Great Lakes Dredge & Dock CORP
Form 10-Q
November 12, 2008
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UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

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

For the quarterly period ended September 30, 2008

OR

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

For the transition period from to

Commission file number:

001-33225

Great Lakes Dredge & Dock Corporation

(Exact name of registrant as specified in its charter)

Delaware	**20-5336063**
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)

2122 York Road, Oak Brook, IL	**60523**
(Address of principal executive offices)	(Zip Code)

(630) 574-3000

(Registrant s telephone number, including area code)

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

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

Large Accelerated Filer o	Accelerated Filer x	Non-Accelerated Filer o (Do not check if a smaller reporting company)	Smaller reporting company o

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

As of November 7, 2008, 58,478,829 shares of the Registrant s Common Stock, par value $.0001 per share, were outstanding.

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Great Lakes Dredge & Dock Corporation and Subsidiaries

Quarterly Report Pursuant to Section 13 or 15(d) of the

Securities Exchange Act of 1934

For the Quarterly Period ended September 30, 2008

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PART I Financial Information

GREAT LAKES DREDGE & DOCK CORPORATION AND SUBSIDIARIES

Condensed Consolidated Balance Sheets

(Unaudited)

(in thousands, except share and per share amounts)

	September 30 2008	December 31 2007
ASSETS		
CURRENT ASSETS:		
Cash and cash equivalents	$ 11,523	$ 8,239
Accounts receivable net	98,963	115,709
Contract revenues in excess of billings	26,510	13,828
Inventories	30,776	29,157
Prepaid expenses	5,282	6,710
Other current assets	29,089	16,980
Total current assets	202,143	190,623
PROPERTY AND EQUIPMENT Net	309,040	296,721
GOODWILL	97,799	96,225
OTHER INTANGIBLE ASSETS Net	1,063	1,006
INVENTORIES Noncurrent	35,213	21,315
INVESTMENTS IN JOINT VENTURES	9,339	9,589
OTHER	7,627	8,883
TOTAL	$ 662,224	$ 624,362
LIABILITIES AND STOCKHOLDERS EQUITY		
CURRENT LIABILITIES:		
Accounts payable	$ 78,524	$ 77,552
Accrued expenses	25,143	24,067
Billings in excess of contract revenues	7,672	5,437
Current portion of equipment debt	1,551	1,273
Total current liabilities	112,890	108,329
REVOLVING CREDIT FACILITY	49,710	21,500
7 3/4% SENIOR SUBORDINATED NOTES	175,000	175,000
DEFERRED INCOME TAXES	84,493	79,836
OTHER	10,627	9,301
Total liabilities	432,720	393,966
COMMITMENTS AND CONTINGENCIES		

MINORITY INTEREST		468		2,061
STOCKHOLDERS EQUITY				
Common stock $.0001 par value; 90,000,000 authorized, 58,478,829 and 58,459,824 shares issued and outstanding at September 30, 2008 and December 31, 2007, respectively.		6		6
Additional paid-in capital		262,647		260,669
Accumulated deficit		(32,645)		(32,810)
Accumulated other comprehensive income (loss)		(972)		470
Total stockholders equity		229,036		228,335
TOTAL	$	662,224	$	624,362

See notes to the unaudited condensed consolidated financial statements.

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Great Lakes Dredge & Dock Corporation and Subsidiaries

Condensed Consolidated Statements of Operations

(Unaudited)

(in thousands, except per share data)

	Three Months Ended September 30, 2008	Three Months Ended September 30, 2007	Nine Months Ended September 30, 2008	Nine Months Ended September 30, 2007
Contract revenues	$ 142,809	$ 116,460	$ 423,852	$ 358,817
Costs of contract revenues	125,193	103,114	372,656	313,594
Gross profit	17,616	13,346	51,196	45,223
General and administrative expenses	10,971	9,554	32,373	26,834
Amortization of intangible assets	177	66	308	197
Operating income	6,468	3,726	18,515	18,192
Interest expense, net	(4,301)	(3,375)	(12,853)	(14,217)
Equity in earnings of joint ventures	61	790	250	1,689
Minority interest		22	(231)	3
Income before income taxes	2,228	1,163	5,681	5,667
Income tax provision	(827)	(519)	(2,530)	(2,380)
Net income	$ 1,401	$ 644	$ 3,151	$ 3,287
Basic earnings per share	$ 0.02	$ 0.01	$ 0.05	$ 0.07
Basic weighted average shares	58,473	56,265	58,466	45,694
Diluted earnings per share	$ 0.02	$ 0.01	$ 0.05	$ 0.07
Diluted weighted average shares	58,499	57,190	58,476	50,107

See notes to unaudited condensed consolidated financial statements.

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Great Lakes Dredge & Dock Corporation and Subsidiaries

Condensed Consolidated Statements of Cash Flows

(Unaudited)

(in thousands, except per share amounts)

	Nine Months Ended September 30, 2008	2007
Operating Activities		
Net income	$ 3,151	$ 3,287
Adjustments to reconcile net income to net cash flows from operating activities:		
Depreciation and amortization	21,256	20,141
Earnings of joint ventures	(250)	(1,689)
Distribution from equity joint ventures	500	1,400
Minority interest	231	(3)
Deferred income taxes	4,180	829
Gain on dispositions of property and equipment	(525)	(556)
Amortization of deferred financing fees	1,464	2,185
Stock based compensation expense	302	
Changes in assets and liabilities:		
Accounts receivable	16,746	(12,245)
Contract revenues in excess of billings	(12,682)	2,201
Inventories	(15,517)	(13,887)
Prepaid expenses and other current assets	(8,789)	(4,204)
Accounts payable and accrued expenses	(2,367)	2,861
Billings in excess of contract revenues	2,235	(10,553)
Other noncurrent assets and liabilities	1,059	308
Net cash flows from operating activities	10,994	(9,925)
Investing Activities		
Purchases of property and equipment	(32,906)	(77,175)
Dispositions of property and equipment	799	28,378
Repayment of loan to related party		1,703
Purchase of minority interest	(5)	
Changes to restricted cash	787	
Net cash flows used in investing activities	(31,325)	(47,094)
Financing Activities		
Repayments of long-term debt	(1,469)	(19,685)
Borrowings under revolving loans, net of repayments	28,210	14,500
Cash proceeds from conversion of warrants		91,768
Financing fees		(2,101)
Dividends	(2,987)	
Repayment of capital lease debt	(139)	(1,393)
Net cash flows from financing activities	23,615	83,089
Net change in cash and equivalents	3,284	26,070
Cash and equivalents at beginning of period	8,239	3,640
Cash and equivalents at end of period	$ 11,523	$ 29,710
Supplemental Cash Flow Information		

Cash paid for interest	$	8,328	$	8,891
Cash paid for income taxes	$	4,724	$	6,757
Non-cash Investing Activity				
Capital expenditures in accounts payable	$	3,793	$	2,546

See notes to unaudited condensed consolidated financial statements.

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GREAT LAKES DREDGE & DOCK CORPORATION AND SUBSIDIARIES

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited)

(in thousands, except per share amounts)

1. Basis of presentation

The accompanying unaudited condensed consolidated financial statements have been prepared in accordance with accounting principles generally accepted in the United States of America (GAAP). for interim financial information. Accordingly, these financial statements do not include all the information in the notes required by generally accepted accounting principles for complete financial statements. In the opinion of management, the unaudited condensed consolidated financial statements include all adjustments (consisting of normal recurring adjustments) considered necessary for a fair presentation of the financial position, results of operations and cash flows as of and for the dates presented. The unaudited condensed consolidated financial statements and notes herein should be read in conjunction with the audited consolidated financial statements of Great Lakes Dredge & Dock Corporation and Subsidiaries (the Company or Great Lakes) and the notes thereto, included in the Company s Annual Report filed on Form 10-K for the year ended December 31, 2007.

The Company s cost structure includes significant annual equipment-related costs, principally depreciation, maintenance, insurance and long-term equipment rentals, which have averaged approximately 22% to 25% of total costs of contract revenues over the last three years. During the year, both equipment utilization and the timing of these cost expenditures fluctuate significantly. Accordingly, the Company allocates these equipment costs to interim periods in proportion to revenues recognized over the year, to better match revenues and expenses. Specifically, at each interim reporting date, the Company compares the actual revenues earned to date on its dredging contracts to expected annual revenues and recognizes equipment costs on the same proportionate basis. In the fourth quarter, any over or under allocated equipment costs are recognized such that the expense for the year equals the actual equipment costs incurred during the year. As a result of this methodology, the recorded expense in any interim period may be higher or lower than the actual equipment costs incurred in that interim period.

The condensed consolidated results of operations for the interim periods presented herein are not necessarily indicative of the results to be expected for the full year.

2. Comprehensive income

Total comprehensive income (loss) is comprised of the Company s net income (loss) and net unrealized gains (losses) on cash flow hedges as discussed in Note 4 below. Total comprehensive income (loss) for the three months ended September 30, 2008 and 2007 was ($2,338) and $781, respectively. Total comprehensive income for the nine months ended September 30, 2008 and 2007 was $1,709 and $4,948, respectively.

3. Earnings per share

Basic earnings (loss) per share is computed by dividing net income (loss) available to common stockholders by the weighted average number of common shares outstanding during the reporting period. Diluted earnings (loss) per share is computed similar to basic earnings (loss) per share except that it reflects the potential dilution that could occur if dilutive securities or other obligations to issue common stock were exercised or converted into common stock. Options to purchase 356,744 shares of common stock were outstanding during the three month and nine month period ended September 30, 2008 but were not included in the computation of earnings per share (EPS) because the options were determined to be anti-dilutive. The potentially dilutive impact of 145,736 issued restricted stock units (RSUs) is included in the calculation of diluted earnings per share based on the application of the treasury stock method. At January 1, 2007, warrants to purchase 18.4 millions shares of the Company s common stock were outstanding and exercisable. By December 31, 2007 all of these warrants had been exercised or redeemed. The potentially dilutive impact of shares that were issuable pursuant to the exercise of these warrants prior to the redemption date is included in the calculation of diluted earnings per share at September 30, 2007 based on the application of the treasury stock method. The computations for basic and diluted earnings per share from continuing operations are as follows:

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	Three Months Ended September 30, 2008		Three Months Ended September 30, 2007		Nine Months Ended September 30, 2008		Nine Months Ended September 30, 2007	
Numerator:								
Net income - numerator for basic and diluted earnings per share	$	1,401	$	644	$	3,151	$	3,287
Denominator:								
Denominator for basic earnings per share - weighted average shares outstanding		58,473		56,265		58,466		45,694
Dilutive impact of warrants to purchase common stock				925				4,413
Dilutive impact of restricted stock units issued		26				10		
Denominator for diluted earnings per share adjusted weighted average shares		58,499		57,190		58,476		50,107
Basic earnings per share	$	0.02	$	0.01	$	0.05	$	0.07
Diluted earnings per share	$	0.02	$	0.01	$	0.05	$	0.07

4. Fair value measurements

In September 2006, the Financial Accounting Standards Board (FASB) issued Statement of Financial Accounting Standards (SFAS) No. 157 Fair Value Measurements (SFAS 157). SFAS 157 introduces a framework for measuring fair value and expands required disclosure about fair value measurements of assets and liabilities. SFAS 157 for financial assets and liabilities was effective for fiscal years beginning after November 15, 2007. The Company adopted the standard for those assets and liabilities as of January 1, 2008 and the adoption did not have a material effect on the Corporation s consolidated financial condition, results of operations or cash flows.

SFAS 157 defines fair value as the exchange price that would be received for an asset or paid to transfer a liability (an exit price) in the principal or most advantageous market for the asset or liability in an orderly transaction between market participants on the measurement date. SFAS 157 also establishes a fair value hierarchy which requires an entity to maximize the use of observable inputs and minimize the use of unobservable inputs when measuring fair value. The standard describes three levels of inputs that may be used to measure fair value:

Level 1 Quoted prices in active markets for identical assets or liabilities.

Level 2 Observable inputs other than Level 1 prices such as quoted prices for similar assets or liabilities; quoted prices in markets that are not active; or other inputs that are observable or can be corroborated by observable market data for substantially the full term of the assets or liabilities.

Level 3 Unobservable inputs that are supported by little or no market activity and that are significant to the fair value of the assets or liabilities.

The Company utilizes the market approach to measure fair value for its financial assets and liabilities. The market approach uses prices and other relevant information generated by market transactions involving identical or comparable assets or liabilities. At September 30, 2008, the

Company held certain derivative contracts, which the Company s uses to manage commodity price and interest rate risk. Such instruments are not used for trading purposes. The fair value of these derivative contracts is summarized as follows:

		Fair Value Measurements at Reporting Date Using		
Description	**September 30, 2008**	**Quoted Prices in Active Markets for Identical Assets (Level 1)**	**Significant Other Observable Inputs (Level 2)**	**Significant Unobservable Inputs (Level 3)**
Fuel hedge contracts	$ (1,617)	$	$ (1,617)	$
Interest rate swap contracts	40			40
Total assets measured at fair value	$ (1,577)	$	$ (1,617)	$ 40

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Fuel Hedge Contracts

As of September 30, 2008, the Company was party to various swap arrangements to hedge the price of a portion of its diesel fuel purchase requirements for work in its backlog to be performed through September 2009. As of September 30, 2008, there were 5.6 million gallons remaining on these contracts. Under these agreements, the Company will pay fixed prices ranging from $2.45 to $4.08 per gallon. At September 30, 2008 and December 31, 2007, the fair value asset (liability) on these contracts was estimated to be ($1,617) and $775, respectively, and is recorded in other current assets (accrued expenses). Ineffectiveness related to these fuel hedge arrangements was determined to be immaterial. The remaining gains included in accumulated other comprehensive income at September 30, 2008 will be reclassified into earnings over the next twelve months, corresponding to the period during which the hedged fuel is expected to be utilized. The fair values of fuel hedges are corroborated using inputs that are readily observable in public markets therefore, the Company has categorized these fuel hedges as Level 2.

Interest Rate Swap Contracts

In February 2004, the Company entered into an interest rate swap arrangement, which is effective through December 15, 2013, to swap a notional amount of $50 million from a fixed rate of 7.75% to a floating LIBOR-based rate in order to manage the interest rate paid with respect to the Company s 7.75% senior subordinated debt. The interest rate swaps contain a provision whereby the counterparties have the right to terminate the contracts at any time after December 15, 2008. The current portion of the fair value asset of the swap at September 30, 2008 and December 31, 2007 was $1,026 and $351, respectively, and is recorded in current assets. The long term portion of the fair value liability of the swap at September 30, 2008 and December 31, 2007 was $986 and $717, respectively, and is recorded in other long term liabilities. The swap is not accounted for as a hedge; therefore, the changes in fair value are recorded as adjustments to interest expense in each reporting period.

The Company verifies the fair value of the interest rate swaps using a quantitative model that contains both observable and unobservable inputs. The unobservable inputs relate primarily to the termination provision of the interest rate swap contracts. The Company believes that these unobservable inputs are significant and accordingly the Company has categorized these interest rate swap contracts as Level 3.

		Fair Value Measurements Using Significant Unobservable Inputs (Level 3) Interest Rate Swap
Balance at January 1, 2008	$	(365)
Transfers to Level 3		
Total gains or (losses) (realized or unrealized):		
Included in earnings		(405)
Included in other comprehensive income		
Purchases and settlements		
Balance at September 30, 2008	$	40

The carrying values of other financial instruments included in current assets and current liabilities approximate fair values due to the short-term maturities of these instruments. The carrying value of the Company s variable rate debt (primarily bank debt) approximates fair values, based on prevailing market rates. The fair value of the Company s $175,000 of 7.75% senior subordinated notes was $136,500 at September 30, 2008, based on indicative market prices.

5. Share-based compensation

The Company s 2007 Long-Term Incentive Plan (the Incentive Plan), as approved by the Board of Directors on September 18, 2007, permits the grant of stock options, stock appreciation rights, restricted stock and RSUs to its employees for up to 5.8 million shares of common stock. The Company believes that such awards better align the interests of its employees with those of its shareholders and attract and retain the best possible talent.

On May 20, 2008, the Company granted non-qualified stock options (NQSOs) and RSUs to certain employees pursuant to the plan. In accordance with SFAS 123R, *Share-Based Payment,* the compensation cost charged to income related to these stock-based compensation arrangements was $126 and $190 for the three months and nine months ended September 30, 2008.

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Non-qualified stock options

The NQSO awards were granted with an exercise price equal to the market price of the Company s common stock at the date of grant. The option awards generally vest in three equal annual installments commencing on the first anniversary of the grant date and have 10-year exercise periods.

The fair value of the NQSOs is determined at the grant date using a Black-Scholes option pricing model, which requires the Company to make several assumptions. The risk-free interest rate is based on the U.S. Treasury yield curve in effect for the expected term of the option at the time of grant. The annual dividend yield on our common stock is based on our estimate of future dividends during the expected term of the NQSOs. The expected life of the NQSOs was determined based upon a simplified assumption that the NQSOs will be exercised evenly from vesting to expiration under the guidance of Staff Accounting Bulletin No. 110, Topic 14, Share-Based Payment, as the Company does not have sufficient historical exercise data to provide a reasonable basis upon which to estimate the expected life.

The volatility assumptions were based upon historical volatilities of comparable companies whose shares are traded using daily stock price returns equivalent to the expected term of the option. Due to a lack of sufficient historical information (the Company s shares were not publicly traded until December of 2006) historical volatility data for the Company was not considered in determining expected volatility. The Company also considered implied volatility data for comparable companies, using current exchange traded options. There is not an active market for options on the Company s common stock and, as such, implied volatility for the Company s stock was not considered. Additionally, the Company s general policy is to issue new shares of registered common stock to satisfy stock option exercises or grants of restricted stock.

The weighted-average grant-date fair value of options granted during the nine months ended September 30, 2008 was $2.24. The fair value of each option was estimated using the following assumptions:

	2008
Expected volatility	45.0%
Expected dividends	1.3%
Expected term (in years)	5.5 - 6.5
Risk free rate	3.0%

A summary of option activity under the Incentive Plan as of September 30, 2008, and changes during the nine months then ended is presented below:

Options	**Shares**	**Exercise Price**	**Weighted-Average Remaining Contract Term (yrs)**	**Aggregate Intrinsic Value ($000 s)**

Outstanding as of January 1, 2008						
Granted	356,774	$	5.41			
Exercised						
Forfeited or Expired						
Outstanding as of September 30, 2008	356,774	$	5.41	5.6	$	321
Vested at September 30, 2008						
Vested or expected to vest at September 30, 2008	334,038					

There were no NQSOs exercisable as of September 30, 2008, and therefore no NQSOs were exercised during the nine months ended September 30, 2008.

Restricted stock units

RSUs generally vest in one installment on the third anniversary of the grant date. A summary of the status of the Company s non-vested RSUs as of September 30, 2008, and changes during the nine months ended September 30, 2008 is presented below:

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Nonvested Restricted Stock Units	Shares	Grant Date Price	Weighted-Average Grant-Date Fair Value
Non-vested as of January 1, 2008			
Granted	145,736	$ 5.41	$ 5.41
Vested			
Forfeited			
Outstanding as of September 30, 2008	145,736	$ 5.41	$ 5.41
Vested at September 30, 2008			
Vested or expected to vest at September 30, 2008	125,747		

The fair value of RSUs was based upon the Company s stock price on the date of grant. RSUs generally vest over three years.

As of September 30, 2008, there was $1.2 million of total unrecognized compensation cost related to non-vested NQSOs and RSUs granted under the Plan. That cost is expected to be recognized over a weighted-average period of 1.4 years.

Director Compensation

As of May 20, 2008, the Company uses a combination of cash and stock-based compensation to attract and retain qualified candidates to serve on our Board of Directors. Compensation is paid to non-employee directors. Stock-based compensation is paid pursuant to the Incentive Plan and was granted by the Compensation Committee. For the 2008 fiscal year each non-employee director will receive $60,000, 50% in cash and 50% payable in unrestricted shares of the Company s common stock. Directors who are not outside directors receive no additional compensation for services as members of the Board or any of its committees. All of our directors in 2008 to date were outside directors other than Douglas B. Mackie. In addition, Thomas Souleles and Douglas Grissom waived their right to director s compensation for the 2008 fiscal year. During the nine months ended September 30, 2008 19,005 shares of the Company s common stock were issued to non-employee directors.

6. Accounts receivable

Accounts receivable at September 30, 2008 and December 31, 2007 are as follows:

	September 30 2008	December 31 2007
Completed contracts	$ 17,821	$ 28,048
Contracts in progress	58,422	68,197
Retainage	23,970	20,953
	100,213	117,198
Allowance for doubtful accounts	(1,250)	(1,489)
Total accounts receivable	$ 98,963	$ 115,709

7. Contracts in progress

The components of contracts in progress at September 30, 2008 and December 31, 2007 are as follows:

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	September 30 2008	December 31 2007
Costs and earnings in excess of billings:		
Costs and earnings for contracts in progress	$ 392,769	$ 216,701
Amounts billed	(366,603)	(203,347)
Costs and earnings in excess of billings for contracts in progress	26,166	13,354
Costs and earnings in excess of billings for completed contracts	344	474
Total contract revenues in excess of billings	$ 26,510	$ 13,828
Prepaid contract costs (included in prepaid expenses)	$ 747	$ 2,618
Billings in excess of costs and earnings:		
Amounts billed	$ (79,097)	$ (61,067)
Costs and earnings for contracts in progress	71,425	55,630
Total billings in excess of contract revenues	$ (7,672)	$ (5,437)

8. Intangible assets

The net book value of intangible assets is as follows:

As of September 30, 2008:	Cost	Acquisitions	Accumulated Amortization	Net
Demolition segment customer relationships	1,093	207	833	467
Demolition Backlog		158	99	59
Software and databases	1,209		672	537
	$ 2,302	$ 365	$ 1,604	$ 1,063

As of December 31, 2007	Cost	Acquisitions	Accumulated Amortization	Net
Demolition segment customer relationships	1,093		730	363
Software and databases	1,209		566	643
Total	$ 2,302	$	$ 1,296	$ 1,006

On April 30, 2008 the Company acquired the remaining 15% interest in North American Site Developers, Inc. (NASDI Inc) resulting in the recognition of additional intangible assets (See Note 15).

9. Investment in joint ventures

The Company has a 50% ownership interest in Amboy Aggregates (Amboy), whose primary business is the dredge mining and sale of fine aggregate. The Company accounts for its investment in Amboy using the equity method. The following table includes Amboy s summarized financial information for the periods presented.

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	Three Months Ended September 30, 2008		Three Months Ended September 30, 2007		Nine Months Ended September 30, 2008		Nine Months Ended September 30, 2007	
Revenue	$	5,103	$	6,778	$	15,739	$	18,019
Gross profit	$	500	$	1,861	$	1,682	$	4,680
Net income	$	122	$	1,580	$	500	$	3,378
Great Lakes 50% share	$	61	$	790	$	250	$	1,689

Amboy has a revolving loan with a bank for up to $3,000 which contains certain restrictive covenants, including limitations on the amount of distributions to its joint venture partners. The Company does not guarantee any of the outstanding borrowings and accrued interest under the bank agreement. It is the intent of the joint venture partners to periodically distribute Amboy s earnings, to the extent allowed by Amboy s bank agreement. For the nine months ended September 30, 2008 and 2007, the Company received distributions from Amboy totaling $500 and $1,400, respectively.

The Company and its Amboy joint venture partner also each own a 50% interest in land, which is adjacent to the Amboy property and is used in connection with the Amboy operations. The Company s recorded share of the property is $1,047 and is reflected in investments in joint ventures.

10. Accrued expenses

Accrued expenses at September 30, 2008 and December 31, 2007 are as follows:

	September 30 2008		December 31 2007	
Payroll and employee benefits	$	9,077	$	10,778
Insurance		7,425		6,553
Interest		4,416		950
Income and other taxes		1,043		4,690
Fuel hedge liability		1,617		
Other		1,565		1,096
Total accrued expenses	$	25,143	$	24,067

11. Income taxes

The Company provides for income taxes in interim periods based on an estimated annual effective tax rate adjusted for items that are discrete to each period. Significant items impacting the effective tax rate at September 30, 2008 and 2007 include amounts associated with FASB Interpretation No. 48, Accounting for Uncertainties in Income Taxes (FIN 48). Effective January 1, 2007, Great Lakes adopted FIN 48, which requires a company to evaluate whether the tax position taken by a company will more likely than not be sustained upon examination by the appropriate taxing authority. It also provides guidance on how a company should measure the amount of benefit that the company is to recognize in its financial statements.

The uncertain tax positions of the Company as of September 30, 2008 and December 31, 2007, totaled $1,940 and $1,867, respectively. At September 30, 2008 and December 31, 2007, approximately $646 and $599, respectively, of the total gross unrecognized tax benefits represent the amount that, if recognized, would affect the effective income tax rate in future periods. The Company does not anticipate the total amount of unrecognized tax benefits will significantly change over the next twelve months. The Company s continuing practice is to record interest and penalties related to income tax matters in income tax expense. Such interest and penalties are not significant for the three and nine months ended September 30, 2008 and 2007.

The Company files income tax returns at the U.S. federal level and in various state and foreign jurisdictions. U.S. federal income tax years prior to 2004 are closed and no longer subject to examination. With few exceptions, the statute of limitations in state taxing jurisdictions in which the Company operates has expired for all years prior to 2004. The Company is currently undergoing an examination by the State of Illinois for the 2005 and 2004 tax years. An Internal Revenue Service examination of the 2005 tax year is in process as of September 30, 2008. In foreign jurisdictions in which the Company operates, all significant years prior to 2004 are closed and are no longer subject to examination.

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While the Company does not expect material adjustments will result from such examinations, it is possible that federal, state or foreign authorities may challenge tax positions taken by the Company, and seek payment for additional taxes and penalties. While no assurance can be given, the Company does not believe the results of these examinations will have a material effect on its financial position, results of operations, or cash flows.

12. Segment information

The Company operates in two reportable segments: dredging and demolition. The Company s financial reporting systems present various data for management to run the business, including profit and loss statements prepared according to the segments presented. Management uses operating income to evaluate performance between the two segments. Segment information for the periods presented is as follows:

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2008	2007	2008	2007
Dredging				
Contract revenues	$ 123,816	$ 93,707	$ 334,515	$ 310,989
Operating income	6,603	3,162	13,635	15,992
Demolition				
Contract revenues	$ 18,993	$ 22,753	$ 89,337	$ 47,828
Operating income	(135)	564	4,880	2,200
Total				
Contract revenues	$ 142,809	$ 116,460	$ 423,852	$ 358,817
Operating income	6,468	3,726	18,515	18,192

In addition, foreign dredging revenue of $50,837 and $118,959 for the three and nine months ended September 30, 2008, respectively, was primarily attributable to work done in Bahrain. The majority of the Company s long-lived assets are marine vessels and related equipment. At any point in time, the Company may employ certain assets outside of the U.S., as needed, to perform work on the Company s foreign projects.

13. Commitments and contingencies

Commercial commitments

Great Lakes has a secured $155,000 bank credit facility, which matures in June 2012. This credit facility provides for revolving loans, letters of credit and swingline loans. As of September 30, 2008, Great Lakes had $49,709 of revolver borrowings and $26,333 of letters of credit outstanding under this facility.

During the three-months ended September 30, 2008, one of the lenders supporting the Company s $155,000 revolving credit facility defaulted under the company s credit agreement. This lender is responsible for $10,000 or 6.5% of the overall line of credit. While the default of this lender may reduce overall availability, the Company continues to have adequate capacity under the revolving credit agreement to fund its operations, provide working capital, meet debt service requirements and finance capital expenditures. Accordingly, the Company does not believe that the loss of this lender will have a material effect on its financial position, result of operations or cash flows.

Great Lakes obtains its performance, bid and payment bonds through a bonding agreement with a surety company. The bonds issued under the bonding agreement are customarily required for dredging and marine construction projects, as well as demolition projects. As of September 30, 2008, Great Lakes had outstanding bonds valued at $402,989; however, the revenue value remaining in backlog related to these projects totaled approximately $248,805.

Great Lakes has a $24,000 international letter of credit facility that it uses for the performance and advance payment guarantees on the Company s foreign contracts. As of September 30, 2008, Great Lakes had $16,341 of letters of credit outstanding under this facility.

Great Lakes has also issued $175,000 of senior subordinated notes, which mature in December 2013.

Great Lakes obligations under its bank credit facility and bonding agreement are secured by liens on a substantial portion of Great Lakes assets. As of December 31, 2007, the net book value of the Company s operating equipment securing the Company s obligations under it bank credit facility and bonding agreement was approximately $77,000 and $83,000, respectively. Great Lakes obligations under its international letter of credit facility are secured by the Company s foreign accounts receivable. Great Lakes obligations under its senior subordinated notes are unsecured.

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Great Lakes bank credit facility, bonding agreement and senior subordinated notes contain various restrictive covenants, including a limitation on dividends, limitations on redemption and repurchases of capital stock, limitations on the incurrence of indebtedness and requirements to maintain certain financial covenants.

Certain foreign projects performed by the Company have warranty periods, typically spanning no more than one to three years beyond project completion, whereby the Company retains responsibility to maintain the project site to certain specifications during the warranty period. Generally, any potential liability of the Company is mitigated by insurance, shared responsibilities with consortium partners, and/or recourse to owner-provided specifications.

As is customary with negotiated contracts and modifications or claims to competitively-bid contracts with the federal government, the government has the right to audit the books and records of the Company to ensure compliance with such contracts, modifications or claims and the applicable federal laws. The government has the ability to seek a price adjustment based on the results of such audit. Any such audits have not had and are not expected to have a material impact on the financial position, operations or cash flows of the Company.

In the ordinary course of business, the Company negotiates contract related claims for additional compensation. These amounts are not recognized in contract revenues until such claims are settled. During September 2008, the Company came to agreement with a customer on additional compensation due to the Company related to its performance of an ongoing dredging project. This agreement provides for additional revenue of approximately $13,300 over the duration of the contract. As a result of percent complete accounting, the Company recorded an incremental $6,000 in contract revenue as of September 30, 2008 related to work performed on this contract from the fourth quarter of 2006 through September 30, 2008. Future revenue from this claim will be recorded along with the costs associated with performing this work.

Legal proceedings and other contingencies

Various legal actions, claims, assessments and other contingencies arising in the ordinary course of business are pending against Great Lakes and certain of its subsidiaries. These matters are subject to many uncertainties, and it is possible that some of these matters could ultimately be decided, resolved, or settled adversely. For a discussion of these matters, please refer to Note 18 Commitments and Contingencies reported in Great Lakes Annual Report on Form 10-K for the year ended December 31, 2007, as updated by our Quarterly Report on Form 10-Q for the quarters ended March 31, 2008 and June 30, 2008. Except as noted below, there have been no material changes or developments in these matters since December 31, 2007.

In February 2004, the Company was served with a subpoena to produce documents in connection with a federal grand jury convened in the United States District Court for the District of South Carolina. The Company believes that the grand jury was convened to investigate the United States dredging industry in connection with work performed for the U.S. Army Corps of Engineers. On September 30, 2008, the Company received notification from the Department of Justice that the investigation has been closed and there will be no further activity.

The Company s results continue to be negatively impacted from the increase in reserves related to injury claims from our hourly workforce residing in Texas. In the normal course of business, the Company is party to various personal injury lawsuits for which it maintains insurance to cover claims that arise subject to a deductible. In 2006 and 2005, there was a substantial increase in suits filed in Texas due, in large part, to two Texas law firms aggressively pursuing personal injury claims on behalf of dredging workers resident in Texas. During the first half of 2007, Maritime Jobs for Texas, a coalition of maritime employers worked to reform Texas venue law with regard to the type of personal injury suits the dredging industry has recently faced. On May 24, 2007, the Texas legislature passed a bill which removed in part certain venue rules favorable to would-be plaintiffs. As enacted, these legislative reforms could alleviate the increasing number of meritless personal injury suits facing the industry in Texas. Since the passage of this legislation, the Company has been served with one personal injury lawsuit in Texas. In addition, with the settlement of several claims throughout 2007, the inventory of claims at the end of the year was significantly less compared to the start of the year. During the third quarter of 2008, no new personal injury lawsuits related to our hourly workforce in Texas were commenced against the Company. The Company s recorded self-insurance reserves represent its best estimate of the outcomes of outstanding claims and the Company does not believe that there will be a material adverse impact to the Company s financial position or results of operations or cash flows related to outstanding claims. However, the occurrence of new claims of a similar nature is not possible to predict and, while the Company does not believe that additional claims would have a material impact on the Company s financial position, it is possible they could be material to future results of operations and cash flows in future periods.

On April 24, 2006, a class action complaint (Reed Complaint) was filed in the U.S. District Court for the Eastern District of Louisiana, on behalf of Louisiana citizens who allegedly suffered property damage from the floodwaters that flooded New Orleans and surrounding areas when Hurricane Katrina hit the area on August 29, 2005. Other plaintiffs have filed similar class action complaints, as well one mass tort (collectively with the Reed Complaints, the Katrina Claims). Great Lakes maintains $150 million in insurance coverage for the Katrina Claims. The Reed Complaint names as defendants the U.S. government, Great Lakes Dredge & Dock Company, and numerous other dredging companies, which completed dredging projects on behalf of the Army Corps of Engineers in the Mississippi River Gulf Outlet (MRGO) between 1993 and 2005. The Reed Complaint alleges that dredging of MRGO caused the destruction of the Louisiana wetlands, which had provided a natural barrier against some storms and hurricanes. The Reed Complaint alleges that this loss of natural barriers contributed to the failure of the levees as Katrina floodwaters damaged plaintiffs property. The Reed Complaint asserts claims of negligence, warranty, concealment, and violations of the Water Pollution Control Act. All these cases raise the same claims as the Reed Complaint. One dredging company has filed a cross-claim seeking contribution and indemnification. The amount of claimed damages is not stated, but is presumed to be significant. On March 9, 2007, the District Court dismissed with prejudice the Reed Complaint and one mass tort claim against Great Lakes and those plaintiffs have filed an appeal to the U.S. Court of Appeals for the Fifth Circuit (the Fifth Circuit). Briefing on the appeal is now complete, and the Fifth Circuit held oral argument on September 4, 2008. The Fifth Circuit has now taken the appeal under advisement and the parties are awaiting a ruling. In addition and as previously reported, on October 19, 2006, Great Lakes filed for exoneration or limitation of liability under the Limitation of Liability Act in the U.S. District Court for the Eastern District of Louisiana. Roughly 40,000 claims by individuals, businesses, and the State of Louisiana were filed against Great Lakes, asserting the same basis theory of liability as in the Reed Complaint and seeking damages significantly in excess of the $55 million limitation bond posted by Great Lakes. On September 7, 2007, Great Lakes filed a motion to dismiss all claims against it in the limitation proceeding. The District Court granted the motion on June 12, 2008, dismissing the limitation claims with prejudice. The claimants filed a notice of appeal in the Fifth Circuit. Briefing is expected to begin during the fourth quarter of 2008, and oral arguments are expected to take place on this appeal during the second or third quarter of 2009. Great Lakes believes that the Katrina Claims will not have a material adverse impact on its financial condition or results of operations and cash flows.

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14. Effects of recently issued accounting pronouncements

In December 2007, the FASB issued SFAS No. 141(R), *Business Combinations* (SFAS 141(R)), which replaces SFAS No. 141, *Business Combinations*. SFAS 141(R) establishes principles and requirements for how an acquirer in a business combination recognizes and measures in its financial statements the identifiable assets acquired, the liabilities assumed, and any controlling interest; recognizes and measures the goodwill acquired in the business combination or a gain from a bargain purchase; and determines what information to disclose to

enable users of the financial statements to evaluate the nature and financial effects of the business combination. FAS 141(R) is to be applied prospectively to business combinations for which the acquisition date is on or after an entity s fiscal year that begins after December 15, 2008. Great Lakes will assess the impact, if any, that SFAS 141(R) will have on the Company s consolidated financial condition, results of operations or cash flows.

In December 2007, the FASB issued SFAS No. 160, *Noncontrolling Interests in Consolidated Financial Statements an amendment of ARB No. 51* (SFAS 160). SFAS 160 requires that a noncontrolling interest in a subsidiary be reported as equity and the amount of consolidated net income specifically attributable to the noncontrolling interest be identified in the consolidated financial statements. It also calls for consistency in the manner of reporting changes in the parent s ownership interest and requires fair value measurement of any noncontrolling equity investment retained in a deconsolidation. SFAS 160 is effective for fiscal years, and interim periods within those fiscal years, beginning on or after December 15, 2008. Earlier adoption is prohibited. Adoption of SFAS 160 as of January 1, 2009 is not expected to have a material impact on the Company s consolidated financial condition, results of operations or cash flows.

In March 2008, the FASB issued Statement of Financial Accounting Standards No. 161, Disclosures about Derivative Instruments and Hedging Activities, an amendment of FASB Statement No. 133 (SFAS 161). SFAS 161 requires entities to provide greater disclosure about how and why the entity uses derivative instruments, how the instruments and related hedged items are accounted for under SFAS 133, and how the instruments and related hedged items affect the financial position, results of operations, and cash flows of the entity. SFAS 161 is effective for fiscal years beginning after November 15, 2008. The principal impact to the Company of adopting SFAS 161 will be to require the Company to expand its disclosure regarding its derivative instruments.

15. Minority interest acquisition

On April 30, 2008 the Company acquired the remaining 15% minority interest in NASDI Inc., which it did not previously own, from Christopher A. Berardi, the President of NASDI Inc. Additionally, the Company entered into a series of transactions for the purpose of restructuring the Company s arrangements with Mr. Berardi.

As a result of these transactions, the operations of NASDI Inc. were contributed into NASDI, LLC, a newly formed Delaware limited liability company, which issued Class A and Class B member interests. The Company is the owner of 100% of the Class A interests, which provide a $28,000 liquidation preference with respect to proceeds upon disposition of NASDI, LLC. The Company also owns 65% of the Class B interests, with the remaining 35% owned by Mr. Berardi. The holders of Class B interests are entitled to receive periodic distributions of future profits based on available cash flows from operations on a pro rata basis in proportion to their percentage ownership interest.

Pursuant to the terms of the NASDI, LLC Limited Liability Company Agreement, the Company has the ability to call Mr. Berardi s 35% interest upon Mr. Berardi s termination of employment, upon a change in control related to the Company or any time after December 31, 2010. The call payment is based on a formula that considers NASDI, LLC s average annual EBITDA for a two year period, as adjusted for the Class A liquidation preference and outstanding indebtedness of NASDI, LLC. The call payment is limited, in certain situations, to a maximum of $1,500.

The Company also entered into an employment agreement with Mr. Berardi that establishes the terms of Mr. Berardi s salary and benefits. Additionally, in the event of sale of all or a material portion of NASDI, LLC, Mr. Berardi is entitled to a cash payment equal to 35% of the proceeds received by the Company in connection with the sale of NASDI, LLC to a third party, but such payment shall not exceed $9,800.

The acquisition was accounted for as a purchase, with a purchase price of $1,939 equal to the fair value of consideration received by Mr. Berardi, including the 35% interest in Class B shares, a cash payment of $5 and the fair value of future obligations to Mr. Berardi by the Company. Accordingly, the assets and liabilities associated with this 15% interest were adjusted to their estimated fair values. This allocation of purchase price is preliminary and is subject to change in future periods based on refinements of the amounts and assumptions used in the allocation. A summary of the allocation of purchase price to the assets acquired is as follows:

Property, plant and equipment	$	(28)
Intangible assets		365
Goodwill		1,574
Total	$	1,911

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16. Subsequent events

On November 3, 2008 the Company entered into a sale-leaseback with Banc of America Leasing & Capital, LLC, for a piece of ancillary equipment, the GL 177. The Company sold the vessel to Banc of America Leasing & Capital, LLC, for $16,665. The Company will lease it through November 2018 under a long term operating lease.

17. Supplemental unaudited condensed consolidating financial information

Included in the Company s long-term debt is $175,000 of 7.75% senior subordinated notes which will mature on December 15, 2013. The payment obligations of the Company under the senior subordinated notes are guaranteed by the Company s domestic subsidiaries (the Subsidiary Guarantors). Such guarantees are full, unconditional and joint and several. The following supplemental financial information sets forth, on a combined basis, the balance sheets, statements of operations and statements of cash flows for the Subsidiary Guarantors, the Company s non-guarantor subsidiary and for the Company, exclusive of its subsidiaries (GLDD Corporation).

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GREAT LAKES DREDGE & DOCK CORPORATION AND SUBSIDIARIES

CONDENSED CONSOLIDATING BALANCE SHEET

AS OF SEPTEMBER 30, 2008

UNAUDITED

(in thousands)

	Guarantor Subsidiaries	Other Subsidiary	GLDD Corporation	Eliminations	Consolidated Totals
ASSETS					
CURRENT ASSETS:					
Cash and cash equivalents	$ 11,513	$ 10	$	$	$ 11,523
Accounts receivable net	98,963				98,963
Receivables from affiliates	7,620	2,739	28,378	(38,737)	
Contract revenues in excess of billings	26,510				26,510
Inventories	30,776				30,776
Prepaid expenses and other current assets	21,818		12,553		34,371
Total current assets	197,200	2,749	40,931	(38,737)	202,143
PROPERTY AND EQUIPMENT Net	309,040				309,040
GOODWILL	97,799				97,799
OTHER INTANGIBLE ASSETS Net	1,063				1,063
INVESTMENTS IN SUBSIDIARIES	2,750		500,878	(503,628)	
INVENTORIES	35,213				35,213
INVESTMENTS IN JOINT VENTURES	9,339				9,339
OTHER ASSETS	1,713		5,914		7,627
TOTAL	$ 654,117	$ 2,749	$ 547,723	$ (542,365)	$ 662,224
LIABILITIES AND STOCKHOLDERS EQUITY					
CURRENT LIABILITIES:					
Accounts payable	78,431		120	(27)	78,524
Payables to affiliates	38,737			(38,737)	
Accrued expenses	20,449		4,694		25,143
Billings in excess of contract revenues	7,672				7,672
Current portion of equipment debt	1,551				1,551
Total current liabilities	146,840		4,814	(38,764)	112,890
REVOLVING CREDIT FACILITY			49,710		49,710
7 3/4% SENIOR SUBORDINATED DEBT			175,000		175,000
DEFERRED INCOME TAXES	1,343	(1)	83,151		84,493
OTHER	6,700		3,927		10,627
Total liabilities	154,883	(1)	316,602	(38,764)	432,720
MINORITY INTEREST			468		468
STOCKHOLDERS EQUITY	499,234	2,750	230,653	(503,601)	229,036
TOTAL	$ 654,117	$ 2,749	$ 547,723	$ (542,365)	$ 662,224

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GREAT LAKES DREDGE & DOCK CORPORATION AND SUBSIDIARIES
CONDENSED CONSOLIDATING BALANCE SHEET
AS OF DECEMBER 31, 2007

UNAUDITED

(in thousands)

	Guarantor Subsidiaries	Other Subsidiary	GLDD Corporation	Eliminations	Consolidated Totals
ASSETS					
CURRENT ASSETS:					
Cash and cash equivalents	$ 8,233	$ 6	$	$	$ 8,239
Accounts receivable net	115,709				115,709
Receivables from affiliates	7,712	2,789	19,507	(30,008)	
Contract revenues in excess of billings	13,828				13,828
Inventories	29,157				29,157
Prepaid expenses and other current assets	15,805		7,885		23,690
Total current assets	190,444	2,795	27,392	(30,008)	190,623
PROPERTY AND EQUIPMENT Net	296,721				296,721
GOODWILL	96,225				96,225
OTHER INTANGIBLE ASSETS Net	1,006				1,006
INVESTMENTS IN SUBSIDIARIES	2,795		454,481	(457,276)	
NOTES RECEIVABLE FROM AFFILIATES			22,702	(22,702)	
INVENTORIES	21,315				21,315
INVESTMENTS IN JOINT VENTURES	9,589				9,589
OTHER ASSETS	1,764		7,119		8,883
TOTAL	$ 619,859	$ 2,795	$ 511,694	$ (509,986)	$ 624,362
LIABILITIES AND STOCKHOLDERS EQUITY					
CURRENT LIABILITIES:					
Accounts payable	77,542		10		77,552
Payables to affiliates	30,008			(30,008)	
Accrued expenses	19,091		4,976		24,067
Billings in excess of contract revenues	5,437				5,437
Current portion of equipment debt	1,273				1,273
Total current liabilities	133,351		4,986	(30,008)	108,329
REVOLVING CREDIT FACILITY			21,500		21,500
7 3/4% SENIOR SUBORDINATED DEBT			175,000		175,000
NOTES PAYABLE TO AFFILIATES	22,702			(22,702)	
DEFERRED INCOME TAXES	1,278		78,558		79,836
OTHER	7,577		1,724		9,301
Total liabilities	164,908		281,768	(52,710)	393,966
MINORITY INTEREST			2,061		2,061
STOCKHOLDERS EQUITY	454,951	2,795	227,865	(457,276)	228,335
TOTAL	$ 619,859	$ 2,795	$ 511,694	$ (509,986)	$ 624,362

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GREAT LAKES DREDGE & DOCK CORPORATION AND SUBSIDIARIES

CONDENSED CONSOLIDATING STATEMENT OF OPERATIONS

FOR THE THREE MONTHS ENDED SEPTEMBER 30, 2008

UNAUDITED

(in thousands)

	Guarantor Subsidiaries	Other Subsidiary	GLDD Corporation	Eliminations	Consolidated Totals
CONTRACT REVENUES	$ 142,809	$	$	$	142,809
COST OF CONTRACT REVENUES	(125,192)		(1)		(125,193)
GROSS PROFIT	17,617		(1)		17,616
OPERATING EXPENSES					
General and administrative expenses	(10,424)	(15)	(532)		(10,971)
Amortization of intangibles	(177)				(177)
Total operating income	7,016	(15)	(533)		6,468
INTEREST EXPENSE (Net)	(32)		(4,269)		(4,301)
EQUITY IN EARNINGS (LOSS) OF SUBSIDIARIES	(26)		7,145	(7,119)	
EQUITY IN EARNINGS OF JOINT VENTURE	61				61
INCOME (LOSS) BEFORE INCOME TAXES	7,019	(15)	2,343	(7,119)	2,228
INCOME TAX (PROVISION) BENEFIT	126	(11)	(942)		(827)
NET INCOME (LOSS)	$ 7,145	$ (26)	$ 1,401	$ (7,119)	$ 1,401

GREAT LAKES DREDGE & DOCK CORPORATION AND SUBSIDIARIES

CONDENSED CONSOLIDATING STATEMENT OF OPERATIONS

FOR THE THREE MONTHS ENDED SEPTEMBER 30, 2007

UNAUDITED

(in thousands)

	Guarantor Subsidiaries	Other Subsidiary	GLDD Corporation	Eliminations	Consolidated Totals
CONTRACT REVENUES	$ 116,460	$	$	$	$ 116,460

COST OF CONTRACT REVENUES	(103,114)				(103,114)
GROSS PROFIT	13,346				13,346
OPERATING EXPENSES					
General and administrative expenses	(8,961)	(16)	(577)		(9,554)
Amortization of intangibles	(66)				(66)
Total operating income	4,319	(16)	(577)		3,726
INTEREST EXPENSE0Net	(577)		(2,798)		(3,375)
EQUITY IN EARNINGS (LOSS) OF SUBSIDIARIES	(10)		5,662	(5,652)	
EQUITY IN EARNINGS OF JOINT VENTURE	790				790
MINORITY INTEREST				22	22
INCOME (LOSS) BEFORE INCOME TAXES	4,522	(16)	2,287	(5,630)	1,163
INCOME TAX (PROVISION) BENEFIT	1,056	6	(3,946)	2,365	(519)
NET INCOME (LOSS)	$ 5,578	$ (10)	$ (1,659)	$ (3,265)	$