed centrally by corporate management and we now place greater emphasis on our standard contractual terms and conditions.

Management accountability

A broad management approach to the tender review process has been implemented under which tenders are first reviewed at the regional level where the technical, operational, legal and financial aspects of the proposal are considered in detail. Different levels of approval are applied, up to CEO and Board approval level, according to tender value.

Risk management

A formal risk assessment process is undertaken for each project tender consisting of a legal risk assessment that compares the contractual terms and conditions of the proposed tender to our standard terms and conditions. The financial impact of any deviation from our standard terms and conditions is quantified and a risk mitigation plan is proposed. In addition, we conduct an operational risk assessment that analyses factors such as the impact of weather, supplier delays, strikes and other factors to quantify the potential financial impact of such events.

Supply Chain Management

Stolt Offshore spent some \$450 million in 2003 in the course of delivering largely fixed price contracts. Critical to the control of project expenditure is the Supply Chain Management (SCM) function. New SCM procedures have been implemented to ensure a consistent understanding and approach to these activities throughout the Group world-wide. In this way we now make the best use of our Group buying power to source the best commercial, technical and delivered solutions to satisfy our project needs.



Above, top
Johan Rasmussen
Corporate Vice President and General Counsel

Above, middle
Peter Jessup
Vice President, Supply Chain Management

Above, bottom
David Nicholson
Group Project Controller



SCM, 2003 spend \$450 million

1 SAM 2%	4 NE 2%
2 NEC 35%	5 NAMEX 27%
3 AFMED 34%	

Refinancing. We are strengthening our balance sheet as part of a major financial restructuring.

As a result of ongoing losses on a small number of large contracts in Africa during 2003, the Company found it increasingly difficult to remain in compliance with its covenants. Financial restructuring discussions with our lenders commenced in the second half of 2003 after presentation of the 'Blueprint for financial recovery.'

Following extensive discussions with our major creditors, an equity issue was arranged to accelerate the financial restructuring of the Company by raising approximately \$100 million through a private placement.

The refinancing plan included the following elements:

- ▶ A Private Placement of 45.5 million new Common Shares at \$2.20 per share to raise \$100 million. This was completed on 13 February 2004.
- ▶ A Subsequent Issue of approximately 24.0 million new Common Shares to shareholders who did not participate in the Private Placement.
- ▶ An option for Stolt-Nielsen S.A. to subscribe for 22.7 million Common Shares in consideration for the conversion of up to \$50 million of subordinated loans on the same terms as for those in the proposed equity issue. An irrevocable undertaking in this regard was obtained from Stolt-Nielsen S.A. on 13 February 2004.
- ▶ The conversion of the Company's Class B Shares, all of which were owned by a subsidiary of Stolt-Nielsen S.A., to Common Shares on a 2:1 basis.
- ▶ A new bonding facility of \$100 million, which was made available on 12 February 2004.
- ▶ A change to the covenants on existing credit facility agreements to better suit the Company's financial circumstances, which was completed on 12 February 2004.

As a result of this refinancing, and when the Subsequent Issue is completed the number of shares outstanding will have increased from 93.3 million Common Share Equivalents to 185.5 million Common Shares with the free float increasing from 34.6 million Common Shares to 106.1 million Common Shares.

New equity and free float*

In millions (except % voting rights)	SNSA	Other shareholders	Total
Voting rights (incl. Class B Shares) 30 Nov 2003	69.2%	30.8%	100%
Existing Common Shares	41.7	34.6	76.3
Class B Shares replacement (2:1 basis)	17.0	–	17.0
Private Placement and Subsequent Share Issue	–	69.5	69.5
Subordinated debt conversion	22.7	–	22.7
Sale of shares	(2.0)	2.0	–
Total	79.4	106.1	185.5
Voting rights (Expected after Subsequent Issue)	43%	57%	100%

*information correct as at 31 March 2004.

\$100m

Private Placement

\$50m

Subsequent Issue (to be completed)

\$50m

Subordinated Debt conversion

Common Shares

Conversion of Class B Shares to Common Shares



Stuart Jackson
Chief Financial Officer

Management team



Tom Ehret
Chief Executive Officer

Tom Ehret joined Stolt Offshore as Chief Executive Officer in March 2003, prior to which he served as Vice Chairman of the Management Board of Technip-Coflexip and President of its Offshore Branch.

He has an excellent track record of company turnaround and growth management and is on a clear mission to do the same with his new team at Stolt Offshore.

Having trained as a mechanical engineer, Tom started working life as an R&D engineer before entering into project management. He has since worked in a variety of positions, both technical and commercial, for various offshore engineering and construction companies.

He speaks French, German and English and has worked in France, the U.S. and the U.K.



Stuart Jackson
Chief Financial Officer

Stuart joined Stolt Offshore in April 2003 as Chief Financial Officer. The focus of his role has been to mastermind the financial restructuring of the Company following completion of the 'Blueprint for financial recovery.'

Prior to joining Stolt Offshore, Stuart was Managing Director of NRG Energy Inc's UK operations and completed a leveraged management buyout and restructuring of the principal businesses. He previously headed the trading, finance, commercial and HR functions of Humber Power Limited. Stuart held senior finance positions at LASMO plc based in the Far East and North Africa having completed five years heading the Group corporate finance function in London. Stuart commenced his career at Marathon Oil in the treasury and engineering development groups. Stuart is an honours graduate of Loughborough University of Technology, and an FCMA.



Bruno Chabas
Chief Operating Officer

Bruno Chabas was appointed Chief Operating Officer in October 2002.

He has responsibility for all the day-to-day commercial and operational activity of the five regions as well as the trunkline business.

Since joining the Company in 1992 Bruno has held various positions in the U.K., France and the U.S., latterly serving as Chief Financial Officer. He has experienced the Company's rapid growth and has lived through all the major acquisitions.

Bruno holds an MA in Economics from the University of Science at Aix-en-Provence and an MBA from Babson College in Massachusetts.



Jean-Luc Laloë
Corporate VP Strategic Planning

Jean-Luc Laloë joined the corporate team in May 2003, and brings 25 years of experience in the international offshore construction industry.

In his role as Corporate VP Strategic Planning, he has managed the development and implementation of the 'Blueprint for recovery and value growth', which he continues to oversee, and is conducting the ongoing divestment programme of non-core assets and businesses.

With a Masters degree in Aeronautical & Space Engineering, Jean-Luc began his career as a naval architect. He has since held a broad variety of positions at several international locations with Technip-Coflexip, including Executive VP – North America; Managing Director – United Kingdom; VP Special Projects in Paris; CFO for Brazil; and VP Strategic Planning in Paris.



Mark Preece
Corporate VP Business Development

Mark Preece joined Stolt Offshore in February 2004 as Corporate VP Business Development.

He has extensive commercial, operations management and business development experience gained both in the U.K. and internationally.

Previously he was Managing Director with Bibby Line Ltd and with Stena Offshore/Coflexip/Technip was Managing Director, Canada and Caspian; Senior VP U.K. and International Business Development (and Board Member of Genesis Oil and Gas); General Manager – Business Development; Sales and Marketing Manager; and Project Manager.

In his earlier offshore career he was a Ship's Master and a Marine Superintendent. Mark is a Master Mariner with an MBA from Henley Management College.



Keith Tipson
Corporate VP Human Resources

Keith Tipson joined Stolt Offshore at the beginning of November 2004 as Corporate VP Human Resources.

His role as a member of the corporate team will be to develop and implement the Group HR strategy and develop the global HR team. He has responsibility for Resourcing, Performance and Reward, People Development and Internal Communications. His previous experience has been in the engineering project sector with the Dowty Group and latterly with Alstom where he held the position of Senior Vice President Human Resources, Power Sector based in Paris.



Johan Rasmussen
Corporate VP and General Counsel

Johan was appointed General Counsel to Stolt Offshore in 1996.

In his role as Corporate VP Legal Counsel he provides the essential ingredients of legal, contracting and risk management expertise to the corporate team. He is also the functional head for the Group legal and contract support teams within the regions and businesses, setting quality standards, levels of resourcing and development of the team.

Before joining Stolt-Nielsen Seaway in 1988, Johan who has a Masters Degree in Law from the University of Oslo, worked within a subdivision of the Norwegian Ministry of Defence and was also a Deputy Judge for two years in Haugesund District Court.



Ken London
Corporate VP Health, Safety, Environment and Quality (HSEQ)

Ken London was appointed to a Group HSEQ position in 1999.

He is responsible for developing the Group strategy for HSEQ improvement and for maintaining the overall framework and guidelines for the management of Stolt Offshore's assets, people and processes through setting the standards for HSEQ support across the Group.

Ken holds a BSc in Electronic and Electrical Engineering from Edinburgh University and is a Chartered Member of the Institute of Marine Engineers. He joined Stolt Offshore in 1994 as a Senior Engineer becoming Engineering Manager before taking up his current role.



Alan West

Corporate VP Marine Operations

Alan West holds the position of Corporate VP Marine Operations and as such is responsible for the management and maintenance of the Group's ships and assets.

He is also responsible for the ploughing and trenching, marine and operations, technical support and crewing of the offshore spreads and for onshore and offshore marine and operational people.

Alan has a degree in Mechanical Engineering, an MSc in Marine Technology and an MBA. He is a Chartered Mechanical Engineer and is a Member of the Royal Institution of Naval Architecture.

He has extensive experience as a Project Engineer, progressing to Project Manager and then to VP Subsea Construction Product Line in 1995, a position he held prior to his present one.



Allen Leatt

Chief Technology Officer

Allen Leatt joined Stolt Offshore's corporate team in September 2003 as Chief Technology Officer responsible for the Engineering and Supply Chain Management standards of the Group, as well as the R & D programme.

Allen has a degree in Engineering, is a Chartered Engineer and holds an MBA. He began his career in marine civil engineering with John Laing Construction Ltd, and then spent six years at SubSea Offshore Ltd., as a Project Engineer and Project Manager. He joined what is now Technip in 1988 where he held a number of management and executive positions, ultimately Executive Vice President for their SURF Product Line based in Paris, before joining Stolt Offshore.



Jean-Pierre Capron

VP Africa & Mediterranean (AFMED)

Jean-Pierre Capron joined Stolt Offshore in the middle of this year as Regional VP of the Africa & Mediterranean Region (AFMED).

He has full responsibility for the commercial and operational activity in the region. Jean-Pierre has particular experience of turnaround situations, as COO of Technip in the mid-80s, Chairman and CEO of Renault Vehicules Industriels in the early 90s and latterly Chairman and CEO of Compagnie de Fives-Lille.

He is a graduate from both Ecole Polytechnique and Ecole Nationale Supérieure des Mines de Paris, and started his professional life as an underground engineer in a coal mine. Jean-Pierre is based in the Nanterre office.



Jeff Champion

VP Asia Pacific (APAC)

Jeff Champion is presently Vice President Asia Pacific based in Jakarta.

He is responsible for all the day-to-day operational activity of the region and contributing to the strategy development of the new AME region.

Jeff has over 30 years' experience in Europe, the Middle East and South East Asia on major oil and gas related construction contracts. He has had wide experience of both general and project management on behalf of both clients and main contractors.

Jeff speaks English, French and basic Indonesian.



Quinn Hébert

VP North America & Mexico (NAMEX)

Quinn Hébert is Regional VP for the NAMEX region, a role he has been in since 1999.

Quinn joined Stolt Offshore from Ceanic Corporation when it was bought in 1998. He was the VP General Counsel and Secretary of that organisation and was heavily involved in the sale negotiations. He became the VP Corporate Counsel and VP Commercial of the region before being appointed to the Regional Manager position.

Quinn qualified at the Boston College Law School and began his legal career in a private practice in Louisiana and obtained significant experience in the corporate sector. It was in 1993 when he left to join American Oilfield Divers, which later changed its name to Ceanic Corporation.



Oeyvind Mikaelson

VP Northern Europe & Canada (NEC)

Oeyvind Mikaelson was appointed Regional VP for the new NEC region in 2003 and has full profit and loss responsibility for the region.

The initial focus of the role has been to integrate the two previous regions of the U.K. and Norway.

He began his career as a Contracts Manager with Kvaerner followed by two years with Norske Shell as a Cost and Contracts Engineer. He joined Stolt Offshore in Norway in 1992 and has held positions in joint venture administration, contracts administration, project management and sales and marketing. In 2001, he was appointed VP Subsea Construction product line and was based in Aberdeen. He held this position prior to his present appointment.



Philippe Lamoure

VP South America (SAM)

Philippe Lamoure is VP South America region, a role he has fulfilled since 1995.

The South America region has been an area of the Company that has constantly turned in good performance over the years.

Philippe, who has a degree in Commercial Business Administration, completed his military service in the French Navy as a diver, before moving into the commercial diving business in 1974. Since then he has held Operations Manager positions in Marseille and Rio De Janeiro, was Resident Manager in Tunisia and VP France, Africa and Middle East based in Marseille. He moved to Rio de Janeiro in 1995 to take on his present position. In 1992 Philippe attended the Management Development Programme at Harvard Business School.



Johann Stulemeyer

Worldwide Trunklines Manager

Johann Stulemeyer joined Stolt Offshore as a project manager in 1998 and now holds the position of Worldwide Trunklines Manager with responsibility for all aspects of large diameter pipelay projects around the world.

Johann has had 24 years in the offshore construction industry employed initially as a diver, and more recently as an engineer and Project Manager. With an engineering degree and fluent in English, Dutch and Greek, Johann has worked mainly in the Middle East and the North Sea on civil engineering and offshore construction projects. Since joining Stolt Offshore, he has managed projects in the North Sea, Middle East and Africa and been responsible for world-wide tenders for subsea construction work. He has also been a ship operations manager.

Board of Directors

As a Nasdaq listed company, Stolt Offshore is required to comply with a number of corporate governance requirements. Among these requirements is a provision in the Nasdaq Marketplace Rules requiring all listed companies to have a Board of Directors composed of a majority of independent directors. While the Company is not required to comply with this provision until July 2005, the Board has agreed and resolved to prospectively comply with this requirement.



Mr Jacob Stolt-Nielsen Chairman

Mr Jacob Stolt-Nielsen has served as Chairman of the Board since 1993. He is also currently Chairman of the Board of Stolt-Nielsen S.A. and served as Chief Executive Officer of Stolt-Nielsen S.A. from 1959 until 2000. He founded Stolt-Nielsen Seaway AS in 1973. He holds a degree from the Handelsgymnasium, Haugesund, Norway. Mr Jacob Stolt-Nielsen is a Norwegian citizen.



Mr Mark Woolveridge Deputy Chairman

Mr Woolveridge has been a Director since 1993 and has served as Deputy Chairman of the Board since 2002. He held a number of positions with BP since 1968 and most recently served as Chief Executive of BP Engineering from 1989 until his retirement in 1992. He was also General Manager, Oil and Gas Developments, responsible for field development projects in the UK and Norwegian sectors of the North Sea, and served on the Board of BP Oil Ltd. He holds a Masters degree from Cambridge University and is a Fellow of the Royal Academy of Engineering and of the Institute of Mechanical Engineers. Mr Mark Woolveridge is a British citizen.



Mr Tom Ehret

Mr Ehret was appointed to the Board of Directors in November 2003 and has served in the position of Chief Executive Officer of Stolt Offshore since March 2003. He came to the Company from his position as Vice Chairman of the Management Board of Technip-Coflexip and President of its Offshore Branch. Mr Ehret has experience of working with Comex, FMC Corporation, Comex Houlder Diving Limited, Stena Offshore, Coflexip Stena and latterly Technip Coflexip. He has worked in all the major disciplines both technical and commercial and has been a Project Manager, New Product Development Manager, Marketing and Sales Manager, Managing Director, CEO and COO. Mr Tom Ehret is a French citizen.



Mr James B. Hurlock

Mr Hurlock is a retired partner from the law firm of White & Case LLP and served as Chairman of its Management Committee from 1980 to 2000. He participated in the formation and served on the Board of Northern Offshore Ltd. which during the 1970s operated diver lock-out submarines and provided other services to the offshore oil industry. He holds a BA degree from Princeton University, an MA Jurisprudence from Oxford University and a JD from Harvard Law School. Mr James B. Hurlock is a U.S. citizen.



Mr Haakon Lorentzen

Mr Lorentzen is Managing Director of Lorentzen Empreendimentos SA of Rio de Janeiro, a diversified holding company with investments in Aracruz Celulose SA, Cia. Norsul Navegação and a diversified IT portfolio. He is also Director of Aracruz Celulose, Iseiasnet, Advicenet, Intellibridge, CEAL, and WWF Brazil. He holds a Bachelors degree in Economics from Pontificia Universidade Caalica do Rio de Janeiro and a Harvard Business School Post Graduate Degree. Born in Norway, Mr Haakon Lorentzen is a resident of Brazil.



Mr J. Frithjof Skouverøe

Mr Skouverøe has been a Director since 1993. He is owner and Chairman of Concentus AS, a Norwegian/Swedish Industrial Group. He is also a member of the Board of Ocean Rig ASA, an offshore drilling contractor listed on the Oslo Stock Exchange. He was Chairman of the Board and Chief Executive Officer of Seaway from 1990 until it was acquired by Stolt-Nielsen S.A. in 1992. From 1985 to 1990, he was President and Second Vice Chairman of Seaway. He served as President of Stolt-Nielsen Seaway Contracting A/S, a predecessor of Seaway, from 1982 until 1985. He holds an MBA from INSEAD and a Masters degree in Mechanical Engineering from the Technical University of Norway. Mr J. Frithjof Skouverøe is a Norwegian citizen.



Mr Niels G. Stolt-Nielsen

Mr Niels G. Stolt-Nielsen has been a Director since 1999 and was appointed Interim Chief Executive Officer in 2002. He has also served on the Board of Stolt-Nielsen S.A. since 1996 and has served as Chief Executive Officer of Stolt-Nielsen S.A. since 2000. From 1996 until 2001 he held the position of Chief Executive Officer of Stolt Sea Farm. Mr Stolt-Nielsen previously worked in Stolt-Nielsen Transportation Group. He is the son of Mr Jacob Stolt-Nielsen. He graduated from Hofstra University in 1990 with a BSc in Business and Finance. Mr Niels G. Stolt-Nielsen is a Norwegian citizen.

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Management's discussion and analysis



Stuart Jackson
Chief Financial Officer

Overview

Stolt Offshore S.A., a Luxembourg company, together with its subsidiaries (collectively, 'the Company') is one of the largest offshore services contractors in the world. The Company designs, procures, builds, installs and services a range of offshore surface and subsurface infrastructure for the global oil and gas industry. The Company specialises in creating and applying innovative and efficient solutions in response to the technical complexities faced by offshore oil and gas companies as they explore and develop production fields in increasingly deeper water and more demanding offshore environments.

Operational difficulties, bank discussions and operational changes

During fiscal year 2002, the Company experienced unanticipated operational difficulties related to a number of major projects. Consequently, in fiscal year 2002 there was an aggregate negative impact of \$58.8 million on its net income attributable to changes in original estimates on major projects. The most significant components of the adverse developments occurred on the Burullus, Shell EA, Bonga and Conoco CMS 3 projects, which are described below in 'Results of operations – Summary of major projects for 2003, 2002, 2001'. With the exception of the Conoco CMS 3 project, all of these projects lie within the Africa, Mediterranean and Caspian Sea ('AFMED') region. The operational difficulties resulted in increased costs being realised due to, among other factors: (i) extensive changes in work scope, trenching difficulties, fabrication and local logistics cost overruns with respect to the Burullus project; (ii) fabrication cost overruns caused by community unrest in the Company's local yard at Warri, Nigeria, with respect to the Shell EA and Bonga projects; (iii) longer than expected offshore ship operations due to repairs and scope changes with respect to the Shell EA project; (iv) schedule changes, changes in installation scope and increased subcontractor costs with respect to the Bonga project; and (v) pipeline burial problems in the North Sea with respect to the Conoco CMS 3 project.

Primarily as a consequence of these adverse developments, the Company announced in December 2002 that, as of 28 February 2003, it anticipated being potentially in breach of certain financial covenants contained in its \$440 million credit facility, and its \$55/45 million credit/guarantee facility (the 'Existing Credit Facility Agreements'). In light of these developments, in December 2002 the Company sought, and by 3 January 2003 had obtained, amendments to these facilities to avoid financial covenant defaults. The amendments included revised financial covenants and a requirement that Stolt-Nielsen S.A. ('SNSA') continue to provide financial support to the Company through the provision of a committed line of credit in the amount of \$50 million until 30 November 2003 (the 'SNSA Liquidity Line').

In October 2002, the Company appointed Niels G. Stolt-Nielsen as interim Chief Executive Officer and Jan Chr. Engelhardt as interim Chief Financial Officer and commenced a search for new senior management.

New management and continuing operational difficulties

In March 2003, the Company appointed Tom Ehret as Chief Executive Officer and Stuart Jackson as Chief Financial Officer, with the following objectives: to lead the Company's commercial and financial recovery, to design and execute a financial recovery plan, to sell and, in some cases, outsource non-essential businesses, to restructure the Company's cost and asset base, and to raise new capital and secure new performance bond facilities. Mr Ehret and Mr Jackson commenced a comprehensive review of the Company's major projects, operations and procedures and initiated a plan for restructuring the Company's operations.

In June 2003, the Company announced that its new senior management had reviewed the Company's major projects and had identified substantially poorer than anticipated financial performance and cost overruns on three major projects and several smaller projects. Throughout the first and second quarters of fiscal year 2003, the Company continued to experience operating difficulties on major projects primarily in the AFMED region. The Company announced that these difficulties would have an additional negative impact on earnings, primarily as a result of the following: (i) poor performance of nominated subcontractors and delays in resolution of outstanding claims with respect to variation orders on the Burullus project, and (ii) higher than anticipated costs on the Bonga and OGGs projects due to late delivery of materials, adverse weather conditions and political unrest in the Niger Delta region that increased local support and logistics costs.

As a result of these problems, the Company found it increasingly difficult to remain in compliance with the revised financial covenants under the Existing Credit Facility Agreements. Consequently, the Company engaged in further discussions with its lenders under these facilities regarding amendments to or additional waivers of these facilities to avoid defaults with respect to the financial covenants contained in the facilities. On 1 July 2003, the Company announced that it had obtained a waiver of potential defaults to the financial covenants contained in these facilities through 30 November 2003. The waivers included a requirement that the Company's net losses for the second and third quarters of fiscal year 2003 would not exceed \$75 million in the aggregate. As a condition to receipt of the waivers, SNSA agreed to provide to the Company a \$50 million subordinated loan (the 'Subordinated Note') and to extend the availability of the committed line of credit to November 2004. On 9 July 2003, the Company announced that on the basis of current projections it did not expect to be in compliance with the revised financial covenants at the end of fiscal year 2003 and had reclassified its long-term bank debt as short-term accordingly.

The Company continued to experience significant deterioration in the second and third quarters of fiscal year 2003 with respect to major projects, particularly in the AFMED region. These operational problems were exacerbated by its continued inability to collect cost overruns believed to be owed to it by customers with respect to work performed on major projects. During this time, the Company engaged in numerous discussions with the lenders under its Existing Credit Facility Agreements regarding amendments to or additional waivers of these facilities to avoid defaults with respect to the financial covenants contained in these facilities.

During the second half of fiscal year 2003, the cost overruns on major projects, the continued delay in the Company's recovery of amounts owed to it, and the delayed settlement of claims and variation orders with respect to major projects had a significant negative impact on the Company's liquidity. Consequently, while the Company was engaged in discussions with its primary creditors to amend the financial covenants in its Existing Credit Facility Agreements, the Company took measures to ensure that it had sufficient liquidity to fund its operations and to provide for a potentially protracted period of negotiation with certain major customers regarding settlement of claims and variation orders. These measures included borrowing to its maximum availability under the Existing Credit Facility Agreements and closing its positions under foreign exchange contracts, which had positive value.

By July 2003, the Company's new senior management had developed and begun to implement a strategy for financial recovery, which the Company has referred to from time to time as the 'Blueprint business plan'. This strategy includes a stronger operational focus on (i) the Company's capabilities in the design, installation and maintenance of subsea construction, umbilical, riser and flowline systems ('SURF') in deep water and harsh environments; (ii) Conventional services in shallow water environments where doing so is complementary to the Company's deep water SURF business ('Conventional'); and (iii) subsea inspection, maintenance and repair ('IMR') services to maintain an ongoing market presence in key deep water areas and adjacent shallow water environments. See Note 20 to the consolidated financial statements for a detailed description of these service capabilities.

The first stages of the plan for financial recovery, involving changes in the Company's personnel, operating structure and business processes, were substantially completed in the second half of fiscal year 2003. The changes included the establishment of clear lines of regional accountability within the realigned operating structure, responsibility for project execution, the adoption of revised policies in connection with the Company's tendering and contracting practices, changes in management, including the appointment of a corporate vice president of project controls, as well as regional project control managers to emphasise regional project responsibility and the implementation of new procedures for sales and marketing, project management,

Management's discussion and analysis continued

marine operations technology and engineering, strategic planning and supply chain management. The Company realigned its operating structure into five geographical regions: AFMED, Northern Europe and Canada ('NEC'), North America and Mexico ('NAMEX'), South America ('SAM') and Asia and the Middle East ('AME'). The Company's Corporate segment includes all activities that cover more than one region and also includes management and corporate services provided for the benefit of all the Company's businesses (see 'Segment geographic coverage' below). The Company's senior management was restructured with new appointments to 30 out of 40 posts; a plan was commenced to reduce the total workforce by 21% through disposals of businesses (1,100 posts) and headcount reduction (400 posts), and a 2004 target was set of a 15% (\$15 million) reduction in selling, general, and administrative ('SG&A') costs.

In addition, the new management team identified a number of businesses and assets for disposal that were not critical to the success of the Company's refocused operations. The Company expects to receive \$100 million to \$150 million in proceeds by the end of 2004, if the Company is able to dispose of certain non-core assets and businesses it has identified for sale, including Serimer DASA (its surface welding business), Paragon Engineering Services, Inc., Paragon Litwin S.A. and Paragon Italia S.r.l. (the 'Paragon Companies'), the survey business (the business whereby the seabed environment is surveyed as well as pipelines and structures installed on it, in order to determine their accurate position and condition), the ROV drill support business (a fleet of 44 remotely operated vehicles, controlled from the surface via an umbilical and designed to operate in depths of up to 3,000 metres. ROVs are used for construction or observation) and several ships. See further discussion at 'Factors affecting the Company's results of operations – Businesses and assets offered for sale'.

In September 2003, the Company announced that it expected higher than previously projected losses for fiscal year 2003, partially as a result of the continued earnings deterioration on the Burullus, Bonga and OGGs projects, but primarily resulting from decisions that were then under consideration relating to the implementation of the Company's plan for financial recovery. As a result of these developments, the Company was in potential breach of the revised financial covenants under the waiver agreements it had obtained on 1 July 2003. The Company sought and obtained from its lenders under the Existing Credit Facility Agreements new waivers of these revised financial covenants. These new waivers would expire on 15 October 2003 and replaced the revised waivers that were set to expire on 12 September 2003. In addition, the Company announced that it was engaged in discussions with its principal lenders for the restructuring of its debt obligations.

During the fourth quarter of fiscal year 2003, the Company continued to engage in restructuring discussions with its lenders, and received three subsequent covenant waiver extensions, including an extension announced on 29 December 2003, which provided for covenant relief through 30 April 2004 subject to certain conditions.

For the fiscal year ended 30 November 2003, the Company reported a net loss of \$418.1 million. There was an aggregate negative impact of \$216.0 million on net income attributable to changes in original estimates on major projects. The most significant components of the adverse developments occurred on the Bonga, Burullus, Sanha Bomboco, OGGs, and the Duke Hubline projects, which are described below in 'Factors affecting the Company's results of operations – Revisions of cost estimates on major projects'. Impairment charges totalling \$176.5 million were recorded against the carrying value of a number of ships, barges, mobile assets and onshore equipment. A further charge of \$9.1 million was recorded in respect of the Company's share of impairment of fixed assets owned by the three equity joint ventures, NKT Flexibles I/S ('NKT Flexibles'), Kingfisher D.A. and Sonastolt.

The Private Placement, the Subsequent Issue and the Debt Conversion

As part of the Company's ongoing discussions with the lenders under its Existing Credit Facility Agreements, the Company also considered a number of alternatives for restructuring its debt obligations and reducing its overall debt levels. In February 2004, the Company issued and sold 45.5 million common shares (the 'Private Placement') that raised gross proceeds of \$100.1 million and are being traded on the Oslo stock exchange. This will be followed by an issuance of common shares expected to generate approximately \$53 million in gross proceeds in 2004 (the 'Subsequent Issue'). This issuance is expected to be completed in May 2004. On 20 April 2004, SNSA converted the \$50 million Subordinated Note into equity (the 'Debt Conversion'), thus providing a potential \$200 million increase in shareholders' equity before deduction of expenses. See 'Liquidity and capital resources – Equity and funding transactions since 30 November 2003'.

The New Bonding Facility and the Intercreditor Deed

In February 2004, the Company entered into a new \$100 million performance bond facility (the 'New Bonding Facility'), which provides it with the ability to offer bank guarantees and other forms of surety that are often required in order to bid on and win new business. In addition, the Company entered into an intercreditor deed that incorporates changes to and supersedes the covenants and security arrangements in the Existing Credit Facility Arrangements. See 'Liquidity and capital resources – equity and funding transactions since 30 November 2003' below.

Outlook

As described in Note 15 to the consolidated financial statements, the Company's credit facilities contain various financial covenants, including but not limited to, minimum consolidated tangible net worth, maximum consolidated debt to net worth and maximum consolidated debt to EBITDA. These financial covenants were revised by the Intercreditor Deed. The Company's latest forecasts for fiscal year 2004 indicate that there will be a narrow margin of compliance with the debt to EBITDA ratio covenant at the end of the fourth quarter of 2004. The Company's ability to remain within its covenants at the second and third quarter-ends is dependent on (i) its operating performance; (ii) the successful completion of the Subsequent Issue during the second quarter of 2004, (iii) its ability to recover variation orders and claims from customers where additional contract costs are incurred and (iv) the success of the Company's plans to divest certain assets and businesses.

The Company has consequently made contingency plans in the event that the Company is unable to comply with its covenants as follows: (i) the Company has the option of raising unsecured debt finance as an alternative means of repaying bank facilities; (ii) the Company can defer discretionary capital expenditure, (iii) the Company has the option of raising further equity, and (iv) the Company can seek to obtain a waiver of covenant breaches if they were to arise.

The majority of the loss-making projects have been completed and most disputes over claims and variation orders have been settled since the end of fiscal year 2003. These issues were resolved after year-end, but because they relate to events that occurred prior to 30 November 2003, the impact of this settlement on the OGGs and Burullus projects was accounted for as a receivable in fiscal year 2003. As noted in 'Other subsequent events', significant additional costs to completion have been identified on the Sanha Bomboco and Bonga projects in March 2004. However, there were some strong regional performances, particularly in the NEC region, where offshore activity was exceptionally high, and the SAM region.

The Company was less successful in fiscal year 2003 than in previous years in winning new contracts to replenish its order book, and the Company's backlog at 17 February 2004 stood at \$849 million, of which \$556 million is expected to be executed in fiscal year 2004. This compares to a backlog at 17 February 2003 of \$1.5 billion, of which \$1.0 billion was for fiscal year 2003. Starting in December 2003, the definition of backlog was changed to exclude future revenues from letters of intent and options and only to include signed agreements. As of 31 March 2004, the Company has in excess of \$900 million of additional recently awarded contracts in fiscal year 2004, including the Langedale and Greater Plutonio contracts, as described in further detail in 'Other Subsequent Events'.

Background and recent history

A publicly traded company since May 1993, the Company was established through the merger of the businesses of two leading diving support services companies, Comex Services S.A. and Stolt-Nielsen Seaway A/S, which were acquired by SNSA in separate transactions in 1992. At the time of acquisition, Comex Services S.A. was a leading world-wide subsea services contractor, which pioneered deepwater saturation diving and subsea construction using both manned and unmanned techniques. Stolt-Nielsen Seaway A/S operated principally in the North Sea and pioneered the development and use of specially designed, technologically sophisticated diving support ships and remotely operated vehicles ('ROVs') to support operations in hostile deepwater environments.

In August 1998, the Company acquired the Houston-based Ceanic Corporation ('Ceanic'), a publicly traded subsea contractor, for approximately \$219 million. Ceanic provided a range of subsea services and products to the offshore oil and gas industry in the Gulf of Mexico and inland underwater services to domestic and governmental customers. With this acquisition the Company acquired a substantial fleet of ships mostly designed for shallow water work, ROVs and other related technologies. The Company's acquisition of Ceanic was strategically important in

that it provided significant operations in the Gulf of Mexico. These operations, combined with the Company's deepwater technology and expertise, allow the Company to participate in the growing deepwater construction market in the Gulf of Mexico.

In December 1998, the Company acquired the ROV business of Dolphin A/S for \$16.9 million. This acquisition, which included 21 ROVs mostly on long-term contracts to Norwegian oil companies, strengthened the Company's position in the ROV drill support market in Norway.

On 7 December 1999, the Company completed a transaction to form a joint venture entity, NKT Flexibles, a manufacturer of flexible flowlines and risers for the offshore oil and gas industry. The Company owns 49% of NKT Flexibles and the remaining 51% is owned by NKT Holdings A/S. The total consideration for the Company's share in the joint venture was \$36 million, funded partly by cash and partly by the issuance of Class A Shares. This investment secured the Company's supply of flexible pipeline products. During fiscal year 2003, Stolt Offshore contributed a further \$12.6 million of capital.

On 16 December 1999, the Company acquired the French offshore construction and engineering company ETPM S.A. ('ETPM'), a wholly owned subsidiary of Groupe GTM S.A. Groupe GTM was subsequently acquired by Groupe Vinci S.A. ('Vinci'). The total consideration for this acquisition, including debt assumed, was approximately \$350 million, funded partly by cash and partly by the issuance of 6.1 million Common Shares at a guaranteed value of \$18.50 per share. ETPM had a significant market position in West Africa (now a part of the Company's AFMED region), which is now one of the fastest-growing markets for the Company's services. In order to fund these investments, in February and May 2000, the Company issued a total of 19.7 million Class A Shares to SNSA for approximately \$200 million. These Class A Shares have since been converted to Common Shares on a one-for-one basis.

On 18 July 2001, the Company acquired the Paris-based engineering company Ingerop Litwin S.A. from Vinci. On 4 September 2001, the Company acquired a controlling interest in the Houston-based engineering company, Paragon Engineering Services, Inc. The consideration paid for these two acquisitions was \$16.7 million, including deferred consideration in respect of Paragon. This included \$4.3 million, which was the net present value of deferred consideration in relation to the Paragon Companies, which is due for payment in March 2005 and is discussed further below in 'Businesses and assets offered for sale'. The intent of these acquisitions at the time was to add conceptual design and detailed engineering skills as a stand-alone resource for the Company. These functions will in the future be performed by engineering departments embedded with the individual regions, rather than being provided by separate subsidiary companies. As described in 'Businesses and assets offered for sale', these two companies have been identified for divestment.

In August 2002, the Company sold the assets of Big Inch Marine Systems, Inc, a wholly owned subsidiary located in Houston, Texas, specialising in the design and manufacture of connection flanges for large diameter subsea pipelines. This disposal realised \$23.5 million of proceeds, and resulted in a gain on sale of \$8.0 million.

On 20 February 2004, the Company and the Sonastolt joint venture sold to Oceaneering International Inc. their ROV drill support business, consisting of a fleet of 44 ROVs and certain ancillary equipment, together with related contracts and employees, for approximately \$48 million. The Company's share of net proceeds was \$28 million, excluding proceeds due to the Sonastolt joint venture and transaction costs, and a gain of \$5.5 million on disposal was recorded in the first quarter of fiscal year 2004.

Business segments

During fiscal year 2003, the Company realigned the geographical segments it uses to manage its business. The Company consolidated its United Kingdom, Norwegian and Eastern Canadian operations into the NEC region and redefined its remaining geographic segments. Each region is headed by a vice president who is responsible for managing all aspects of the projects within the region, from initial tender to completion. Under its new management structure, each region is accountable for profits and losses for such projects.

The Company's operations are managed through seven regional offices: Nanterre, France (for the AFMED region); Aberdeen, United Kingdom (for the United Kingdom area) and Stavanger, Norway (for the Norwegian area) for the NEC region; Houston, Texas in the United States for the NAMEX region; Rio de Janeiro, Brazil for the SAM region; Jakarta, Indonesia for the AME region; and Sunbury, United Kingdom for Corporate activities. The Company assembles and constructs offshore infrastructure equipment at fabrication yards in Nigeria, Angola and the United States (New Orleans, Louisiana).

The Company has business segments based on the geographic distribution of the activities as follows:

Segment geographic coverage

Africa, Mediterranean and the Caspian Sea Region (AFMED)

Includes all activities in Africa, the Mediterranean and Caspian Sea, but excludes Azerbaijan

Northern Europe and Canada Region (NEC)

Includes all activities in Northern Europe, Eastern Canada, Greenland and Azerbaijan

North America and Mexico Region (NAMEX)

Includes activities in the United States, Mexico, Central America, and Western Canada

South America Region (SAM)

Includes all activities in South America and the islands of the southern Atlantic Ocean

Asia and the Middle East Region (AME)

Includes all activities in Asia Pacific, India, and the Middle East, but excludes the Caspian Sea

Corporate

Includes all activities that serve more than one region. These include:

- ▶ Paragon Engineering Services, Inc., Paragon Litwin S.A., and Paragon Italia S.r.l. (a subsidiary of Paragon Litwin) which provide engineering services for the onshore and offshore oil and gas industry;
- ▶ NKT Flexibles, a joint venture that manufactures flexible pipeline and risers;
- ▶ Seaway Heavy Lifting Ltd. ('SHL'), a joint venture with a subsidiary of the Russian oil company Lukoil-Kaliningradmorneft plc, which operates the heavy lift ship *Stanislav Yudin*;
- ▶ Serimer DASA, a contract surface welding services entity employed both onshore and offshore by pipelay contractors;
- ▶ Assets which have global mobility including construction and flowline lay support ships, ROVs, trenchers, ploughs, and other mobile assets that are not allocated to any one region; and
- ▶ Management and corporate services provided for the benefit of all the Company's businesses.

Critical accounting policies

The Company's significant accounting policies are described in Note 2 to the consolidated financial statements. The preparation of the Company's financial statements requires management to make estimates and judgements that affect the amounts reported in the Company's financial statements and accompanying notes. The Company bases its estimates on historical experience and on various other assumptions that the Company believes to be reasonable under the circumstances. Actual results may differ from these estimates under different assumptions or conditions. Management has identified the following policies as critical because they may involve a high degree of judgement and complexity.

Project accounting – Revenue recognition and the use of the 'percentage-of-completion' accounting method

Substantially all of the Company's projects are accounted for on the percentage-of-completion method, which is standard for the Company's industry. Under the percentage-of-completion method, estimated contract revenues are accrued based on the ratio of costs incurred to date to the total estimated costs, taking into account the level of physical completion. Estimated contract losses are recognised in full when determined. Contract revenues and total cost estimates are reviewed and revised periodically as work progresses and as change orders are approved, and adjustments based on the percentage of completion are reflected in contract revenues in the reporting period, when these estimates are revised. To the extent that these adjustments result in a reduction or elimination of previously reported contract revenues or costs, the Company would recognise a charge against current earnings that may be significant depending on the size of the project or the adjustment.

The percentage-of-completion method requires the Company to make reasonably dependable estimates of progress toward completion of such contracts, and contract costs. As discussed in 'Revision of estimates on major projects', in fiscal years 2002 and 2003, the Company experienced frequent and significant deterioration of results as compared with original estimates with respect to results relating to a number of projects, including the Conoco CMS 3, Bonga, Burullus and OGGs projects. Although actual results differed significantly from original estimates on these projects, the Company does not believe its original estimates were unreliable. Rather, the Company believes it sufficiently assesses its business risks in a manner that allows it to evaluate

Management's discussion and analysis continued

the outcomes of its projects for purposes of making reasonably dependable estimates. Nevertheless, the Company's business risks have involved, and will continue to involve, unforeseen difficulties, including weather, economic instability, labour strikes, localised civil unrest, and engineering and logistical changes, particularly in major projects. The Company does not believe its business is subject to the types of inherent hazards described in AICPA Statement of Position ("SOP") No. 81-1 'Accounting for Performance of Construction-Type and Certain Production-Type Contracts', that would indicate that the use of the percentage-of-completion method is not preferable.

If the Company was unable to make reasonably dependable estimates, the Company would be obliged to use the 'zero-estimate-of-profit' method or the 'completed-contract' method. Under the zero-estimate-of-profit method, the Company would not recognise any profit before a contract is completed. Under the completed-contracts method, all costs, revenues and profits are accumulated in the balance sheet accounts until project completion. Under both of these methods, the Company would not recognise project profits until project completion but would recognise a project loss as soon as the loss became evident. If the Company is unable to continue to use the percentage-of-completion method of accounting, the Company's earnings may be materially adversely impacted, resulting in, among other things, a potential default under our Existing Credit Facility Agreements.

Project accounting – revenue recognition on variation orders and claims

A major portion of the Company's revenue is billed under fixed-price contracts. Due to the nature of the services performed, variation orders and claims are commonly billed to the customers in the normal course of business and are recognised as contract revenue where recovery is probable and can be reasonably estimated. In addition, some contracts contain incentive provisions based upon performance in relation to established targets, which are recognised in the contract estimates when the targets are achieved. Many of the delays and cost overruns discussed in 'Revisions of estimates on major projects', were the subject of claims and variation orders. Throughout fiscal year 2003, the Company had significant difficulty resolving these claims and variation orders, and a significant amount of judgement was required to assess collectibility.

Tangible fixed assets, goodwill and other intangible assets

This subject is included under 'Critical accounting policies' due to the subjectivity of the estimates used in determining fair values and preparing cash flow projections for assets over which there are impairment issues and because of the large net book value of such assets.

Fixed assets are recorded at cost, and depreciation is recorded on a straight-line basis over the useful lives of the assets, except for ships, which are considered to have a residual value of 10%. Management uses judgement to estimate the remaining useful life of an asset, particularly when it has been upgraded.

Goodwill represents the excess of the purchase price over the fair value of net assets acquired in a business combination, and is not subject to amortisation. Rather the balance is reviewed for impairment on an annual basis or whenever events or changes in circumstances indicated that the carrying value may not be recoverable. The only goodwill in the Company's balance sheet is \$6.0 million in respect of the acquisition of the Paragon Companies.

In accordance with SFAS No. 144 'Accounting for the Impairment or Disposal of Long-lived Assets', tangible fixed assets, and other intangible assets, subject to amortisation, are required to be reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. In performing the review for recoverability, the Company estimates the future cash flows expected to result from the use of the asset and its eventual disposition. If the undiscounted future cash flow is less than the carrying amount of the asset, the asset is deemed impaired. The amount of the impairment is measured as the difference between the carrying value and the fair value of the asset. The fair value is determined either through the use of an external valuation, or by means of an analysis of future cash flows on the basis of expected utilisation and daily charge-out rates. Where cash flow forecasts are used, any impairment charge is measured by comparing the net present value of future cash flows, discounted using the Company's weighted average cost of capital. Management's judgement is required to determine the appropriate business assumptions to be used in forecasting future cash flows. When the Company records an impairment charge, this creates a new cost base for the assets that have been impaired. The Company has discussed its significant impairment charges in fiscal years 2003, 2002, and 2001 in 'Results of Operations – Impairments'.

In addition, management's judgement was required in applying the criteria for classifying assets held for sale as specified in paragraph 30 of SFAS No. 144. In particular, management was required to assess whether or not it was probable that the sale would be completed within one year, by carefully evaluating the status of

negotiations with potential purchasers of each business and asset. Specifically, the lack of acceptable offers in respect of the ships that have been offered for sale has resulted in their being excluded from the total of assets held for sale. Nevertheless, these assets were separately tested for impairment as described above. Assets held for sale are valued at the lower of carrying amount and fair value, less the cost to sell. Where fair value less costs to sell is lower than the cost, the Company records an impairment charge for the difference.

Recognition of provisions for legal claims, suits and complaints

The Company, in the ordinary course of business, is subject to various claims, suits and complaints. Management, in consultation with internal and external advisers, will provide for a contingent loss in the financial statements if the contingency had been incurred at the date of the financial statements and the amount of the loss can be reasonably estimated. In accordance with SFAS No. 5 'Accounting for Contingencies', as interpreted by FASB Interpretation No. 14 'Reasonable Estimation of the Amount of a Loss', if the Company has determined that the reasonable estimate of the loss is a range and that there is no best estimate within the range, the Company will provide for the lower amount of the range. The provision is subject to uncertainty and no assurance can be given that the amount provided in the financial statements is the amount that will be ultimately settled. The results of the Company may be adversely affected if the provision proves not to be sufficient. The notable legal claims made against the Company are discussed fully in Note 25 to the consolidated financial statements and are summarised in 'Legal matters'.

Income taxes

The Company accounts for income taxes in accordance with SFAS No. 109, 'Accounting for Income Taxes' which requires that the deferred tax assets and liabilities be recognised using enacted tax rates for the effect of temporary differences between book and tax bases of recorded assets and liabilities. SFAS No. 109 also requires that the deferred tax assets be reduced by a valuation allowance if it is more likely than not that some portion of the entire deferred tax asset will not be realised.

As a part of the process of preparing consolidated financial statements, the Company is required to estimate income taxes in each of the jurisdictions in which it operates. This process involves estimating the actual current tax exposure together with assessing deferred tax assets and liabilities based on the difference between the financial statement carrying amounts and the tax bases of assets and liabilities. The Company regularly reviews its deferred tax assets for recoverability and, if it is more likely than not that the deferred tax asset is irrecoverable, the Company establishes a valuation allowance based on historical taxable income, projected future taxable income, and the expected timing of the reversals of existing temporary differences. If the Company continues to operate at a loss or is unable to generate sufficient future taxable income, or if there is a material change in the actual effective tax rates or time period within which the underlying temporary differences become taxable and deductible, the Company could be required to establish a valuation allowance, based on a test of recoverability, against all or a significant portion of its deferred tax assets resulting in a substantial increase in its effective tax rate and a material adverse impact on its operating results.

Accounting for derivatives

It is the policy of the Company to apply hedge accounting in accordance with SFAS No. 133 'Accounting for Derivative Instruments and Hedging Activities' when accounting for derivative instruments such as forward currency contracts and currency swaps. This standard requires gains and losses resulting from changes in the market value of derivative contracts to be deferred in the Company's accounts until such time the underlying transaction affects earnings. It also requires management to ensure that adequate documentation is in place at the inception of the hedging contract to support its treatment as an effective hedge for an underlying business transaction. The judgement of management is required to estimate the fair value of instruments that have no quoted market prices, and forecast the probable date and value of the underlying transaction.

During August 2003, the Company closed out the majority of its foreign exchange positions to ensure that it had sufficient liquidity to fund its operations and to provide for a potentially protracted period of negotiation with certain major customers regarding settlement of claims and variation orders. The Company realised a \$28.2 million gain when these positions were closed. This gain was deferred in Other Comprehensive Income in the Consolidated Statement of Shareholders' Equity and is being released to the income statement in line with the underlying transactions. At 30 November 2003, the gain arising from the closing of the foreign exchange positions which was still deferred in Other Comprehensive Income was \$16.8 million.

At 30 November 2003, the Company did not hold a significant number of derivative instruments as financial institutions were unwilling to provide these instruments because of the Company's weak financial position. As a result, the Company has a significant exposure to future foreign exchange fluctuations, as discussed in 'Market risk, foreign exchange and interest rate exposure'.

Factors affecting the Company's results of operations

Business environment

The market for the Company's services is dependent upon the success of exploration and the level of investment in offshore exploration and production by the major oil companies. Such investment is cyclical in nature.

Following a period of increasing oil prices in recent years, there has been a progressive increase in investment in offshore exploration and production by the major oil companies. The impact of this investment takes time to flow through to the offshore construction sector. The Company expects to see a continued expansion of demand in fiscal year 2004 for its services, with this trend continuing over the next few years. However, management believes that, for offshore contractors to survive, the oil companies which form their customer base will need to share more of the risks and rewards associated with offshore fixed price projects in challenging geographic areas. It is the strategy of the Company to be a fixed price contractor, but it will not accept contractually onerous terms, which it has in the past. As noted above, the Company was less successful in fiscal year 2003 than in previous years in winning new contracts to replenish its order book, particularly for execution during the third and fourth quarters of fiscal year 2004. This is partly attributable to the more stringent tendering practices adopted in fiscal year 2003 as well as other competitive factors. As a result, after eliminating other factors such as disposal of certain assets and businesses, revenues for fiscal year 2004 are expected to be lower than 2003.

Seasonality

Over the past three years, a significant portion of the Company's revenue has been generated from work performed in the North Sea and North America. Adverse weather conditions during the winter months in these regions usually result in low levels of activity, although this is less apparent than in the past due to technological advances. Further, offshore West Africa, optimal weather conditions exist from October to April, and most offshore operations are scheduled for that period. As a result, full-year results are not likely to be a direct multiple of any particular quarter or combination of quarters. Additionally, during certain periods of the year, the Company may be affected by delays caused by adverse weather conditions such as hurricanes or tropical storms in the Gulf of Mexico. During periods of curtailed activity due to adverse weather conditions, the Company continues to incur operating expenses, but the Company's revenues from operations are delayed or reduced.

Ship utilisation

The following table sets forth the average ship utilisation by quarter for the Company's fleets of dynamically positioned Deepwater and Heavy Construction Ships, Light Construction and Survey Ships, and Pipelay Barges and Anchor ships. The utilisation rate is calculated by dividing the total number of days for which the ships were engaged in project-related work in a quarter by 87.5 days per quarter or 350 days annually, expressed as a percentage. The remaining 15 days are attributable to routine maintenance.

Utilisation rate For the year ended 30 November	Qtr 1 %	Qtr 2 %	Qtr 3 %	Qtr 4 %	Year %
Deepwater and Heavy Construction Ships					
2003	79	75	92	64	77
2002	72	84	82	82	80
2001	80	85	93	94	88
Light Construction and Survey Ships					
2003	37	68	61	53	54
2002	68	52	69	57	61
2001	43	52	85	84	66
Trunkline Barges and Anchor Ships					
2003	67	63	61	62	63
2002	63	55	31	46	48
2001	34	47	66	75	56

The progressive decline over the past three years in the utilisation of the Deepwater and Heavy Construction Ships and Light Construction and Survey Ships is evidence of surplus capacity in the Company's fleet, which the Company has reflected in the impairment charges recorded in the fourth quarter of fiscal year 2003 and which is being addressed by the ship disposal programme under way. The bases for recording these impairment charges are described in 'Impairments'.

Utilisation of Deepwater and Heavy Construction Ships was reduced in fiscal year 2003 because of several factors. The *Seaway Kestrel* had 55 days' unpaid transit from Egypt to North America via Norway, and only 10 days' work in the fourth quarter of fiscal year 2003. An impairment charge has been recorded in respect of both the *Seaway Kestrel* and the *Seaway Explorer*, which only had three days' work in the fourth quarter of fiscal year 2003. The utilisation of the *Seaway Falcon* dropped from working 234 to 175 days in fiscal year 2003, with 48 days of dry-dock and eight days unpaid transit. The *Northern Admiral* went off charter at the beginning of fiscal year 2003.

Utilisation of Light Construction and Survey ships was adversely affected in fiscal year 2003 by the *Seaway Legend*, which had 30 days of dry-dock and no work in the fourth quarter of fiscal year 2003. The *Seaway Invincible*, which had no utilisation at all in fiscal year 2003, was offered for sale in September 2003 and sold in March 2004. Impairment charges were booked against both these ships. The *Stephaniturm* and the *Seaway Commander* went off charter at the start of fiscal year 2003.

The increase in utilisation of Pipelay Barges and Anchor ships in fiscal year 2003 was attributable to the high level of activity for the *Seaway Orion*, the *American Star* and the *DLB 801*. Offsetting this was the *LB 200*, which had only 75 days' work during the first quarter of fiscal year 2003, and was then laid-up. An impairment charge of \$55.7 million has been recorded against the *LB 200* pipelay barge.

In fiscal year 2002, the utilisation of all ships was lower than fiscal year 2001 due to the following factors: utilisation of Deepwater and Heavy Construction Ships was reduced due to a decrease in the utilisation of the *Seaway Falcon* which had 50 days of unpaid transit, and the dry-docking of the *Seaway Polaris*. Utilisation of Light Construction and Survey ships was adversely affected by the eight-month lay-up of the survey ship the *Seaway Invincible*. The decrease in utilisation of Pipelay Barges and Anchor ships was due to reduced utilisation of Gulf of Mexico and African fleets, including the *DLB 801*, which was laid up for most of the year, and the *American Recovery*, which was eventually sold later in fiscal year 2002.

In fiscal year 2004, the Company expects ship utilisation to decline further due to the lack of demand for certain ships and barges, most notably the *LB 200* pipelay barge, which is expected to have a dry-dock for approximately 60 days in fiscal year 2004 and to remain unutilised until the start of the Langed project in 2005. The overall utilisation rate is expected to improve if the current ship disposal programme is successful in eliminating surplus ship capacity, but the outlook is not sufficiently favourable as to obviate the need to record impairment charges against certain assets which are held for use, notably the *LB 200*, the *Seaway Kestrel* and the *Seaway Explorer*.

Revisions of cost estimates on major projects

During the course of major projects the original estimate for the current period and/or future periods may change. The effect of such a change, which can be positive or negative, is accounted for in the period of change. These revisions to estimate will not result in restating amounts in previous period. Revisions of estimates are calculated on a regular basis.

In fiscal year 2003, there was a negative impact of \$216.0 million attributable to revisions of estimates on major projects as compared to \$58.8 million negative impact in fiscal year 2002 and a positive impact of \$2.4 million in fiscal year 2001. The most significant revision to estimates occurred on the following projects:

- ▶ \$67.8 million of losses were recorded on the \$200 million lump sum SURF project offshore Nigeria (AFMED region) for Shell Nigeria ('SNEPCO') (the 'Bonga project'), due primarily to the following factors: the *Seaway Polaris* was delayed on previous projects and arrived to perform the work later in the season than planned, involving more downtime for cargo barges and tugs; the customer required the Company to invest considerably more than expected in proving engineering solutions before their acceptance; the poor performance of the *Seaway Polaris* resulted in extended costs and additional project management costs were incurred due to the extended duration on the project. This is a loss-making contract and as of 30 November 2003 the Company has provided fully for the estimated loss. A \$4.8 million negative revision to estimate also occurred on this project in fiscal year 2002. As of 30 November 2003, this project was 71% complete. As of the end of March 2004, this project was 79% complete.

Management's discussion and analysis continued

- ▶ \$51.7 million of losses were recorded on the \$145 million Conventional project for the Burullus Gas Company in the Scarab/Saffron Field off the coast of Egypt (the 'Burullus project'). This downgrade was caused by a number of unforeseen difficulties, including the priority assigned by the client to meeting the promised first gas date, which resulted in 20 additional *Seaway Hawk* and *Seaway Kestrel* days; dewatering operations which led to 62 additional *Seaway Hawk* days and 16 additional *Seaway Kestrel* days; soil and trenching problems necessitated the mobilisation of a new set of equipment; and an umbilical entanglement required 50 additional *Seaway Kestrel* days. There were overruns on project management, engineering, and logistics costs. This is a loss-making contract and as of 30 November 2003 the Company had provided fully for the estimated loss. A \$35.2 million downgrade was also recorded on the Burullus project in fiscal year 2002. This project was completed in the third quarter of fiscal year 2003.
- ▶ \$41.5 million of losses occurred on the \$240 million lump sum Conventional project offshore Angola (AFMED region) for Chevron Texaco (the 'Sanha Bomboco project'), due to several factors: engineering costs exceeded budgeted costs because design and installation engineering had to be reworked due to the change of installation vessels (which had secondary impacts on procurement and fabrication), and the change of concept in favour of a single lift module; the electricity and instrumentation engineering involved rework, delay in completion and schedule clashes; and procurement for existing platforms overran due to underestimated work for module fabrication. Offshore operations overran due to a change of vessels; subcontractor problems were caused by under-estimating costs of contracts and changes in scope; there were overruns on transport, fabrication at Lobito and hook-up costs. This is a loss-making contract and as of 30 November 2003 the Company had provided fully for the estimated loss. As of 30 November 2003, the project was 72% complete. As of the end of March 2004, this project was 92% complete.
- ▶ \$29.3 million of losses were recorded on the \$135 million lump sum Conventional offshore gas gathering system project (the 'OGGS project') offshore Nigeria (AFMED region) for Shell Petroleum Development Company of Nigeria Limited ('SPDC'), acting on behalf of itself and partners, including the Nigerian National Oil Company, due primarily to several unforeseen incidents and events which disrupted the project. These included community unrest and strikes which led to extended standby periods for the *Seaway Orion* and the *LB 200*; a barge was beached with a cargo of pipes; the *Challenger* survey ship was hijacked for a week; the supply of coated pipe to the *LB 200* from the subcontractor's yard was inadequate. This project was completed in the fourth quarter of fiscal year 2003.
- ▶ \$16.1 million of losses were recorded on the \$83 million combined lump sum and day rate Conventional project in the United States (NAMEX region) for Algonquin Gas Transmission Company, a subsidiary of Duke Energy Field Services, LLC (the 'Duke Hubline project'), due primarily to a disagreement with the client over responsibility for budget overruns on the cost-plus element of the project. As discussed in 'Legal matters', this dispute was settled amicably in February 2004, in line with the \$37 million receivable recorded as of 30 November 2003. This project was completed in the fourth quarter of fiscal year 2003.

During fiscal year 2003, the Company modified its estimating, tendering and contracting procedures in order to reduce the amount of unanticipated costs and improve the Company's ability to recover costs from its customers. Greater selectivity is exercised in choosing which tenders to respond to, and a thorough analysis of the commercial and operational risks as well as a detailed tender budget is prepared in order to facilitate the decision to tender. Careful consideration is given to vessel schedule conflicts and to the current backlog to ensure the Company has sufficient resources to perform its obligations.

Under these revised procedures, when a target project is identified by the Company's regional marketing staff, the decision to prepare and submit a competitive bid is taken by Management in accordance with delegated authority limits. Cost estimates are prepared on the basis of a detailed standard costing manual, and the selling price and contract terms are based on the Company's minimum commercial standards and market conditions. Before the tender package is submitted to the customer, it is subject to detailed review; this review is performed by representatives of regional, legal and finance departments; major project tenders are also subject to approval by the Company's senior management, and very large tenders are also subject to approval by the Chief Operating Officer, the Chief Executive Officer or the Company's Board of Directors. The information required to be contained in the internal review packages is uniform across the Company, in order to allow management to consistently weigh the risks and benefits of tenders for various projects. A separate Estimating Department has been created in the AFMED region to centralise the expertise on making reasonably dependable estimates of contract revenues and contract costs.

Management strictly applies its strengthened contracting principles in respect of not undertaking variations to work scope without prior agreement of scope, schedule and price.

Businesses and assets offered for sale

As a part of its new strategic focus, the Company identified a number of assets and businesses which it no longer considers essential to be performed in-house in order to execute core operations. Services such as surveying, surface welding and ROV drill support services are not central to the Company's focus on the SURF market. Nevertheless, such services will remain part of the Company's project bidding and when customers in the future require such services, the Company will purchase them from third parties. Further, the Company has reorganised its engineering functions and integrated them into the regional structure. Consequently, the Company no longer requires engineering services to be provided by the Paragon Companies, which have been offered for sale. These businesses do not meet the criteria for disclosure as discontinued operations, either because the Company expects to sign an agreement for continuing utilisation of those businesses on an outsourced basis, or because the operations will continue to be performed in-house at a lower level of operation. In addition, the Company has designated a number of other operating assets that it considers duplicative or that could be more cost-effectively procured through outsourcing.

The business and assets offered for sale as of 30 November 2003 are further discussed as follows:

1. ROV drill-support: This business involves around 200 employees world-wide, 44 ROVs and certain ancillary equipment, together with related contracts, and is operated from bases in West Africa, South America and the North Sea. On 20 February 2004, the Company and the Sonastolt joint venture in Angola with Sociedade Nacional de Combustiveis de Angola – Sonangol U.E.E. ('Sonangol'), which is majority owned (55%) by the Company and provides local offshore support personnel and equipment, sold this business to Oceaneering International, Inc. for a sale price of approximately \$48 million. The Company received approximately \$28 million in cash after settling the interests of Sonangol, its joint venture partners in Angola, and transaction costs.
2. Serimer DASA: This is a wholly owned specialised surface welding services and welding equipment manufacturing company with its head office near Paris, France. In addition, the Company has a sales office in Texas, United States. Serimer DASA provides automatic surface welding services primarily to offshore pipelaying contractors. The Company expects to dispose of this business by the end of the second quarter of fiscal year 2004.
3. Paragon Companies: This includes Paragon Engineering Holdings Inc., Paragon Engineering Services Inc, Paragon Litwin, and Paragon Italia S.r.l.. These engineering businesses, which were acquired in fiscal year 2001, are expected to be sold by the end of the second quarter of fiscal year 2004. Certain of the engineering services they have provided to the Company will be re-integrated into the Company's business, and the Company expects to retain approximately 100 engineers from the Paragon Companies.
4. Survey Business: This business consists of two owned ships (the *Seaway Legend* and the *Elang Laut*), one ship on charter (the *Seaway Petrel*), their marine equipment, spare parts and additional equipment, including five survey ROVs. The Company intends to sell this business by the third quarter of fiscal year 2004. The Company intends to outsource its survey work to the buyer of this business.
5. Assets in the Lobito Yard, Angola: A large quantity of equipment located in the Lobito Yard on long-term lease to Sonamet Industrial S.A.R.L. ('Sonamet'), a joint venture with Sonangol in which the Company has a 55% interest, was under negotiation for sale to Sonamet at 30 November 2003. The sale was completed in the first quarter of fiscal year 2004 for no gain or loss.
6. Since 30 November 2003 the Company has disposed of the *Annette*, the *Seaway Rover*, the *Seaway Invincible* and the *Seaway Pioneer*. Proceeds from these sales were \$3.0 million and were received during the first and second quarter of fiscal year 2004, and a gain of \$0.6 million in total was recorded.

Ships

The Company has identified the following ships for sale as of 30 January 2004:

- ▶ The *Seaway Kingfisher*, a 90-metre dedicated inspection, maintenance and repair construction ship, which was acquired in 1998 through a joint venture in which the Company owns a 50% interest.
- ▶ The *Seaway Kestrel*, a 98-metre dynamically positioned reeled flex-lay, pipelay and diving support ship, which the Company acquired as part of the ETPM acquisition in 1999.
- ▶ The *Seaway Explorer*, an 81-metre dynamically positioned subsea construction ship, which the Company acquired as part of the ETPM acquisition in 1999.

The Company is not confident of selling the *Seaway Kestrel* and the *Seaway Explorer* within 12 months, because the market for dynamically positioned offshore support ships over ten years old is limited, and the Company's goal is to obtain an acceptable price for the ships. For that reason not all ships that are described as offered for sale meet the criteria requiring them to be included in the total of assets held for sale.

Furthermore, the *American Eagle* was sold in the fourth quarter of fiscal year 2003 and the *Annette*, the *Seaway Rover*, the *Seaway Pioneer* and the *Seaway Invincible* were sold in the first and second quarters of fiscal year 2004, resulting in a gain of \$0.6 million.

Exchange rates

The Company reports its financial results in US dollars. It has foreign currency denominated expenses, assets and liabilities. As a consequence, movements in exchange rates can affect the Company's profitability, the comparability of its results between periods and the carrying value of its assets and liabilities.

When the Company incurs expenses that are not denominated in the same currency as the related revenues, foreign exchange rate fluctuations could adversely affect its profitability. The majority of the Company's net operating expenses are denominated in the functional currency of the individual operating subsidiaries. The US dollar is the functional currency of the most significant subsidiaries within the AFMED, NAMEX, SAM and AME regions. In the NEC region, the functional currencies are the Norwegian kroner, Canadian dollar, US dollar and the British pound sterling. The Company's exposure to currency rate fluctuations results from its net investments in foreign subsidiaries, primarily in the United Kingdom, Norway, France and Brazil, and from its share of the local currency earnings in its operations in the AFMED and NEC regions. The Company is also exposed to fluctuations in several other currencies resulting from operating expenditures and one-off liabilities. With the exception of the AFMED region, the Company's operating expenses are generally denominated in the same currency as associated revenues, thereby mitigating the impact of exchange rate movements on operating profit. In the case of the AFMED region, where revenues are substantially all in US dollars, and expenditures are principally in euros, the Company may use derivative instruments to hedge the foreign exchange exposure. See 'Market risk, foreign exchange and interest rate exposure' below.

In addition, even where revenues and expenses are matched, the Company must translate non-US dollar denominated results of operations, assets and liabilities to US dollars to prepare its consolidated financial statements. To do so, balance sheet items are translated into US dollars using the relevant exchange rate at the fiscal year-end for assets and liabilities, and income statement and cash flow items are translated using exchange rates which approximate the average exchange rate during the relevant period. Consequently, increases and decreases in the value of the US dollar versus other currencies will affect the Company's reported results of operations and the value of assets and liabilities in the consolidated balance sheet even if the Company's results of operations or the value of those assets and liabilities has not changed in their original currency.

The Company's major foreign currency exposures are to the euro, British pound sterling and Norwegian kroner. Until August 2003, the Company managed these exposures by entering into derivative instruments. During August 2003, the Company closed out the majority of its foreign exchange positions. At 30 November 2003, the Company did not hold a significant number of derivative instruments as financial institutions were unwilling to provide these instruments as a result of the Company's weak financial position. As a result, the Company has a significant exposure to future foreign exchange fluctuations. See Note 26 to the consolidated financial statements.

Impairment charges

As discussed in 'Consolidated results – Impairments' below, the Company recognised aggregate impairment charges of \$176.5 million in fiscal year 2003 in respect of its tangible fixed assets.

Restructuring charges

As described in 'Consolidated results – Restructuring charges' below, \$16.2 million was incurred in connection with the Company's plan for financial recovery, which included the elimination of non-essential businesses or businesses that can be outsourced, and the restructuring of the Company's cost and asset base.

Results of operations

Summary of major projects

Angostura project

A lump sum Conventional project offshore Trinidad and Tobago (NAMEX region), under execution during 2003 to 2004 for BHP Billiton.

Bonga project

A lump sum SURF project offshore Nigeria (AFMED region), executed during 2001 to 2004 for Shell Nigeria ('SNEPCO').

Burullus project

A lump sum SURF project offshore Egypt (AFMED region) executed during 2001 to 2003 for the Burullus Gas Company.

Conoco CMS 3 project

A lump sum SURF project offshore United Kingdom (NEC region) executed during 2001 to 2003 for ConocoPhillips (UK) Ltd.

Duke Hubline project

A combined lump sum and day rate Conventional project in the United States (NAMEX region), executed during 2002 to 2003 for Algonquin Gas Transmission Company, a subsidiary of Duke Energy Field Services LLC.

Erha project

A lump sum SURF project offshore Nigeria (AFMED region), to be executed during 2002 to 2006 for ExxonMobil Nigeria ('EEPNL').

Girassol project

A lump sum SURF project offshore Angola (AFMED region), comprising the building and installation of two riser towers in 1,400 metres of water and the installation of associated pipelines and umbilicals, executed during 1998 to 2003 for a consortium led by Total Angola. This project was performed as a joint venture with Saipem S.A.

OGGS project

A lump sum Conventional offshore gas gathering system project offshore Nigeria (AFMED region), executed during 2002 to 2004 for Shell Petroleum Development Company of Nigeria Limited ('SPDC'), acting on behalf of itself and partners, including the Nigerian National Oil Company.

Sanha Bomboco project

A lump sum Conventional project offshore Angola (AFMED region) under execution during 2002 to 2004 for ChevronTexaco led by Cabinda Gulf Oil Company (CABGOC).

Shell EA project

A lump sum EPIC project executed during 2001 to 2003 for Shell in Nigeria (AFMED region).

Skirne Byggve project

A lump sum SURF project offshore Norway (NEC region) executed during 2002 to 2003 for Total.

Yokri project

A lump sum Conventional project in Nigeria (AFMED region) under execution during 2001 to 2004 jointly with a local partner for SPDC, acting on behalf of itself and partners, including the Nigerian National Oil Company.

Management's discussion and analysis continued

Business segment results

The following tables show annual net operating revenue and net (loss) income before tax (after minority interests) for each of the Company's business segments for the past three fiscal years.

For the year ended 30 November (in millions)	2003 \$	%	2002 \$	%	2001 \$	%
Net operating revenue						
AFMED	673.8	45.4	702.7	48.9	520.2	41.5
NEC	387.6	26.2	335.6	23.3	325.3	25.9
NAMEX	200.6	13.5	190.5	13.3	276.7	22.0
SAM	56.0	3.8	52.0	3.6	50.5	4.0
AME	26.8	1.8	25.7	1.8	39.4	3.1
Corporate	137.5	9.3	131.0	9.1	43.8	3.5
Total	1,482.3	100.0	1,437.5	100.0	1,255.9	100.0

For the year ended 30 November (in millions)	2003 \$	%	2002 \$	%	2001 \$	%
Net (loss) income before tax (after minority interests)						
AFMED	(285.2)	(68.1)	(36.6)	(25.5)	24.5	382.8
NEC	23.1	5.5	10.8	7.5	13.0	203.1
NAMEX	(32.3)	(7.8)	(116.0)	(80.7)	(36.2)	(565.5)
SAM	18.2	4.3	5.4	3.8	5.5	85.9
AME	(6.6)	(1.6)	(3.3)	(2.3)	0.0	0.0
Corporate	(136.0)	(32.4)	(4.0)	(2.8)	(0.4)	(6.3)
Total	(418.7)	(100.0)	(143.7)	(100.0)	6.4	100.0

Africa, Mediterranean and Caspian Sea region (AFMED)

Net operating revenue

AFMED's net operating revenue decreased marginally in fiscal year 2003 by \$28.9 million to \$673.8 million. The continued high level of activity in West Africa on the major Conventional and SURF projects (the OGGs and Yokri projects for SPDC, the Bonga project for SNEPCO and the Sanha Bomboco project for ChevronTexaco) were the main drivers for the sustained high level of revenue, generating 64% of the revenues for fiscal year 2003. The Burullus and OGGs projects were completed in fiscal year 2003 and ongoing disputes with the respective customers settled in the first quarter of fiscal year 2004 in line with the reported position at 30 November 2003. It is anticipated that the Bonga, Sanha Bomboco and Yokri projects will be completed in fiscal year 2004, while the Erha project will continue until 2006.

Net operating revenue in fiscal year 2002 was \$702.7 million, up from \$520.2 million in fiscal year 2001. This increase was largely due to high levels of activity in Nigeria with the Shell EA, Yokri and OGGs projects running in conventional water depths for Shell, and the TotalFinaElf Amenam project close to completion. Some of these projects had negative margins due to problems with tendering, execution, Nigeria fabrication/sourcing obligations, and logistics. Much activity took place in Egypt on the Burullus project. Turnover in Angola was down from its fiscal year 2001 level due to lower activity on the lump sum SURF project offshore Angola for a consortium led by Total Angola (the 'Girassol project').

Revenue for fiscal year 2004 is expected to be more in line with lower 2001 levels, as the major ongoing projects of the last couple of years are fully completed, and the start-up phase commences on the BP Greater Plutonio project (discussed in 'Other subsequent events') below. As a result, the offshore activity levels are expected to significantly decrease in the second half of the year, with a sharp drop in the utilisation of key assets such as the *Seaway Polaris*. A significant increase in offshore activity is foreseen for 2005 although the senior management of the AFMED region is seeking to target a turnover of around \$500-\$550 million per annum while project management resources are strengthened and other key organisational issues relating to the recent headcount reduction are tackled.

Net (loss) income before tax

In fiscal year 2003 AFMED reported a net loss before tax of \$285.2 million. This is mainly due to \$65.1 million of fixed asset impairment charges together with negative revisions on several large loss-making contracts, including the OGGs, Sanha Bomboco, Bonga and Burullus projects. As discussed in 'Revisions of estimates on major projects', settlement on all outstanding claims and variation orders on the OGGs and Burullus projects was achieved with the respective customers in fiscal year 2004, and the impact has been fully reflected in fiscal year 2003 results because the settlements related to work completed before 30 November 2003.

The net result before tax for fiscal year 2002 was a loss of \$36.6 million compared with a net income before tax of \$24.5 million in fiscal year 2001. This degradation in trading performance was due to loss-making turnkey projects, mainly the OGGs and Burullus projects.

The Company believes that AFMED's prospects for fiscal year 2004 are better than in fiscal year 2003, assuming the remaining loss-making contracts (including the Bonga, Sanha Bomboco and Yokri projects) can be successfully concluded. Although the anticipated losses at completion of these projects have been provided for in the fiscal year 2003 accounts, there are considerable risks with the remaining work to be performed on these projects, and any losses over and above those provided in fiscal year 2003 will affect the fiscal year 2004 results. As noted in 'Other subsequent events', significant additional costs to completion have been identified on the Sanha Bomboco and Bonga projects in March 2004. The offshore activities of projects with more acceptable margins, including the Benguela Belize, Erha, and Okpoho projects, are expected to have a positive impact on the results for fiscal year 2004. However the lower level of ship utilisation anticipated in the second half of fiscal year 2004 will depress the overall results for the AFMED region. The Company is trying to secure short-term charter work to minimise this effect.

Northern Europe and Canada region (NEC)

Net operating revenue

NEC's net operating revenue increased by \$52.0 million to \$387.6 million in fiscal year 2003. Offshore activity was particularly high in the Norwegian sector of the North Sea with the Vigdis Extension and Skirne Byggve projects being completed during the year. In the Dutch sector the NAM K7 and K15 SURF project for Nederlandse Aardolie Maatschappij B.V. was also satisfactorily completed during fiscal year 2003. Revenue from the significant IMR project for BP was lower than the previous year. Other significant projects performed during the year included Draugen for Norsk Shell A/S and Lyse Rogass for Lyse Rogass A/S in the Norwegian sector and Cleaver Bank for Shell UK Exploration in the U.K. sector.

Fiscal year 2003 ended on a commercially successful note with the Langed contract award from the Ormen Lange licence group, for a North Sea pipeline that will be the longest in the world. This contract, which is worth approximately \$250 million represents full utilisation of the *LB 200* pipelay barge in 2005 and 2006.

Net operating revenue increased to \$335.6 million in fiscal year 2002 from \$325.3 million in fiscal year 2001. In the Norwegian sector, there was a difficult market situation in both fiscal years 2002 and 2001, with no significant conventional lump sum or pipelay projects. The small increase in fiscal year 2002 revenue was mainly related to the activity level in the subsea construction market. In the U.K. sector in fiscal year 2002 there was a continuation of the increased project activity from fiscal year 2001, including a Number of SURF projects (notably the Conoco CMS 3 project, ATP Helvellyn for Bluewater Industries Inc. and Mirren and Madoes for BP Exploration), as well as the ongoing IMR contracts.

The Company expects NEC's revenue in fiscal year 2004 to be lower than in fiscal year 2003 due to the lack of larger SURF projects in the current backlog, with the majority of the SURF projects to be executed in fiscal year 2004 being for shorter duration with lower revenue levels. Current indications are that activity levels on the various IMR frame agreements within the NEC region will be similar to fiscal year 2003.

Net (loss) income before tax

In fiscal year 2003, NEC reported net profit before tax of \$23.1 million, which includes \$0.1 million for fixed asset impairment charges and unbilled receivables of \$6.1 million on the Conoco CMS 3 written off in fiscal year 2003. Technical problems were encountered on the Skirne Byggve project and it is anticipated that the rectification works associated with these will result in insurance claims being submitted in fiscal year 2004. The anticipated expenditure associated with the rectification work has been estimated at \$10.0 million and has been fully provided for in the fiscal year 2003 results pending the outcome of these claims. The Allseas Corrib project was terminated as a consequence of the ultimate customer not having received all of the planning permissions required for the project to proceed. Termination negotiations are completed and the Company has recovered all costs incurred, but will lose the revenues and profits that it expected.

The net result before tax for fiscal year 2002 was a profit of \$10.8 million compared with a net income before tax of \$13.0 million in fiscal year 2001. This included an adverse variance attributable to the Conoco CMS 3 project. Seabed soil conditions encountered during the project differed significantly from those that had been anticipated, leading to significant increases in the duration of work and associated expenditures. The figures for fiscal year 2001 included two Norwegian loss-making projects with a total loss of \$4.9 million.

The Company anticipates that the net income before tax for fiscal year 2004 of the NEC region will improve in comparison with fiscal year 2003, based on current backlog figures and forecast margins.

North America and Mexico region (NAMEX)

Net operating revenue

NAMEX's net operating revenue in fiscal year 2003 increased by \$10.1 million to \$200.6 million. The major Conventional project undertaken and completed in the year was the Duke Hubline project, and the region commenced the start-up phase on the Conventional Angostura Project for BHP Billiton in Trinidad and Tobago. The level of SURF activity was lower than the previous year due to lack of a dedicated SURF ship available in the NAMEX region. However, IMR activity levels were higher than prior years as a result of continued hurricane repair work in the first quarter related to damage to offshore installations from Hurricane Lili in the Gulf of Mexico.

Net operating revenue in fiscal year 2002 decreased to \$190.5 million from \$276.7 million in fiscal year 2001. This was due to reduced activity on the pipelay project for Gulfstream Natural Gas LLC that was completed in early fiscal year 2002, and reduced subsea construction activity as a result of depressed market conditions. There was an upturn in activity in the final quarter of fiscal year 2002 to repair damage caused by Hurricane Lili.

The Company expects NAMEX's revenue prospects for fiscal year 2004 to be slightly lower than for fiscal year 2003, because the projects to be performed are smaller than in fiscal year 2003. The Company's potential for SURF work in fiscal year 2004 has improved as a result of the addition of a year-round dedicated ship in the region. In addition, the Company's work on the second phase of the Angostura project will continue, and the segment is actively pursuing other Conventional projects in the Caribbean.

Net (loss) income before tax

Net loss before tax for NAMEX was \$32.3 million in fiscal year 2003, which includes \$12.4 million of tangible fixed asset impairment charges, compared to a net loss of \$116.0 million in fiscal year 2003. The majority of this loss was generated in the Conventional business segment and is attributable to the Duke Hubline project, where unexpected extreme weather conditions, poor sub-contractor performance and changes in site conditions resulted in disputes over the level of charges invoiced to the customer on a cost plus basis. The region's reported net loss for fiscal year 2003 reflects the full impact of the settlement that has now been achieved with Duke Energy on all outstanding invoices, receivables and claims.

The net result before tax for fiscal year 2002 was a loss of \$116.0 million compared with a net loss before tax of \$36.2 million in fiscal year 2001. This is largely due to the \$103.0 million goodwill impairment charge relating to the 1998 acquisition of Ceanic. Offsetting the impairment charge in 2002 were the gain of \$8.0 million on the asset sale of Big Inch Marine Systems, as well as improved results on subsea construction projects. There was a neutral result on the Gulfstream project.

The Company expects NAMEX's net results for fiscal year 2004 to improve now that the loss-making Hubline project is completed and due to, among other things, changes implemented by the Company with respect to managing contract risks.

South America region (SAM)

Net operating revenue

SAM's net operating revenue increased in fiscal year 2003 by \$4.0 million to \$56.0 million. The increase was mainly due to the very high ship utilisation on the two long-term charter contracts operating in the SAM region. Moreover, the other regional assets operating in Brazil, including contracts for ROV drill support and survey, also performed well in fiscal year 2003, with improved utilisation levels compared to fiscal year 2002.

Since fiscal year 2002, when the Company's office in Argentina was closed, all of the revenues of the SAM segment are generated in Brazil. Net operating revenue in fiscal year 2002 increased slightly to \$52.0 million from \$50.5 million in fiscal year 2001 due to the continued good performance and stable utilisation levels of the long-term charters.

Management's discussion and analysis continued

Net (loss) income before tax

Net profit before tax for SAM was \$18.2 million in fiscal year 2003, an increase of \$12.8 million from fiscal year 2002. The increase is primarily attributable to the increasing benefits of performing recurring work under long-term contracts, allowing the segment to benefit from cumulative years of operational experience and knowledge in specialised services that reduce contract risks and improve performance year-on-year. The net profit for fiscal year 2002 of \$5.4 million was virtually unchanged from the fiscal year 2001 result.

The increase of regional profitability for fiscal year 2003, compared to both fiscal years 2002 and 2001, has been due to a number of factors including a record level of asset utilisation, a reassessment of future maintenance requirements, and a change in the basis of allocation of certain ship fixed costs, including depreciation.

Revenue in SAM for fiscal year 2004 is expected to be marginally lower than in fiscal year 2003 and the level of operating profits will also be lower than the exceptional level achieved in fiscal year 2003, but both still are expected to be higher than the historical levels of fiscal years 2002 and 2001.

Asia and the Middle East region (AME)

Net operating revenue

AME's net operating revenue increased marginally in fiscal year 2003 by \$1.1 million to \$26.8 million. The majority of the revenue in fiscal year 2003 continued to be derived in Indonesia from shallow water IMR, Conventional and survey projects, where the activity levels were still lower than expected and well below the high level achieved in fiscal year 2001.

Net operating revenue in fiscal year 2002 decreased by \$13.7 million to \$25.7 million from \$39.4 million in fiscal year 2001 due to a downturn in the market for construction and shallow water work in Indonesia and drill support ROV work throughout the AME region.

The Company expects revenues in AME for fiscal year 2004 to be higher than those experienced in fiscal year 2003, as several larger projects in Indonesia are already in hand and are due to be executed in fiscal year 2004. In addition, the AME region has been expanded and strengthened commercially to take responsibility for the growing markets of India and the Middle East.

Net (loss) income before tax

AME's net result before tax was a loss of \$6.6 million, compared to a net loss before tax of \$3.3 million in fiscal year 2002. This is mainly attributable to the low volume of overall activity in Indonesia, which has resulted in an under-utilisation of certain regional assets, as well as continuing competitive pricing pressures, which have depressed project margins. The deterioration in the net loss to \$3.3 million in fiscal year 2002 from a break-even result in 2001 was attributable to a write-down of assets due to a goodwill impairment charge of \$1.6 million in respect of the Indonesian subsidiary, and to a drop in market conditions for construction and drill support ROVs.

The Company believes that AME will achieve improved net results in fiscal year 2004, as AME expects to see higher activity levels and improved asset results, due to the disposal of several underperforming assets (eight ROVs, three air dive units, and two small drilling rigs) which took place in the first quarter of fiscal year 2004.

Corporate

Net operating revenue

Net operating revenue increased marginally in fiscal year 2003 by \$6.5 million to \$137.5 million. This was attributable to higher sales achieved by Serimer DASA on offshore welding work for customers other than the Company and stable revenue levels in the Paragon Companies.

Net operating revenue increased in fiscal year 2002 to \$131.0 million from \$43.8 million in 2001. Of this increase, \$68.7 million is attributable to the inclusion of revenues from both Paragon Engineering Services, Inc. and Paragon Litwin for a full financial year. In fiscal year 2001, these businesses were only consolidated for part of the year subsequent to each respective acquisition.

Corporate's revenue prospects for fiscal year 2004 are expected to be significantly lower than for fiscal year 2003 levels due to the planned divestment of these non-core businesses, including Serimer DASA and the Paragon Companies in fiscal year 2004.

Net (loss) income before tax

Corporate reported a net loss before tax for fiscal year 2003 of \$136.0 million, compared to a net loss before tax of \$4.0 million in fiscal year 2002. The majority of the overall loss was due to asset write-offs of \$99.0 million on certain Group ships (notably the *Seaway Kestrel* and the *Seaway Explorer*), mobile assets and the Radial Friction Welding ('RFW') ship-mounted welding system, as well as a further net loss of \$10.0 million, being the Company's share of losses from the NKT Flexibles joint venture investment. In addition, restructuring charges totalling \$4.5 million were recorded in Corporate in respect of redundancies, real estate exit costs and professional fees. External consultancy fees in relation to the Company's financial restructuring were \$6.2 million. The remaining losses attributable to Corporate are because insufficient revenue was earned by certain ships and equipment to cover fixed costs, including depreciation.

Corporate reported a net loss before tax for fiscal year 2002 of \$4.0 million compared with a net loss before tax of \$0.4 million in fiscal year 2001. The increased loss in fiscal year 2002 was primarily due to certain non-recurring items related to asset impairments of \$8.1 million and goodwill impairment charges of \$1.8 million on the NKT Flexibles joint venture. Fiscal year 2002 was also affected by under-recoveries of costs on Group ships totalling \$18.0 million.

The expected net income before tax for Corporate for fiscal year 2004 is dependent upon the successful divestment of Serimer DASA and the Paragon Companies, the expenses relating to the refinancing and external advisors' fees, and the level of utilisation of Group assets.

Consolidated results

Net operating revenue

Net operating revenue increased slightly to \$1,482.3 million in fiscal year 2003 from \$1,437.5 million in fiscal year 2002, as the Company worked through its high level of backlog. Net operating revenue in fiscal year 2002 increased to \$1,437.5 million from \$1,255.9 million in fiscal year 2001. This reflects the continued growth in the market for the Company's services, particularly on major projects in AFMED, in addition to increased year-on-year revenue from Paragon Engineering Services and Paragon Litwin, which were acquired during 2001, and which are expected to be sold in 2004.

Equity in net income of non-consolidated joint ventures

Equity in net income of non-consolidated joint ventures in fiscal year 2003 was \$0.4 million, compared to income of \$5.3 million and \$11.7 million in fiscal years 2002 and 2001, respectively. The results for fiscal year 2003 were negatively impacted by the Company's share of losses of \$10.0 million from the investment in NKT Flexibles, which included \$6.6 million with respect to the Company's share of tangible fixed asset impairments. (See 'Results of operations – Impairments'.)

Income in fiscal year 2002 was adversely affected by the Company's share of losses in the NKT Flexibles joint venture of \$14.0 million which included \$8.1 million of tangible fixed asset impairment charges. This was partially offset by \$7.0 million of income in respect of the Company's share of the net income of the Sonamet non-consolidated joint venture, resulting from improved performance of the Lobito Yard in fiscal year 2002.

Selling, general, and administrative ('SG&A') expenses

SG&A expenses in fiscal year 2003 were \$102.5 million, compared to \$89.7 million and \$81.3 million in fiscal years 2002 and 2001, respectively. The increase in fiscal year 2003 was mainly due to external advisors' fees incurred in connection with the financial restructuring programme. The increase in fiscal year 2002 over fiscal year 2001 was due to the introduction of a new management performance incentive scheme, a small number of senior executive redundancy and severance payments, professional fees in connection with an aborted share offering, and increased salary costs for newly hired corporate staff. As discussed in Note 2 to the consolidated financial statements, the reported amounts for fiscal years 2001 and 2002 have been restated to reflect the reorganisation of the Company's management structure.

Impairments

In accordance with SFAS No. 144, long-lived assets, to be held in use, are tested for recoverability whenever events or changes in circumstances indicate that the carrying amount may not be recoverable. Assets held for sale are measured at the lower of cost and fair value less cost to sell. The Company recognised aggregate impairment charges of \$176.5 million in fiscal year 2003 in respect of its tangible fixed assets, as set forth in the following table:

Charges for impairment of Company-owned tangible fixed assets

Ships:

A sales brochure was published in September 2003 by Derrick Offshore, a shipbroker acting for the Company, offering several of the Company's ships for sale. These included the *Seaway Kestrel*, the *Seaway Explorer*, the *Seaway Invincible* and the *Seaway Rover*. The broker provided guidance as to the prices that could be obtained under current market conditions. These prices were at a level substantially below the carrying values of the ships, and were confirmed by a formal valuation in January 2004. An impairment charge was recorded against the carrying value of the several owned ships, measured on the basis of the broker's valuation.

Two categories of assets have been identified based upon the criteria under SFAS No. 144

1) Held for sale – \$2.2m

The *Seaway Invincible* and the *Seaway Rover* meet the 'held for sale' criteria under SFAS No. 144, on the basis that they have been marketed for sale since the final quarter of the fiscal year 2003 and they have been sold since 30 November 2003, for no gain or loss.

2) Held for use – \$42.0m

The *Seaway Kestrel* and the *Seaway Explorer* are being actively marketed, but no sales agreement has yet been concluded, and management does not consider that it will be probable to sell these ships within one year.

LB 200 pipelay barge – \$55.7m

As part of the business restructuring initiated by the Company's new management team, a separate Trunkline business unit was established in the fourth quarter of fiscal year 2003, specifically dedicated to the marketing and operation of the *LB 200* pipelay barge. An in-depth review was then performed to determine the predicted world-wide demand for Trunkline lay, and the available barges capable of performing this type of work. The outcomes from bid processes during the fourth quarter of fiscal year 2003 were also evaluated. This review resulted in a revised forecast of utilisation and future daily charge-out rates for the *LB 200*. The Company estimated that future cash flows attributable to the *LB 200* pipelay barge were less than its carrying value, and an impairment charge was recorded on the basis of a fair value calculation using discounted cash flows. An external ship-broker reviewed this calculation at the Company's request and validated the underlying market assumptions.

Radial Friction Welding (RFW), abandoned – \$42.7m

The RFW programme was started in June 1995 to design and fabricate a high quality ship-mounted welding system for use on 6 to 12-inch flowlines, at a production rate of 200 pipe joints per day. The system was designed not only for welding normal high tensile carbon steels, but also for the emerging premium market for corrosion resistant alloys. However, it proved too large and complex to install on one of the Company's existing ships and fabrication was suspended in December 2000. In fiscal year 2002, the Company launched a joint feasibility study with a third party shipowner to install the equipment on an existing ship, which would be operated as a specialised deep-sea construction ship by a joint venture. The study indicated that adaptation of the existing ship would necessitate substantial additional investment, so the Company commissioned an agent to identify and attract a further outside investor. The Company received a status note from this agent on 28 November 2003, confirming that he had been unable to attract any further investors to join the project, which meant that the proposed joint venture could not proceed. Although efforts to find alternative uses for the RFW will continue the asset is not expected to generate future cash flows from use or from sale. It is therefore no longer appropriate to carry this asset other than at scrap value, and an impairment charge has been recorded to reduce the carrying value to nil, which represents the fair value as at 30 November 2003.

Other ships and offshore equipment – \$28.8m

At the time of preparation of the annual operating budget for fiscal year 2004 and three-year plan in October 2003, the Company's senior management assessed the level of expected future utilisation of all its long-lived assets in the light of the business strategies established in the new management's business plan, and a number of assets are expected to be under-utilised in new management's plans. The major items included a ship (the *Seaway Defender*), three remote-operated MATIS™ pipe-connectors, nine ROVs, the Smartleg platform-deck installation equipment, three trenchers/ploughs, hardsuit diving equipment, and four pipe carousels. The Company estimated that future cash flows attributable to these assets were less than their carrying values and an impairment charge was recorded on the basis of fair value calculations performed by the Company using discounted cash flows.

Lobito yard assets – \$5.1m

This category comprises a large quantity of the Company's equipment located at the Lobito fabrication yard on long-term lease to Sonamet, including cranes, tractors, cutting and welding equipment, generators, and vehicles. A buy-out proposal from Sonamet to acquire the equipment was received in the fourth quarter of fiscal year 2003, and the carrying amount was reduced to the expected sales price. The assets were sold to Sonamet at that price after the end of fiscal year 2003.

Total charges for impairment of Company-owned tangible fixed assets – \$176.5m

The fiscal year 2002 charge of \$4.0 million for impairment of fixed assets was made up of adjustments to the carrying value of several small fixed assets.

In addition to the above, included in 'Equity in net income of non-consolidated joint ventures' in fiscal year 2003 are charges totalling \$9.1 million in respect of the Company's share of tangible fixed asset impairments booked by three of the Company's equity joint ventures, as follows:

Charges for impairment of tangible fixed assets in equity joint ventures

NKT flexibles – \$6.6m

An impairment charge of \$6.6 million was recorded in respect of the Company's 49% share of the impairment of the fixed assets of NKT Flexibles I/S, which identified excess manufacturing capacity following a reduction in its anticipated future revenue and market share in the fourth quarter of fiscal year 2003. The impairment was measured on the basis of discounted cash flows prepared by the NKT Flexibles joint venture.

Kingfisher D.A. – \$1.4m

An impairment charge was recorded in the books of the joint venture that owns the *Seaway Kingfisher*, following an outside valuation of the ship. The Company's 50% equity share of this impairment charge was \$1.4 million.

Sonastolt – \$1.1m

This joint venture owns seven ROVs that were sold at a loss in February 2004 in connection with the sale of the Company's ROV drill support business to Oceaneering International, Inc. The impairment was based on the difference between the carrying value of the ROVs and the net proceeds agreed under the sale contract.

Total charges for impairment of tangible fixed assets in equity joint ventures – \$9.1m

The fiscal year 2002 charge of \$8.1 million represented the Company's share of a fixed asset impairment loss booked by the NKT Flexibles joint venture. During 2002, NKT management revised its strategy to focus on efficiency on the basis of slower growth in the next few years than initially forecast. The Company performed an impairment test based on the cash flow projections in the business plan, and determined that the goodwill was fully impaired.

No impairment charges with respect to the Company's joint ventures were recorded in fiscal year 2001.

Management's discussion and analysis continued

Impairment of goodwill and other intangible assets

No charges for impairment of goodwill or other intangible assets were recorded in fiscal year 2003. Goodwill at 30 November 2003 amounted to \$6.0 million in respect of the acquisition of Paragon Engineering Services in fiscal year 2001. Impairment tests performed during the first six months of fiscal year 2003 under SFAS 142 indicated, in light of the subsidiary's continuing profitability, the value of goodwill was not impaired. The Company updated this exercise at 30 November 2003, when Paragon Engineering Services met the 'held for sale' criteria. No impairment charge was required.

In fiscal year 2002, the continuing poor returns obtained on certain investments made in 1998 and 1999 led the Company to perform an impairment review of all goodwill recognised on past acquisitions. As a result, impairment charges totalling \$106.4 million were recorded against goodwill, of which \$103.0 million related to the entire remaining goodwill on the 1998 acquisition of Ceanic. The remainder of the charge eliminated the outstanding goodwill of \$1.8 million on the acquisition of Danco A/S, which holds the Company's investment in NKT Flexibles, and of \$1.6 million in respect of the Company's Indonesian subsidiary, PT Komaritim.

Several factors were taken into account in the analysis and supporting projected cash flows that resulted in the impairment charge of \$103.0 million to eliminate the entire remaining goodwill on acquisition of Ceanic Corporation. The acquisition was made in 1998 as part of a strategy to establish a presence in one of the world's most important offshore markets, at a price that reflected rising oil prices and favourable investment conditions. Since then the Gulf of Mexico offshore contractor market has experienced an unprecedented downturn. As a result, the Company's former North America region was loss-making in fiscal years 2000 and 2001, and again performed below management's expectations in fiscal year 2002. Market analysts' reports indicated that the major oil companies were directing their development funds away from U.S. waters and towards overseas targets, particularly West Africa, where the per-barrel recovery costs are lower. The Company foresaw no significant upturn in demand in the Gulf of Mexico market and revised earlier assumptions of long-term market growth in its impairment model and eliminated the remaining goodwill. The Company's strategy is still to maintain a strong competitive presence in the Gulf of Mexico, and is planning to expand its service offering to the ultra-deepwater market in this and other regions. The goodwill in connection with the acquisition of Ceanic was previously amortised over 25 years.

The NKT Flexibles joint venture has been loss-making since the Company acquired its 49% share in 2000, and the market for flexible pipes has not grown as quickly as expected. As a consequence, the joint venture has suffered from excess production capacity and has not met its performance targets. During fiscal year 2002, NKT Flexibles' management revised its strategy to focus on efficiency and predicted slower growth in the next few years than initially forecast. The Company performed an impairment test for the goodwill in Danco A/S based on the cash flow projections in the NKT Flexibles business plan, and determined that the goodwill was fully impaired. An impairment adjustment of \$1.8 million was recorded in fiscal year 2002. This goodwill was previously amortised over ten years on a straight-line basis.

The PT Komaritim subsidiary in Indonesia was loss-making for several years, and in fiscal year 2002 once again underperformed management's expectations. The Indonesian market continues to be characterised by high competition in the shallow water sector, an environment in which the Company is unable to fully leverage its technology and core expertise. The Company determined, on the basis of projected cash flows, that the goodwill was fully impaired, and a charge of \$1.6 million was recorded in the year ended 30 November 2002. This goodwill was previously amortised over 20 years on a straight-line basis.

In fiscal year 2001, the Company recorded a charge of \$7.9 million for the write-down of the Comex trade name.

Restructuring charges

In fiscal year 2003, restructuring charges of \$16.2 million were incurred in connection with the Company's plan for financial recovery, which included the elimination of non-essential businesses and businesses that can be outsourced, and the restructuring of the Company's cost and asset base.

As discussed in Note 18 of the consolidated financial statements, real estate costs of \$2.7 million were incurred in the AFMED region, where a provision of \$1.8 million was recorded for the accrued rental fees of office space vacated by Paragon Litwin. The balance of \$0.9 million of unamortised leasehold improvements for these offices was also written off in fiscal year 2003, as the fair value was determined to be nil.

Personnel and redundancy costs of \$13.3 million were incurred for severance payments, vacation paid-in-lieu and outplacement fees, and were principally incurred in the AFMED, NEC and NAMEX regions due to the need to reduce staffing levels in the Aberdeen, Stavanger, Nanterre and Houston offices to reflect lower levels of business expected in these regions in fiscal year 2004. The Company expects the majority of the provision outstanding as of 30 November 2003 to be paid before 30 November 2004, although this is dependent on the outcome of consultative processes with works councils in France and Norway that commenced in fiscal year 2003 and that the law in those countries requires to be fully complete before the restructuring can be regarded as closed.

External advisors' fees totalling \$0.3 million were incurred in fiscal year 2003 in connection with the Company's asset disposals.

There were no restructuring charges in fiscal year 2002 or 2001.

(Loss) gain on sale of fixed assets

In fiscal year 2003, the loss of \$0.3 million resulted from the disposal of surplus equipment in the AME region. The gain of \$8.0 million in fiscal year 2002 represented the gain from the sale of the assets of Big Inch Marine Systems, Inc.

In 2001, the Company recognised a gain of \$1.2 million on the sale of Hard Suits Inc., a specialised diving company.

Other operating (loss) income, net

In fiscal year 2003, the Company incurred other operating losses of \$1.1 million compared to other operating income of \$0.1 million in fiscal year 2002 and other income of \$1.1 million in fiscal year 2001. No significant individual transactions are included in these results.

Net interest expense

In fiscal year 2003, net interest expense increased to \$24.8 million from \$18.2 million in fiscal year 2002. This resulted from increased borrowings from SNSA under the Subordinated Note, and from the decision to fully draw down the Company's Existing Credit Facility Agreements in August 2003 in order to assure liquidity during the restructuring process. This included additional borrowings in August 2003 of \$10 million under the \$55/45 million credit/guarantee facility, which is defined in 'Liquidity and capital resources - Description of indebtedness'.

The decrease in fiscal year 2002 from \$26.8 million in fiscal year 2001 resulted largely from lower interest rates. The Company also exercised an option on a finance lease to purchase two ships, the *Seaway Polaris* and *DLB 801*, and refinanced them with bank borrowings at a lower interest rate.

Foreign currency exchange (losses) gains

During fiscal year 2003 the Company recorded a foreign exchange related loss of \$8.9 million compared to a \$0.2 million gain in fiscal year 2002. This loss resulted from the weakening of the US dollar against the euro, the British pound sterling, and the Norwegian kroner in the second half of fiscal year 2003. For every \$0.01 change in the exchange rate between the US dollar and the euro, the impact on the Company's results is approximately \$2 million.

Income tax benefit (provision)

The Company recorded a net tax benefit of \$0.7 million in fiscal year 2003, as compared to net tax charges of \$8.2 million and \$20.6 million in fiscal years 2002 and 2001 respectively.

The tax benefit in fiscal year 2003 comprised a net release to current tax of \$0.03 million, a charge for revenue-based withholding taxes of \$6.6 million, and a deferred tax benefit of \$7.3 million. The Company has recognised deferred tax assets for Net Operating Losses carried forward ('NOLs') in Scandinavia and the United Kingdom. While the Company has NOLs in several other countries, it has recorded valuation allowances against the corresponding deferred tax assets in those instances where management does not consider it more likely than not that future taxable profits to realise the corresponding tax benefit exist.

Under United Kingdom Tonnage Tax legislation, a portion of tax depreciation previously claimed by the Company may be subject to tax in the event that a significant number of vessels are sold without being replaced. This contingent liability reduces progressively to nil over the seven years following entry into the tonnage tax regime. Management has made no provision for the contingent liability relating to ships that management does not consider that it is probable that it will sell. The contingent liability in respect of all ships as of 30 November 2003 was \$33.7 million.

In the normal course of its business the Company's activities become subject to enquiry and audit by tax authorities across a number of jurisdictions. During the year two of these enquiries were in Norway and the Netherlands. The Norway enquiry was concluded and in fiscal year 2004 the Company received a Norwegian kroner tax refund of \$7.8 million equivalent. The enquiry in the Netherlands is ongoing and is expected to be concluded in fiscal year 2004. Management is actively working to close out this and all other open tax enquiries and believes that it has adequate reserves to cover any taxes that may become payable in respect of such enquiries.

The Company recorded a net tax charge of \$8.2 million in fiscal year 2002, compared to a net tax charge of \$20.6 million in fiscal year 2001. The tax charge in fiscal year 2002 included withholding taxes of \$14.0 million imposed by tax authorities in certain countries. Additionally, in the NAMEX region, the Company did not recognise a deferred tax asset for the losses incurred, and took a further \$10.8 million valuation allowance against the deferred tax asset brought forward from fiscal year 2001 because of the continuing losses in the region. The Company also reviewed its position under the U.K. tonnage tax regime whereby taxable income is calculated by reference to the tonnage of the vessel, and released a further \$21.3 million of deferred tax liability in respect of fixed asset timing differences. This liability is not expected to materialise due to the Company's intention to remain permanently in the tonnage tax regime. This was partially offset by a valuation allowance against its net operating losses, due to the uncertainty of the Company's ability to generate sufficient future taxable earnings to realise the tax benefit of offsetting the prior operating losses.

Depreciation and amortisation

Depreciation and amortisation in fiscal year 2003 remained relatively static at \$93.5 million compared to \$92.1 million in fiscal year 2002 and \$91.8 million in fiscal year 2001.

Net (loss) income before tax

The net (loss) income before tax was adversely affected by a number of significant charges/(credits), which are summarised in the following table.

Significant charges/(credits) (in millions)	2003 \$	2002 \$	2001 \$
Revisions of estimates on major projects	216.0	58.8	(2.4)
Charge for impairment of Company-owned tangible fixed assets	176.5	4.0	-
Share of impairment charge of tangible fixed assets in equity joint ventures	9.1	8.1	-
Charge for impairment of goodwill and other intangible assets	-	106.4	7.9
Restructuring charge	16.2	-	-
Increase in provision for the Technip patent settlement (see 'Legal matters' below)	7.8	-	-
Loss/(gain) on sale of fixed assets	0.3	(8.0)	(1.2)
Total significant charges	425.9	169.3	4.3

Liquidity and capital resources

Cash requirements, contractual obligations and commercial commitments

The primary cash uses of the Company are to fund working capital, acquisitions of fixed assets, expenditures and dry-dock costs.

During the second half of fiscal year 2003, cash requirements increased significantly due to cost overruns on certain major projects, the continued delay in the recovery of amounts owed to the Company, and the delayed settlement of claims and variation orders with respect to major projects. Consequently, while engaged in discussions with its primary creditors to amend the financial covenants in the Existing Credit Facility Agreements, the Company also took measures to ensure that it had sufficient liquidity to fund its operations and to provide for a potentially protracted period of negotiation with certain major customers regarding settlement of claims and variation orders. These measures included borrowing to the maximum availability under the Existing Credit Facility Agreements and closing out positions under foreign exchange contracts.

The following table sets forth the Company's contractual obligations and other commercial commitments as of 30 November 2003:

Contractual obligations (in millions)	Total \$	Less than 1 year \$	1-3 years \$	4-5 years \$	After 5 years \$
Long-term debt ⁽¹⁾⁽²⁾⁽³⁾	385.0	91.5	293.5	-	-
Operating lease obligations	96.6	25.8	39.3	17.8	13.7
Other ⁽⁴⁾	349.5	173.3	141.0	32.1	3.1

- (1) Represents principal amounts, but not interest. See Note 15 to the consolidated financial statements.
- (2) For a description of the Company's long-term debt, refer to 'Description of indebtedness' and Note 15 to the consolidated financial statements.
- (3) Excludes SNSA Subordinated Note of \$50.0 million, which is summarised in 'Description of indebtedness' below.
- (4) Other includes performance bonds, bid bonds, advance payment bonds, guarantees or standby letters of credit in respect to a performance obligation of the Company. For further information regarding bank guarantees, see 'Off-balance sheet arrangements'.

During fiscal year 2004, the Company expects to pay approximately \$23 million for interest payable on its debt, and miscellaneous cash outflows are expected to be approximately \$13 million. While cash provided from operations is expected to be approximately \$55 million and, as described in 'Equity and funding transactions since 30 November 2003', the Company intends to raise additional cash through equity offerings. In addition to funding the cash outflows above, the cash provided from these activities is expected to be used to repay \$91.5 million of bank debt in fiscal year 2004, detailed as follows:

As of 31 March 2004, \$45.0 million has been repaid under the \$440 million credit facility. This includes \$15.0 million from the Duke Hubline settlement. The Company is committed to repaying the equivalent of 50% of the proceeds of the Subsequent Issue, which is expected to be completed by the end of May. The estimated gross proceeds from the Subsequent Issue are approximately \$53.0 million, resulting in a repayment of \$26.5 million. Furthermore under the terms of the \$55/45 million credit/guarantee facility twice yearly repayments of \$10.0 million each are made in January and July.

Cash management constraints

Cash operations for the Company are managed under central treasury department control, and cash surpluses and requirements are identified using consolidated cash flow forecasts. These treasury operations are subject to two principal constraints. First, under the terms of the Company's New Bonding Facility, all surplus cash in excess of \$75 million is required to be retained in a reserved bank account. Second, the Company does not always have the ability to freely transfer funds across international borders. For example, certain subsidiary companies in France which show a negative net asset position are unable to release funds to central treasury without approval from the subsidiary's Board of Directors. In addition, approval from the Central Bank of Brazil is required in order to obtain remittances from Brazil.

The main uncertainties with respect to the Company's primary sources of funds are as follows: the ability to obtain borrowings from financial institutions at commercially acceptable terms; being able to issue share capital at terms acceptable to the Company; the ability to agree, in a timely fashion, with customers the amounts due as claims and variation orders; the availability of cash flows from joint ventures; and the timing of asset or business disposals through its divestment programme. In addition, due to the uncertainties associated with the timings of cash flows from project contracts, and the uncertainties referred to earlier, it is difficult to accurately forecast the timing of inflows and outflows of cash.

Future compliance with debt covenants

As described in Note 15 to the consolidated financial statements, the Company's credit facilities contain various financial covenants, including but not limited to, minimum consolidated tangible net worth, maximum consolidated debt to net worth and maximum consolidated debt to EBITDA. The Company's latest forecasts for fiscal year 2004 indicate that there will be a narrow margin of compliance with the debt to EBITDA ratio covenant at the end of the fourth quarter of 2004. The Company's ability to remain within these covenants at the end of the second and third quarters of fiscal year 2004 is dependent on (i) its operating performance, (ii) the successful completion of the Subsequent Issue during the second quarter of fiscal year 2004, (iii) its ability to recover variation orders and claims from customers, where additional contract costs are incurred, and (iv) the success of the Company's plans to divest certain assets and businesses.

Management's discussion and analysis continued

The Company has consequently made contingency plans in the event that the operational results for the year fall below the latest updated estimates as follows: (i) the Company has the option of raising unsecured debt finance as an alternative means of repaying bank facilities; (ii) the Company has identified discretionary capital expenditures that can be deferred; (iii) the Company has the option of raising further equity; and (iv) the Company can seek to obtain a waiver of covenant breaches if they were to arise.

Sources of cash

The Company's principal sources of funds since the beginning of fiscal year 2003 have been cash from operations, borrowings from commercial banks and SNSA, and the issuance of share capital. Also, the Company monetised substantially all of its open forward contracts in August 2003 in order to provide \$28.2 million of additional liquidity during the restructuring period. As of 29 February 2004, apart from the facilities which were negotiated and agreed as described below in 'Equity and funding transactions since 30 November 2003', the Company has no other borrowing facilities available, and it has limited ability to pledge assets to secure new credit facilities. SNSA has indicated that it can no longer provide financial support to the Company beyond its existing guarantees of certain of the Company's outstanding bank guarantees. The Company's New Bonding Facility requires the Company to maintain in a restricted account a cash amount equal to a certain proportion of all bank guarantees under the facility.

Therefore, the Company's only readily available funds for ongoing operations are, first, the available borrowings under the Existing Credit Facility Agreements, which are fully drawn and are expected to remain fully drawn, and second, the Company's cash on hand and cash flows from operations going forward in excess of the amount that the Company is required to maintain in the restricted cash accounts. This requirement is in addition to the requirement to have all unrestricted cash in excess of \$75 million retained in a reserved bank account.

As at 30 November 2003, the Company had \$81.9 million of unrestricted cash on hand.

As of 26 March 2004, the Company had \$211.1 million of unrestricted cash on hand, of which \$156.0 million is deposited with the agent managing the New Bonding Facility in compliance with the relevant conditions.

Summary cash flows (in millions)	2003 \$	2002 \$	2001 \$
Net cash (used in) provided by operating activities	(27.5)	84.7	16.7
Net cash used in investing activities	(12.7)	(76.4)	(83.4)
Net cash provided by (used in) financing activities	109.4	(8.4)	72.5
Effect of exchange rate changes on cash	1.1	0.1	(0.4)
Cash and cash equivalents at the end of the year	81.9	11.7	11.7

Cash flows (used in) provided by operating activities

Cash flow from operations is derived principally from the collection of receivables due from customers under project contracts. The timing of invoice preparation for long-term contracts is typically based on progress towards the completion of work, either defined as agreed project 'milestones' or an otherwise agreed staged payment schedule. Cash flows do not always coincide with the recognition of revenues, as customers are generally required to make advance payments at project commencement. It is the intention of the Company, when negotiating a contract, to arrange for cash to be received from the customer in advance of the requirement to pay suppliers, thus ensuring a neutral impact on liquidity.

Net cash used in operating activities during fiscal year 2003 was \$27.5 million compared to net cash provided by operating activities of \$84.7 million during fiscal year 2002. This resulted from cash used in operations of \$135.1 million, only partially offset a reduction in working capital of \$93.5 million and dividends of \$14.1 million received from non-consolidated joint ventures. In fiscal year 2002, cash provided by operating activities was due to positive cash flow from operations of \$48.9 million, a reduction in working capital of \$22.6 million, and dividends of \$13.2 million from non-consolidated joint ventures. Average accounts receivable decreased to 99 days at 30 November 2003 from 114 days at 30 November 2002. Average accounts payable days decreased to 102 at 30 November 2003 from 120 in fiscal year 2002.

The other year-to-year fluctuations in cash flows from operating activities are due to fluctuations in net operating income as discussed under 'Commentary by segment' above.

Cash flows provided by (used in) investing activities and capital expenditures

Net cash used in investing activities in fiscal year 2003 was \$12.7 million compared to net cash used in investing activities of \$76.4 million in fiscal year 2002. This mainly comprises net cash inflows of \$31.9 million in respect of repayments from and advances to joint ventures, other investments and other non-current financial assets partially offset by the payment of \$12.5 million for the final settlement of the NKT Flexibles share price guarantee, a further investment in the Sonamet and NKT Flexibles joint ventures of \$14.2 million, asset sales proceeds of \$4.0 million and the purchase of fixed assets of \$21.9 million.

In addition to capital expenditure outflows, which are project specific and, which are typically included in the contract price, the Company, in the normal course of its business, makes routine capital expenditures. The table below sets forth information with respect to the Company's capital expenditures for fixed assets in each of the last three fiscal years. The ongoing capital expenditures will be funded with cash from operations.

Category of capital investment (in millions)	2003 \$	2002 \$	2001 \$
Equipment and asset development	8.1	28.9	38.0
Capacity upgrades to ships and other equipment	12.3	24.1	21.2
Other	1.5	1.6	3.7
Total capital investment	21.9	54.6	62.9

The four largest capital expenditure projects during fiscal year 2003 are set out in the table below.

Asset (in millions)	Description of capital expenditure project	\$
Mobile Assets	SCR pull-in system	3.7
<i>Seaway Polaris</i>	J-Lay tower upgrade	5.1
<i>Seaway Osprey</i>	New knuckle jib crane	2.6
Computer software	Asset supply chain management software	1.8
Total		\$13.2

The reduction of capital expenditure in fiscal year 2003 reflects the cash constraints under which the Company operated in fiscal year 2003, which caused the Company to defer non-essential capital expenditures. Management expects capital expenditures in fiscal year 2004 to amount to approximately \$50.8 million, of which \$2.7 million was committed as of 29 February 2004.

Net cash used in investing activities in fiscal year 2002 was \$76.4 million compared to \$83.4 million in fiscal year 2001. This mainly comprises the payment of \$58.9 million to Vinci in respect of the partial settlement of the share price guarantee issued in connection with the acquisition of ETPM, and the payment of \$1.7 million for the settlement of the NKT Flexibles share price guarantee. This was partially offset by \$23.5 million from the sale of the assets, including those of Big Inch Marine Systems, Inc. Investments made in the purchase of fixed assets were \$54.6 million, and \$15.2 million was received in respect of investments in non-consolidated joint ventures.

In fiscal year 2001, the acquisition of Paragon Engineering Services and Litwin accounted for \$0.1 million, net of cash acquired, \$62.9 million was used to purchase fixed assets, and \$26.1 million was paid in respect of investments in non-consolidated joint ventures.

Cash flows (used in) provided by financing activities

Net cash provided by financing activities in fiscal year 2003 was \$109.4 million, compared to net cash used by financing activities in fiscal year 2002 of \$8.4 million. Sources of financing in fiscal year 2003 were a net increase of \$149.6 million in long-term debt and the monetisation of hedges with proceeds of \$16.8 million. These funds were used to repay bank overdrafts of \$13.8 million, to pay dividends to a minority shareholder of \$2.2 million and to repurchase treasury shares of \$1.0 million. Furthermore, outstanding SNSA funding was reduced by \$40.0 million.

Net cash used in financing activities in fiscal year 2002 was \$8.4 million, compared to net cash provided by financing activities of \$72.5 million in fiscal year 2001. Sources of financing in fiscal year 2002 were the receipt of a \$64.0 million loan from SNSA to fund settlement of share price guarantees and an increase in bank overdrafts of \$10.2 million. These funds were used to repay capital lease purchase obligations totalling \$23.7 million on the *Seaway Polaris* and *DLB 801*, and repurchase shares from

SNSA for \$56.5 million. In fiscal year 2001, net cash provided by financing activities comprised an increase in long-term debt of \$70.0 million, a \$3.3 million additional drawdown on short-term facilities, a \$2.6 million decrease of restricted cash and a \$3.8 million repayment of capital lease obligations.

Description of indebtedness

As part of its financing arrangements, the Company has the following facilities outstanding as of 30 November 2003.

The \$440 million credit facility

The Company's principal credit facility is an amended \$440 million secured multi-currency five-year term facility. The facility was entered into on 22 September 2000 with a syndicate of banks, led by DnB NOR Bank ASA, Bank of America Securities LLC, Salomon Brothers International Limited, HSBC Bank plc and ING Barings LLC, Bank of America N.A. and Citibank N.A. as syndication agents and joint book managers, ING Barings LLC as documentation agent and DnB NOR Bank ASA as facility agent and security trustee. The available amount under the facility reduced to \$330.0 million on 31 August 2003, in accordance with scheduled reductions. This facility bore a variable interest rate of up to LIBOR + 3.25%. In February and March 2004, the Company made prepayments under the facility of \$45 million such that the available amount of the facility reduced to \$285.0 million. The Company expects that it will prepay additional amounts prior to the termination date, including 50% of the gross proceeds resulting from the Subsequent Issue, such that the available amount will further reduce.

All amounts outstanding under this facility are secured by a full and unconditional guarantee provided by the Company and the execution of certain security documents by the Company, including mortgages on certain ships owned by the Company. The facility contains affirmative and negative covenants, including financial covenants relating to the Company's minimum tangible net worth, ratio of consolidated debt to consolidated tangible net worth and ratio of consolidated debt to earnings before interest, tax, depreciation and amortisation ('EBITDA'). These covenants have been changed or are superseded under the terms of the Intercreditor Deed (see 'Equity and funding transactions since 30 November 2003' below).

The \$55/45 million credit/guarantee facility

On 9 July 2002, the Company entered into an amended \$55/45 million credit/guarantee facility agreement with a term of four years. This facility permitted the Company to borrow up to \$55 million and to request the provision of bank guarantees in relation to the Company's performance obligations of up to \$45 million. As of 30 November 2003, the \$55 million credit portion of this facility was fully drawn and \$9.7 million was available for issuance of new bank guarantees under the guarantee portion. The amount available for borrowing was reduced by \$10 million in January 2004, in accordance with a scheduled reduction of this facility. Amounts available for borrowings or guarantees will be further reduced by \$10 million on each consecutive six-month period ending thereafter until the termination of this facility in July 2006. The Company can allocate the \$10 million reduction between the credit portion of this facility and the guarantee portion of this facility. SNSA and SNTG have jointly and severally guaranteed the Company's obligations to the banks providing bank guarantees pursuant to the guarantee portion of this facility.

All amounts outstanding under this facility are secured by a full and unconditional guarantee provided by the Company and the execution of certain security documents by the Company, including mortgages on certain ships owned by the Company. The affirmative and negative covenants and events of default contained in this facility are substantially identical to those contained in the \$440 million credit facility described above.

The \$44 million guarantee facility

The Company is a party to a \$44 million secured guarantee facility as guarantor. Under this facility, Citibank N.A., certain other financial institutions as banks and DnB NOR Bank ASA, as facility agent, security trustee and issuing bank agreed to the issuance of bank guarantees. As of 30 November 2003, \$23.5 million was outstanding, having been drawn in fiscal year 2003 under this facility, which ceased to be available for further drawings on 30 November 2003 and is therefore considered as fully drawn. This facility is jointly and severally guaranteed by SNSA and SNTG providing bank guarantees pursuant to this facility. In addition, ships owned by the subsidiaries of SNTG (Bermuda) are also pledged in support of the bank guarantees.

The \$28 million reimbursement facility

The Company had entered into an amended and restated secured reimbursement agreement dated 27 August 2003, between the Company, as borrower, and DnB NOR Bank ASA as bank. Under this facility, DnB NOR Bank ASA, as bank, agreed to extend the term of a letter of credit until 15 September 2004. The letter of credit was issued in connection with the Duke Hubline project. As the Company's contractual dispute relating to the Duke Hubline project has been settled, this facility will no longer be required, and the letter of credit is expected to be released before the end of the second quarter of 2004.

Other bank guarantee arrangements

The Company has arrangements with a number of financial institutions to issue bank guarantees on its behalf. As of 30 November 2003, the aggregate amount of guarantees issued under these facilities was \$238.1 million and at 31 March 2004 it was \$182.3 million. Of this amount, \$4.8 million was guaranteed by SNSA. The bonds under these facilities were issued to guarantee the Company's project performance and that of its subsidiaries and joint ventures to third parties in the normal course of business. As of 21 April 2004, the Company has no bank guarantee capacity available under these arrangements.

The Subordinated Note

Under the Company's existing credit facilities, the Company is permitted to borrow up to \$100.0 million from SNSA (the 'Subordinated Note') provided that this debt is subordinate and junior to all indebtedness due under the \$440 million credit facility, the \$55/45 million credit/guarantee facility and the \$44 million guarantee facility (described below). On 30 May 2003, pending the formal agreement of this facility, the Company drew the full amount of \$50.0 million which was outstanding at 30 November 2003. On 30 June 2003, as a condition to the receipt of waivers of potential defaults and amendments to the financial covenants contained in the Company's existing credit facility agreements, SNTG signed a formal agreement with the Company for a \$50.0 million subordinated loan bearing an interest rate of 12% per annum up to 12 February 2004. This Subordinated Note is fully subordinated to all indebtedness owed under and pursuant to the \$440.0 million credit facility, the \$55/45 million credit/guarantee facility and the \$44.0 million guarantee facility. The Company and SNTG have irrevocably agreed to convert the Subordinated Note in return for the issuance of 22,727,272 Common Shares. The conversion of the Subordinated Note was completed on 20 April 2004.

The SNSA liquidity line

SNSA has extended to the Company a committed line of credit in the amount of \$50 million pursuant to a facility agreement, dated as of 30 June 2003 and restated as of 21 August 2003 for working capital and other corporate purposes. This line remains available to the Company until 28 November 2004. However, SNSA has informed the Company that SNTG's ability to fund a draw down under the SNSA liquidity line is limited by the terms of SNSA's existing credit facilities and may be prohibited in certain circumstances. The Company has advised SNSA that it does not expect to utilise this liquidity line.

Interest rates

The Company pays a variable interest rate on outstanding borrowings at a rate equal to LIBOR + 3.25% per annum. The Company is permitted to repay all or any portion of the principal amount outstanding, along with any accrued interest, at any time, however, the SNSA liquidity line will become fully subordinated to the \$440 million credit facility and the \$55/45 million credit/guarantee facility upon the occurrence of an event of default under those facilities. In addition, the Company is prohibited under the terms of its Existing Credit Facility Agreements from repaying any amounts under the SNSA liquidity line at any time that an event of default or potential event of default has occurred and is continuing or, as a result of such payment, would occur under its Existing Credit Facility Agreements. The SNSA liquidity line may be utilised for working capital and other corporate purposes. As of 30 November 2003, there were no amounts outstanding under the SNSA liquidity line.

Covenants and restrictions

The financial covenants contained in the Company's credit facilities, and the waivers obtained during fiscal year 2003, are summarised in Note 15 to the consolidated financial statements. These have been amended by the Intercreditor Deed, which is discussed in 'Equity and funding transactions since 30 November 2003' below.

As described in Note 15 to the consolidated financial statements, the Company's credit facilities contain various financial covenants, including but not limited to, minimum consolidated tangible net worth, ratio of consolidated debt to consolidated tangible net worth and ratio of consolidated debt to EBITDA. The Company announced in December 2002 that it was potentially in breach of certain financial covenants

Management's discussion and analysis continued

contained in its Existing Credit Facility Agreements. In light of these developments, in December 2002, the Company sought, and by 3 January 2003 obtained, amendments as of 20 November 2002 to these facilities to avoid financial covenant defaults. The amendments included revised financial covenants and a requirement that SNSA continue to provide financial support through the provision of the SNSA liquidity line until November 2004.

As a result of certain operational problems on major projects, the Company found it increasingly difficult to remain in compliance with the revised financial covenants under its Existing Credit Facility Agreements. Consequently, it engaged in further discussions with its banks for amendments to or waivers of financial covenants. On 1 July 2003, the Company announced that it had obtained a waiver of potential defaults and amendments to the financial covenants contained in these facilities through 30 November 2003.

On 17 September 2003, the Company announced that it expected higher than previously projected losses for 2003. As a result, the Company was in potential breach of the revised financial covenants under the waiver agreements obtained on 1 July 2003. The Company sought and obtained from its lenders under the existing credit facility agreements new waivers of these revised financial covenants. These new waivers expired on 15 October 2003 and replaced the original waivers, which were set to expire on 30 November 2003.

During late 2003, the Company continued to engage in restructuring discussions with its lenders under the Company's Existing Credit Facility Agreements. As part of these ongoing discussions, the Company received four subsequent covenant waiver extensions, which provided for covenant relief for the period 15 October 2003 through 30 April 2004 subject to certain conditions.

Equity and funding transactions since 30 November 2003

On 12 February 2004, the Company and certain of its subsidiaries entered into the New Bonding Facility with certain financial institutions for the issuance of bank guarantees of up to \$100 million. As described in more detail in Note 28 to the consolidated financial statements, the issuance of bank guarantees under this New Bonding Facility is subject to a number of conditions. This facility is available to the Company for a period of 18 months.

The Company also entered into the Intercreditor Deed, which among other things, (i) allowed it to pledge existing collateral for the New Bonding Facility; (ii) provided for certain prepayments under the \$440 million credit facility (discussed above); and (iii) reset the financial covenants to better reflect the Company's business and financial performance. See Note 28 to the consolidated financial statements.

In addition to entering into the New Bonding Facility and the Intercreditor Deed, the Company has taken a number of steps to improve its financial position, liquidity and gearing. Since 30 November 2003, the Company has taken the following additional steps:

- ▶ issued and sold 45.5 million Common Shares in a private placement, raising gross proceeds of \$100.1 million, which was completed on 13 February 2004. The Company is using the net proceeds from the Private Placement as follows: (i) to provide cash collateral for the New Bonding Facility, (ii) working capital, (iii) prepayment of certain amounts under the \$440 million credit facility and scheduled repayments of existing debt obligations, (iv) capital expenditures, and (v) general corporate purposes. Of the gross from the Subsequent Issue, 50% was used for prepayments under the \$440 million credit facility.
- ▶ converted on 20 April 2004 the \$50 million of subordinated debt into 22,727,272 Common Shares. Following the completion of the conversion, the Company's outstanding debt was reduced by \$50.0 million.
- ▶ obtained shareholder approval to raise approximately \$52.8 million in gross proceeds through the issuance of 24 million Common Shares, expected to be completed in May 2004.
- ▶ reduced its debt by prepayments under the \$440 million credit facility and other credit facilities. As of 31 March 2004, the Company had prepaid its debt by approximately \$55 million since 30 November 2003.

Off-balance sheet arrangements

The Company does not engage in off-balance sheet financing in the form of special purpose entities or similar arrangements. The Company engages in operating leases in the normal course of the Company's business in respect of ship charter hire, office facilities and equipment.

The Company also arranges for bank guarantees, which collectively refers to performance bonds, bid bonds, advance payment bonds, guarantees or standby letters of credit in respect of a performance obligation of the Company to be provided to its customers in connection with the Company's work on specific projects. These guarantees are issued under the \$55/45 million credit/guarantee facility, the \$44 million guarantee facility, the \$28 million reimbursement facility and other bank guarantee arrangements. The total amount outstanding in respect of bank guarantees as of 30 November 2003 was \$324.9 million. The purpose of the bank guarantees generally is to enable the Company's customers to recover cash paid to the Company in advance of performing its obligations under the contract or to obtain cash compensation should the Company be unable to fulfil its performance obligations under the Company's contracts.

Investments in and long-term funding to non-consolidated joint ventures

The Company offers heavy lift floating crane services through SHL. SHL charters the heavy lift barge *Stanislav Yudin* from a subsidiary of Lukoil Kaliningradmorneft plc, the Company's joint venture partner in SHL. The barge operates world-wide providing heavy lift services to a range of offshore companies, including occasional projects for the Company. The charter hire period was recently extended for a further five-year period until 2010.

The Company also manufactures flexible flowlines and dynamic flexible risers through NKT Flexibles. During fiscal year 2002, and again in fiscal year 2003, NKT Flexibles management revised the joint venture's strategy and downgraded expectations for growth in future years. The Company's equity share of the net loss in NKT Flexibles in fiscal year 2003 included \$6.6 million and in fiscal year 2002 included \$8.1 million in respect of fixed asset impairment charges recorded by the joint venture. On 3 December 2002, the Company made a capital contribution of \$12.6 million in cash to NKT Flexibles. On the same date, NKT Flexibles repaid an outstanding loan for \$12.6 million due to the Company. In addition, a 100% provision was recorded in November 2003 in respect of advances of \$3.1 million made to NKT Flexibles during fiscal year 2003.

The Company's joint ventures in Angola with Sonangol (conducted via Sonamet), provide strategic access to the offshore Angolan market through the operation of the Sonamet fabrication yard at Lobito. The Sonamet fabrication yard enables the Company to offer locally manufactured structures and components for offshore projects. The provision of local content is an important strategic advantage in the West African offshore market, as there are local content requirements. In addition to local manufacturing materials, the Company also provides local offshore support personnel and equipment through Sonastolt.

The Company created a joint venture with Technip and Saipem S.A. ('Saipem') to bid for work on the Dalia field development in Block 17 offshore Angola, which the Company was awarded in May 2003 by Total E&P Angola. The joint venture has responsibility for project management, engineering, procurement, onshore commissioning and offshore hook-up of the FPSO. The total contract value amounts to approximately \$430 million, of which the Company's share is 27.5%. As of 30 November 2003, the percentage of completion of the project was too low to require any profit to be included in the Company's consolidated statement of operations for fiscal year 2003.

The remainder of the Company's joint ventures have been formed either with a national oil company, such as the State Oil Company of the Azerbaijan Republic ('SOCAR') in Azerbaijan, or on a project-specific basis to enhance the range of services provided to the customer. The Company typically has interests ranging from 25% to 50% in these joint ventures.

Where joint ventures are project specific, the Company will typically be obliged to contribute its proportionate share of funding requirements. In addition the Company may be liable for the failure of its joint venture partners to fulfil their obligations. The Company will normally also have an obligation to meet its proportionate share of funding needs in long-term joint ventures. However such joint venture investments would require unanimity among joint venture partners.

As of 30 November 2003 and 2002 our investments in and long-term funding to non-consolidated joint ventures comprised the following:

(in thousands)	Geographical location	Segment	Ownership %	2003 \$	2002 \$
NKT Flexibles	Denmark	Corporate	49.0%	10,987	5,827
Mar Profundo Girassol	West Africa	AFMED	50.0%	100	8,618
Sonamet	West Africa	AFMED	55.0%	7,406	(501)
Sonastolt	West Africa	AFMED	55.0%	9,623	6,331
SHL	Cyprus	Corporate	30.0%	4,312	2,600
Stolt/Subsea 7	Norway	NEC	50.0%	2,133	1,551
Kingfisher D.A.	Norway	NEC	50.0%	3,777	4,346
Dalia FPSO	West Africa	AFMED	27.5%	4,624	–
Other	Various	AFMED, NEC		–	2
Total				42,962	28,774

The investments in the Sonamet and Sonastolt joint ventures where the Company owns more than 50% of the voting interest, but its ability to control the operation of the investees is restricted by the significant participating interest held by another party, are not consolidated but rather are accounted for under the equity method of accounting.

The company accrues losses in excess of the investment value in a joint venture when it is committed to provide ongoing financial support to the joint venture.

Taxation in respect of joint ventures, which have a legal status of partnership, has been included in the results of the relevant subsidiaries, which hold the investments in the joint ventures. Undistributed reserves of all other joint ventures will not be taxed on distribution.

The tables below set out a summary of audited financial information for fiscal years 2003, 2002 and 2001 for our non-consolidated joint ventures, representing 100% of the respective amounts included in the joint ventures' audited financial statements:

Income statement data

For the year ended 30 November (in thousands)	2003 \$	2002 \$	2001 \$
Net operating revenue	323,519	298,212	296,305
Gross profit	29,009	37,930	27,599
Net income	3,518	9,203	24,329

Balance sheet data

As of 30 November (in thousands)	2003 \$	2002 \$
Current assets	469,205	159,033
Non-current assets	88,055	97,621
Current liabilities	464,666	161,283
Long-term liabilities	7,610	12,833

Legal matters

Technip

In 1996, Coflexip SA and Coflexip Stena Offshore Limited (now known as Technip S.A. and Technip Offshore Limited) ('Technip'), commenced legal proceedings in the U.K. High Court against three subsidiaries of the Company for infringement of a certain patent held by Technip on flexible flowline laying technology. The claim related to the Company's use of the flexible lay system on the *Seaway Falcon*. The claim was heard by the U.K. High Court in 1998 and on 27 January 1999 the disputed patent was held valid in favour of Technip. Following this judgement, Technip claimed damages relating to lost profit for five projects, plus legal costs and interest. However, the damages claim was stayed pending the appeal by both parties against the January 1999 decision. The Court of Appeal dismissed the defendant's appeal and maintained the validity of the patent. The Company applied for leave to appeal the Court of Appeal decision to the House of Lords, which was denied. As a result, the equipment part as well as the process part of the patent was held valid.

During fiscal year 2001, Technip submitted an amended claim for damages claiming the lost profits on a total of 15 projects. In addition there was a claim for alleged price depreciation on certain other projects. The total claim was for GBP 63 million (approximately \$118 million), plus interest, legal fees and a royalty for each time that the flexible lay system tower on the *Seaway Falcon* was brought into U.K. waters. The Company estimated that the total claim would be approximately GBP 88 million (approximately \$165 million). In the alternative, Technip claimed a reasonable royalty for each act of infringement, interest and legal costs. Technip did not quantify the claim.

During fiscal year 2003, the U.K. High Court held that the same patent, the subject of the proceedings against the Company, was invalid in a separate and unrelated litigation between a company of the Halliburton group and Technip. That decision has been appealed by Technip.

In light of the decision in the Halliburton case, the Company applied to the U.K. High Court to stay the damages inquiry in the Stolt Offshore case, pending the resolution of the Halliburton case. The High Court denied the request. The Company appealed this decision to the Court of Appeal and the Court of Appeal, subsequent to a hearing in January 2004, decided that the Company could not benefit from the patent being revoked in the Halliburton case. However, the Court of Appeal did not decide on whether or not to stay the damages inquiry, nor on whether or not to recommend that leave to appeal to the House of Lords be given. These two issues were expected to be considered by the Court of Appeal after the decision in the Halliburton case was known. The damages inquiry in the infringement case with Technip was scheduled to be heard beginning in late April 2004.

As of 30 November 2002 the Company, in consultation with its advisers, had assessed that the range of possible outcomes for the resolution of damages was \$1.5 million to \$130.0 million and determined that no amount within the range was a better estimate than any other amount. Consequently, in accordance with SFAS No.5 'Accounting for Contingencies', as interpreted by FASB Interpretation No.14 'Reasonable Estimation of the Amounts of a Loss', the Company provided \$1.5 million in the financial statements, being the lower amount of the range.

As of 30 November 2003, the Company, in consultation with its advisers, provided for an increased contingency reserve of \$9.3 million related to this litigation.

On 18 March 2004, the Company announced that it and Technip had reached a settlement of this matter. The settlement involves (i) a cash payment by the Company of an amount within the amount of its contingency reserve described above, (ii) Technip's grant of a licence to the Company for the use of the allegedly infringing technology covering the North Sea area for future periods for an annual fee, (iii) the termination of arbitration proceedings in the United States with respect to an unrelated matter, with neither party making payment to the other, and (iv) a transfer to Technip of a portion of the Company's equity interest in a project joint venture involving Technip and the Company. The Company estimates that the reduction in future profits from the transfer of this interest is approximately \$6.0 million. Technip has not granted to the Company a licence to use the allegedly infringing technology or process in any other jurisdiction.

Management's discussion and analysis continued

Duke Hubline project

In October 2003, the Company commenced arbitration proceedings against Algonquin Gas Transmission Company ('Algonquin Gas Transmission'), claiming approximately \$57.8 million in unpaid invoices for work performed on the Duke Hubline project on an offshore gas pipeline off the coast of Massachusetts, U.S. Algonquin Gas Transmission, the owner of the pipeline, challenged its obligation to pay any of the invoice amounts and asserted counterclaims totalling an additional \$39.0 million for alleged mismanagement and inadequate performance by the Company. Due to Algonquin Gas Transmission's non-payment of invoiced amounts, the Company was unable to pay certain of its subcontractors employed to work on the pipeline, three of which filed lawsuits against the Company in Louisiana U.S. State courts for non-payment of amounts invoiced. These same subcontractors claimed liens over the pipeline, which liens are the subject of proceedings commenced by them against the Company and Algonquin Gas Transmission in Massachusetts U.S. State court.

The Company's dispute with Algonquin Gas Transmission was referred to mediation in late January 2004, at which the parties reached a 'settlement in principle' whereby (i) Algonquin Gas Transmission agreed to pay the Company \$37.0 million in full and final settlement of the parties' claims and counterclaims and (ii) the Company agreed to withdraw the arbitration proceedings and use its best efforts to secure the release of the above-mentioned subcontractor liens. The settlement of \$37 million has been included in the Company's reported results for fiscal year 2003. A definitive settlement agreement was executed on 26 February 2004 reflecting the terms of the 'settlement in principle' and Algonquin Gas Transmission paid the settlement amount to the Company in March 2004. The Company has also reached agreements in principle to settle the related subcontractor litigation. The related \$28 million letter of credit is expected to be released before the end of the second quarter of fiscal year 2004. See 'Description of indebtedness – the \$28 million reimbursement facility'.

Other legal matters

In connection with a major West African contract, the Company received a letter dated 12 December 2003 from the customer notifying the Company of a potential claim for an unspecified amount of liquidated damages. The claim relates to delays in completion of certain milestones. The Company believes that the customer does not have a valid case for liquidated damages, and on that basis has not recorded a provision. A similar notification letter received from the customer in December 2002 on a different project was settled amicably in the Company's favour during fiscal year 2003.

In addition, in the course of its business, the Company becomes involved in contract disputes from time to time due to the nature of its activities as a contracting business involved in several long-term projects at any given time. The Company makes provisions to cover the expected risk of loss to the extent that negative outcomes are likely and reliable estimates can be made. However, the final outcomes of these contract disputes are subject to uncertainties as to whether or not they develop into a formal legal action and therefore the resulting liabilities may exceed the liability the Company may anticipate.

Furthermore, the Company is involved in legal proceedings from time to time incidental to the ordinary conduct of its business. Litigation is subject to many uncertainties, and the outcome of individual matters is not predictable with assurance. It is reasonably possible that the final resolution of any litigation could require the Company to make additional expenditures in excess of reserves that it may establish. In the ordinary course of business, various claims, suits and complaints have been filed against the Company in addition to the one specifically referred to above. Although the final resolution of any such other matters could have a material effect on the Company's operating results for a particular reporting period, the Company believes that they should not materially affect its consolidated financial position.

For accounting purposes, the Company expenses legal costs as they are incurred.

Other subsequent events

Below is a summary of events that occurred after 30 November 2003, which the Company considers to be of significance.

The Company has been informed by the U.S. Securities and Exchange Commission (SEC) that it is conducting an informal inquiry into the Company's revenue recognition policies and practices with respect to claims and variation orders. The SEC has requested that the Company voluntarily produce information and documents in response to the inquiry and the Company is co-operating fully with the SEC.

On 18 December 2003, an agreement was reached with the customer on the OGGG project in Nigeria. The agreement covers all claims of whatever nature, whether formally made or not and all facts and circumstances as at 30 November 2003 which may give rise to any claims whatsoever under the contract. In addition, it was agreed that the Company should perform its outstanding work as stipulated under the contract. A total of \$43.8 million in cash has been received under the terms of agreement. Because it relates to conditions that existed prior to 30 November 2003, the impact of this settlement was accounted for as a receivable in fiscal year 2003.

On 31 December 2003, the pipelay ship the *Seaway Polaris* dropped a pipe, which it was laying for the Bonga project in Nigeria. The Company believes it will successfully obtain reimbursement (estimated at up to \$20 million) under the customer's all risk insurance policy and there is no net cost to the Company in respect of this incident. There will be an additional loss of potential income of up to \$5 million as a result of non-achievement of milestone bonuses, none of which had yet been booked as income as of 30 November 2003. The Bonga project was 71% complete as at 30 November 2003, with an estimated revenue at completion of \$249.5 million, including \$15.0 million of potential revenue related to an incentive scheme which will take effect in fiscal year 2004. This is a loss-making contract, and therefore the forecast loss at completion is accrued in the fiscal year 2003 result.

An agreement was reached on 28 January 2004 with Burullus Gas Company of Egypt for the settlement of unagreed variation orders. The impact of this settlement has been included in the Company's results for fiscal year 2003 as part of the outstanding receivables as of 30 November 2003. As of 31 March 2004, substantially all of the proceeds from the settlement have been received in cash, and were included in receivables as of 30 November 2003. The settlement includes notice of final acceptance for all work except for the obligation on the Company to complete repairs to the 24-inch export pipeline for an additional agreed contracted sum.

On 18 February 2004, the Company announced the award of the Greater Plutonio contract. The contract was awarded by BP to a consortium the Company formed with Technip, and represents the largest contract ever to be awarded to the Company. The total value of the contract was \$730 million, of which the Company's share is approximately \$550 million. The Greater Plutonio project involves the engineering, procurement, fabrication, and installation of umbilicals, risers and flowlines for the development of Bloc 18 offshore Angola (the AFMED region). Many of the construction activities will take place at depths of 1,200 to 1,500 metres. The Company expects that activities on this project will continue through 2007.

On 20 February 2004, the Company and its Sonastolt joint venture sold to Oceaneering International, Inc. their ROV Drill Support Business, consisting of a fleet of 44 ROVs and certain ancillary equipment, together with related contracts and employees, for approximately \$48 million. The sale realised approximately \$28 million in cash to the Company after settling the interests of Sonangol, its joint venture partners in Angola and transaction costs. Further cash was received from the joint venture in the form of dividends and loan repayments.

On 25 February 2004, SNSA completed the sale of 2,000,000 Common Shares of the Company in offshore transactions with institutional investors at the market price of 24 Norwegian kroner per share (approximately \$3.46 per share at current exchange rates).

On 26 February 2004, the Company reached a final settlement agreement with Algonquin Gas Transmission Company relating to the Company's claims for payment of unpaid invoices relating to the Duke Hubline project. The cash element of this settlement has been provided for in the Company's results for fiscal year 2003 and should therefore not affect the Company's results for fiscal year 2004. See 'Legal matters – Duke Hubline project'.

On 18 March 2004, the Company announced the settlement of the patent litigation with Technip. The Company does not expect the settlement to have a material impact on the Company's results for fiscal year 2004. See 'Legal matters – Technip'.

On 22 March 2004, the Company announced that, in addition to the 2005 Langede pipeline work scope awarded to the Company in November 2003, the Langede Group, with Norsk Hydro as operator, had exercised its option to award the Company the 2006 work scope for the Langede pipeline, which on completion, will be the longest offshore pipeline in the world. The Company will be responsible for the installation of 362 kilometres of 42-inch diameter pipeline. The two-year programme is valued at approximately \$250 million and will keep the *LB 200* pipeline barge occupied throughout 2005 and 2006.

In March 2004 the Company significantly increased its estimate of the range of costs to complete two major West African projects, Bonga and Sanha Bomboco, due to unexpected delays in completing offshore work and events outside the normal exposure and risk aspects of the contracts. The Company expects to recover a substantial portion of the increased expenditure through agreed variation orders.

On 20 April 2004, SNSA completed a previously announced debt for equity swap, under which SNTG subscribed for an additional 22,727,272 Common Shares in consideration for the cancellation of the Subordinated Note. Following this operation, the number of Common Shares in issue was 161,489,487. Through its wholly owned subsidiary SNTG, SNSA retains approximately a 49% holding following the completion of the Debt Conversion. Upon completion of the Subsequent Issue, SNSA expects to own, directly or indirectly, approximately 43% of the outstanding Common Shares of the Company.

In addition to the foregoing, the Company has disposed of certain assets and businesses as part of the Company's divestment programme, as described in 'Businesses and assets offered for sale' above. Also, as described under 'Funding and equity transactions since 30 November 2003', the Company increased its equity by approximately \$150 million (before transaction related expenses) in 2004.

Research and development and intellectual property

To support its engineering and operational activities, the Company holds a number of patents, trademarks, software and other intellectual property. The Company has 102 patents in force in 45 countries and currently a portfolio of 145 additional developments under patent application. A limited number of its patents are held in common with other industrial partners. The Company also conducts some of its operations under licensing agreements, allowing it to make use of specific techniques or equipment patented by third parties. The Company does not consider that any one patent or technology represents a significant percentage of its net operating revenue. As discussed under 'Legal matters', the Company recently settled a dispute with a competitor who was claiming damages for infringement of a patented technology.

The Company's research and development programmes have concentrated both on the requirements of its customers, who are constantly seeking to develop oil and gas reserves in deeper waters, and increasing the efficiency of its offshore equipment and operations. The Company has research and development programmes aimed at developing new and extending existing technology for the installation, repair and maintenance of offshore structures, particularly in ultra deep water (beyond 1,500 metres). Recent successes include the riser bundle tower system, which was designed, built, and installed in 1,400 metres of water for the Girassol project in Angola, and the MATIS™ pipeline connection system. The Company's research and development activities are in general carried out internally using both dedicated research personnel and as part of specific projects. Where appropriate, external research and development is performed either through strategic technological alliances or joint industry collaborative projects. The Company's expenditures on Company-sponsored research and development were approximately \$1 million in each of fiscal years 2003, 2002 and 2001.

Inflation

The Company's business transactions in high-inflation countries such as Brazil and Nigeria are substantially denominated in stable currencies, such as the US dollar, and inflation therefore does not materially affect the consolidated financial results.

Market risk, foreign exchange and interest rate exposure

The Company is exposed to market risk, including changes in interest rates and currency exchange rates. To manage the volatility relating to these exposures on a consolidated basis, wherever possible the Company enters into derivative instruments to hedge currency exposures in accordance with the Company's policies. The financial impact of these instruments is offset by corresponding changes in the underlying exposures being hedged. The Company does not hold or issue derivative instruments for trading purposes.

The Company's reporting currency is the US dollar. The majority of net operating expenses are denominated in the functional currency of the individual operating subsidiaries. The US dollar is the functional currency of the most significant subsidiaries within the AFMED, NAMEX, SAM and AME regions. In NEC region, the functional currencies are the Norwegian kroner, the British pound sterling, Canadian and US dollars. The Company's exposure to currency rate fluctuations results from its net investments in foreign subsidiaries, primarily in the U.K., Norway, France and Brazil, and from its share of the local currency earnings in its operations in the AFMED, NEC and SAM regions. The Company does not use derivative instruments to hedge the value of investments in foreign subsidiaries. The net translation of adjustments arising on the above currency exposures were gains of \$25.4 million, \$41.7 million and \$4.4 million for fiscal years 2003, 2002 and 2001, respectively. These are recorded in Other comprehensive income in the Consolidated statement of shareholders' equity.

The Company is also exposed to fluctuations in several other currencies resulting from operating expenditures and one-off liabilities. The Company's currency rate exposure policy prescribes the range of allowable hedging activity. The Company primarily uses forward exchange contracts to hedge capital expenditures and operational non-functional currency exposures on a continuing basis for periods consistent with the Company's committed exposures. All of the instruments used are hedged against forecasted underlying operating exposures and are designated as cash flow hedges. The Company does not engage in currency speculation. There is a greater risk of foreign exchange fluctuations affecting the Company's operating results in fiscal year 2004 due to the Company's inability to gain access to forward, exchange contract facilities.

The Company's exposure to third-party interest rate fluctuations results from floating-rate long-term credit facilities tied to LIBOR.

The Company uses a value-at-risk ('VAR') model to estimate the maximum potential loss on financial instruments that could occur from adverse movements in either interest rates or foreign exchange rates. The VAR model uses historical foreign exchange rates and interest rates to estimate the volatility and correlation of these rates in future periods. It estimates a potential one-day loss in the fair market value of the instruments using statistical modelling techniques and including substantially all market risk exposures, specifically excluding joint venture investments. The VAR model estimates were made assuming normal market conditions and a 95% confidence level.

The 95% confidence level signifies the Company's degree of confidence that actual losses would not exceed the estimated losses shown in the table below. The amounts shown here disregard the possibility that interest rates and foreign currency rates could move favourably. The VAR model assumes that all movements in these rates would be adverse. Actual experience has shown that gains and losses tend to offset each other over time, and it is highly unlikely that the Company could experience losses such as these over an extended period of time. These amounts should not be considered to be projections of future losses, since actual results may differ significantly depending upon activity in the global financial markets.

Management's discussion and analysis continued

The fair value losses shown in the table below have no impact on the Company's results or financial condition.

VAR As of 30 November (in millions)	2003 \$	2002 \$
Interest rates	0.1	0.2
Foreign exchange rates	2.1	2.4

The decrease in the VAR from \$2.4 million to \$2.1 million is attributable to the increased volatility in the exchange rates between the US dollar and each of the euro, British pound sterling and the Norwegian kroner, which was more than offset by a significant reduction in the financial instruments held by the Company during the second half of fiscal year 2003.

A discussion of the Company's accounting policies for financial instruments is included below in 'Critical accounting policies – accounting for derivatives' and in Note 2 to the consolidated financial statements. Disclosure relating to financial instruments is included in Note 26 to the consolidated financial statements.

Impact of new accounting standards

In December 2003, the Financial Accounting Standards Board ('FASB') issued a revision to Interpretation No. 46 'Consolidation of Variable Interest Entities, an Interpretation of Accounting Research Bulletin ('ARB') No. 51' ('FIN 46R' or the 'Interpretation'). FIN 46R clarifies the application of ARB No. 51 'Consolidated Financial Statements,' to certain entities in which equity investors do not have the characteristics of a controlling financial interest or do not have sufficient equity at risk for the entity to finance its activities without additional subordinated financial support. FIN 46R requires the consolidation of these entities, known as Variable Interest Entities ('VIEs'), by the primary beneficiary of the entity. The primary beneficiary is the entity, if any, that will absorb a majority of the entity's expected losses, receive a majority of the entity's expected residual returns, or both.

Among other changes, the revisions of FIN 46R (a) clarified some requirements of the original FIN 46, which had been issued in January 2003, (b) eased some implementation problems, and (c) added new scope exceptions. FIN 46R deferred the effective date of the interpretation for public companies, to the end of the first reporting period ending after 15 March 2004, except that all public companies must at a minimum apply the provisions of the interpretation to entities that were previously considered 'special-purpose entities' under FASB literature prior to the issuance of FIN 46R by the end of the first reporting period ending after 15 December 2003. The Company is currently assessing the impact of the adoption of FIN 46 on its financial position, cash flows and results of operations.

On adoption of FIN 46R, it is possible the Company will consolidate two VIEs, Sonamet and Sonastolt. The Company has 55% majority ownership of these two joint ventures in Angola, but they are not currently consolidated due to the significant participating influence of the other main shareholder, Sociedade Nacional de Combustiveis de Angola – Sonongal U.E.E. ('Sonongal'). Sonamet operates a fabrication yard at Lobito, which manufactures structures and components for offshore projects. This offers the Company a strategic advantage in the West African offshore market, where contractors are often required to utilise a specified proportion of local resources. Sonastolt is a provider of local and offshore support personnel and equipment.

(in millions)	Sonamet \$	Sonastolt \$
Total assets	176.2	91.1
Maximum exposure to loss	7.4	32.4

The maximum exposure to loss refers to the maximum loss that the Company could be required to record in its income statement as a result of its involvement with a VIE. It does not consider the probability of such losses actually being incurred.

In December 2003, the revised Statement of Financial Accounting Standard ('SFAS') 132 'Employers' Disclosures about Pensions and Other Post-retirement Benefits – an amendment of SFASs No. 87, 88, and 106' ('SFAS 132R'). This Statement revises employers' disclosures about pension plans and other post-retirement benefit plans. It does not change the measurement or recognition of those plans required by SFAS No. 87 'Employers' Accounting for Pensions', No. 88 'Employers' Accounting for Settlements and Curtailments of Defined Benefit Pension Plans and for Termination Benefits', and No. 106 'Employers' Accounting for Post-retirement Benefits Other Than Pensions'. SFAS No. 132R This Statement retains the disclosure requirements contained in SFAS No. 132 'Employers' Disclosures about Pensions and Other

Post-retirement Benefits', which it replaces. It requires additional disclosures to those in the original SFAS No. 132 about the assets, obligations, cash flows, and net periodic benefit cost of defined benefit pension plans and other defined benefit post-retirement plans. The required information should be provided separately for pension plans and for other post-retirement benefit plans. The Company will adopt the disclosure requirements of SFAS 132R during the fiscal year 2004.

Changes in share capital

During fiscal year 2003, the Company settled the minimum share price guarantee in respect of the remaining 879,121 Class A Shares (subsequently converted to Common Shares) issued to NKT Holdings A/S as consideration for the Company's purchase of its share in NKT Flexibles. The 879,121 shares had been previously issued to NKT Holdings A/S with a minimum guaranteed price averaging \$15.30 per share. In March 2003, the Company repurchased the shares for cash of \$13.5 million. \$1.0 million of the outlay represented the market price at the date of repurchase by the Company, and the remaining \$12.5 million represented the settlement of the guarantee. The 879,121 Common Shares were held as Treasury Shares as of 30 November 2003.

During fiscal year 2002, the Company settled the minimum share price guarantee in respect of the 6,142,857 Class A Shares (subsequently converted to Common Shares) issued to Groupe Vinci S.A. as consideration for the acquisition of ETPM S.A. Under the terms of the sale and purchase agreement, these shares were issued to Vinci with a minimum guarantee price of \$18.50 per share. In May 2002, the Company repurchased these shares for cash of \$113.6 million to settle the guarantee. \$54.7 million of the outlay represented the market price of the shares repurchased by the Company, and the remaining \$58.9 million represented the settlement of the guarantee.

During fiscal year 2002, the Company settled the minimum share price guarantee in respect of 249,621 of the 1,758,242 Class A Shares (subsequently converted to Common Shares) issued to NKT Holdings A/S as consideration for the Company's purchase of its share in NKT Flexibles. The 249,621 shares had been previously issued to NKT Holdings A/S with a minimum guaranteed price of \$13.65 per share. In February 2002, the Company repurchased the shares for cash of \$3.4 million. \$1.8 million of the outlay represented the market price at the date of repurchase by the Company, and the remaining \$1.6 million represented the settlement of the guarantee.

As of 30 November 2003, the Company had outstanding 76.3 million Common Shares and 34.0 million Class B Shares (which were economically equivalent to 17.0 million Common Shares and were all owned by SNTG) making a total of 93.3 million Common Share equivalents.

In February 2004, as described in Note 28 to the consolidated financial statements, the Private Placement of 45.5 million Common Shares raised gross proceeds of \$100.1 million, and the 34.0 million Class B Shares held by SNTG were converted into 17.0 million Common Shares on a two-for-one basis. This share conversion has the effect of aligning the economic and voting interests of the Company's shareholders, as there is now only one class of shares issued by the Company. Further, on 20 April 2003 SNSA completed the Debt Conversion of \$50 million of subordinated debt in return for the issuance of 22,727,272 Common Shares.

The total number of Common Shares outstanding at the completion of those transactions will be 161.5 million. SNSA ceased to be a majority shareholder of the Company in February 2004.

Related party transactions

Corporate services agreement

Pursuant to a corporate services agreement, SNSA supplies through its subsidiaries, financial, risk management, public relations and other services to the Company for an annual fee based on costs incurred in rendering those services. The fee is subject to negotiation and agreement between the Company and SNSA on an annual basis. The fees of these management services were \$3.4 million, \$3.2 million and \$3.7 million for fiscal years 2002, 2001 and 2000, respectively.

Captive insurance company

SNSA owns Marlowe Insurance Ltd., a Bermuda captive insurance company through which the Company's assets and activities are insured. The Company owns a separate class of non-voting preference shares which gives the Company an entitlement to receive a dividend in respect of profits earned by Marlowe Insurance Ltd. in respect of the Company's policies. The relationship among the shareholders and the obligations of each shareholder are set forth in a shareholder's agreement. The Company does not intend, and it is not currently aware of any intention on the part of SNSA, to change this relationship in the future.

Registration rights agreement

The Company has entered into a registration rights agreement with SNTG, which gives SNTG the right to require the Company (a 'demand right') to file up to five registration statements under the U.S. Securities Act of 1933, as amended, covering SNTG's Common Shares, subject to the limitations on such demand rights contained in the agreement. Additionally, SNTG has the right to include its Common Shares in registration statements that the Company may file on its behalf or on behalf of other shareholders.

Service mark agreement

The Company and SNSA are parties to an agreement under which the Company has been granted the right to use the Stolt name and logo, without payment of any royalty, so long as SNSA or its affiliates own more than one-third of the Company's voting shares.

Cross-default in certain credit and guarantee facilities

As described in more detail in Note 27 to the consolidated financial statements, SNSA has guaranteed \$4.8 million of bank guarantees issued under other bank guarantee arrangements, while SNSA and SNTG jointly and severally have guaranteed bank guarantees issued under the guarantee portion of the \$55/45 million credit/guarantee facility, as well as bank guarantees issued under the \$44 million guarantee facility. Additionally, certain actions or events undertaken by SNSA and SNTG including without limitation, incurring unpermitted liens, defaulting under certain debt facilities, and failing to comply with non-appealable court orders, will result in a cross-default under these facilities.

Other matters

As described in Note 15 to the consolidated financial statements, on 30 June 2003, as a condition to the receipt of waivers of potential defaults and amendments to the financial covenants contained in the Existing Credit Facility Agreements, SNTG agreed to provide the Company with a \$50 million subordinated loan bearing an interest rate of 12% per annum. The subordinated debt is fully subordinated to all indebtedness owed under and pursuant to the Existing Credit Facility Agreements. Subsequent to 30 November 2003, the Company and SNTG have irrevocably agreed to convert, before 31 December 2004, the subordinated debt in return for the issuance of 22,727,272 Common Shares to SNTG or a subsidiary thereof, representing a conversion price of \$2.20 per share.

As described in Note 21 to the consolidated financial statements, in May 2002 SNSA advanced \$64.0 million to the Company in order to assist the Company to repurchase the 6,142,857 Common Shares previously issued to Vinci and to settle the share price guarantee. The Company subsequently issued these and other shares to SNSA during fiscal year 2002. The proceeds of \$38.4 million from the issue of the shares were used to repay the debt due to SNSA. In November 2002, the Company issued 6,019,287 Common Shares to SNSA for proceeds of \$25.6 million to repay the remaining outstanding portion of the \$64.0 million loan.

In February 2003 the Company made a drawdown of \$50.0 million against the SNSA Liquidity Line, discussed in 'Description of indebtedness'. This amount was repaid in March 2003.

In June 2003 the Company made a single drawdown of \$15 million against the SNSA Liquidity Line. This amount was repaid in the third quarter of 2003.

During each fiscal year 2003, 2002 and 2001 the Company made a payment of \$50,000 for marketing services to a company in which a non-executive Director has an interest.

In the light of the fact that, after the completion of the Private Placement, the Share Conversion and the Debt Conversion, the Company will no longer be a majority-owned subsidiary, SNSA has informed the Board of Directors that SNSA will be subject to certain contractual restrictions under Existing Credit Facility Agreements on its ability to make investments and provide guarantees or other financial support to the Company.

The Company routinely engages in transactions with a range of other related parties whose relationship with the Company arises through the joint ventures discussed above in 'Investments in and long-term funding to non-consolidated joint ventures'.

In December 2002, the Company made a capital contribution of \$12.6 million in NKT Flexibles. In the same month, NKT Flexibles repaid an outstanding loan for \$12.6 million due to the Company.

As discussed in 'Impairments' above, a proposal was received from Sonamet in the fourth quarter of fiscal year 2003 to acquire a large quantity of the Company's equipment located at the Lobito fabrication yard, which were leased to Sonamet on a long-term basis. The carrying amount was reduced to the expected sales price, and the assets were sold to Sonamet at that price after the end of fiscal year 2003.

Forward-looking statements

Certain statements in this Annual Report, including the message from the Chairman and the operational review from the Chief Executive Officer, describe plans, expectations, beliefs, intentions or strategies regarding the future and constitute 'forward-looking statements' as defined in the U.S. Private Securities Litigation Reform Act of 1995. These statements may be identified by the use of words like 'anticipate', 'believe', 'estimate', 'expect', 'intend', 'may', 'plan', 'project', 'will', 'should', 'seek' and similar expressions. Actual and future results and trends could differ materially from those set forth in such statements due to various factors. Such factors include, among others: (i) the level of the Company's indebtedness, operating restrictions contained in its financing arrangements, its ability to comply with financial and other covenants in its financing agreements, its ability to refinance its indebtedness on acceptable terms as it comes due and the impact of floating interest rates on its debt service costs; (ii) the Company's ability to deliver fixed price projects in accordance with customer expectations and the parameters of its bids and avoid cost overruns; (iii) the Company's ability to collect receivables, negotiate variation orders and collect the related revenues; (iv) capital expenditures by oil and gas companies; (v) oil and gas prices; (vi) delays or cancellation of projects included in the Company's backlog; (vii) general economic conditions and competition in the industries and markets in which the Company operates; (viii) prevailing prices for the Company's products and services; (ix) the loss of, or deterioration of the Company's relationship with, any significant customers; (x) the outcome of legal proceedings; (xi) uncertainties inherent in operating internationally, including economic, political and social instability, boycotts or embargoes, labour unrest, changes in foreign governmental regulations, corruption and currency fluctuations; (xii) liability to third parties for the failure of the Company's joint venture partners to fulfil their obligations; (xiii) changes in, or the Company's failure to comply with, applicable laws and regulations; (xiv) cost and availability of raw materials; (xv) operating hazards, including spills, environmental damage, personal or property damage and business interruptions caused by weather, mechanical failures or human error; (xvi) the impact of accounting for projects on a percentage-of-completion method, which could reduce or eliminate reported profits; (xvii) adverse weather conditions; (xviii) the Company's ability to keep pace with technological changes; and (xix) other factors which are described from time to time in the Company's public filings with the SEC, including but not limited to the Company's Annual Report on Form 20-F. Copies of these filings may be obtained by contacting the Company or the SEC.

Selected consolidated financial data

For the year ended 30 November (in millions, except per share data)	2003 \$	2002 \$	2001 \$	2000 \$	1999 \$
Net operating revenue	1,482.3	1,437.5	1,255.9	983.4	640.7
Net operating (loss) income	(380.5)	(123.6)	36.4	(4.9)	24.2
Net (loss) income	(418.1)	(151.9)	(14.2)	(34.4)	16.2
Net (loss) income per Common Share and Common Share equivalent					
Basic	(4.51)	(1.79)	(0.16)	(0.44)	0.27
Diluted	(4.51)	(1.79)	(0.16)	(0.44)	0.27
Weighted average number of Common Shares and Common Share equivalent outstanding ^(a) :					
Basic	92.6	85.0	87.2	78.8	59.1
Diluted	92.6	85.0	87.2	78.8	59.5

The Company has never paid a dividend.

As of 30 November (in millions, except per share data)	2003 \$	2002 \$	2001 \$	2000 \$	1999 \$
Total assets	1,242.6	1,458.6	1,560.3	1,402.8	843.3
Current assets less current liabilities (including current portion of long-term debt and capital lease obligations and debt due to SNSA)	(159.8)	34.6	78.2	12.7	31.9
Non-current assets	608.9	868.2	987.3	1,008.3	591.2
Long-term debt, including long-term debt due to SNSA, and capital lease obligations (including current portion)	385.0	335.0	358.7	292.5	200.7
Deferred long-term taxes, accrued pensions and other long-term liabilities	38.1	43.4	63.1	61.0	14.5
Shareholders' equity	107.3	517.1	660.0	669.4	408.4
Book value per Common Share and Common Share equivalent ^(a)	1.16	5.54	7.57	7.68	6.90
Total number of Common Shares and Common Share equivalent outstanding ^(a)	92.7	93.3	87.2	87.2	59.2

(a) All share data and per share data have been restated to reflect the share reclassification on 7 March 2001 whereby Class A Shares were reclassified as Common Shares on a one-for-one basis.

Independent auditors' report

To Stolt Offshore S.A.

We have audited the accompanying consolidated balance sheet of Stolt Offshore S.A. (a Luxembourg company) and its subsidiaries as of 30 November 2003 and 2002, and the related consolidated statements of operations, shareholders' equity and cash flows for the years ended 30 November 2003 and 2002. The consolidated financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on the consolidated financial statements based on our audit. The consolidated financial statements of the Company for the year ended 30 November 2001, before the reclassification and inclusion of disclosures discussed in Note 2 to the financial statements, were audited by other auditors who have ceased operations. Those auditors expressed an unqualified opinion on those financial statements in their report dated 30 January 2002.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, such consolidated financial statements present fairly, in all material respects, the consolidated financial position of Stolt Offshore S.A. and subsidiaries as of 30 November 2003 and 2002 and the consolidated results of its operations and its cash flows for the years ended 30 November 2003 and 2002, in conformity with accounting principles generally accepted in the United States of America.

As discussed above, the consolidated financial statements of the Company for the year ended 30 November 2001 were audited by other auditors who ceased operations. As described in Note 2, these consolidated financial statements have been revised to reflect reclassifications and disclosures to conform to the 2003 presentation. Our audit procedures with respect to the reclassifications included agreeing the previously reported line items or disclosure amounts to the Company analyses, comparing reclassification amounts in the analyses to supporting documentation and testing the mathematical accuracy of the analyses into the previously issued financial statements. Our audit procedures with respect to the disclosures included agreeing the additional disclosures to the Company's underlying records obtained from management. In our opinion such reclassifications and disclosures are appropriate and have been properly applied. However, we were not engaged to audit, review or apply any procedures to the 2001 consolidated financial statements of the Company other than with respect to such reclassifications and disclosures and, accordingly, we do not express an opinion or any other form of assurance on the 2001 consolidated financial statements taken as a whole.

Deloitte & Touche LLP
Glasgow, United Kingdom
29 April 2004

To Stolt Offshore S.A.

We have audited the accompanying consolidated balance sheets of Stolt Offshore S.A. (a Luxembourg company) and its subsidiaries as of 30 November 2001 and 2000, and the related consolidated statements of operations, shareholders' equity and cash flows for each of the three years in the period ended 30 November 2001. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with generally accepted auditing standards in the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Stolt Offshore S.A. and subsidiaries as of 30 November 2001 and 2000 and the results of their operations and their cash flows for each of the three years in the period ended 30 November 2001, in conformity with accounting principles generally accepted in the United States.

Arthur Andersen⁽¹⁾
Glasgow, United Kingdom
30 January 2002

(1) This report is a copy of the previously issued report covering the years ended 30 November 2001, 2000 and 1999. The predecessor auditors have not reissued their report.

Consolidated statements of operations

For the year ended 30 November (in thousands, except per share data)		2003 \$	2002 \$	2001 \$
Net operating revenue		1,482,273	1,437,488	1,255,938
Operating expenses		(1,566,524)	(1,374,354)	(1,144,290)
Gross (loss) profit – \$		(84,251)	63,134	111,648
– %		(5.7%)	4.4%	8.9%
Equity in net income of non-consolidated joint ventures		403	5,287	11,655
Selling, general, and administrative expenses ('SG&A')	Note 2	(102,508)	(89,678)	(81,306)
Impairment of tangible fixed assets	Note 9	(176,522)	(3,983)	–
Impairment of goodwill	Note 10	–	(106,435)	–
Impairment of intangible assets	Note 10	–	–	(7,932)
Restructuring charges	Note 18	(16,233)	–	–
(Loss) gain on sale of fixed assets		(328)	8,003	1,234
Other operating (loss) income, net		(1,056)	65	1,066
Net operating (loss) income		(380,495)	(123,607)	36,365
Non-operating (expense) income				
Interest expense		(27,886)	(18,873)	(29,271)
Interest income		3,093	633	2,451
Foreign currency exchange (losses) gains, net		(8,905)	212	(323)
(Loss) income before minority interests and taxes		(414,193)	(141,635)	9,222
Minority interests		(4,549)	(2,062)	(2,806)
(Loss) income before income taxes		(418,742)	(143,697)	6,416
Income tax benefit (provision)	Note 12	655	(8,158)	(20,619)
Net loss		(418,087)	(151,855)	(14,203)
Earnings per Common Share				
Net loss per Common Share and Common Share equivalent:				
Basic		(4.51)	(1.79)	(0.16)
Diluted		(4.51)	(1.79)	(0.16)
Weighted average number of Common Shares and Common Share equivalents outstanding				
Basic	Note 22	92,624	85,010	87,201
Diluted	Note 22	92,624	85,010	87,201

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

Consolidated balance sheets

As of 30 November (in thousands)	2003 \$	2002 \$
Assets		
Current assets		
Cash and cash equivalents	81,910	11,672
Restricted cash deposits	Note 4 2,108	1,732
Trade receivables (net of allowance for doubtful debt of \$15.772 million in 2003 and \$5.861 million in 2002)	Note 5 358,330	428,102
Inventories and work-in-progress	Note 6 22,100	17,525
Receivables due from related parties and short-term advances to non-consolidated joint ventures	Note 11 27,565	62,438
Forward contracts	Note 26 957	23,438
Prepaid expenses and other current assets	34,654	45,468
Assets held for sale	Note 8 106,152	–
Total current assets	633,776	590,375
Fixed assets, at cost	Note 9 933,336	1,188,607
Less accumulated depreciation and amortisation	Note 9 (418,731)	(405,764)
Total fixed assets, net	514,605	782,843
Goodwill	Note 10 5,999	5,999
Other intangible assets	Note 10 248	4,717
Deposits and non-current receivables	33,381	38,548
Investments in and advances to non-consolidated joint ventures	Note 11 42,962	28,774
Deferred taxes	Note 12 8,314	3,101
Prepaid pension asset	Note 13 3,375	4,247
Total assets	1,242,660	1,458,604
Liabilities and shareholders' equity		
Current liabilities		
Bank overdrafts and lines of short-term credit	Note 14 2,473	15,966
Short-term payables due to Stolt-Nielsen S.A. (SNSA)	Note 17 18,394	633
Subordinated note due to SNSA	Note 15 50,000	–
Current maturities of long-term debt and capital lease obligations	Note 15 91,504	17
Accounts payable and accrued liabilities	Note 16 430,772	387,634
Accrued salaries and benefits	36,988	51,853
Advance billings	33,181	40,168
Deferred short-term taxes	Note 12 4,471	–
Other current liabilities	67,932	59,509
Liabilities held for sale	Note 8 57,855	–
Total current liabilities	793,570	555,780
Long-term debt and capital lease obligations	Note 15 293,506	335,007
Deferred long-term taxes	Note 12 2,000	7,189
Other long-term liabilities	26,408	26,886
Accrued pension liability	Note 13 9,726	9,326
Minority interests	10,175	7,359
Commitments and contingencies	Note 25	
Shareholders' equity	Note 21	
Common Shares, \$2.00 par value – 140,000,000 shares authorised (2002: 140,000,000), 76,262,215 shares issued and 75,383,094 shares outstanding (2002: 76,262,215 shares issued and outstanding)	152,524	152,524
Class B Shares, \$2.00 par value – 34,000,000 shares authorised, issued and outstanding (2002: 34,000,000)	68,000	68,000
Treasury Shares – 879,121 Common Shares (2002: nil)	(1,002)	–
Paid-in surplus	404,230	416,677
Deficit	(535,579)	(117,492)
Accumulated other comprehensive income (loss)	19,102	(2,652)
Total shareholders' equity	107,275	517,057
Total liabilities and shareholders' equity	1,242,660	1,458,604

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

Consolidated statement of shareholders' equity

(in thousands, except share data)	Common Shares \$	Class A Shares \$	Class B Shares \$	Paid-in surplus \$	Retained earnings (Deficit) \$	Treasury Shares \$	Accumulated other comprehensive loss \$	Total shareholders' equity \$	Comprehensive income (loss) \$
Balance, 30 November 2000	45,446	94,860	68,000	463,379	66,639	-	(68,875)	669,449	
Reclassification of Class A Shares to Common Shares	94,860	(94,860)	-	-	-	-	-	-	
Net loss	-	-	-	-	(14,203)	-	-	(14,203)	(14,203)
Translation adjustment in respect of SFAS No.133	-	-	-	-	-	-	(2,238)	(2,238)	(2,238)
Gain on hedging reclassified into earnings	-	-	-	-	-	-	2,238	2,238	2,238
Translation adjustments, net	-	-	-	-	-	-	4,389	4,389	4,389
Comprehensive loss	-	-	-	-	-	-	-	-	(9,814)
Exercise of share options	151	-	-	236	-	-	-	387	
Balance, 30 November 2001	140,457	-	68,000	463,615	52,436	-	(64,486)	660,022	
Purchase of 6,392,478 Treasury Shares at market value ^(a)	-	-	-	-	-	(56,493)	-	(56,493)	
Settlement of share price guarantee ^(a)	-	-	-	(60,557)	-	-	-	(60,557)	
Sale of 6,392,478 Treasury Shares	-	-	-	-	(18,073)	56,493	-	38,420	
Issuance of 6,019,287 Common Shares	12,038	-	-	13,542	-	-	-	25,580	
Net loss	-	-	-	-	(151,855)	-	-	(151,855)	(151,855)
Net gains in respect of derivative instruments, net of tax of \$3,184	-	-	-	-	-	-	22,169	22,169	22,169
Translation adjustments, net	-	-	-	-	-	-	41,700	41,700	41,700
Minimum pension liability adjustment, net of tax of \$915	-	-	-	-	-	-	(2,035)	(2,035)	(2,035)
Comprehensive loss	-	-	-	-	-	-	-	-	(90,021)
Exercise of share options	29	-	-	77	-	-	-	106	
Balance, 30 November 2002	152,524	-	68,000	416,677	(117,492)	-	(2,652)	517,057	
Purchase of 879,121 Treasury Shares at market value ^(b)	-	-	-	-	-	(1,002)	-	(1,002)	
Settlement of share price guarantee ^(b)	-	-	-	(12,447)	-	-	-	(12,447)	
Net loss	-	-	-	-	(418,087)	-	-	(418,087)	(418,087)
Net losses in respect of derivative instruments, net of tax of \$1,068	-	-	-	-	-	-	(362)	(362)	(362)
Minimum pension liability adjustment, net of tax of \$326	-	-	-	-	-	-	(3,282)	(3,282)	(3,282)
Translation adjustments, net	-	-	-	-	-	-	25,398	25,398	25,398
Comprehensive loss	-	-	-	-	-	-	-	-	(396,333)
Balance, 30 November 2003	152,524	-	68,000	404,230	(535,579)	(1,002)	19,102	107,275	

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

(a) Purchase of 249,621 Treasury Shares from NKT Holdings A/S and 6,142,857 Treasury Shares from Vinci. Further details are provided in Note 3.

(b) Purchase of 879,121 Treasury Shares from NKT Holdings A/S. Further details are provided in Note 3.

Consolidated statements of cash flows

For the year ended 30 November (in thousands)	2003 \$	2002 \$	2001 \$
Cash flows (used in) provided by operating activities			
Net loss	(418,087)	(151,855)	(14,203)
Adjustments to reconcile net loss to net cash (used in) provided provided by operating activities			
Depreciation and amortisation	93,499	92,110	91,750
Impairment of goodwill and other intangibles	–	106,435	7,932
Impairment of tangible fixed assets	176,522	3,983	–
Amortisation of dry-dock costs	13,967	15,378	8,441
Undistributed equity in net income of non-consolidated joint ventures	(403)	(5,287)	(11,655)
Dividends from non-consolidated joint ventures	14,054	13,195	12,235
Minority interest in consolidated subsidiaries	4,548	2,062	2,806
Deferred tax	(5,514)	(5,906)	(4,433)
Loss (gain) on sale of fixed assets	328	(8,003)	(1,234)
Changes in operating assets and liabilities, net of acquisitions			
Decrease (increase) in trade receivables	109,349	43,980	(141,003)
Decrease (increase) in prepaid expenses, other current assets and long-term receivables	8,922	(18,198)	10,024
Net realised and unrealised mark to market hedging transactions	(11,469)	–	–
(Increase) decrease in inventories and work-in-progress	(3,940)	2,965	8,241
(Decrease) increase in accounts and notes payable	(59,666)	(11,992)	91,021
(Decrease) increase in accrued salaries and benefits	(7,173)	5,295	635
Increase (decrease) in other short-term and other long-term liabilities	68,858	21,147	(25,928)
Payments of dry-dock costs	(11,315)	(20,632)	(17,893)
Net cash (used in) provided by operating activities	(27,520)	84,677	16,736
Cash flows provided by (used in) investing activities			
Acquisition of subsidiaries, net of cash acquired	–	–	(61)
Settlement of share price guarantees	(12,447)	(60,557)	–
Purchase of fixed assets	(21,895)	(54,634)	(62,868)
Proceeds from sale of tangible fixed assets	3,961	23,526	5,590
Investment in non-consolidated equity investees	(14,248)	–	–
Increase in investments and other long-term financial assets	(2,382)	(13,638)	(26,715)
Decrease in investments and other long-term financial assets	34,306	28,855	626
Net cash provided by (used in) investing activities	(12,705)	(76,448)	(83,428)
Cash flows provided by (used in) financing activities			
Net (decrease) increase in bank overdraft	(13,846)	10,184	3,332
Drawdown of existing bank credit lines	230,000	–	69,985
Repayments of existing bank credit facilities	(80,000)	–	–
(Increase) decrease in restricted cash deposits securing capital lease, long-term debt	(361)	(146)	2,628
Proceeds from monetisation of hedges	16,827	–	–
Repayments of capital lease obligations	(18)	(23,657)	(3,845)
Drawdown of short-term SNSA funding	15,000	64,000	–
Repayment of short-term SNSA funding	(55,000)	–	–
Repurchase of Treasury Shares	(1,002)	(56,493)	–
Exercise of share options	–	106	387
Dividends paid to minority interests	(2,194)	(2,352)	–
Net cash provided by (used in) financing activities	109,406	(8,358)	72,487
Effect of exchange rate changes on cash	1,057	131	(440)
Net increase in cash and cash equivalents	70,238	2	5,355
Cash and cash equivalents at beginning of year	11,672	11,670	6,315
Cash and cash equivalents at end of year	81,910	11,672	11,670

Details of non-cash transactions are provided in Note 2.

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

Notes to the consolidated financial statements

1. The Company

Stolt Offshore S.A., a Luxembourg company, together with its subsidiaries (collectively, 'the Company') is one of the largest offshore services contractors in the world. The Company designs, procures, builds, installs and services a range of offshore surface and subsurface infrastructure for the global oil and gas industry. The Company specialises in creating and applying innovative and efficient solutions in response to the technical complexities faced by offshore oil and gas companies as they explore and develop production fields in increasingly deeper water and more demanding offshore environments.

The market for the Company's services is dependent upon the success of exploration and the level of investment in offshore exploration and production by the major oil companies. Such investment is cyclical in nature.

2. Accounting policies

Going concern

The financial statements have been prepared on the basis that the Company is a going concern. The Company's latest forecasts for fiscal year 2004 indicate that there will be a narrow margin of compliance with the debt to EBITDA ratio covenant at the end of the fourth quarter of 2004. The Company's ability to remain within its covenants is dependent on (i) its operating performance, (ii) the successful completion of the Subsequent Issue ('Subsequent Issue') during the second quarter of fiscal year 2004, (iii) its ability to recover variation orders and claims from customers where additional contract costs are incurred, and (iv) the success of the Company's plans to divest certain assets and businesses.

The Company has consequently made contingency plans in the event that it is unable to comply with its covenants as follows: (i) the Company has the option of raising unsecured debt finance as an alternative means of repaying bank facilities; (ii) the Company can defer discretionary capital expenditures; (iii) the Company has the option of raising further equity; and (iv) the Company can seek to obtain a waiver of covenant breaches if they were to arise.

Principles of consolidation

The consolidated financial statements have been prepared in accordance with accounting principles generally accepted in the United States and include the accounts of all majority-owned companies in which the Company has operating control. All significant inter-company transactions and balances have been eliminated.

The Company has invested in several joint ventures. These include Seaway Heavy Lifting ('SHL') and NKT Flexibles I/S ('NKT Flexibles'), Sonamet, Sonastolt and project-specific joint ventures. In these joint ventures, the Company has economic and voting interests of 27.5% to 55%. The Company accounts for its investments in non-consolidated joint ventures under the equity method, including circumstances where the Company owns more than 50% of the voting interest, but the Company's ability to control the operation of the investee is restricted by the significant participating interest held by another party. This applies to Sonamet and Sonastolt, where certain operating decisions require unanimous agreement of the Board, which has equal representation from the two principal joint venture partners.

The 2002 and 2001 consolidated financial statements have been revised to reflect reclassifications and disclosures to conform with the 2003 presentation as follows:

Presentation of financial statements

- ▶ Following a review of the various types of expenses included in the operating and overhead expense categories, it was decided that it would be more appropriate for the cost associated with tendering and product line management to be taken out of Operating expenses and into the renamed category 'Selling, general and administrative expenses' ('SG&A'). At the same time it was decided that the cost associated with Health, Safety, Environment and Quality ('HSE&Q') should be taken from SG&A into Operating expenses. The rationale for these changes is that tendering is a sales-related activity, and under the new group organisational structure, the regional management is focused on the general management of the Company. Prior year reported amounts have been reclassified for comparability. HSE&Q costs are reclassified because they are incurred in relation to project work.
- ▶ There has been a reclassification of selling costs of \$16.7 million and \$17.3 million in 2002 and 2001 respectively, from Operating expenses to SG&A in the consolidated statement of operations. The changes are a result of the costs associated with tendering and product line management taken out of Operating expenses and into SG&A (\$19.0 million and \$18.9 million respectively for 2002 and 2001) and the cost associated with Health, Safety, Environment and Quality from SG&A to Operating expenses (\$2.3 million and \$1.6 million respectively for 2002 and 2001).

- ▶ There has been a reclassification of \$4.0 million for 2002 from Operating expenses to 'Impairment of tangible fixed assets'.
- ▶ There has been a reclassification of components making up the balance of \$17.5 million for 2002 in 'Inventories and Work in progress'.
- ▶ Reclassifications within the tables for 2002 and 2001 respectively in Note 20 'Segment and related information' to reflect the redefined regional structure and the redefined service capabilities.
- ▶ Reclassification of gains on disposals of assets of \$1.2 million in 2001 from 'Non-operating (expense) income' to 'Gain on sale of fixed assets' in the consolidated statement of operations.
- ▶ Reclassification of other income (loss) of \$1.1 million in 2001 from 'Non-operating (expense) income' to 'Other operating income (loss), net' in the consolidated statement of operations.
- ▶ Reclassification of 'Dividends from non-consolidated joint ventures' of \$12.2 million in 2001 from 'Net cash used in investing activities' to 'Net cash provided by operating activities'; and reclassification of \$0.6 million in 2001 from 'Increase in investments and other non-current financial assets' to 'Decrease in investments and other non-current financial assets' in the consolidated statements of cash flows.
- ▶ Reclassifications within the table reconciling the Company's effective tax rate to the statutory tax rate in 2001 in Note 12, 'Income taxes'.

Use of estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosures of contingent assets and liabilities as of the dates of the financial statements and reported amounts of revenues and expenses during the year.

In the preparation of these consolidated financial statements, estimates and assumptions have been made by management including costs to complete projects, an assessment of percentage of completion of projects, recognition of revenue in respect of variation orders and claims, the selection of useful lives of tangible and intangible fixed assets, expected future cash flows from long-lived assets to support impairment tests, provisions necessary for trade receivables, the carrying value of non-consolidated joint ventures, income tax valuation allowances, provisions for legal disputes, assessment of the probability of occurrence of hedged transactions and other similar evaluations. Actual results could differ from those estimates.

Revenue recognition

Long-term contracts are accounted for using the percentage-of-completion method. The Company applies Statement of Position 81-1 'Accounting for Performance of Certain Construction-Type Projects'. Revenue and gross profit are recognised each period based upon the advancement of the work-in-progress unless the stage of completion is insufficient to enable a reasonably certain forecast of gross profit to be established. In such cases, no gross profit is recognised during the period. The percentage-of-completion is calculated based on the ratio of costs incurred to date to total estimated costs. The percentage-of-completion method requires the Company to make reasonably dependable estimates of progress toward completion of such contracts and contract costs. Provisions for anticipated losses are made in the period in which they become known.

A major portion of the Company's revenue is billed under fixed-price contracts. However, due to the nature of the services performed, variation orders and claims are commonly billed to the customers in the normal course of business and are recognised as contract revenue where recovery is probable and can be reasonably estimated. In addition, some contracts contain incentive provisions based upon performance in relation to established targets, which are recognised in the contract estimates when deemed realisable. As at 30 November 2003, no significant revenue relating to unagreed claims or disputed receivables was included in reported turnover or receivables that has not been subsequently collected in full.

During the course of multi-year projects the accounting estimate for the current period and/or future periods may change. The effect of such a change, which can be upward as well as downward, is accounted for in the period of change. These revisions to estimate will not result in restating amounts in previous periods. Revisions of estimates are calculated on a regular basis.

The financial reporting of the Company's contracts depends on estimates, which are assessed continually during the term of these contracts. Recognised revenues and profits are subject to revisions as the contract progresses to completion and

refinements in estimates are reflected in the period in which the facts that give rise to the revision become known. Additional information that enhances and refines the estimating process that is obtained after the balance sheet date but before issuance of the financial statements is reflected in the financial statements. The net (adverse) positive effect on net loss of significant revisions to contract estimates was \$(216.0) million in 2003, \$(58.8) million in 2002 and \$2.4 million in 2001. The net effect of these revisions on net (loss) income per share was \$(2.23) in 2003, \$(0.69) in 2002 and \$0.03 in 2001.

Translation of inter-company balances

Long-term inter-company balances which are not planned or anticipated to be settled in the foreseeable future are revalued. In accordance with Statement of Financial Accounting Standard ('SFAS') No. 52, these results are included under other comprehensive income/(loss) ('OCI').

Cash and cash equivalents

Cash and cash equivalents include time deposits and certificates of deposit with an original maturity of three months or less.

Inventory

In determining the cost of inventory the weighted average cost method is used. Inventory is valued at the lower of cost and net realisable value, with adequate provisions made against slow-moving and obsolete items.

Assets held for sale

The Company classifies assets and disposal groups as being held for sale in accordance with SFAS No. 144, 'Accounting for the Impairment or the Disposal of Long-Lived Assets', when the following criteria are met: management has committed to a plan to sell the asset (disposal group); the asset (disposal group) is available for immediate sale in its present condition; an active programme to locate a buyer and other actions required to complete the plan to sell the asset (disposal group) have been initiated; the sale of the asset (disposal group) is probable, and transfer of the asset (disposal group) is expected to qualify for recognition as a completed sale, within one year; the asset (disposal group) is being actively marketed for sale at a price that is reasonable in relation to its current fair value and actions required to complete the plan indicate that it is unlikely that significant changes to the plan will be made or that the plan will be withdrawn.

Long-lived assets or disposal groups classified as held for sale are measured at the lower of their carrying amount or fair value less cost to sell. These assets are not depreciated once they meet the criteria to be held for sale.

Fixed assets

Fixed assets are recorded at cost. Interest costs incurred between the date that financing is provided for an asset and the date that the asset is ready for use are capitalised. No interest was capitalised for the years-ended 30 November 2003, 2002 or 2001.

Depreciation of fixed assets is recorded on a straight-line basis over the useful lives of the assets as follows:

Construction support ships, to be held for use:

▶ Deepwater heavy construction ships	9 to 25 years
▶ Light construction and survey ships	10 years
▶ Pipelay barges and anchor ships	7 to 20 years
Operating equipment	7 to 10 years
Buildings	20 to 33 years
Other assets	5 to 10 years

Ships are depreciated to a residual value of 10% of acquisition cost, which reflects management's estimate of salvage or otherwise recoverable value. No residual value is assumed with respect to other fixed assets.

Costs for fitting out construction support ships are capitalised and amortised over a period equal to the remaining useful life of the related equipment.

Depreciation expense was \$91.2 million for the year ended 30 November 2003 (2002: \$85.7 million and 2001: \$86.0 million).

Dry-docking costs

The Company accounts for dry-dock costs on a deferral basis. Capitalised dry-dock costs are amortised over the period between vessel dockings, which is typically between two and five years. Amortisation of capitalised dry-dock costs was \$14.0 million for the year ended 30 November 2003 (2002: \$15.4 million and 2001: \$8.4 million). The unamortised portion of capitalised dry-dock costs of \$24.8 million (2002: \$27.4 million) is included in 'Deposits and non-current receivables' in the accompanying consolidated balance sheets.

Maintenance and repair costs, which are expensed as incurred, were \$48.3 million for the year ended 30 November 2003 (2002: \$43.6 million and 2001: \$42.1 million).

Impairment of long-lived assets

In accordance with SFAS No. 144, long-lived assets and intangibles with finite lives are tested for recoverability whenever events or changes in circumstances indicate that the carrying amount may not be recoverable. In performing the review for impairment, the Company estimates the future cash flows expected to result from the use of the asset and its eventual disposition. If the undiscounted future cash flow is less than the carrying amount of the asset, the asset is deemed impaired. The amount of the impairment is measured as the difference between the carrying value and the fair value of the asset.

Goodwill and other intangible assets

Goodwill represents the excess of the purchase price over the fair value of net assets acquired in a business combination. Goodwill arising on acquisitions prior to 30 June 2001 was amortised on a straight-line basis over 10 to 30 years and goodwill is reviewed for impairment whenever events or changes in circumstances indicate that the carrying value may not be recoverable. Goodwill arising on acquisitions after 30 June 2001 is not amortised but is tested for impairment annually or earlier, whenever impairment indicators arise.

Intangibles with indefinite lives are not amortised, but tested for impairment annually or earlier, whenever impairment indicators arise.

In accordance with SFAS No.142, 'Goodwill and Other Intangible Assets', from 1 December 2002, goodwill arising on acquisitions prior to 1 July 2001 is no longer amortised but is tested for impairment annually or earlier, whenever impairment indicators arise.

Impairment of goodwill

The Company tests goodwill for impairment annually and on an interim basis when conditions require. The first impairment test on adoption of SFAS No. 142 was performed in the second quarter of 2003. The impairment test is performed at the reporting unit level. The goodwill impairment test has two steps. The first one identifies potential impairment by comparing the fair value of a reporting unit with its carrying value including goodwill. If the fair value of the reporting unit exceeds the carrying amount, goodwill is not impaired and the second step is not necessary. If the carrying value exceeds the fair value, the second step calculates the possible impairment loss by comparing the implied fair value of goodwill with the carrying amount. If the implied goodwill is less than the carrying amount, a write-down is required.

Impairment of investments in non-consolidated joint ventures

The Company reviews its investments in non-consolidated joint ventures periodically to assess whether there is a decline, other than temporary, in the carrying value of the investment. The Company considers whether there is an absence of an ability to recover the carrying value of the investment. This is assessed by reference to projected undiscounted cash flows for the joint venture.

Income taxes

The Company accounts for income taxes under the provisions of SFAS No.109, 'Accounting for Income Taxes'. SFAS No.109 requires recognition of deferred tax assets and liabilities for the estimated future tax consequences of events attributable to differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax bases and operating loss and tax credit carry forwards. Deferred tax assets and liabilities are measured using enacted rates in effect for the year in which the differences are expected to be recovered or settled. The effect on deferred tax assets and liabilities of changes in tax rates is recognised in income from continuing operations for the period that includes the enactment date. Deferred tax assets are reduced through the establishment of a valuation allowance at such time as, based on available evidence, it is more likely than not that the deferred tax assets will be not realised.

Notes to the consolidated financial statements continued

Debt costs

Costs incurred in connection with issuance of debt such as facility fees, are treated as a deferred charge and classified as a non-current asset. Such costs are amortised over the life of the debt as additional interest. If the debt expires or is terminated, the deferred costs are expensed immediately.

Restructuring charges

The Company accounts for restructuring charges in respect of existing post-employment plans, which includes statutory legal requirements to pay redundancy costs, under SFAS No. 112 'Employer's Accounting for Post Employment Benefits'. In these circumstances the Company recognises a provision for redundancy costs at the date that it is probable that the employee will be entitled to the benefits and when these can be reasonably estimated.

Where the termination costs are of a 'one-time' involuntary nature the Company applies SFAS No. 146 'Accounting for Costs Associated with Exit and Disposal Activities'. This includes costs for redundancies, which are over and above the statutory requirements, and the costs for vacated property. The Company provides for these costs at fair value at the date the termination plans are communicated to employees and when the Company is committed to the plan, and it is unlikely that significant changes will be made to the plan.

Recognition of provisions for legal claims, suits and complaints

The Company, in the ordinary course of business, is subject to various claims, suits and complaints. Management, in consultation with internal and external advisers, will provide for a contingent loss in the financial statements if the contingency had been incurred at the date of the financial statements and the amount of the loss can be reasonably estimated. In accordance with SFAS No. 5 'Accounting for Contingencies', as interpreted by FASB Interpretation No. 14 'Reasonable Estimation of the Amount of a Loss', if the Company has determined that the reasonable estimate of the loss is a range and that there is no best estimate within the range, the Company will provide the lower amount of the range.

Research and development expenditure

The costs of research and development are expensed as incurred.

Minority interest

The Company records minority interest expense, which reflects the portion of the earnings of the consolidated operations that are applicable to the minority interest partners. The minority interest amounts recorded in the accompanying consolidated financial statements primarily represent the share of minority partners' interest of 33 1/3% in Alto Mar Girassol and the minority partners' 37% interest in Paragon Engineering Holdings Inc., the acquisition of which is discussed further in Note 3.

Treasury shares

Capital stock acquired, that is not retired, is treated as if it had been retired or carried at cost and reflected as a separate reduction from shareholders' equity. As at 30 November 2003, 879,121 Common Shares (2002: nil) were held as treasury shares by an indirect, wholly owned subsidiary of the Company.

Earnings per share

Earnings per share are computed using the weighted average number of common and Class B shares and equivalents outstanding during each period. Class B shares have only 50% of the economic rights of Common Shares.

Stock-based compensation

The Company has elected to account for its stock-based compensation awards to employees and Directors under Accounting Principles Board ('APB') Opinion No.25 and to provide the disclosures required by SFAS No.123, 'Accounting for Stock Based Compensation' in Note 23 Under APB Opinion No. 25, compensation cost is measured at intrinsic value, which is the difference between the exercise price and the market price at the date of grant.

The Company accounts for awards granted to Directors and key employees under APB Opinion No. 25; no compensation cost has been recognised because options are granted at the market price at the date of grant. Had compensation cost for all share option grants in fiscal years 2003, 2002 and 2001 been determined consistent with SFAS No. 123, the Company's net loss and net loss per share would be changed to the following pro forma amounts:

For the year ended 30 November (in thousands, except per share data)	2003 \$	2002 \$	2001 \$
Net loss, as reported	(418,087)	(151,855)	(14,203)
Stock-based compensation included in reported net income	-	-	-
Total stock-based employee compensation expense determined under the fair value method, net of tax	(2,499)	(3,239)	(3,534)
Net loss pro forma	(420,586)	(155,094)	(17,737)
Loss per share, as reported			
Basic	(4.51)	(1.79)	(0.16)
Diluted	(4.51)	(1.79)	(0.16)
Loss per share pro forma			
Basic	(4.54)	(1.82)	(0.20)
Diluted	(4.54)	(1.82)	(0.20)

Foreign currency translation

The Company, incorporated in Luxembourg, operates primarily in a US dollar economic environment given the nature of its business. As a result, the Company's reporting currency and functional currency is the US dollar.

The Company translates the financial statements of its subsidiaries from their functional currencies (usually local currencies) into US dollars. Assets and liabilities denominated in foreign currencies are translated at the exchange rates in effect at the balance sheet date. Revenue and expenses are translated at exchange rates which approximate the average exchange rates prevailing during the period. The resulting translation adjustments are recorded in a separate component of accumulated other comprehensive loss as 'Translation adjustments, net' in the accompanying consolidated statements of shareholders' equity. Exchange gains and losses resulting from transactions denominated in a currency other than that of the functional currency are included in 'Foreign currency exchange gains (losses), net' in the accompanying consolidated statements of operations. The functional currencies of the companies that comprise the NEC region are dependent upon on the geographical location of the activities and are either Norwegian kroner, British pounds, Canadian dollars, or US dollars. The US dollar is the functional currency of the most significant subsidiaries within the AFMED, NAMEX, SAM, and AME regions. During 2003, the Company changed the functional currency of one of its entities which performs contracts in AFMED from euros to US dollars, reflecting the increased significance of US dollar cash flows. The Company believes that the US dollar is the currency of the primary economic environment in which it operates.

Foreign exchange gains and losses on intercompany transactions of a long-term nature are reported as 'Translation adjustment net'.

Derivatives and hedges

The Company uses derivative instruments, primarily foreign exchange forward contracts, to reduce its exposure to currency fluctuations. All of the instruments used are hedges against forecasted underlying operating exposures, which are designated as cash flow hedges. The Company does not enter into open speculative positions. The Company accounts for derivatives in accordance with SFAS No. 133 'Accounting for Derivative Instruments and Hedging Activities', as amended, which requires that all derivative instruments be reported on the balance sheet at fair value and establishes criteria for designation and effectiveness of hedging relationships. If the derivative is designated as a cash flow hedge, the effective portions of the changes in the fair value of the derivative instrument are recorded in other comprehensive income ('OCI') in the consolidated statement of shareholders' equity until the hedged item affects earnings, and ineffective portions of changes in cash flow hedges are recognised in the consolidated statement of operations immediately. If the derivative instrument is terminated or settled prior to the expected maturity or realisation of the underlying item, hedge accounting is discontinued prospectively.

Consolidated statements of cash flows

The following table sets forth non-cash financing and investing activities and selected cash flow information. The table summarises acquisitions accounted for under the purchase method in respect of the Paragon and Litwin acquisitions; the issue of shares to Stolt-Nielsen S.A. ('SNSA') in return for reduction of debt; the monetisation of forward contracts, which in part settled trade payables and short-term funding due to SNSA, the replacement of external debt with SNSA short-term funding and Subordinated Note; and an increase in the investment in Sonamet, a non-consolidated joint venture.

For the year ended 30 November (in thousands)	2003 \$	2002 \$	2001 \$
Estimated fair value of tangible assets acquired less liabilities assumed or created	–	–	(4,755)
Goodwill and identifiable intangible assets acquired	–	–	11,389
Cash acquired	–	–	10,020
Purchase price			
Cash	–	–	(9,959)
Deferred consideration	–	–	(6,695)
Sale of 6,392,478 Common Shares to SNSA	–	38,420	–
Issuance of 6,019,287 Common Shares to SNSA	–	25,580	–
Repayment of loan due to SNSA	–	(64,000)	–
Monetisation of forward contracts	11,392	–	–
Payment of SNSA trade payables	(1,392)	–	–
Repayment of short-term SNSA funding	(10,000)	–	–
Repayment of existing bank credit facilities	(100,000)	–	–
Drawdown of SNSA subordinated note	50,000	–	–
Drawdown of short-term SNSA funding	50,000	–	–
Reduction in receivables from Sonamet joint venture	4,513	–	–
Increase in investment in non-consolidated joint ventures	(4,513)	–	–
Interest paid	(18,291)	(16,306)	(27,200)
Income taxes paid	(9,299)	(11,006)	(13,709)

Interest paid includes \$0.3 million paid to SNSA in the year ended 30 November 2003 (2002: \$0.6 million, 2001: \$0.4 million).

Impact of new accounting standards

In December 2003, the FASB issued a revision to Interpretation No. 46 'Consolidation of Variable Interest Entities, an Interpretation of ARB No. 51' ('FIN 46R' or the 'Interpretation'). FIN 46R clarifies the application of ARB No. 51 'Consolidated Financial Statements', to certain entities in which equity investors do not have the characteristics of a controlling financial interest or do not have sufficient equity at risk for the entity to finance its activities without additional subordinated financial support. FIN 46R requires the consolidation of these entities, known as Variable Interest Entities ('VIEs'), by the primary beneficiary of the entity. The primary beneficiary is the entity, if any, that will absorb a majority of the entity's expected losses, receive a majority of the entity's expected residual returns, or both.

Among other changes, the revisions of FIN 46R (a) clarified some requirements of the original FIN 46, which had been issued in January 2003, (b) eased some implementation problems, and (c) added new scope exceptions. FIN 46R deferred the effective date of the Interpretation for public companies, to the end of the first reporting period ending after 15 March 2004, except that all public companies must at a minimum apply the provisions of the Interpretation to entities that were previously considered 'special-purpose entities' under the FASB literature prior to the issuance of FIN 46R by the end of the first reporting period ending after 15 December 2003. The Company is currently assessing the impact of the adoption of FIN 46R on its financial position, cash flows and results of operations.

On adoption of FIN 46R, it is possible the Company will consolidate two VIEs, Sonamet and Sonastolt. The Company has 55% majority ownership of these two joint ventures in Angola, but they are not currently consolidated due to the significant participating influence of the other main shareholder, Sociedade Nacional de Combustiveis de Angola – Sonongal U.E.E. ('Sonongal'). Sonamet operates a fabrication yard at Lobito, which manufactures structures and components for offshore projects. This offers the Company a strategic advantage in the West African offshore market, where contractors are often required to utilise a specified proportion of local resources. Sonastolt is a provider of local and offshore support personnel and equipment.

(in millions)	Sonamet	Sonastolt
Total assets	\$176.2	\$91.1
Maximum exposure to loss	\$7.4	\$32.4

The maximum exposure to loss refers to the maximum loss that the Company would be required to record in its income statement as a result of its involvement with a VIE. It does not consider the probability of such losses actually being incurred.

In December 2003, the FASB revised SFAS No. 132 'Employers' Disclosures about Pensions and Other Post-retirement Benefits – an amendment of FASB Statements No. 87, 88, and 106' ('SFAS 132R'). This Statement revises employers' disclosures about pension plans and other post-retirement benefit plans. It does not change the measurement or recognition of those plans required by SFAS No. 87 'Employers' Accounting for Pensions', No. 88 'Employers' Accounting for Settlements and Curtailments of Defined Benefit Pension Plans and for Termination Benefits', and No. 106 'Employers' Accounting for Post-retirement Benefits Other Than Pensions'. This Statement retains the disclosure requirements contained in SFAS No. 132, Employers' Disclosures about Pensions and Other Post-retirement Benefits, which it replaces. It requires additional disclosures to those in the original SFAS No. 132 about the assets, obligations, cash flows, and net periodic benefit cost of defined benefit pension plans and other defined benefit post-retirement plans. The required information should be provided separately for pension plans and for other post-retirement benefit plans. The Company will adopt the disclosure requirements of SFAS No. 132R during the fiscal year 2004.

3. Business acquisitions

On 30 March 2001, the Company acquired 82% of the voting rights and 63% of the economic rights of a newly created company, Paragon Engineering Holdings, Inc. ('PEH'). PEH subsequently, in fiscal year 2001, purchased 60% of the share capital of Paragon Engineering Services, Inc. ('Paragon'), a Houston-based engineering service company. On 18 July 2001, the Company purchased the entire share capital of the Paris-based engineering company Ingerop Litwin ('Litwin'). The consideration, including acquisition costs, paid to acquire PEH, Paragon and Litwin was \$16.7 million of which \$4.3 million was the net present value at the date of acquisition of the deferred consideration payable on the Paragon acquisition by 30 March 2005. Additionally, from 30 March 2005, the Paragon sale agreement provides for a further payment to be made to a former shareholder of Paragon. This payment is contingent upon a multiplier of the future earnings of Paragon, as defined in the agreement,

Notes to the consolidated financial statements continued

exceeding the deferred consideration. No recognition of the contingent payment has been made in the financial statements of the Company as it is not certain beyond reasonable doubt that this payment will be made and currently it is not possible to quantify the amount.

PEH, Paragon, and Litwin are currently held for sale. See Note 8 'Assets held for sale' below. It is expected that the liability for the final payment to be made to the former Paragon shareholder will be transferred to the purchaser of the Paragon companies, because the obligation to make this payment resides with PEH, which is held for sale and included in the Paragon disposal group.

The results of PEH and Paragon have been included in the consolidated results of operations from 4 September 2001, when the Company assumed effective control of the entity. The amount, which represents the minority shareholders' interests in the results of Paragon, effectively 63%, has been recorded as minority interest expense in the results of operations of the Company. The results of Litwin have been included in the consolidated results of operations from 18 July 2001.

An external valuation during fiscal year 2002 indicated the Company's share of the fair value of the acquired intangible assets to be \$5.2 million. Of this \$5.2 million, \$1.7 million was allocated to the 'Paragon' trade name which is considered to have an indefinite useful life; \$1.4 million was allocated to order backlog which is being amortised over the period to 30 November 2004; and \$1.2 million was allocated to non-compete agreements, which are being amortised over the period to 31 March 2005. The remaining \$0.9 million of acquired intangible assets relating to software patents and a favourable leasehold have a weighted-average useful life of approximately six years. The Company considers each reporting period whether a useful life can be determined for the trade name and reviews the trade name for impairment at least annually. No impairment charge has been recorded during fiscal year 2003 in respect of the Paragon and Litwin companies. As the Paragon and Litwin companies are now held for sale, amortisation was discontinued as of 30 November 2003, when the held for sale criteria were met.

On 10 March 2003 and on 20 February 2002, the Company settled share price guarantees to NKT Holdings A/S. NKT Holdings A/S is the Company's joint venture partner in NKT Flexibles. NKT Holdings A/S originally acquired the Company's shares in exchange for a 49% interest in NKT Flexibles in December 1999. The difference between the share price guarantees and the market prices on the settlement dates of \$12.4 million and \$1.6 million respectively were paid in cash and similar amounts were deducted from paid-in surplus.

On 3 May 2002, the Company settled a share price guarantee to Groupe Vinci S.A. ('Vinci'), which was issued in 1999 as part of the Company's consideration in acquiring an interest in the French offshore and construction company ETPM S.A. The difference between the share price guarantee and the market price on the settlement date of \$58.9 million was paid in cash and a similar amount was deducted from paid-in surplus.

4. Restricted cash balances

Restricted cash balances comprise both funds held in a separate Company bank account, which will be used to settle accrued taxation liabilities, and deposits made by the Company as security for certain third-party obligations. There are no other significant conditions on the restricted cash balances.

5. Trade receivables

Trade receivables at 30 November 2003 of \$358.3 million (2002: \$428.1 million) are net of allowances for doubtful accounts of \$15.8 million (2002: \$5.9 million). Included in trade receivables at 30 November 2003 was \$168.0 million (2002: \$261.9 million) of unbilled receivables. As at 30 November 2003, the amount included in unbilled trade receivables with respect to disputed variation orders and claims was \$nil (2002: \$46.2 million). Of the \$46.2 million related to disputed variation orders and claims, as at 30 November 2002, \$6.1 million was written off during 2003. Cash has been collected in settlement of the remaining disputed variations orders and claims at 30 November 2002.

As of 30 November 2003, an amount of \$37.0 million was included in Trade receivables in respect to invoiced work on the Duke Hubline project. As described in Note 25 – Commitments and contingencies, a settlement was reached with Algonquin Gas Transmission whereby payment of the invoices was included as a part of a negotiated settlement.

Concentration of credit risk

Substantially all of the Company's trade accounts receivable are from companies in the oil and gas exploration and production sector. The Company performs ongoing credit evaluations of its customers' financial condition and limits the amount of credit extended when deemed necessary but generally requires no collateral.

As at 30 November 2003 accounts receivable include \$116.3 million (2002: \$102.9 million) in respect of the largest customer and \$36.6 million (2002: \$35.9 million) in respect of the second largest customer.

6. Inventories and work-in-progress

Inventories and work-in-progress are stated at the lower of cost or market value and comprise the following:

As of 30 November (in thousands)	2003 \$	2002 \$
Materials and spares	13,648	11,710
Consumables	7,677	5,107
Work-in-progress and mobilisations	775	708
Total^(a)	22,100	17,525

(a) Net of reserve of \$8.0 million as of 30 November 2003 (2002: \$6.3 million).

Mobilisations relate to costs incurred to prepare and mobilise vessels for new contracts. These costs are recognised as operating expenses over the estimated primary term of the contract.

7. Employee loans

Included in prepaid expenses and other current assets are loans to employees of \$2.1 million (2002: \$2.3 million). Included in deposits and non-current receivables are loans to employees of \$0.1 million (2002: \$0.1 million).

8. Assets held for sale

As a part of the Company's new strategic focus the Company is actively seeking to dispose of certain assets that are not essential to the Company's core business. As at 30 November 2003 the following assets and asset disposal groups are classified as 'Held for sale' in accordance with SFAS No. 144 'Accounting for the Impairment or Disposal of Long-lived Assets':

- ROV drill-support: This business involves around 200 employees world-wide, 44 ROVs and certain ancillary equipment, together with related contracts, and is operated from bases in West Africa, South America and the North Sea. On 20 February 2004, the Company and a non-consolidated equity investee, Sonastolt sold the business to Oceaneering International, Inc. for a sale price of approximately \$48 million. The Company received approximately \$28 million in cash after settling the interests of Sonangol, its joint venture partners in Angola, and transaction costs. The sale resulted in a gain of \$5.5 million being recorded, in the first quarter of fiscal year 2004.
- Serimer DASA: This is a wholly owned specialised surface welding services and surface welding equipment manufacturing company with its head office near Paris, France. In addition the Company has a sales office in Texas, United States. Serimer DASA provides automatic surface welding services primarily to offshore pipelaying contractors. The Company expects to dispose of this business by the end of the second quarter of fiscal year 2004.
- Paragon Companies: This includes Paragon Engineering Holdings Inc., Paragon Engineering Services Inc, Paragon Litwin, and Paragon Italia S.r.l. These engineering businesses, which were acquired in 2001, are expected to be sold by the end of the second quarter of fiscal year 2004. Certain of the engineering services they have provided will be re-integrated into the Company's business, and the Company expects to retain approximately 100 engineers from the Paragon Companies.
- Survey Business: This business consists of two owned ships (the *Seaway Legend* and the *Elang Laut*), one ship on charter (the *Seaway Petrel*), their marine equipment, spare parts and additional equipment, including five survey ROVs. The Company expects to sell this business by the third quarter of fiscal year 2004. The Company intends to outsource its survey work to the buyer of this business.

5. Assets in the Lobito Yard, Angola: A large quantity of equipment located in the Lobito Yard on long-term lease to Sonamet, a non-consolidated equity investee of the Company, was under negotiation for sale to Sonamet at 30 November 2003. The sale was completed in the first quarter of fiscal year 2004 for net proceeds of \$5.4 million at no gain or loss. An impairment charge was recorded against these assets during fiscal year 2003, as described in Note 9.
6. Since 30 November 2003 the Company has disposed of the *Annette*, the *Seaway Rover*, the *Seaway Invincible*, and the *Seaway Pioneer*. Proceeds from these sales were \$3.0 million and were received during the first and second quarter of fiscal year 2004, and a gain of \$0.6 million was recorded.

These assets do not meet the criteria for disclosure as discontinued operations, either because (i) the Company expects to sign an agreement for continuing utilisation of those businesses on an outsourced basis, or (ii) the operations and cash flows from the disposal groups will not be eliminated from the Company's operations because they will continue to be performed in-house at a lower level of operation or purchased from third parties when required.

As at 30 November 2003 the Company's disposal groups held for sale comprised assets of \$106.2 million and liabilities of \$57.9 million, detailed as follows:

Assets	\$ thousands
Trade receivables	42,427
Receivables due from related parties and joint ventures	30
Prepayments and other current assets	8,079
Net fixed assets	52,400
Deposits and non current receivables	646
Goodwill and other intangible assets	2,570
Total assets held for sale	106,152
Liabilities	\$ thousands
Short-term payables due to SNSA	29
Accounts payable and accrued liabilities	26,352
Accrued salaries and benefits	12,317
Advance billings	3,016
Other current liabilities	6,742
Deferred taxes	414
Other long-term liabilities	7,265
Accrued pension liability	1,720
Total liabilities held for sale	57,855

The allocation of assets held for sale to regions is as follows:

Region	\$ thousands	
	Assets	Liabilities
AFMED	10,410	-
NEC	3,650	-
NAMEX	1,865	-
SAM	3,210	-
AME	1,249	-
Corporate	85,768	57,855
Total assets held for sale	106,152	57,855

9. Fixed assets, net

Fixed assets comprise the following:

As of 30 November (in thousands)	2003 \$	2003 %	2002 \$	2002 %
Construction support ships	618,562	66	768,400	65
Operating equipment	277,287	30	354,402	30
Land and buildings	24,196	3	20,625	2
Other assets	13,291	1	45,180	3
Subtotal	933,336	100	1,188,607	100
Less: Accumulated depreciation and amortisation	(418,731)		(405,764)	
Total	514,605		782,843	

The Company recognised aggregate impairment charges of \$176.5 million in fiscal year 2003 in respect of its tangible fixed assets, as set forth in the following table:

\$
(in millions)

Ships

A sales brochure was published in September 2003 by Derrick Offshore, a shipbroker acting for the Company, offering several of the Company's ships for sale. These included the *Seaway Kestrel*, the *Seaway Explorer*, the *Seaway Invincible* and the *Seaway Rover*. The broker provided guidance as to the prices that could be obtained under current market conditions. These prices were at a level substantially below the carrying values of the ships, and were confirmed by a formal valuation in January 2004. An impairment charge was recorded against the carrying value of certain ships, measured on the basis of the broker's valuation.

Two categories of assets have been identified based upon the criteria under SFAS No. 144.

1) Held for sale – \$2.2m

The following two ships included here meet the 'held for sale' criteria under SFAS No. 144. They have been marketed for sale since the final quarter of the fiscal year 2003 and they have been sold since 30 November 2003, at no gain or loss. The *Seaway Invincible* and the *Seaway Rover*.

2) Held for use – \$42.0m

The following two ships are being actively marketed, but no sales agreement has yet been concluded, and management does not consider that it will be probable that these ships will be sold within one year. The *Seaway Kestrel* and the *Seaway Explorer*.

LB 200 Pipelay Barge, held for use – \$55.7m

As part of the business restructuring initiated by the Company's new management team, a separate trunkline business unit was established in the fourth quarter of fiscal year 2003, specifically dedicated to the marketing and operation of the LB 200 pipelay barge. An in-depth review was then performed to determine the predicted world-wide demand for trunkline lay, and the available barges capable of performing this type of work. The outcomes from bid processes during the fourth quarter of fiscal year 2003 were also evaluated. This review resulted in a revised forecast of utilisation and future daily charge-out rates for the LB 200, and an impairment charge was recorded on the basis of a fair value calculation using discounted cash flows. An external shipbroker reviewed this calculation at the Company's request and validated the underlying market assumptions.

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Radial Friction Welding (RFW), held for use – \$42.7m

The RFW program was started in June 1995 to design and fabricate a high quality ship-mounted welding system for use on 6- to 12-inch flowlines, at a production rate of 200 pipe joints per day. The system was designed not only for welding normal high tensile carbon steels, but also for the emerging premium market for corrosion resistant alloys. However, it proved too large and complex to install on one of the Company's existing ships and fabrication was suspended in December 2000. In fiscal year 2002, the Company launched a joint feasibility study with a third party ship-owner to install the equipment on an existing ship, which would be operated as a specialised deep-sea construction ship by a joint venture. The study indicated that adaptation of the existing ship would necessitate substantial additional investment, so the Company commissioned an agent to identify and attract a further outside investor. The Company received a status note from this agent on November 28, 2003, confirming that he had been unable to attract any further investors to join the project, which meant that the proposed joint venture could not proceed. Although efforts to find alternative uses for the RFW will continue, the market trend has moved away from corrosion-resistant alloys, and more competitive welding technologies have emerged. It is no longer appropriate to carry this asset other than at scrap value, which management considers to be close to \$nil, and an impairment charge has been recorded to reduce the carrying value to \$nil.

Other Ships and Offshore Equipment, held for use – \$28.8m

At the time of preparation of the annual operating budget for fiscal year 2004 and three-year plan in October 2003, the Company's senior management assessed the level of expected future utilisation of all its assets in the light of the business strategies established in the new management's business plan, and a number of assets were found to be under-utilised. The major items included a ship (*Seaway Defender*), three remote-operated MATIS™ pipe-connectors, nine Remotely Operated Vehicles ('ROVs'), the smartleg platform-deck installation equipment, three trenchers/ploughs, hardsuit diving equipment, and four pipe carousels. An impairment charge was recorded on the basis of fair value calculations performed by the Company using discounted cash flows.

Lobito Yard assets, held for sale – \$5.1m

This category comprises a large quantity of the Company's equipment located at the Lobito fabrication yard on long-term lease to Sonamet a non-consolidated equity investee company in which the Company holds a 55% interest. The equipment includes cranes, tractors, cutting and welding equipment, generators, and vehicles. A buy-out proposal from Sonamet to acquire the equipment was received in the fourth quarter of fiscal year 2003, and an impairment charge was recorded to reduce the carrying value to the expected sales price. The assets were sold to Sonamet at that price after the end of fiscal year 2003.

Total impairment charges in respect of Company-owned fixed assets \$176.5m

The fiscal year 2002 charge of \$4.0 million for impairment of fixed assets was made up of adjustments to the carrying value of several small fixed assets.

10. Goodwill and other intangible assets.

As at 30 November 2003, there was goodwill of \$6.0 million (2002: \$6.0 million). Intangible assets of \$2.6 million are classified as assets held for sale at 30 November 2003 as they relate to the Paragon Companies. (See Note 8 'Assets held for sale' above.) There are intangible assets of \$0.2 million at 30 November 2003 (2002: \$4.7 million).

The amortisation expense for the year ended 30 November 2003 was \$2.3 million (2002: \$6.4 million, 2001: \$5.7 million) and related to other intangible assets with finite lives.

The goodwill at 30 November 2003 relates to Paragon (see Note 3). As the acquisition was made after 1 July 2001 goodwill has not been amortised in the current or prior periods in accordance with SFAS No. 141.

Impairment

There was no impairment charge recorded for goodwill during fiscal year 2003. Impairment charges recorded for 2002 and 2001 were \$106.4 million for goodwill and \$7.9 million for intangible assets, as discussed below.

In fiscal year 2002, the continuing poor returns obtained on certain investments made in 1998 and 1999 led the Company to perform an impairment review of all goodwill on acquisition in accordance with SFAS No. 121 'Accounting for the Impairment of Long-Lived Assets and for Long-Lived Assets to be Disposed of'. As a result, impairment charges totalling \$106.4 million were recorded against goodwill, of which \$103.0 million related to the entire remaining goodwill on the 1998 acquisition of Ceanic Corporation. The remainder of the charge eliminated the outstanding goodwill of \$1.8 million on the acquisition of Danco A/S, which holds the Company's investment in NKT Flexibles, and of \$1.6 million in respect of the Company's Indonesian subsidiary, PT Komaritim.

Several factors were taken into account in the analysis and supporting projected cash flows that resulted in the impairment charge of \$103.0 million to eliminate the entire remaining goodwill on acquisition of Ceanic Corporation. The acquisition was made in 1998 as part of a strategy to establish a presence in one of the world's most important offshore markets, at a price that reflected rising oil prices and favourable investment conditions. Since then the Gulf of Mexico offshore contractor market has experienced an unprecedented downturn. As a result, the Company's North America region was loss-making for the two years ended 30 November 2001, and again performed below management's expectations in fiscal year 2002. Market analysts' reports, at the end of fiscal year 2002, indicated that the major oil companies were directing their development funds away from U.S. waters and towards overseas targets, particularly West Africa, where the per-barrel recovery costs are lower. The Company forecast no significant upturn in demand in the Gulf of Mexico market in 2003 and had therefore revised earlier assumptions of long-term market growth in its impairment model and eliminated the remaining goodwill. The Ceanic goodwill was previously amortised over 25 years.

The NKT Flexibles joint venture has been loss-making since the Company acquired its 49% share in 2000, and the market for flexible pipes has not grown as quickly as expected. As a consequence, the joint venture has suffered from excess production capacity and has not met its performance targets. During fiscal year 2002, NKT Flexibles management revised its strategy to focus on efficiency and predicted slower growth in the next few years than initially forecast. The Company performed an impairment test for the goodwill in Danco A/S based on the cash flow projections in the NKT Flexibles business plan, and determined that the goodwill was fully impaired. An impairment charge of \$1.8 million was recorded in November 2002. This goodwill was previously amortised over ten years on a straight-line basis.

The PT Komaritim subsidiary in Indonesia was loss-making for several years, and in fiscal year 2002 once again underperformed management's expectations. The Indonesian market continued to be characterised by high competition in the shallow water sector, an environment in which the Company is unable to fully leverage its technology and core expertise. The Company determined, on the basis of projected cash flows, that the goodwill was fully impaired, and a charge of \$1.6 million was recorded in the year ended 30 November 2002. This goodwill was previously amortised over 20 years on a straight-line basis.

During the year ended 30 November 2001, in light of the increased world-wide recognition of the Stolt Offshore name, the Company reviewed the carrying value of its former trade name Comex for possible impairment in accordance with SFAS NO, 121 'Accounting for the Impairment of Long-Lived Assets and for Long-Lived Assets to be Disposed Of'. The Company determined that the value of the trade name had been impaired and recorded a charge of \$7.9 million in its results of operations for the write-down of the trade name.

11. Investments in and advances to non-consolidated joint ventures

As of 30 November (in thousands)	Geographical location	Business segment	Ownership %	2003 \$	2002 \$
NKT Flexibles I/S (‘NKT Flexibles’)	Denmark	Corporate	49	10,987	5,827
Mar Profundo Girassol	West Africa	AFMED	50	100	8,618
Sonamet	West Africa	AFMED	55	7,406	(501)
Sonastolt	West Africa	AFMED	55	9,623	6,331
Seaway Heavy Lifting Limited	Cyprus	Corporate	30	4,312	2,600
Stolt/Subsea 7	Norway	NEC	50	2,133	1,551
Kingfisher D.A.	Norway	NEC	50	3,777	4,346
Dalia FPSO	West Africa	AFMED	27.5	4,624	–
Other	AFMED & NEC			–	2
Total				42,962	28,774

The Company accrues losses in excess of the investment value when the Company is committed to provide ongoing financial support to the joint venture.

In December 2002, the Company made a cash investment of \$12.6 million in NKT Flexibles. In the same month, NKT Flexibles repaid \$12.6 million of debt to the Company.

During fiscal year 2003 \$4.5 million of the Company’s receivables from Sonamet were converted into an equivalent amount of equity in this joint venture. The Company also invested a further \$1.7 million of cash in return for equity. The other partners also made contributions and the percentage of ownership of the respective investors was maintained.

In addition to the above, included in ‘Equity in net income of non-consolidated joint ventures’ are charges totalling \$9.1 million in respect of tangible fixed asset impairments booked in relation to three of the Company’s equity joint ventures, as follows:

Share of impairment charges in respect of tangible fixed assets owned by joint ventures

\$ (in millions)

NKT Flexibles – \$6.6m

The Company’s portion of an impairment charge recorded in respect of the fixed assets of NKT Flexibles, which identified excess manufacturing capacity following a reduction in its anticipated future revenue and market share in the fourth quarter of fiscal year 2003. The impairment was measured on the basis of discounted cash flows prepared by the joint venture.

Kingfisher D.A. – \$1.4m

The Company’s portion of an impairment charge recorded on the *Seaway Kingfisher*, which is owned by Kingfisher D.A., following an outside valuation of the ship.

Sonastolt – \$1.1m

The Company’s portion of an impairment charge in connection with the sale of the Company’s ROV drill support business based on the difference between the carrying value of the ROVs and the net proceeds agreed under the sale contract with Oceaneering. (See Note 8.)

Total impairment charges in respect of tangible fixed assets owned by joint ventures

9.1

The fiscal year 2002 charge of \$8.1 million was the Company’s share of a fixed asset impairment loss booked by the NKT Flexibles I/S joint venture.

Taxation in respect of joint ventures, which have a legal status of partnership, has been included in the results of the relevant subsidiaries, which hold the investments in the joint ventures. Undistributed reserves of all other joint ventures will not be taxed on distribution.

Summarised financial information for the Company’s non-consolidated joint ventures, representing 100% of the respective amounts included in the joint ventures’ financial statements, is as follows:

Income statement data

For the year ended 30 November (in thousands)	2003 \$	2002 \$	2001 \$
Net operating revenue	323,519	298,212	296,305
Gross profit	29,009	37,930	27,599
Net income	3,518	9,203	24,329

Balance sheet data

As of 30 November (in thousands)	2003 \$	2002 \$
Current assets	469,205	159,033
Non-current assets	88,055	97,621
Current liabilities	464,666	161,283
Long-term liabilities	7,610	12,833

For commercial reasons, the Company has structured certain contractual services through its joint ventures. The income statement data for the non-consolidated joint ventures presented above includes the following expenses related to transactions with the Company in 2003, 2002 and 2001 respectively: charter hire of \$2.9 million, \$16.7 million and \$5.1 million and other expenses of \$57.7 million, \$36.7 million and \$60.5 million. The joint ventures also received revenue of \$55.3 million, \$29.4 million and \$39.5 million from the Company. The balance sheet data includes amounts payable to joint ventures by the Company of \$29.8 million and \$5.4 million, short-term amounts receivable by the Company of \$27.6 million and \$62.4 million, and long-term receivables of the Company of \$6.7 million at both 30 November 2003 and 2002 respectively.

Details of guarantees provided to third parties by the Company in respect of performance by joint ventures are disclosed in Note 27 ‘Guarantees’, below.

12. Income taxes

The income tax benefit (provision) is as follows:

For the year ended 30 November (in thousands)	2003 \$	2002 \$	2001 \$
Current	(6,638)	(14,064)	(25,052)
Deferred	7,293	5,906	4,433
Income tax benefit (provision)	655	(8,158)	(20,619)

For the year to 30 November 2003 \$3.6 million of deferred tax was debited to other OCI (2002: \$2.2 million, 2001 \$nil).

The tax effects of temporary differences and net operating loss carry forwards (‘NOLs’) at 30 November 2003 and 2002 are as follows:

As of 30 November (in thousands)	2003 \$	2002 \$
Deferred tax assets:		
Net operating loss carry forwards, accrued expenses and provisions not currently deductible	136,740	96,015
Less: valuation allowance	(109,175)	(74,275)
Net deferred tax assets	27,565	21,740
Deferred tax liabilities:		
Fixed asset timing differences	(25,669)	(25,828)
Net deferred tax (liability)	1,896	(4,088)
Short-term deferred tax asset	53	–
Short-term deferred tax liability	(4,471)	–
Long-term deferred tax asset	8,314	3,101
Deferred tax liability	(2,000)	(7,189)
	1,896	(4,088)

Notes to the consolidated financial statements continued

The Company accounts for income taxes in accordance with SFAS No.109 'Accounting for Income Taxes'. SFAS No.109 requires that the tax benefit of such NOLs be recorded as an asset to the extent that management assesses the utilisation of such NOLs to be 'more likely than not'.

United States

The Company recorded an additional valuation allowance of \$9.6 million against a deferred tax asset for fixed asset and other timing differences. The Company has recognised no deferred tax benefit against the results for fiscal year 2003. Therefore the Company has continued to recognise a 100% valuation allowance. At 30 November 2003 the Company has estimated NOLs of \$87.0 million, none of which expire within ten years.

Scandinavia

The Company has recognised a net long-term deferred tax asset of \$8.1 million, after recording a valuation allowance of \$10.1 million in respect of 2003. The net deferred tax asset represents NOLs in Norway, net of fixed asset and other timing differences. At 30 November 2003 the Company has estimated NOLs of \$56.2 million, which will expire within six to ten years.

Based on the history of operating profits and expectations of the future, management has determined that the operating income of the Company will more likely than not be sufficient to realise the net deferred tax asset of \$8.1 million. The valuation allowance has been created in respect of long-term timing differences that are not expected to crystallise as taxable deductions in the near future.

United Kingdom

At 30 November 2003 the Company had approximately \$88.0 million of losses, future interest deductions and other short-term timing differences that could lead to a future tax deduction. Included in this total is \$11.3 million in respect of NOLs, none of which expire within five years. However the Company does not believe that these will all materialise as tax deductible items and therefore has adjusted the Valuation Allowance to only recognise a net deferred tax asset of \$9.7 million. This asset is set against deferred tax liabilities of \$9.7 million carried in respect of fixed asset timing differences in respect of non-tonnage tax activities.

Withholding and local taxes relate to non-U.K. activities undertaken by some of the Company's subsidiaries against which the deferred tax assets cannot be offset. The Company is looking at ways to realise the value of such tax assets. It has not recognised any benefit for non-U.K. tax losses incurred by its U.K. subsidiaries.

The Company's U.K. shipping subsidiaries continued to be taxed under the U.K. tonnage tax regime, whereby taxable income is computed by reference to the tonnage of the vessels rather than by reference to profit. In prior years the Company released part of its deferred tax liability for the ships within the tonnage tax regime on the basis that the former management had no intention of selling the ships. The new management does intend to sell a ship and has therefore reinstated its deferred tax liability for the ship within the tonnage tax regime. The Company recorded a net benefit in the year of \$1.0 million, as a result of being taxable under the tonnage tax regime.

The tax effect of the impaired shipping assets (as described in Note 9) is \$13.6 million. In prior years the Company had released its deferred tax liability for the anticipated use of those assets within the tonnage tax regime. For this reason, instead of adjusting its valuation allowance, the Company has made a separate disclosure for the tax effect of the impaired assets that are within the tonnage tax regime.

Under U.K. tonnage tax legislation a proportion of tax depreciation previously claimed by the Company may be subject to tax in the event that a significant number of vessels are sold and are not replaced. This contingent liability decreases over the first seven years following entry into the tonnage tax regime, to \$nil. Management has made no provision for the contingent liability for ships that management does not consider probable to be sold. The contingent liability in respect of these ships at 30 November 2003 was \$33.7 million (2002: \$46.2 million).

France

The Company's subsidiaries in France have operated in countries where the taxes are computed by reference to turnover from business operations, rather than by reference to profits.

In relation to its French based activities, the Company has estimated French NOLs of \$75.2 million at 30 November 2003 which begin to expire from 2005 onwards. Management has recorded a valuation allowance against the French NOLs as they do not consider it more likely than not of having taxable profits to realise the asset.

Other

The Company has NOLs of approximately \$9.0 million in Australia at 30 November 2003. Management has recorded a 100% valuation allowance against these NOLs as they do not consider it more likely than not of having taxable profits to realise the asset.

The Company's net operating losses expire as follows:

(in thousands)	2003 \$	2002 \$
2003	–	809
2004	–	12,677
2005	15,483	15,248
2006	–	187
2007	18,683	7,645
2008	2,883	–
Thereafter	201,631	149,424

Withholding and remittance taxes have not been recorded on the undistributed earnings of the Company's subsidiaries primarily because, under the current tax laws of Luxembourg and the countries in which substantially all of the Company's subsidiaries are incorporated, no taxes would be assessed upon the payments or receipt of dividends. Earnings retained by subsidiaries incorporated in those countries, which impose withholding, or remittance taxes are considered by management to be permanently reinvested in such subsidiaries. The undistributed earnings of these subsidiaries as of 30 November 2003 were not significant.

The income tax benefit (provision) at the Company's effective tax rate differs from the income tax benefit (provision) at the statutory rate. Principal reconciling items include the following:

For the year ended 30 November 2003 (in thousands)	U.S. \$	Scandinavia \$	U.K. \$	France \$	Other \$	Total \$
Loss before income taxes and minority interest	(32,665)	(47,751)	(68,341)	(214,040)	(51,396)	(414,193)
Statutory tax rate	34.0%	28.0%	30.0%	35.3%	33.7% ^(a)	
Tax at statutory rate	11,106	13,370	20,502	75,660	17,339	137,977
Profits (losses) subject to turnover-based taxes	–	–	–	(68,499)	10,090	(58,409)
Withholding and local taxes	(158)	–	(1,770)	(711)	(3,374)	(6,013)
Change in valuation allowance	(9,948)	(9,452)	(5,667)	(6,491)	(2,106)	(33,664)
U.K. tonnage tax	–	–	29	–	–	29
Non-deductible amortisation	(1,086)	–	–	–	–	(1,086)
Non-deductible impairment charge	–	–	(13,605)	–	(22,961)	(36,566)
Profits subject to tonnage tax regime	–	–	1,014	–	–	1,014
Other permanent differences	(32)	204	(98)	(430)	(2,271)	(2,627)
Income tax benefit (provision)	(118)	4,122	405	(471)	(3,283)	655

For the year ended 30 November 2002 (in thousands)	U.S. \$	Scandinavia \$	U.K. \$	France \$	Other \$	Total \$
Loss before income taxes and minority interest	(121,410)	(2,898)	(9,156)	(29,952)	21,781	(141,635)
Statutory tax rate	34%	28%	30%	35%	32% ^(a)	
Tax at statutory rate	41,279	812	2,747	10,428	(6,895)	48,371
Profits (losses) subject to turnover-based taxes	-	-	-	(8,053)	7,685	(368)
Withholding and local taxes	(410)	-	(2,846)	(13,923)	3,208	(13,971)
Change in valuation allowance	(15,551)	(515)	(8,317)	(1,317)	(4,442)	(30,142)
U.K. tonnage tax	-	-	(56)	-	-	(56)
Profits subject to tonnage tax regime	-	-	4,458	-	-	4,458
Non-deductible amortisation	(2,510)	-	-	-	-	(2,510)
Change in tax regime	-	-	21,307	-	-	21,307
Non-deductible impairment charge	(35,016)	-	-	-	(1,172)	(36,188)
Other permanent differences	86	79	(1,607)	1,880	503	941
Income tax benefit (provision)	(12,122)	376	15,686	(10,985)	(1,113)	(8,158)

For the year ended 30 November 2001 (in thousands)	U.S. \$	Scandinavia \$	U.K. \$	France \$	Other \$	Total \$
(Loss) income before income taxes and minority interest	(45,886)	(3,221)	7,333	(21,910)	72,906	9,222
Statutory tax rate	34%	28%	30%	36%	40% ^(a)	
Tax at statutory rate	15,601	902	(2,200)	7,982	(29,162)	(6,877)
Profits subject to turnover-based taxes	-	-	-	-	26,353	26,353
Withholding and local taxes	-	-	(1,212)	173	(8,484)	(9,523)
Change in valuation allowance	(13,587)	-	(7,075)	(7,642)	(18,117)	(46,421)
Change in tax regime	-	-	15,200	-	-	15,200
Imputed interest deduction	-	-	-	-	5,381	5,381
Non-deductible amortisation	(1,682)	-	(382)	(2,920)	-	(4,984)
Other permanent differences	(332)	123	(62)	(467)	990	252
Income tax benefit (provision)	-	1,025	4,269	(2,874)	(23,039)	(20,619)

(a) The statutory tax rate for the 'other' category represents a weighted average of various local statutory tax rates including certain revenue-based income taxes.

13. Pension commitments

The Company operates both defined contribution and defined benefit pension plans, depending on location, covering certain qualifying employees. Contributions under the defined contribution pension plans are determined as a percentage of gross salary. The expense relating to these plans for the years ended 30 November 2003, 2002 and 2001 was \$4.5 million, \$4.5 million and \$1.6 million, respectively.

The Company operates both funded and unfunded defined benefit pension plans. The benefits under the defined benefit pension plans are based on years of service and salary levels. Plan assets of the funded schemes are primarily comprised of marketable securities.

The following tables provide a reconciliation of benefit obligation and plan assets for the UK and Norwegian schemes. These are primarily funded schemes, although these also include the benefit obligations in relation to an unfunded Norwegian state pension plan.

As of 30 November (in thousands)	2003 \$	2002 \$
Change in benefit obligation		
Benefit obligation at beginning of year	27,277	20,900
Service cost	2,842	2,107
Members' contributions	73	-
Interest cost	1,774	1,392
Actuarial loss (gains)	1,085	(635)
Foreign currency exchange rate changes	2,606	3,911
Benefits paid from plan assets	(561)	(398)
Benefit obligation at end of year	35,096	27,277
Change in plan assets		
Fair value of plan assets at beginning of year	22,782	18,474
Actual return on plan assets	(377)	(1,511)
Members' contributions	73	-
Foreign currency exchange rate changes	1,461	3,473
Company contributions	2,781	2,692
Benefits paid from plan assets	(561)	(398)
Plan amendments	-	52
Fair value of plan assets at end of year	26,159	22,782

Notes to the consolidated financial statements continued

The following table sets forth the funded status of the funded defined benefit pension plans and a reconciliation to prepaid benefit cost:

For the year ended 30 November (in thousands)	2003 \$	2002 \$
Funded status of the plans	(8,937)	(4,495)
Unrecognised net loss	12,341	8,773
Unrecognised prior service benefit	242	273
Unrecognised net transition obligation	(271)	(304)
Prepaid pension asset	3,375	4,247

The weighted average assumptions used are as follows:

For the year ended 30 November	2003 %	2002 %	2001 %
Discount rate	5.9	6.2	6.2
Expected return on plan assets	6.9	7.0	7.0
Rate of compensation increase	3.2	3.2	3.2

Net periodic pension benefit costs for funded defined benefit schemes include the following components:

For the year ended 30 November (in thousands)	2003 \$	2002 \$	2001 \$
Service cost	2,820	2,107	1,735
Interest cost	1,793	1,392	1,165
Expected return on plan assets	(1,661)	(1,394)	(1,308)
Amortisation of transition obligation	(52)	557	(41)
Recognised net actuarial losses	675	42	38
Amortisation of prior service benefit	49	(303)	86
Benefit cost	3,624	2,401	1,675

Included at 30 November 2003 are funded pension plans, which had accumulated benefit obligations in excess of plan assets. The projected benefit obligations of these plans were \$30.9 million at 30 November 2003 (2002: \$13.4 million) and the fair value of assets under these plans were \$21.3 million (2002: \$8.6 million). The accumulated benefit obligations under the plans were \$26.2 million at 30 November 2003 (2002: \$10.6 million).

For the year ended 30 November 2003, the Company has recorded an adjustment for minimum liability of \$6.0 million (2002: \$2.9 million), which is included in the accrued pension liability balance, for one of its plans. This is prescribed by SFAS No. 87 'Employers' Accounting for Pensions', when the accumulated benefit obligation in the plan exceeds the fair value of the underlying plan assets. The corresponding entry of \$5.4 million (net of deferred tax of \$0.6 million), (2002: \$2.0 million and \$0.9 million respectively) was recorded as a component of accumulated other comprehensive income.

The following tables provide a reconciliation of the benefit obligation and accrued pension liability of the unfunded plans. As the plans are unfunded, the benefit obligation is equal to the unfunded status of the plans and the accrued pension liabilities.

For the year ended 30 November (in thousands)	2003 \$	2002 \$
Benefit obligation at beginning of year	6,376	4,992
Service cost	483	489
Actuarial losses	12	-
Plan amendments	(3,652)	-
Interest cost	395	302
Benefits paid from plan assets	(22)	(119)
Foreign currency exchange rate changes	1,220	712
Benefit obligation at end of year ^(a)	4,812	6,376

(a) The benefit obligation at 30 November 2003 of \$4.8 million includes liabilities held for sale of \$1.7 million.

The weighted average assumptions used are as follows:

For the year ended 30 November	2003 %	2002 %	2001 %
Discount rate	5.0	5.0	6.2
Expected return on plan assets	n/a	n/a	n/a
Rate of compensation increase	2.1	3.8	3.0

Net periodic pension benefit costs include the following components:

For the year ended 30 November (in thousands)	2003 \$	2002 \$	2001 \$
Service cost	483	489	301
Interest cost	395	302	223
Plan amendment	3,652	-	-
Benefit cost	4,530	791	524

In Indonesia, retirement indemnities, for which the Company has accrued \$0.6 million at 30 November 2003 (2002: \$0.4 million), are paid as a lump sum upon retirement. They are primarily based upon the employees' years of service and salary levels. Accrued retirement indemnities are classified in other long-term liabilities.

14. Bank overdraft and lines of short-term credit

As of 30 November 2003, the Company has available committed and uncommitted, third-party bank overdrafts and lines of credit and short-term loan notes totalling \$8.5 million (2002: \$57.3 million). Amounts borrowed pursuant to these facilities bear interest at the rate of 11.4% as at 30 November 2003. The weighted average interest rate was 6.0% and 3.5% for the years ended 30 November 2003 and 2002 respectively. As of 30 November 2003 short-term borrowings under these facilities totalled \$2.5 million (2002: \$16.0 million).

15. Long-term debt and capital lease obligations

Long-term debt and capital lease obligations, excluding borrowings from SNSA, comprises the following:

As of 30 November (in thousands)	2003 \$	2002 \$
Credit agreements with a weighted average interest rate of 4.45% (2002: 2.97%)		
\$440 million credit facility, outstanding balance	\$330 million	
\$55/45 million credit/guarantee facility, outstanding balance	\$55 million	385,000
Capital lease obligation	10	24
Total long-term debt and capital lease obligations	385,010	335,024
Less: current portion		
\$440 million credit facility, scheduled repayment	\$71.5 million ^(a)	
\$55/45 million credit/guarantee facility, scheduled repayment	\$20 million ^(a)	91,500
Capital lease obligation	4	17
Total current portion	91,504	17
Long-term bank debt		
\$440 million credit facility, outstanding balance	\$258.5 million	
\$55/45 million credit/guarantee facility, outstanding balance	\$35 million	293,500
Capital lease obligation	6	7
Total long-term portion	293,506	335,007

(a) As of 31 March 2004 \$45.0 million has been repaid under the \$440 million credit facility. The Company is committed to repaying the equivalent of 50% of the proceeds of the Subsequent Issue, which is expected to be completed by the end of May. The estimated gross proceeds from the Subsequent Issue are approximately \$53.0 million, resulting in a repayment of \$26.5 million. Furthermore under the terms of the \$55/45 million credit/guarantee facility twice yearly repayments of \$10.0 million each are made in January and July.

The net book value of ships collateralising this debt was \$339 million as of 30 November 2003. Commitment fees for any unused lines of credit expensed in the year ended 30 November 2003 totalled \$0.9 million (2002: \$0.4 million, 2001: \$0.4 million).

Minimum annual principal repayments of debt for the fiscal years subsequent to 30 November 2003 are as follows:

For the year ending 30 November (in thousands)	\$
2004	91,500
2005	278,500
2006	15,000
	385,000

Facilities

The \$440 million credit facility

The Company's principal credit facility is an amended \$440 million secured multi-currency five-year revolving facility. The facility was entered into on 22 September 2000 with a syndicate of banks, led by DnB NOR Bank ASA, Bank of America Securities LLC, Salomon Brothers International Limited, HSBC Bank plc and ING Barings LLC, Bank of America N.A. and Citibank N.A. as syndication agents and joint book managers, ING Barings LLC as documentation agent and DnB NOR Bank ASA as facility agent and security trustee. The available amount under the facility reduced to \$330.0 million on 31 August 2003, in accordance with scheduled reductions. As at 30 November 2003, this amount was fully drawn. This facility bears a variable interest rate of up to LIBOR + 3.25%. In February and March, 2004, the Company made voluntary pre-payments under the facility of \$45.0 million such that the available amount under the facility reduced to \$285.0 million. The Company expects that it will prepay additional amounts, including 50% of the gross proceeds resulting from the Subsequent Issue, prior to the termination date such that the available amount will further reduce.

All amounts outstanding under this facility are secured by a full and unconditional guarantee provided by the Company and the execution of certain security documents, including mortgages on certain ships owned by the Company. This facility contains affirmative and negative covenants, including financial covenants relating to the consolidated tangible net worth, ratio of consolidated debt to consolidated tangible net worth and ratio of consolidated debt to EBITDA, not to exceed 5.0:1. These covenants have been changed or are superseded under the terms of the Intercreditor Deed. See Note 28 'Subsequent Events' below.

The \$55/45 million credit/guarantee facility

On 9 July 2002, the Company entered into a \$55/45 million credit/guarantee facility agreement with a term of four years. This facility initially permitted the Company to borrow up to \$55.0 million and to request the provision of bank guarantees in relation to the Company's performance obligations of up to \$45.0 million. As of 30 November 2003, the credit portion of this facility was fully drawn and \$9.7 million was available for issuance of new bank guarantees under the guarantee portion. See Note 27 'Guarantees' below. The amount available for borrowing was reduced by \$10.0 million in January 2004, in accordance with a scheduled reduction of this facility. Amounts available for borrowings or guarantees will be further reduced by \$10.0 million on each consecutive six-month period ending thereafter until the termination of this facility in July 2006. The Company can allocate the \$10.0 million reduction between the credit portion of this facility and the guarantee portion of this facility. SNSA and Stolt-Nielsen Transportation Group Ltd. ('SNTG') have jointly and severally guaranteed the Company's obligations to the banks providing bank guarantees pursuant to the guarantee portion of this facility.

All amounts outstanding under this facility are secured by a full and unconditional guarantee provided by the Company and the execution of certain security documents, including mortgages on certain ships owned by the Company. The affirmative and negative covenants and events of default contained in this facility are substantially identical to those contained in the \$440.0 million credit facility described above and were changed or amended under the terms of the Intercreditor deed. See Note 28 'Subsequent events' below.

The SNSA Subordinated Note

Under the Company's existing credit facilities, the Company is permitted to borrow up to \$100.0 million from SNSA (the 'Subordinated Note') provided that this debt is subordinate and junior to all indebtedness due under the \$440 million credit facility, the \$55/45 credit/guarantee facility and the \$44 million guarantee facility (see Note 27). On 30 May 2003, pending the formal agreement of this facility, the Company drew \$50.0 million which was outstanding at 30 November 2003. On 30 June 2003, as a condition to the receipt of waivers of potential defaults and amendments to the financial covenants contained in the Company's existing credit facility agreements, SNTG signed a formal agreement with the Company for a \$50.0 million subordinated loan bearing an interest rate of 12% per annum up to 12 February 2004. This Subordinated Note is fully subordinated to all indebtedness owed under and pursuant to the \$440.0 million credit facility, the \$55/45 million credit/guarantee facility and the \$44 million guarantee facility. The Company and SNTG have irrevocably agreed to convert the Subordinated Note in return for the issuance of 22,727,272 Common shares. The conversion of the Subordinated Note was completed on 20 April 2004. See Note 28 'Subsequent events' below.

The SNSA liquidity line

SNSA has extended to the Company a committed line of credit in the amount of \$50 million pursuant to a facility agreement, dated as of 30 June 2003 and restated as of 21 August 2003 for working capital and other corporate purposes. This line remains available to the Company until 28 November 2004. Pending the formal agreement of this facility the Company made a drawdown of \$50 million in February 2003 which was repaid in March 2003, and a drawdown of \$15.0 million in June 2003, which was repaid in the third quarter of 2003. However SNSA has informed the Company that SNTG's ability to fund a draw down under the SNSA liquidity line is limited by the terms of SNSA's existing credit facilities and may be prohibited in certain circumstances. The Company has advised SNSA that it does not expect to utilise this liquidity line.

Interest rates and repayment

The Company pays a variable interest rate on outstanding borrowings, except for the SNSA Subordinated Note, at a rate equal to LIBOR plus margin per annum. The margin was 3.25% at 30 November 2003. The Company is permitted to repay all or any portion of the principal amount outstanding, along with any accrued interest, at any time, however, the SNSA liquidity line will become fully subordinated to the \$440 million credit facility and the \$55/45 million credit/guarantee facility upon the occurrence of an event of default under those facilities. In addition, the Company is prohibited under the terms of its existing credit facility agreements from repaying any amounts under the SNSA liquidity line at any time that an event of default or potential event of default has occurred and is continuing or, as a result of such payment, would occur under its existing credit facility agreements. The SNSA liquidity line may be utilised for working capital and other corporate purposes. As of 30 November 2004, there were no amounts outstanding under the SNSA liquidity line.

Covenants and restrictions

The Company's credit facilities contain various financial covenants, including but not limited to, minimum consolidated tangible net worth, maximum consolidated debt to consolidated tangible net worth and maximum consolidated debt to EBITDA. The Company announced in December 2002 that it was potentially in breach of certain financial covenants contained in the Company's existing credit facility agreements. In light of these developments the Company obtained amendments to these facilities to avoid financial covenant defaults. The amendments included revised financial covenants and a requirement that SNSA continue to provide financial support through the provision of the SNSA liquidity line until 28 November 2004.

As a result of certain operational problems on major projects, the Company found it increasingly difficult to remain in compliance with the revised financial covenants under the existing credit facility agreements. Consequently, it engaged in further discussions with its banks for amendments to or waivers of financial covenants. On 1 July 2003, the Company announced that it had obtained a waiver of potential defaults and amendments to the financial covenants contained in these facilities through 30 November 2003.

On 17 September 2003, the Company announced that it expected higher than previously projected losses for 2003. As a result, the Company was in potential breach of the revised financial covenants under the waiver agreements obtained on 1 July 2003. The Company sought and obtained from its lenders under the existing credit facility agreements new waivers of these revised financial covenants. These new waivers expired on 15 October 2003 and replaced the original waivers, which were set to expire on 30 November 2003.

Notes to the consolidated financial statements continued

During late 2003, the Company continued to engage in restructuring discussions with its lenders under the existing credit facility agreements. As part of these ongoing discussions, the Company received four subsequent covenant waiver extensions, providing covenant relief for the period 15 October 2003 through 30 April 2004 subject to certain conditions.

On 12 February 2004 the Company entered into an intercreditor override, and security trust deed ("Intercreditor Deed") which, among other things, incorporates changes to and supersedes the covenants and security arrangements in the existing credit facility agreements. Further details are provided in Note 28.

The Company's latest forecasts for fiscal year 2004 indicate that there will be a narrow margin of compliance with the consolidated debt to EBITDA ratio covenant at the end of the fourth quarter of 2004.

The Company's ability to remain within its covenants is dependent on: (i) its operating performance; (ii) the successful completion of the Subsequent Issue during the second quarter of 2004; (iii) its ability to recover variation orders and claims from customers where additional contract costs are incurred; and (iv) the success of the Company's plans to divest certain assets.

The Company has consequently made contingency plans in the event that the operational results for the year fall below the latest updated estimates as follows: (i) the Company has the option of using unsecured debt finance as an alternative means of repaying bank facilities; (ii) the Company can defer discretionary capital expenditure; (iii) the Company has the option of raising further equity, and (iv) the Company can seek to obtain a waiver of certain covenant breaches if they were to arise.

16. Accounts payable and accrued liabilities

Accounts payable and accrued liabilities comprise the following:

As of 30 November (in thousands)	2003 \$	2002 \$
Invoice accruals	212,122	206,953
Trade payables	148,391	168,776
Trade notes payable	–	517
Short-term payables to joint ventures	29,843	5,359
Provision for loss-making contracts	40,416	6,029
	430,772	387,634

17. Related party transactions

Related party transactions included the following charges paid to/received from SNSA:

For the year ended 30 November (in thousands)	2003 \$	2002 \$	2001 \$
Corporate services agreement	3,370	3,243	3,676
Interest charges (see Note 15 'Long-term debt and capital lease obligations' above)	3,496	605	394
Premia payable to captive insurance company	6,600	2,824	–
Receipts under captive insurance policy	(3,004)	(2,800)	–
Other recharges	7,960	5,588	3,801
Total	18,422	9,460	7,871

Corporate services agreement

Pursuant to a corporate services agreement, SNSA supplies through its subsidiaries, financial, risk management, public relations and other services to the Company for an annual fee based on costs incurred in rendering those services. The fee is subject to negotiation and agreement between the Company and SNSA on an annual basis. The fees of these management services were \$3.4 million, \$3.2 million and \$3.7 million for the years 2003, 2002 and 2001, respectively.

Captive insurance company

SNSA owns Marlowe Insurance Ltd., a Bermuda captive insurance company through which the Company's assets and activities are insured. The Company owns a separate class of non-voting preference shares which gives the Company an entitlement to receive a dividend in respect of profits earned by Marlowe Insurance Ltd. in respect of the Company's policies. The relationship among the shareholders and the obligations of each shareholder are set forth in a shareholder's agreement. The Company does not intend, and it is not currently aware of any intention on the part of SNSA, to change this relationship in the future.

Other recharges

SNSA provides various services to the Company, including insurance, payroll administration, information technology, etc. and charges the Company on an arms length basis.

Cross-default in certain credit and guarantee facilities

As described in more detail in Note 27, SNSA has guaranteed \$4.8 million of bank guarantees issued under Other Bank Guarantee Arrangements, while SNSA and SNTG jointly and severally have guaranteed bank guarantees issued under the guarantee portion of the \$55/45 million credit/guarantee facility, as well as bank guarantees issued under the \$44 million guarantee facility. Additionally, certain actions or events undertaken by SNSA and SNTG including without limitation, incurring un-permitted liens, defaulting under certain debt facilities, and failing to comply with non-appealable court orders, will result in a cross-default under these facilities.

Other matters

In the light of the fact that, after the completion of the Private Placement, the Share Conversion and the Debt Conversion, the Company will no longer be a majority-owned subsidiary, SNSA has informed the Board of Directors that SNSA will be subject to certain contractual restrictions under existing credit arrangements on its ability to make investments and provide guarantees or other financial support to the Company.

As described in Note 15 to the consolidated financial statements, on 30 June 2003, as a condition to the receipt of waivers of potential defaults and amendments to the financial covenants contained in the Company's credit facilities, SNTG agreed to provide the Company with a \$50 million subordinated loan bearing an interest rate of 12% per annum, evidenced by the Subordinated Note. The Subordinated Note is fully subordinated to all indebtedness owed under and pursuant to the \$440 million credit facility and the \$55/45 million credit/guarantee facility. Subsequent to 30 November 2003, the Company and SNTG irrevocably agreed to convert the Subordinated Note in return for the issuance of 22,727,272 Common shares to SNTG, representing a conversion price of \$2.20 per share. The conversion of the Subordinated Note was completed on 20 April 2004.

In May 2002 SNSA advanced \$64.0 million to the Company in order to assist the Company to repurchase the 6,142,857 Common Shares previously issued to Vinci and to settle the share price guarantee. The Company subsequently issued these and other shares to SNSA during fiscal year 2002. The proceeds of \$38.4 million from the issue of the shares were used to repay the debt due to SNSA. In November 2002, the Company issued 6,019,287 Common Shares to SNSA for proceeds of \$25.6 million to repay the remaining outstanding portion of the \$64.0 million loan. See Note 21 'Common Shares, Class A shares and Class B shares'.

Short-term payables due to SNSA of \$18.4 million as of 30 November 2003 (2002: \$0.6 million) relate primarily to outstanding insurance premia, corporate services agreement charges and other recharges. The Company is entitled to receive a dividend in respect of the underwriting profits earned on an insurance policy, which is written for the Company. This dividend (\$3.6 million) for the year to 30 November 2003 is expected to be declared and paid in April 2004 and has therefore not been included in the results for the year ended 30 November 2003.

During fiscal year 2003 the Company made a payment of \$50,000 for marketing services to a company in which a non-executive Director has an interest (2002: \$50,000).

18. Restructuring and reorganisation programme

For the year ended 30 November 2003 (in thousands)	Opening balance \$	Expensed in the year \$	Paid in the year \$	Other (a) \$	Closing Balance \$
Real estate costs	–	2,682	–	21	2,703
Personnel and redundancy costs	–	13,233	(715)	119	12,637
Professional fees	–	318	(77)	–	241
Total	–	16,233	(792)	140	15,581

(a) Includes the effect of exchange rate changes.

The restructuring charges recorded in fiscal year 2003 result from the implementation of the new management team's plan for financial recovery, which included the restructuring of the Group's cost and asset base. The first stages of the plan for financial recovery, involving changes in the Company's personnel, operating structure and business processes, were substantially completed in the second half of fiscal year 2003. The senior management tier was restructured, with new appointments to 30 out of 40 posts; a plan was commenced to reduce the total workforce by 21% through disposal of certain businesses (1,100 posts), see Note 8 'Assets held for sale', and headcount reduction (400 posts).

The real estate costs of \$2.7 million were incurred in the AFMED region, where a provision of \$1.8 million was recorded for the accrued rental of office space vacated by Paragon Litwin. The balance of \$0.9 million of unamortised leasehold improvements for these offices was also written off.

The \$13.2 million of personnel and redundancy costs relate to severance payments, vacation paid-in-lieu, and outplacement fees, and were principally incurred in the NEC, AFMED, Corporate and NAMEX segments due to the need to reduce staffing levels in Aberdeen, Stavanger, Corporate Nanterre and Houston offices to reflect lower levels of business expected in 2004. The Company expects the majority of the provision outstanding at year-end 2003 to be paid before year-end 2004, although this is dependent on the outcome of consultative processes with works councils in France and Norway, which commenced in 2003.

The professional fees totalling \$0.3 million relate to fees incurred in connection with asset disposals.

19. Operating leases

Total operating lease commitments as of 30 November 2003 amount to \$96.6 million. Charter hire obligations towards certain construction support, diving support, survey and inspection ships account for \$27.4 million of the total commitments. The remaining obligations relate to office facilities and equipment.

Total minimum annual lease commitments payable and sublease rentals receivable are as follows:

(in thousands)	Operating leases \$	Sublease rentals \$
2004	25,756	3,212
2005	19,854	3,058
2006	19,543	3,016
2007	9,774	2,187
2008	7,929	2,082
Thereafter	13,729	9,990
	96,585	23,545

(in thousands)	\$
Norwegian kroner	41,578
Euros	37,273
US dollars	12,736
British pounds	4,989
Central African franc	9
	96,585

Total operating lease rentals charged as an expense for the year ended 30 November 2003 were \$32.3 million (2002: \$34.0 million and 2001: \$21.4 million).

20. Segment and related information

The Company has reportable segments based on the geographic distribution of where work is carried out.

During 2003, the Company realigned the geographical segments it uses to manage its business. The Company consolidated its United Kingdom, Norwegian and eastern Canadian operations into the Northern Europe and Canada (NEC) region and redefined its remaining geographic segments. Each region is headed by a vice-president who is responsible for managing all aspects of the projects within the region, from initial tender to completion, and, under the Company's new management structure, is accountable for profits and losses for such projects.

The Company's operations are managed through seven regional offices: Nanterre, France for the AFMED region; Aberdeen, United Kingdom (for the U.K. area) and Stavanger, Norway (for the Norwegian area) for the NEC region; Houston, Texas in the United States for the NAMEX region; Rio de Janeiro, Brazil for the SAM region; Jakarta, Indonesia for the AME region; and Sunbury, United Kingdom for Corporate activities. The Company assembles and constructs offshore infrastructure equipment at our fabrication yards in Nigeria (AFMED region) and the United States (New Orleans, Louisiana) (NAMEX region). In addition, the Company via the Sonamet, a non-consolidated equity investee, assembles and constructs offshore infrastructure equipment in the fabrication yard in Angola (AFMED region).

Segment geographic coverage

Africa, Mediterranean and the Caspian Sea region (AFMED)

Includes all activities in Africa, the Mediterranean and Caspian Sea, but excludes Azerbaijan

Northern Europe and Canada region (NEC)

Includes all activities in Northern Europe, Eastern Canada, Greenland and Azerbaijan

North America and Mexico region (NAMEX)

Includes all activities in North America including Mexico, Central America, and Western Canada

South America region (SAM)

Includes all activities in South America and the islands of the southern Atlantic Ocean

Asia and Middle East region (AME)

Includes all activities in Asia Pacific, India, and the Middle East excluding the Caspian Sea

Corporate

Includes all activities that serve more than one region. These include:

- ▶ Paragon Engineering Services, Inc., Paragon Litwin S.A., and Paragon Italia S.r.l. which provide engineering services for the onshore and offshore oil and gas industry;
- ▶ NKT Flexibles, a joint venture that manufactures flexible pipeline and risers;
- ▶ Seaway Heavy Lifting Ltd. (SHL), a joint venture with a subsidiary of the Russian oil company Lukoil-Kaliningradmorneft plc, which operates the heavy lift ship *Stanislav Yudin*.
- ▶ Serimer DASA, a contract surface welding services entity employed both onshore and offshore by pipelay contractors;
- ▶ Assets which have global mobility including construction and flowline lay support ships, ROVs, trenchers, ploughs, and other mobile assets that are not allocated to any one region; and
- ▶ Management and corporate services provided for the benefit of all Stolt Offshore businesses.

Notes to the consolidated financial statements continued

Summarised financial information concerning each of the Company's reportable segments is provided in the following tables:

For the year ended 30 November 2003 (in thousands)	AFMED \$	NEC \$	NAMEX \$	SAM \$	AME \$	Corporate \$	Total \$
Net operating revenue – external	673,816	387,551	200,624	55,984	26,786	137,512	1,482,273
Net operating revenue – internal ^(a)	100,412	101,531	41,900	17,551	1,387	5,066	–
Equity in net income of non-consolidated joint ventures	1,851	3,576	–	–	–	(5,024)	403
Depreciation and amortisation	(17,668)	(3,747)	(779)	(2,178)	(3,267)	(65,860)	(93,499)
Impairment of tangible fixed assets	(65,095)	(101)	(12,366)	–	–	(98,960)	(176,522)
Restructuring charges	(9,808)	(1,636)	(314)	–	–	(4,475)	(16,233)
Research and development expense	–	–	–	–	–	(1,484)	(1,484)
Interest expense	(8,878)	(429)	(1,167)	–	(307)	(17,105)	(27,886)
Interest income	–	–	–	–	–	3,093	3,093
Net income (loss) before tax after minority interest	(285,167)	23,117	(32,312)	18,156	(6,553)	(135,983)	(418,742)
Income tax (expense) benefit	4,138	4,528	(117)	(251)	(440)	(7,203)	655
Net income (loss)	(281,029)	27,645	(32,429)	17,905	(6,993)	(143,186)	(418,087)
Segment assets	494,394	118,939	115,375	78,170	39,685	396,097	1,242,660
Long-lived assets ^(b)	238,291	25,303	41,310	60,469	15,195	210,380	590,948
Investments in and advances to non-consolidated joint ventures	21,753	5,910	–	–	–	15,299	42,962
Capital expenditures	5,417	860	421	1,575	–	13,622	21,895

(a) Internal revenues are eliminated on consolidation of the Company's results and are therefore shown in the table to equal to zero in total. Transactions between reportable segments are accounted for on an arm's length basis.

(b) Long-lived assets include net fixed assets, investments in and advances to non-consolidated joint ventures and deposits and non-current receivables.

As discussed above the Company realigned its operating structure. The table below sets forth restated operating results by business segment for 2002 and 2001.

For the year ended 30 November 2002 (in thousands)	AFMED \$	NEC \$	NAMEX \$	SAM \$	AME \$	Corporate \$	Total \$
Net operating revenue – external	702,764	335,625	190,460	52,012	25,677	130,950	1,437,488
Net operating revenue – internal ^(a)	118,672	91,259	52,119	13,458	1,385	4,590	–
Equity in net income of non-consolidated joint ventures	5,905	10,708	–	–	–	(11,326)	5,287
Depreciation and amortisation	(21,981)	(3,101)	(17,747)	(5,711)	(2,545)	(41,725)	(92,110)
Impairment of goodwill	–	–	(102,987)	–	(1,626)	(1,822)	(106,435)
Impairment of tangible fixed assets	(700)	–	–	–	(1,100)	(2,183)	(3,983)
Research and development expense	–	–	–	–	–	(770)	(770)
Interest expense	(10,803)	(1,246)	(2,613)	(1,859)	(418)	(1,934)	(18,873)
Interest income	–	–	–	–	–	633	633
Net income (loss) before tax after minority interest	(36,638)	10,864	(116,046)	5,470	(3,360)	(3,987)	(143,697)
Income tax (expense) benefit	(6,552)	16,061	(12,122)	(581)	(343)	(4,621)	(8,158)
Net income (loss)	(43,190)	26,925	(128,168)	4,889	(3,703)	(8,608)	(151,855)
Segment assets	585,955	139,096	140,481	88,467	35,230	469,375	1,458,604
Long-lived assets ^(b)	313,132	26,309	66,146	69,179	12,072	363,327	850,165
Investments in and advances to non-consolidated joint ventures	9,394	5,897	–	–	–	13,483	28,774
Capital expenditures	2,331	3,077	350	1,600	690	46,586	54,634

For the year ended 30 November 2001 (in thousands)	AFMED \$	NEC \$	NAMEX \$	SAM \$	AME \$	Corporate \$	Total \$
Net operating revenue – external	520,207	325,352	276,681	50,472	39,437	43,789	1,255,938
Net operating revenue – internal ^(a)	78,311	89,848	78,970	12,674	4,255	4,567	–
Equity in net income of non-consolidated joint ventures	10,902	5,798	–	–	–	(5,045)	11,655
Depreciation and amortisation	(5,984)	(2,554)	(21,546)	(6,003)	(2,015)	(53,648)	(91,750)
Impairment of Comex trade name	–	–	–	–	–	(7,932)	(7,932)
Research and development expense	–	–	–	–	–	(393)	(393)
Interest expense	(2,891)	(576)	(2,942)	(2,285)	(421)	(20,156)	(29,271)
Interest income	–	–	–	–	–	2,451	2,451
Net income (loss) before tax after minority interest	24,529	13,006	(36,191)	5,494	4	(426)	6,416
Income tax (expense) benefit	(19,672)	5,294	–	–	(3,242)	(2,999)	(20,619)
Net income (loss)	4,857	18,300	(36,191)	5,494	(3,238)	(3,425)	(14,203)
Capital expenditures	4,060	430	1,789	18,824	270	37,495	62,868

(a) Internal revenues are eliminated on consolidation of the Company's results and are therefore shown in the table to equal to zero in total.

(b) Long-lived assets include net fixed assets, investments in and advances to non-consolidated joint ventures and deposits and non-current receivables.

During fiscal year 2003, the Company adopted the following classification of its service capabilities, which are conducted within each reporting segment.

Subsea construction, Umbilicals, Risers and Flowlines (SURF): SURF relates to engineering and construction work relating to oil and gas fields that are developed subsea (meaning the production wellhead is on the seabed), as opposed to surface installations (in which the production wellhead is above the surface on a platform). This includes tieback projects, which involve pipelaying, umbilical installation and trenching or ploughing, to connect a new additional subsea development to an existing production facility. The installation of jumpers and spoolpieces, as well as hyperbaric welding, are also typical SURF activities. SURF also includes large multi-year projects encompassing all pipelay, riser and umbilical activities of a complete field development. This category also includes ship charters and rental of equipment and construction support ROVs. During 2003, SURF activities accounted for approximately 40% of total revenue.

Conventional: This comprises engineering and construction activities relating to platforms attached to the seabed and their associated pipelines. Conventional projects involve shallow water activities and proven technology, typically under long-term contracts. Conventional activities include design, construction and installation of fixed platforms. This category also includes selected ship charters and equipment rental in relation to Conventional activities. During 2003, Conventional activities accounted for approximately 35% of total revenue.

Inspection, maintenance and repair (IMR): This comprises, among other things, platform surveys, debris removal and pipeline inspections using ROVs. IMR activities are conducted both under long-term frame agreements with customers and in the spot market. This category also includes ship charters and equipment rental relating to IMR activities. During 2003, IMR activities accounted for approximately 14% of total revenue.

Trunklines: This comprises offshore installation of large-diameter pipelines used to carry oil or gas over long distances (trunklines). Trunkline projects typically are based on large contracts, utilising the *LB 200* pipelay barge. During 2003, 2002 and 2001 there were no trunkline activities.

Corporate: This comprises all activities that serve more than one region. These include: the Paragon Companies, NKT Flexibles, SHL, Serimer DASA and assets that have global mobility including construction and flowline lay support ships, ROVs, trenchers, ploughs and other mobile assets that are not allocated to any one region. During 2003, Corporate activities accounted for approximately 11% of total revenue.

The Company also provides field-decommissioning services at the end of the working life of an offshore oilfield.

The following table shows net operating revenue for 2003, and restated for 2002 and 2001 by service capability:

For the year ended 30 November (in thousands)	2003 \$	2002 \$	2001 \$
SURF	598,738	602,298	603,390
Conventional	518,135	432,864	294,569
IMR	204,052	237,325	290,399
Corporate ^(a)	161,348	165,001	67,580
Total Net Operating Revenue	1,482,273	1,437,488	1,255,938

(a) This relates to Serimer DASA and the Paragon Companies.

During the year ended 30 November 2003, three customers accounted for more than 10% of the Company's revenue. The revenue from these customers was \$651.0 million. These revenues are attributable to the AFMED, NEC, NAMEX, and AME regions. Revenue from the largest customer was \$329.4 million and was attributable to the AFMED, NEC and NAMEX regions. The revenue from the second largest customer was \$175.4 million and was attributable to the AFMED, NEC, NAMEX and AME regions. Revenues from the third largest customer were \$146.1 million and were attributable to the AFMED region. During the year ended 30 November 2002, two customers of the Company each individually accounted for more than 10% of the Company's revenue. The revenue from the largest customer was \$285.8 million and was attributable to the AFMED, NEC and NAMEX regions (2001: \$269.2 million attributable to the AFMED region). The revenue from the second largest customer was \$146.9 million and was attributable to the AFMED, NEC and AME regions.

During the year ended 30 November 2001, in addition to the largest customer described in the comparative information above, another customer accounted for more than 10% of the Company's revenue. The revenue from this customer was \$131.5 million and was attributable to the NAMEX region.

21. Common Shares, Class A Shares and Class B Shares

As of 30 November 2003, the Company had authorised share capital of 140,000,000 Common shares, par value \$2.00 per share, and 34,000,000 Class B shares, par value \$2.00 per share.

At this time, 76,262,215 Common Shares and 34,000,000 Class B Shares were outstanding. SNSA held 55% of the Common Shares and 100% of the Class B Shares which represented an economic interest of 63% of the Company and 69% of the voting rights. Class B Shares were converted into Common Shares on 13 February 2004, on a two-for-one basis.

Notes to the consolidated financial statements continued

Until the conversion of Class B Shares, Common Shares and Class B Shares voted as a single class on all matters submitted to a vote of shareholders, with each share entitled to one vote, with the exception of recapitalisation, reclassification or similar transactions affecting the relative rights, preferences and priorities of the Common Shares and Class B Shares, which required an affirmative vote of the holders of a majority of the outstanding Common Shares and Class B Shares each voting as a separate class. With respect to liquidation and dividend rights, the Class B Shares were entitled to receive \$0.005 per share for each \$0.01 per Common Share.

On 10 March 2003 the Company repurchased 879,121 Common Shares from NKT Holdings A/S as part of the transaction to settle the share price guarantees in respect of the NKT Flexibles joint venture. The difference between the market price at which these shares were repurchased from NKT Holdings A/S and the guaranteed share price was \$12.4 million and was deducted from paid-in surplus as described in Note 3. During fiscal year 2002 the Company repurchased 6,142,857 Common Shares from Vinci and 249,621 Common Shares from NKT Holdings A/S as part of the transaction to settle the share price guarantees in respect of the acquisitions of ETPM and NKT Flexibles respectively. The difference between the market price at which the shares were repurchased from Vinci and NKT Holdings S.A. and the guaranteed price was \$58.9 million and \$1.6 million respectively and was deducted from paid-in surplus as described in Note 3. These repurchased shares, through a series of transactions, were subsequently issued to SNSA for proceeds of \$38.4 million to repay a loan of \$64.0 million provided by SNSA to assist in funding the settlement of the guarantees. These transactions were as follows: on 26 June 2002 the Company issued 3,000,000 Common Shares to SNSA for proceeds of \$24.0 million; on 14 November 2002 the Company issued 3,142,857 Common Shares to SNSA for proceeds of \$13.4 million; and on 19 November 2002 the Company issued 249,621 Common Shares to SNSA for proceeds of \$1.0 million. The difference between the market price at which these shares were repurchased from Vinci and NKT Holdings A/S and the amount of the proceeds from SNSA was \$18.1 million. This was deducted from retained earnings.

On 26 November 2002, the Company issued 6,019,287 Common Shares to SNSA for proceeds of \$25.6 million to repay the remaining outstanding portion of the \$64.0 million loan provided by SNSA to assist in funding the settlement of these guarantees.

On 7 March 2001, the Company reorganised the share structure of the Company by increasing the authorised share capital of the Company from 102,000,000 to 140,000,000 Common Shares and reclassifying all outstanding Class A shares as Common Shares on a one-for-one basis. Luxembourg law requires that 5% of the Company's unconsolidated net profits each year be allocated to a legal reserve before declaration of dividends. This requirement continues until the reserve is 10% of the stated capital of the Company, as represented by Common Shares and Class B shares, after which no further allocations are required until further issuance of shares.

The legal reserve may also be satisfied by allocation of the required amount at the issuance of shares or by a transfer from paid-in surplus. The legal reserve is not available for dividends. The legal reserve for all outstanding Common Shares and Class B shares has been satisfied and appropriate allocations are made to the legal reserve account at the time of each issuance of new shares.

As of 30 November 2003, \$14.8 million of the consolidated deficit represented undistributed earnings of non-consolidated joint ventures (2002: \$7.1 million of consolidated retained earnings).

22. Earnings per share

The computations for the three years ended 30 November 2003 are based upon the following outstanding shares:

For the year ended 30 November	2003	2002	2001
Basic			
Common Shares	75,623,949	68,009,632	70,201,030
Class B Shares	17,000,000	17,000,000	17,000,000
Total	92,623,949	85,009,632	87,201,030
Diluted			
Common Shares	75,623,949	68,009,632	70,201,030
Class B Shares	17,000,000	17,000,000	17,000,000
Total	92,623,949	85,009,632	87,201,030
Basic	92,623,949	85,009,632	87,201,030
Potentially dilutive share options	–	–	–
Diluted	92,623,949	85,009,632	87,201,030

The diluted loss per share for the year ended 30 November 2003 does not include Common Share equivalents in respect of share options of 4,363,801 as their effect would be anti-dilutive (2002: 4,408,370 and 2001: 2,797,534).

As of 13 February 2004, all 34,000,000 Class B Shares outstanding were converted into 17,000,000 Common Shares. See Note 28 'Subsequent events' below.

Subsequent to 30 November 2003, the Company received an irrevocable undertaking from SNSA to convert \$50 million subordinated debt to 22,727,272 Common Shares. If this conversion of the subordinated debt had taken place as of 30 November 2002 the weighted average number of outstanding shares would have been 115,351,221 and the loss per share would have been \$3.61 as compared to \$4.51.

All share data and per share data have been restated to reflect the share reclassification on 7 March 2001 whereby Class A Shares were reclassified as Common Shares on a one-for-one basis.

23. Share option plan

A Compensation Committee appointed by the Company's Board of Directors administers the Plan. Options are awarded at the discretion of the Company to Directors and key employees.

On 28 April 1993, the Company adopted a share option plan (the '1993 Plan') covering 7.7 million Common Shares. After April 2003 it was no longer permissible to grant new options under the 1993 Plan and a revised plan was approved to replace it (the '2003 Plan'). The 2003 Plan covers up to but not exceeding 6.3 million Common Shares. Options may be granted under the 2003 Plan exercisable for periods of up to ten years at an exercise price not less than the fair market value per share at the time the option is granted. Options vest 25% on the first anniversary of the grant date, with an additional 25% vesting on each subsequent anniversary.

A stock option plan for key employees and Directors resident in France (the 'French Plan') was approved in 2003. It covers up to but not exceeding 501,000 Common Shares. Options may be granted under the French Plan exercisable for periods of up to ten years at an exercise price not less than the fair market value per share at the time the option is granted. Options vest 25% on the first anniversary of the grant date, with an additional 25% vesting on each subsequent anniversary.

During fiscal year 2003, 1,214,500 options were granted under the 1993 plan and 35,000 options were granted under the 2003 plan. No options had been granted under the French plan.

The following tables reflect activity under the Plan for the three-year period ended 30 November 2003:

For the year ended 30 November	2003		2002		2001	
	Shares	Weighted average exercise price \$	Shares	Weighted Average exercise price \$	Shares	Weighted average exercise price \$
Outstanding at beginning of year	3,683,292	9.85	3,024,410	10.77	2,533,249	10.00
Granted	1,249,500	1.33	797,750	6.35	640,300	13.43
Exercised	–	–	(14,392)	7.38	(75,612)	6.98
Forfeited	(368,720)	9.72	(124,476)	9.97	(73,527)	11.15
Outstanding at end of year	4,564,072	7.55	3,683,292	9.85	3,024,410	10.77
Exercisable at end of year	2,388,007	10.19	2,001,049	10.28	1,477,306	9.65
Weighted average fair value of options granted		0.78		4.49		9.10

All share data and per share data has been restated to reflect the share reclassification on 7 March 2001 whereby Class A Shares were reclassified to Common Shares on a one-for-one basis.

The fair value of each share option grant is estimated as of the date of grant using the Black-Scholes option pricing model with the following weighted average assumptions:

	2003	2002	2001
Risk-free interest rates	3.75%	5.39%	5.62%
Expected lives of options	7 years	7 years	7 years
Expected volatility	70.34%	69.1%	63.7%
Expected dividend yields	–	–	–

Notes to the consolidated financial statements continued

The following tables summarise information about share options outstanding as of 30 November 2003:

As of 30 November 2003 Range of exercise price	Options outstanding			Options exercisable	
	Options outstanding	Weighted average remaining contractual life (years)	Weighted average exercise price \$	Number exercisable	Weighted average exercise price \$
Common Shares					
\$12.13 – 16.58	671,800	6.72	14.33	421,650	14.79
\$7.82 – 11.20	26,000	8.08	9.19	9,750	9.39
\$4.38 – 7.38	775,600	7.38	6.25	273,963	6.12
\$1.19 – 3.00	1,335,500	8.74	1.44	102,000	2.77
	2,808,900	7.87	5.92	807,363	10.26
Class A Shares					
\$12.13 – 16.58	100,250	4.73	16.16	97,875	16.25
\$7.82 – 11.20	932,112	6.16	10.22	759,959	10.21
\$4.38 – 7.38	53,750	3.26	5.79	53,750	5.79
\$1.19 – 3.00	47,250	1.81	2.77	47,250	2.77
	1,133,362	5.71	10.22	958,834	10.21

As part of the acquisition of the former Ceanic Corporation in 1998, holders of Ceanic share options were entitled to exercise all vested and one-third of the unvested options, or to convert any portion thereof to vested Stolt Offshore S.A. Common Share options. The remaining two-thirds of the unvested Ceanic share options were automatically converted to unvested Stolt Offshore S.A. Common Share options at the date of acquisition. The following table summarises information about these options which are outstanding as at 30 November 2003:

As of 30 November 2003 Range of exercise price	Options outstanding			Options exercisable	
	Options outstanding	Weighted average remaining contractual life (years)	Weighted average exercise price \$	Number exercisable	Weighted average exercise price \$
Common Shares					
\$7.82 – 11.20	523,674	3.93	10.75	523,674	10.75
\$4.38 – 7.38	98,136	3.39	6.28	98,136	6.28
	621,810	3.85	10.05	621,810	10.05

24. Compensation and reward

The Company has in place an incentive compensation plan, which provides for annual cash awards to officers, Directors and employees.

Performance bonus

The performance bonus provides for annual cash rewards to employees. The determination of an employee's individual award will be based on salary and individual performance measured against set criteria. The Compensation Committee appointed by the Company's Board of Directors administers the policy. A charge of \$1.4 million has been recorded in respect of fiscal year 2003 (2002: \$2.8 million, 2001: \$nil).

Net profit sharing

During 1993 the Company adopted a profit sharing plan which distributes 10% of the Company's net income, after specific adjustments, to certain of its employees world-wide. The determination of an employee's individual award will be based on salary and overall contribution to the Company. The Compensation Committee appointed by the Company's Board of Directors administers this plan. No charge in respect of profit sharing has been included in the statement of operations for each of the years ended 30 November 2003, 2002 and 2001.

25. Commitments and contingencies

At 30 November 2003, the Company has committed to purchase \$1.7 million of fixed assets from external suppliers.

Technip

In 1996, Coflexip SA and Coflexip Stena Offshore Limited (now known as Technip S.A. and Technip Offshore Limited) ('Technip'), commenced legal proceedings in the U.K. High Court against three subsidiaries of the Company for infringement of a certain patent held by Technip on flexible flowline laying technology. The claim related to the Company's use of the flexible lay system on the *Seaway Falcon*. The claim was heard by the U.K. High Court in 1998 and on 27 January 1999 the disputed patent was held valid in favour of Technip. Following this judgement, Technip claimed damages relating to lost profit for five projects, plus legal costs and interest. However, the damages claim was stayed pending the appeal by both parties against the January 1999 decision. The Court of Appeal dismissed the defendant's appeal and maintained the validity of the patent. The Company applied for leave to appeal the Court of Appeal decision to the House of Lords, which was denied. As a result, the equipment part as well as the process part of the patent were held valid.

During 2001, Technip submitted an amended claim for damages claiming the lost profits on a total of 15 projects. In addition there was a claim for alleged price depreciation on certain other projects. The total claim was for £63 million (approximately \$118.0 million), plus interest, legal fees and a royalty for each time that the flexible lay system tower on the *Seaway Falcon* was brought into U.K. waters. The Company estimated that the total claim was for £88 million (approximately \$165.0 million). In the alternative, Technip claimed a reasonable royalty for each act of infringement, interest and legal costs. Technip did not quantify the claim.

During fiscal year 2003, the U.K. High Court held that the same patent, the subject of the proceedings against the Company, was invalid in a separate and unrelated litigation between a company of the Halliburton Group and Technip. That decision has been appealed by Technip.

In light of the decision in the Halliburton case, the Company applied to the U.K. High Court to stay the damages inquiry in the Stolt Offshore case, pending the resolution of the Halliburton case. The High Court denied the request. The Company appealed this decision to the Court of Appeal and the Court of Appeal, subsequent to a hearing in January 2004, decided that the Company could not benefit from the patent being revoked in the Halliburton case. However, the Court of Appeal did not decide on whether or not to stay the damages inquiry, nor on whether or not to recommend that leave to appeal to the House of Lords be given. These two issues were expected to be considered by the Court of Appeal after the decision in the Halliburton case was known. The damages inquiry in the infringement case with Technip was scheduled to be heard beginning in late April 2004.

As of 30 November 2002 the Company, in consultation with its advisers, had assessed that the range of possible outcomes for the resolution of damages was \$1.5 million to \$130.0 million and determined that no amount within the range was a better estimate than any other amount. Consequently, in accordance with SFAS No.5 'Accounting for Contingencies', as interpreted by FASB Interpretation No.14 'Reasonable Estimation of the Amounts of a Loss', the Company provided \$1.5 million in the financial statements, being the lower amount of the range.

As of 30 November 2003, the Company, in consultation with its advisers, provided for an increased contingency reserve of \$9.3 million related to this litigation, reflecting the Company's best estimate of the then-expected settlement.

On 18 March 2004, the Company announced that it and Technip had reached a settlement of this matter. The settlement involves (i) a cash payment by the Company of an amount within the amount of its contingency reserve described above, (ii) Technip's grant of a license to the Company for the use of the allegedly infringing technology covering the North Sea area for future periods for an immaterial annual fee, (iii) the termination of arbitration proceedings in the United States with respect to an unrelated matter, with neither party making payment to the other, and (iv) a transfer to Technip of a portion of the Company's minority equity interest in a project joint venture involving Technip and the Company. The Company estimates that the reduction in future profits from this transferred interest is approximately \$6.0 million. Technip has not granted to the Company a licence to use the allegedly infringing technology or process in any other jurisdiction.

Duke Hubline

In October 2003, the Company commenced arbitration proceedings against Algonquin Gas Transmission, claiming approximately \$57.8 million in unpaid invoices for work performed while laying an offshore gas pipeline off the coast of Massachusetts for the Duke Hubline project. Algonquin Gas Transmission, the owner of the pipeline, challenged its obligation to pay any of the invoice amounts and asserted counterclaims totalling an additional \$39.0 million for alleged mismanagement and inadequate performance by the Company. Due to Algonquin Gas Transmission's non-payment of invoiced amounts, the Company was unable to pay certain of its subcontractors employed to work on the pipeline, two of which, Bisso Marine Company and Torch Offshore Inc., filed lawsuits against the Company in Louisiana State Courts for non-payment of amounts invoiced. These same subcontractors claimed liens over the pipeline, which liens are the subject of proceedings commenced by them against the Company and Algonquin Gas Transmission in Massachusetts State Court.

The Company's dispute with Algonquin Gas Transmission was referred to mediation in late January 2004, at which the parties reached a 'settlement in principle' whereby (i) Algonquin Gas Transmission agreed to pay the Company \$37.0 million in full and final settlement of the Company's claims and (ii) the Company agreed to withdraw the arbitration proceedings and use its best efforts to secure the release of the above-mentioned subcontractor liens in full and final settlement of Algonquin Gas Transmission's counter claims. A definitive settlement agreement was executed on 26 February 2004 reflecting the terms of the 'settlement in principle' and Algonquin Gas Transmission paid the settlement amount to the Company. The Company has also reached agreements in principle with Bisso Marine and Torch Offshore to settle the related subcontractor litigation. The LC is expected to be released before the end of the second quarter of fiscal year 2004. The value of the settlement is consistent with the receivable of \$37.0 million, recorded as at 30 November 2003.

Other contingencies

In connection with a major West African contract, the Company received a letter dated 12 December 2003 from the customer notifying the Company of a potential claim for an unspecified amount of liquidated damages. The claim relates to delays in completion of certain milestones. The Company believes that the customer does not have a valid case for liquidated damages, and on that basis has not recorded a provision. A similar notification letter received in December 2002 on a different project was settled amicably during fiscal year 2003.

In addition, in the course of its business, the Company becomes involved in contract disputes from time to time due to the nature of its activities as a contracting business involved in several long-term projects at any given time. The Company makes provisions to cover the expected risk of loss to the extent that negative outcomes are likely and reliable estimates can be made. However, the final outcomes of these contract disputes are subject to uncertainties as to whether or not they develop into a formal legal action and therefore the resulting liabilities may exceed the liability the Company may anticipate.

Furthermore, the Company is involved in legal proceedings from time to time incidental to the ordinary conduct of its business. Litigation is subject to many uncertainties, and the outcome of individual matters is not predictable with assurance. It is reasonably possible that the final resolution of any litigation could require the Company to make additional expenditures in excess of reserves that it may establish. In the ordinary course of business, various claims, suits and complaints have been filed against the Company in addition to the one specifically referred to above. Although the final resolution of any such other matters could have a material effect on the Company's operating results for a particular reporting period, the Company believes that it is a remote likelihood that these matters will materially affect its consolidated financial position.

For accounting purposes, the Company expenses legal costs as they are incurred.

26. Financial instruments

The Company operates in a large number of countries throughout the world and, as a result, is exposed to currency fluctuations largely as a result of incurring operating expenses in the normal course of business. The Company hedges liabilities resulting from future payments to suppliers that require payment in a currency other than the functional currency of the local company. The Company's major foreign currency exposures are to the euro, British pound and Norwegian kroner. Until August 2003 these exposures were managed by the Company by entering into derivative instruments pursuant to the Company's policies in areas such as counter party exposure and hedging practices. During August 2003, the Company closed out the majority of its foreign exchange positions to ensure that it had sufficient liquidity to fund its operations and to provide for a potentially protracted period of negotiation with certain major customers regarding settlement of claims and variation orders. The Company realised a \$28.2 million gain when these positions were closed. This gain was deferred in Other Comprehensive Income ('OCI') and is being released to the results of operations in line with the underlying transactions. At 30 November 2003, the gain arising from the closing of the foreign exchange positions which was still deferred in OCI was \$16.8 million. At 30 November 2003, the Company did not hold a significant number of derivative instruments as financial institutions were unwilling to provide these instruments as a result of the Company's weak financial position. As a result, the Company has a significant exposure to future foreign exchange fluctuations.

Designation of derivative instruments is performed on a specific exposure basis to support hedge accounting. The changes in the fair value of these derivative instruments are offset in part or in whole by corresponding changes in the fair value of cash flows of the underlying exposures being hedged. The Company does not hold or issue derivative instruments for trading purposes.

All of the Company's derivative instruments are over-the-counter instruments entered into with major financial credit institutions to hedge the Company's committed exposures. The Company's derivative instruments are primarily standard foreign exchange forward contracts, which subject the Company to a minimum level of exposure risk and have maturities of less than 24 months. The Company does not consider that it has a material exposure to credit risk from third parties failing to perform according to the terms of derivative instruments.

Notes to the consolidated financial statements continued

The following foreign exchange forward contracts, maturing between 5 December 2003 and 17 November 2004 were outstanding as at 30 November 2003:

As of 30 November (in thousands indicated in local currency)	2003		2002	
	Purchase		Purchase	
Euros	-		380,962	
US dollars	-		-	
Swedish kronor	-		4,364	
Danish kronor	-		18,876	
Norwegian kroner	-		169,200	
British pounds	11,180		6,475	

The Company utilises foreign currency derivatives to hedge committed and forecasted cash flow exposures in respect of receipts from customers and payments to suppliers that are not in the functional currency of the relevant subsidiary of the Company. All of these contracts have been designed as cash flow hedges. In all cases, the terms of the commercial transaction and derivatives are matched so that there is no assumed hedge ineffectiveness.

As at 30 November 2003, the fair value of these derivative instruments recorded in the consolidated balance sheet was \$1.0 million, net of tax, in assets and no liabilities. Gains and losses on the effective portions of these derivative instruments have been deferred in OCI until the underlying transaction is recognised in the results of operations. The gains and losses deferred in OCI are shown net of deferred taxes of \$4.5 million in 2003. These amounts will be reclassified into results of operations as underlying transactions are recognised.

A gain of \$0.8 million has been recognised in operating expenses in the year to 30 November 2003 in respect of discontinuance of cash flow hedges where it was probable that the original forecast transaction will not occur (2002: \$nil, 2001: \$nil). As of 30 November 2003 the fair value of gains classified in OCI, including the gain on the monetised hedges, expected to be released to the consolidated statement of operations in the year ending 30 November 2004 is \$17.8 million.

The following table summarises the estimated fair value amounts of the Company's other financial instruments which have been determined by the Company, using appropriate market information and valuation methodologies. In some cases, judgement is required to develop the estimates of fair values, thus the estimates provided herein are not necessarily indicative of the amounts that could be realised in a current market exchange:

As of 30 November (in millions)	2003		2002	
	Carrying amount	Fair value	Carrying amount	Fair value
	\$	\$	\$	\$
Financial assets				
Cash and cash equivalents	81.9	81.9	11.7	11.7
Restricted cash deposits	2.1	2.1	1.7	1.7
Employee loans	2.1	2.1	2.4	2.4
Forward contracts	1.0	1.0	23.4	23.4
Financial liabilities				
Bank overdrafts	2.5	2.5	16.0	16.0
Short-term payables due to SNSA	68.4	68.4	0.6	0.6
Long-term debt	385.0	385.0	335.0	335.0

The carrying amounts of cash and cash equivalents and bank overdrafts approximate their fair value. The estimated value of the Company's long-term debt is based on interest rates at 30 November 2003 and 2002 using debt instruments of similar risk.

27. Guarantees

The Company arranges for bank guarantees, which collectively refers to bank guarantees, performance bonds, bid bonds, advance payment bonds, guarantees or standby letters of credit in respect of a performance obligation of the Company to be provided to its customers in connection with the Company's work on specific projects.

The total amount outstanding in respect of bank guarantees as of 30 November 2003 was \$324.9 million. The purpose of the bank guarantees generally is to enable the Company's customers to recover cash paid to the Company in advance of performing its obligations under the contract or to obtain cash compensation should the Company be unable to fulfil its performance obligations under the Company's contracts.

The Company has the following facilities available to provide bank guarantees.

The \$55/45 million credit/guarantee facility

On 9 July 2002, the Company entered into a \$55/45 million credit/guarantee facility agreement with a term of four years. Under this facility the Company, amongst others, can request the provision of bank guarantees in relation to the Company's performance obligations of up to \$45.0 million. As of 30 November 2003, the Company had issued \$35.3 million of guarantees under this facility. For further details about this facility see 'Long-term debt and capital lease obligations' above. SNSA and Stolt-Nielsen Transportation Group ('SNTG') have jointly and severally guaranteed the Company's obligations to the banks providing bank guarantees pursuant to the guarantee portion of this facility.

The \$44 million guarantee facility

The Company is a party to a \$44.0 million secured guarantee facility as guarantor. Under this facility, Citibank N.A. and certain other financial institutions as banks and DnB NOR Bank ASA, as facility agent, security trustee and issuing bank agreed to the issuance of bank guarantees. As of 30 November 2003, \$23.5 million of guarantees were outstanding under this facility, which is fully utilised. SNSA and SNTG have jointly and severally guaranteed the Company's obligations to the banks providing guarantees under this facility. In addition, ships owned by the subsidiaries of SNTG (Bermuda) are pledged in support of the bank guarantees.

The \$28 million reimbursement facility

The Company entered into an amended and restated secured reimbursement agreement dated 27 August 2003, between the Company, as borrower, and DnB NOR Bank ASA as bank. Under this facility, DnB NOR Bank ASA, as bank, agreed to extend the term of a letter of credit until 15 September 2004. The letter of credit was issued in connection with the Duke Hubline project. As at 30 November 2003 the amount outstanding for this letter of credit was \$28.0 million. As the Company's contractual dispute relating to the Duke Hubline project has been settled, this facility will no longer be required and the letter of credit is expected to be released before the end of the second quarter of 2004.

Other bank guarantee arrangements

The Company has arrangements with a number of financial institutions to issue bank guarantees on its behalf. As of 30 November 2003, the aggregate amount of guarantees issued under these facilities is \$238.1 million. Of this amount, \$4.8 million is guaranteed by SNSA. The bonds under these facilities were issued to guarantee the Company's project performance and that of its subsidiaries and joint ventures to third parties in the normal course of business. As of 30 November 2003, the Company has no bank guarantee capacity available under these arrangements.

The table below summarises as at 30 November 2003 all outstanding bank guarantees, issued by the Company. The maximum potential amount of future payments represents the notional amounts that could be lost under the guarantees if there is non performance under a contract by the guaranteed parties, without consideration of possible recoveries under recourse provisions or from collateral held or pledged. Such amounts bear no relationship to the anticipated losses on these guarantees and greatly exceed anticipated losses.

(in thousands)	Expire within one year	Expire after one year	Total amount outstanding	Maximum potential amount of future payments
	\$	\$	\$	\$
	2003	2003	2003	2003
Bank guarantees – Joint Ventures	17,629	24,635	42,264	42,264
Bank guarantees – Subsidiaries	118,393	148,145	266,538	266,538
Other guarantees	14,151	1,951	16,102	16,102
Total	150,173	174,731	324,904	324,904

The fair value of guarantees provided in respect of joint ventures at 30 November 2003 was \$0.7 million.

28. Subsequent events

- ▶ The Company has been informed by the U.S. Securities and Exchange Commission (SEC) that it is conducting an informal inquiry into the Company's revenue recognition policies and practices with respect to claims and variation orders. The SEC has requested that the Company voluntarily produce information and documents in response to the inquiry and the Company is co-operating fully with the SEC.
- ▶ On 18 December 2003, an agreement was reached with the customer on the OGGs project in Nigeria. The parties agreed that the terms of this agreement would cover all claims of whatever nature, whether formally made or not, and all facts and circumstances as at 30 November 2003 which may give rise to any claims whatsoever under the contract. In addition, it was agreed that the Company would perform the outstanding work as stipulated under the contract. A total of \$43.8 million in cash has been received and a further \$1.2 million is expected to be received in the second quarter of fiscal year 2004. The impact of this settlement was accounted for as a receivable in fiscal year 2003.
- ▶ On 31 December 2003, the pipelay ship *Polaris* dropped a pipeline, which it was laying for the Bonga project in Nigeria. The Company believes that it will successfully obtain reimbursement of the cost (estimated at up to \$20.0 million) under the customer's 'Builders all risk policy', and therefore there is no net cost to the Company relating to this incident. There will be an additional loss of potential income of up to \$5.0 million as a result of non-achievement of milestone bonuses, none of which had yet been booked as income. The Bonga project was 71% complete as at 30 November 2003, with an estimated revenue at completion of \$249.5 million. This is a loss-making contract, and therefore the full forecast loss at completion is accrued in the result for fiscal year 2003.
- ▶ An agreement was reached on 28 January 2004, with Burullus Gas Company of Egypt for the settlement of unagreed variation orders. The impact of this settlement has been included in the results for fiscal year 2003. Substantially all of the proceeds from the settlement had been received in cash, and were included in receivables as of 30 November 2003. The settlement includes notice of final acceptance for all work except for the obligation on the Company to complete repairs to the 24 inch export pipeline for an additional agreed contracted sum.
- ▶ The \$100 million New Bonding Facility. On 12 February 2004, the Company entered into an agreement ('The New Bonding Facility') with certain financial institutions, whereby these institutions agreed to the issuance of bank guarantees of up to \$100 million. The issuance of bank guarantees under this facility is subject to a number of conditions precedent and conditions subsequent, not all of which have been satisfied. This facility is available to the Company for a period of 18 months. As at 20 April 2004, no bank guarantees had been issued under this facility.

The Company has granted security over two accounts of one of its subsidiaries under a cash management system. Pursuant to this cash management system, the Company must ensure that, in one bank account (Lock Box 1) \$20 million has been deposited prior to the issue of any bank guarantee. Thereafter, any cash collateral provided as security for the issue of a bank guarantee, any net disposal proceeds (that is, the disposal proceeds relating to the sale or disposal of an asset owned by the Company or other ship-owning guarantor, net of reasonable fees and expenses, VAT, any other tax and any other creditor claim which has priority) and insurance proceeds (that is, the insurance proceeds relating to the total loss of a ship) shall be paid into this account.

No withdrawals may be made from this account unless HSBC Bank plc, as agent, consents or, following the end of the availability of the New Bonding Facility, existing bank guarantees are reduced or cancelled. The other bank account, Lock Box 2, is to be used for depositing excess cash of the Company over \$75 million. Transfers in and out of these accounts are strictly controlled and the Company must comply with certain monthly information reporting requirements in relation to both bank accounts.

The New Bonding Facility contains (i) representations and warranties from the Company and certain of the Company's subsidiaries, (ii) both affirmative covenants (including in relation to financial reporting, satisfying agreed disposal targets and complying with the cash management system referred to above) and negative covenants (including a prohibition on incurring indebtedness and the disposal of assets, save as expressly permitted) and (iii) a financial covenant in relation to maintaining an agreed level of minimum consolidated tangible net worth. The New Bonding Facility also contains provisions relating to disclosed permitted disposals, which are disposals of certain of the Company's assets, which do not require the consent of the financial institutions as banks under this facility. The assets constituting disclosed permitted disposals will automatically be released from any security interest to allow its disposal. In addition, certain thresholds in respect of disclosed permitted disposals are required to be satisfied. By 31 May 2004 disclosed permitted disposals must be at least \$50 million and by 31 August 2004 disclosed permitted disposals must be at least \$75 million.

- ▶ Intercreditor Deed. The Company entered into an intercreditor override, and security trust deed, dated 12 February 2004 with its lenders, which among other things (i) allowed it to pledge existing collateral for the New Bonding Facility; (ii) provided for certain prepayments under the \$440 million credit facility (discussed in Note 15); and (iii) reset the financial covenants of the Company's existing credit facility agreements to better reflect the Company's business and financial performance. The Intercreditor Deed incorporates changes to and supersedes the covenants and security arrangements in the existing credit facility agreements.

In addition, the Company has agreed to comply with the following financial covenants (i) consolidated tangible net worth (excluding the effect of the Private Placement and the Debt Conversion) not to be less than \$100.0 million as at 31 May 2004, 31 August 2004 and 28 February 2005 and not less than \$85.0 million as at 30 November 2004, (ii) subject to certain exceptions, the ratio of consolidated debt to consolidated tangible net worth not to exceed 1.25:1 at the end of each of its fiscal quarters through the fiscal quarter ending 30 November 2004, and (iii), subject to certain exceptions, consolidated debt to EBITDA not to exceed 5.0:1. To the extent that these covenants are breached, this will also constitute an event of default under the Existing Credit Facility agreements. The Company has also agreed to re-set the financial covenants referred to in the Intercreditor Deed for fiscal year 2005, beginning on 1 December 2004, at levels approved by an instructing group. Failure to comply with the reset financial covenants by 28 February 2005 will cause the \$440 million credit facility and the \$55/45 million credit/guarantee facility to be placed on demand and, in the case of the guarantee facility under the \$55/45 million credit/guarantee facility, cash collateralised. In addition, the Company has agreed that (i) 100% of the net cash proceeds of the sale of any ship secured under the \$440 million credit facility and the \$55/45 million credit/guarantee facility shall be applied in prepayment of the relevant facility and failure to do so will result in an event of default thereunder and (ii) the \$440 million credit facility shall be prepaid by certain amounts as stated in the Intercreditor Deed. If such prepayments do not occur an event of default will arise thereunder. Also, in relation to the acceleration of indebtedness events of default under the \$55/45 million credit/guarantee facility and the \$44 million guarantee facility, SNSA and SNTG have been specifically excluded from the definition of 'Security Parties' under these facilities so as to prevent any cross-default in respect of these two entities from triggering these events of default.

Further, the override provisions require that the Company appoint two independent non-executive Directors to the Company's Board and require that the Company comply with the relevant listing requirements of the Nasdaq National Market applicable to foreign private issuers that are not 'controlled companies' on an accelerated basis. In addition, the assignment and transfer provisions have been standardised across the existing Credit Facility Agreements and the Company has agreed to provide a risk management report and a contract report to the finance parties under the \$440 million credit facility. Further, in the event that the \$440 million credit facility and the \$55/45 million credit/guarantee facility are not prepaid by \$90 million by 1 December 2004, then the interest rate margin applicable to these facilities will increase retrospectively. The Intercreditor Deed also contains certain pre-consents from the Company's creditors in relation to future bonding finance parties sharing in certain assets secured in favour of the Company's creditors subject to there being no material impairment to such creditor's rights.

Notes to the consolidated financial statements continued

The Intercreditor Deed also contains customary provisions regulating the priority and the enforcement of security interests between those of the Company's creditors that are a party to the Intercreditor Deed. In addition, the Intercreditor Deed provides provision for the application of the proceeds of any enforcement over the assets secured in favour of the Company's creditors towards the payment and discharge of indebtedness under the Existing Credit Facility Agreements and the New Bonding Facility.

In addition the Company has paid or is committed to pay the following amounts outstanding under the \$440 million credit facility:

- i. \$30 million upon receipt of the proceeds of the Private Placement of 13 February 2004.
- ii. \$15 million out of the proceeds to be received from any settlement of the dispute relating to the Duke Hubline project.
- iii. One-half of the gross cash proceeds from the Subsequent Issue, which is scheduled for the second quarter of fiscal year 2004.
- iv. \$20 million on or before 1 December 2004, provided that the budget approved by the lenders in respect of fiscal year 2005 indicates that there is sufficient financial capacity to make such payment.

The Company has taken a number of additional steps to improve its financial position, liquidity and gearing. Since 30 November 2003 the Company has:

- i. Issued and sold, on 13 February 2004, 45,500,000 million Common Shares, raising gross proceeds of \$100.1 million (\$93.5 million net of expenses) through the Private Placement.
- ii. Converted the outstanding 34,000,000 Class B Shares into 17,000,000 Common Shares on 13 February 2004 (the 'Share Conversion').
- iii. SNSA converted the \$50 million Subordinated Note (see Note 15) into 22,727,272 Common Shares, reduced outstanding debt by \$50.0 million.
- iv. Obtained shareholder approval to raise approximately \$52.8 million in gross proceeds through the issuing of 24,000,000 Common Shares in the Subsequent Issue, expected to be completed in May 2004 (the 'Subsequent Issue').
- v. Reduced its debt by prepayments under the \$440 million credit facility and other credit facilities. As of 31 March 2004, the Company had prepaid its debt by approximately \$55.0 million since 30 November 2003.
- vi. In addition to the foregoing, the Company has disposed of certain assets and businesses as part of the Company's divestment programme. See Note 8 Assets held for sale.

The Company intends to use the net proceeds from the Private Placement as follows: (i) to provide cash collateral for the New Bonding Facility, (ii) working capital, (iii) prepayment of certain amounts under the \$440 million credit facility and scheduled repayments of existing debt obligations, (iv) capital expenditures, and (v) general corporate purposes. Of the proceeds from the Subsequent Issue, one half will be used for prepayments under the \$440 million credit facility.

- ▶ On 18 February 2004, the Company announced the award of the Greater Plutonio contract. The contract was awarded by British Petroleum (BP) to a consortium the Company formed with Technip, and represents the largest contract to be awarded to the Company. The total value of the contract was \$730 million, of which the Company's share is approximately \$550 million. The Greater Plutonio project involves the engineering, procurement, fabrication, and installation of umbilicals, risers and flowlines for the development of Bloc 18 offshore Angola (AFMED region). Many of the construction activities will take place at depths of 1,200 to 1,500 metres. It is expected that activities on this project will continue through 2007.

- ▶ On 20 February 2004, the Company and its Sonastolt joint venture sold to Oceaneering International Inc. their ROV Drill Support Business, consisting of a fleet of 44 ROVs and certain ancillary equipment, together with related contracts and employees, for approximately \$48 million. The sale realised approximately \$28 million in cash to the Company after eliminating the joint venture partners' interests and transaction costs. Further cash was received from the joint venture in the form of dividends and loan repayments.
- ▶ On 26 February 2004, the Company reached a final settlement agreement with Algonquin Gas Transmission Company relating to the claims for payment of unpaid invoices and Variation Orders on the Duke Hubline project. The effect of this settlement has been included in the results for fiscal year 2003 and should, hence, not impact on the results for fiscal year 2004. Further details are provided in Note 25.
- ▶ On 18 March 2004 the Company announced that a settlement had been reached with Technip regarding the patent infringement. See Note 25 Commitments and contingencies.
- ▶ On 22 March 2004 the Company announced that, in addition to the 2005 Langede Pipeline work scope awarded to the Company in November 2003, the Langede Group, with Norsk Hydro as operator, had exercised its option to award the Company the 2006 work scope for the Langede Pipeline, which on completion, will be the longest offshore pipeline in the world. The Company will be responsible for the installation of 362 kilometres of 42-inch diameter pipeline. The two-year programme is valued at approximately \$250 million and will keep the *LB 200* pipelay barge occupied throughout 2005 and 2006.
- ▶ In March 2004 the Company significantly increased its estimate of the range of costs to complete two major West African projects, Bonga and Sanha Bomboco, due to unexpected delays in completing offshore work and events outside the normal exposure and risk aspects of the contracts. The Company expects to recover a substantial portion of the increased expenditure through agreed variation orders.
- ▶ On 20 April 2004, SNSA completed a previously announced debt for equity swap, under which SNTG subscribed for an additional 22,727,272 Common Shares in consideration for the cancellation of \$50 million of subordinated loans to the Company. Following this operation, the number of Common Shares in issue was 161,489,487.

Corporate information and stock trading history

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Common Shares – Nasdaq (US dollars) Ticker SOSA

		Qtr1	Qtr2	Qtr3	Qtr4
2003	High	1.88	2.08	2.66	2.75
	Low	1.12	1.11	1.32	1.45

Common Shares – Oslo Stock Exchange (Norwegian kroner) Ticker STO

		Qtr1	Qtr2	Qtr3	Qtr4
2003	High	12.20	13.30	20.00	20.30
	Low	9.91	7.85	8.70	10.00

Shareholder information

Stock listings

Common Shares – on Oslo Stock Exchange under symbol STO and on Nasdaq as an American Depositary Receipt ('ADR') under symbol SOSA.

Shares outstanding (as of 22 April 2004)

Common Shares 160,610,366

This figure excludes 879,121 Common Shares held as ADRs by a subsidiary of Stolt Offshore S.A. in Treasury, as these are considered issued but not outstanding.

Country of incorporation

Luxembourg

Annual General Meeting

27 May 2004 at 3.00 pm
Services Généraux de Gestion S.A.
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www.citibank.com/adr

Auditors

Deloitte & Touche LLP
Glasgow
United Kingdom

Dividends

The Company currently intends to retain any earnings for the future operation and growth of the business. The Board of Directors will review this policy from time to time in light of the Company's earnings, financial condition, prospects, tax consideration and foreign exchange rates. The Company will pay dividends, if any, in US dollars.

