

MARTIN MIDSTREAM PARTNERS LP

Form 10-K

March 04, 2009

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**UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549**

FORM 10-K

Mark One

**Annual Report Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934
For the fiscal year ended December 31, 2008**

OR

**Transition Report Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934
For the transition period from _____ to _____.**

Commission file number 000-50056

MARTIN MIDSTREAM PARTNERS L.P.

(Exact name of registrant as specified in its charter)

Delaware

05-0527861

State or other jurisdiction of
incorporation or organization

(I.R.S. Employer Identification No.)

4200 Stone Road Kilgore, Texas 75662

(Address of principal executive offices) (Zip Code)

903-983-6200

(Registrant's telephone number, including area code)

Securities Registered Pursuant to Section 12(b) of the Act:

NONE

Securities Registered Pursuant to Section 12(g) of the Act:

Title of each class

Name of each exchange on which registered

Common Units representing limited
partnership interests

NASDAQ

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act.

Yes No

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Act.

Yes No

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 the past 90 days.

Yes No

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Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K.

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 Accelerated filer Non-accelerated filer Smaller reporting company

(Do not check if a smaller reporting company)

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

As of June 30, 2008, 12,837,480 common units were outstanding. The aggregate market value of the common units held by non-affiliates of the registrant as of such date approximated \$306,811,495. There were 13,688,152 of the registrant's common units and 850,674 of the registrant's subordinated units outstanding as of March 4, 2009.

DOCUMENTS INCORPORATED BY REFERENCE: None.

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PART I

Item 1. Business

Overview

We are a publicly traded limited partnership with a diverse set of operations focused primarily in the United States Gulf Coast region. Our four primary business lines include:

Terminalling and storage services for petroleum products and by-products;

Natural gas services;

Marine transportation services for petroleum products and by-products; and

Sulfur and sulfur-based products processing, manufacturing, marketing and distribution.

The petroleum products and by-products we collect, transport, store and market are produced primarily by major and independent oil and gas companies who often turn to third parties, such as us, for the transportation and disposition of these products. In addition to these major and independent oil and gas companies, our primary customers include independent refiners, large chemical companies, fertilizer manufacturers and other wholesale purchasers of these products. We operate primarily in the Gulf Coast region of the United States. This region is a major hub for petroleum refining, natural gas gathering and processing and support services for the exploration and production industry.

We were formed in 2002 by Martin Resource Management Corporation (*Martin Resource Management*), a privately-held company whose initial predecessor was incorporated in 1951 as a supplier of products and services to drilling rig contractors. Since then, Martin Resource Management has expanded its operations through acquisitions and internal expansion initiatives as its management identified and capitalized on the needs of producers and purchasers of hydrocarbon products and by-products and other bulk liquids. Martin Resource Management owns an approximate 34.9% limited partnership interest in us. Furthermore, it owns and controls our general partner, which owns a 2.0% general partner interest and incentive distribution rights in us.

Martin Resource Management operated our business segments for several years. Martin Resource Management began operating our natural gas services business in the 1950s and our sulfur business in the 1960s. It began our marine transportation business in the late 1980s. It entered into our terminalling and storage businesses in the early 1990s. In recent years, Martin Resource Management has increased the size of our asset base through expansions and strategic acquisitions.

Primary Business Segments

Our primary business segments can be generally described as follows:

Terminalling and Storage. We own or operate 17 marine terminal facilities and six inland terminal facilities located in the United States Gulf Coast region that provide storage and handling services for producers and suppliers of petroleum products and by-products, lubricants and other liquids. We also provide land rental to oil and gas companies along with storage and handling services for lubricants and fuel oil. We provide these terminalling and storage services on a fee basis primarily under long-term contracts.

Natural Gas Services. Through our acquisitions of Prism Gas Systems I, L.P. (*Prism Gas*) and Woodlawn Pipeline Co., Inc. (*Woodlawn*), we have ownership interests in over 669 miles of gathering and transmission pipelines located in the natural gas producing regions of Central and East Texas, Northwest Louisiana, the Texas Gulf Coast and offshore Texas and federal waters in the Gulf of Mexico as well as a 265 MMcf capacity natural gas processing plant located in East Texas. In addition to our natural gas gathering and processing business, we distribute natural gas liquids (*NGLs*). We purchase NGLs primarily from natural gas processors. We store NGLs in our supply and storage facilities for resale to propane retailers, refineries and industrial NGL users in Texas and the Southeastern United States. We own an NGL pipeline which spans approximately 200 miles running from Kilgore to Beaumont, Texas. We own three NGL supply and storage facilities with an aggregate above ground storage capacity of approximately 3,000 barrels and we lease

approximately 2.2 million barrels of underground storage capacity for NGLs.

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Marine Transportation. We own a fleet of 40 inland marine tank barges, 17 inland push boats and four offshore tug barge units that transport petroleum products and by-products primarily in the United States Gulf Coast region. We provide these transportation services on a fee basis primarily under annual contracts. In addition, our marine segment manages our sulfur segment's marine assets.

Sulfur Services. We process and distribute sulfur predominately produced by oil refineries primarily located in the United States Gulf Coast region. We own one offshore tug barge unit and two inland barges and an inland tug that transports sulfur primarily in the United States Gulf Coast region. We process molten sulfur into prilled, or pelletized, sulfur under both fee-based volume contracts and buy/sell contracts at our facilities in Port of Stockton, California and Beaumont, Texas. We own and operate six sulfur-based fertilizer production plants and one emulsified sulfur blending plant that manufacture primarily sulfur-based fertilizer products for wholesale distributors and industrial users. These plants are located in Illinois, Texas and Utah. In October 2007, we completed the construction of a sulfuric acid production plant in Plainview, Texas which processes molten sulfur into sulfuric acid.

2008 Developments and Subsequent Events

Recent Acquisitions

Acquisition of Martin Resource Management Stanolind Assets. In January 2008, we acquired 7.8 acres of land, a deep water dock and two sulfuric acid tanks at our Stanolind terminal in Beaumont, from Martin Resource Management. In connection with this acquisition, we entered into a lease agreement with Martin Resource Management for use of the sulfuric acid tanks.

Other Developments

Quarterly Distribution. We declared a quarterly cash distribution for the fourth quarter of 2008 of \$0.75 per common and subordinated unit on January 27, 2009, reflecting no change over the quarterly distribution paid in respect of the third quarter of 2008.

Conversion of Subordinated Units. On November 14, 2008, 850,672 of our 1,701,346 outstanding subordinated units owned by Martin Resource Management through a subsidiary converted into common units on a one-for-one basis following our quarterly cash distribution on such date. Additional conversions of our outstanding subordinated units may occur in the future provided that certain distribution thresholds contained in our partnership agreement are met by us.

Business Strategy

The key components of our business strategy are to:

Pursue Organic Growth Projects. We continually evaluate economically attractive organic expansion opportunities in new or existing areas of operation that will allow us to leverage our existing market position, increase the distributable cash flow from our existing assets through improved utilization and efficiency, and leverage our existing customer base.

Pursue Internal Organic Growth by Attracting New Customers and Expanding Services Provided to Existing Customers. We seek to identify and pursue opportunities to expand our customer base across all of our business segments. We generally begin a relationship with a customer by transporting or marketing a limited range of products and services. We believe expanding our customer base and our service and product offerings to existing customers is the most efficient and cost effective method of achieving organic growth in revenues and cash flow. We believe significant opportunities exist to expand our customer base and provide additional services and products to existing customers.

Pursue Strategic Acquisitions. We monitor the marketplace to identify and pursue accretive acquisitions that expand the services and products we offer or that expand our geographic presence. After acquiring other businesses, we will attempt to utilize our industry knowledge, network of customers and suppliers and strategic asset base to operate the acquired businesses more efficiently and competitively, thereby increasing revenues and cash flow.

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We believe that our diversified base of operations provides multiple platforms for strategic growth through acquisitions. While we continue to monitor the marketplace for potential acquisitions, we anticipate that our activities in this area will be limited in 2009 due to general economic conditions and capital constraints.

Pursue Strategic Alliances. Many of our larger customers are establishing strategic alliances with midstream service providers such as us to address logistical and transportation problems or achieve operational synergies. These strategic alliances are typically structured differently than our regular commercial relationships, with the goal that such alliances would expand our business relationships with our customers and suppliers. We intend to pursue strategic alliances with customers in the future.

Expand Geographically. We work to identify and assess other attractive geographic markets for our services and products based on the market dynamics and the cost associated with penetration of such markets. We typically enter a new market through an acquisition or by securing at least one major customer or supplier and then dedicating or purchasing assets for operation in the new market. Once in a new territory, we seek to expand our operations within this new territory both by targeting new customers and by selling additional services and products to our original customers in the territory.

Competitive Strengths

We believe we are well positioned to execute our business strategy because of the following competitive strengths:

Asset Base and Integrated Distribution Network. We operate a diversified asset base that, together with the services provided by Martin Resource Management, enables us to offer our customers an integrated distribution network consisting of transportation, terminalling and midstream logistical services while minimizing our dependence on the availability and pricing of services provided by third parties. Our integrated distribution network enables us to provide customers a complementary portfolio of transportation, terminalling, distribution and other midstream services for petroleum products and by-products.

Strategically Located Assets. We believe we are one of the largest providers of shore bases and one of the largest lubricant distributors and marketers in the United States Gulf Coast region. In addition, we are one of the largest operators of marine service terminals in the United States Gulf Coast region providing broad geographic coverage and distribution capability of our products and services to our customers. Our natural gas gathering and processing assets are focused in areas that have continued to experience high levels of drilling activity and natural gas production.

Specialized Transportation Equipment and Storage Facilities. We have the assets and expertise to handle and transport certain petroleum products and by-products with unique requirements for transportation and storage, such as molten sulfur and asphalt. For example, we own facilities and resources to transport molten sulfur and asphalt, which must be maintained at temperatures between approximately 275 and 350 degrees Fahrenheit to remain in liquid form. We believe these capabilities help us enhance relationships with our customers by offering them services to handle their unique product requirements.

Ability to Grow Our Natural Gas Gathering and Processing Services. We believe that, with our Prism Gas assets, we have opportunities for organic growth in our natural gas gathering and processing operations through increasing fractionation capacity, pipeline expansions, new pipeline construction and bolt-on acquisitions. We believe Prism's assets are well situated in the Haynesville Shale which is one of the four largest U.S. shale deposits. Chesapeake Energy, the largest lease holder in the Haynesville Shale, estimates that the Haynesville Shale will ultimately produce over 500 TCF of natural gas and that this field will be among the top 10 natural gas fields in the world. As the development of the Haynesville Shale is in its early stages, it is too early to estimate the ultimate impact on Prism.

Experienced Management Team and Operational Expertise. Members of our executive management team and the heads of our principal business lines have, on average, more than 29 years of experience in the industries in which we operate. Further, these individuals have been employed by Martin Resource Management, on average, for more than 17 years. Our management team has a successful track record of creating internal growth and completing acquisitions. We believe our management team's experience and familiarity with our industry and businesses are important assets that assist us in implementing our business strategies.

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Strong Industry Reputation and Established Relationships with Suppliers and Customers. We believe we have established a reputation in our industry as a reliable and cost-effective supplier of services to our customers and have a track record of safe, efficient operation of our facilities. Our management has also established long-term relationships with many of our suppliers and customers. We believe we benefit from our management's reputation and track record, and from these long-term relationships.

Terminalling and Storage Segment

Industry Overview. The United States petroleum distribution system moves petroleum products and by-products from oil refinery and natural gas processing facilities to end users. This distribution system is comprised of a network of terminals, storage facilities, pipelines, tankers, barges, rail cars and trucks. Terminals play a key role in moving these products throughout the distribution system by providing storage, blending and other ancillary services.

In the 1990s, the petroleum industry entered a period of consolidation. Refiners and marketers developed large-scale, cost-efficient operations resulting in several refinery acquisitions, combinations, alliances and joint ventures. This consolidation resulted in major oil companies integrating the various components of their businesses, including terminalling and storage. However, major integrated oil companies later concentrated their focus and resources on their core competencies of exploration, production, refining and retail marketing and examined ways to lower their distribution costs. Additionally, the Federal Trade Commission required some divestitures of terminal assets in markets in which merged companies, alliances and joint ventures were regarded as having excessive market power. As a result of these factors, oil and gas companies began to increasingly rely on third parties such as us to perform many terminalling and storage services.

Although many large energy and chemical companies own terminalling and storage facilities, these companies also use third party terminalling and storage services. Major energy and chemical companies typically have a strong demand for terminals owned by independent operators when such terminals are strategically located at or near key transportation links, such as deep-water ports. Major energy and chemical companies also need independent terminal storage when their owned storage facilities are inadequate, either because of lack of capacity, the nature of the stored material or specialized handling requirements.

The Gulf Coast region is a major hub for petroleum refining. Approximately two-thirds of United States refining capacity expansion in the 1990s occurred in this region. Growth in the refining and natural gas processing industries has increased the volume of petroleum products and by-products that are transported within the Gulf Coast region, which consequently has increased the need for terminalling and storage services.

The marine and offshore oil and gas exploration and production industries use terminal facilities in the Gulf Coast region as shore bases that provide them logistical support services as well as provide a broad range of products, including fuel oil, lubricants, chemicals and supplies. The demand for these types of terminals, services and products is driven primarily by offshore exploration, development and production in the Gulf of Mexico. Offshore activity is greatly influenced by current and projected prices of oil and natural gas.

Marine Terminals. We own or operate 17 marine terminals along the Gulf Coast from Tampa, Florida to Corpus Christi, Texas. Our terminal assets are located at strategic distribution points for the products we handle and are in close proximity to our customers. Further, the location and composition of our terminals are structured to complement our other businesses and reflect our strategy to provide a broad range of integrated services in the handling and transportation of petroleum products and by-products. We developed our terminalling and storage assets by acquiring existing terminalling and storage facilities and then customizing and upgrading these facilities as needed to integrate the facilities into our petroleum product and by-product transportation network and to more effectively service customers. We expect to continue to acquire facilities, streamline their operations and customize and upgrade them as part of our growth strategy. We also continually evaluate opportunities to add services and increase access to our terminals to attract more customers and create additional revenues.

We are one of the largest operators of marine service terminals in the Gulf Coast region. These terminals are used to distribute and market lubricants and the full service terminals also provide shore bases for companies that are operating in the offshore exploration and production industry. Customers are primarily oil and gas exploration and production companies and oilfield service companies such as drilling fluid companies, marine transportation companies, and offshore construction companies.

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Shore bases typically provide logistical support including the storing and handling of tubular goods, loading and unloading bulk materials, providing facilities from which major and independent oil companies can communicate with and control offshore operations and leasing dockside facilities to companies which provide complementary products and services such as drilling fluids and cementing services. We generate revenues from our terminals that have shore bases by fees that we charge our customers under land rental contracts for the use of our terminal facility for these shore bases. These contracts generally provide us a fixed land rental fee and additional rental fees that are determined based on a percentage of the sales value of the products and services delivered from the shore base. We also generate revenues through the distribution and marketing of lubricants. Lubricants are used in the operation of offshore drilling rigs, offshore production and transmission platforms, and various ships and equipment engaged in marine transportation. In addition, Martin Resource Management, through contractual arrangements, pays us for terminalling and storage of fuel oil at these terminal facilities.

Our 17 marine terminals are divided generally into three classes of terminals: (i) full service terminals, (ii) fuel and lubricant terminals and (iii) specialty petroleum terminals.

Full Service Terminals. We own or operate eight full service terminals. These terminal facilities provide logistical support services, distribute and market lubricants and provide storage and handling services for fuel oil. The significant difference between our full service terminals and our fuel and lubricant terminals is that our full service terminals generate additional revenues by providing shore bases to support our customer's operating activities related to the offshore exploration and production industry. One typical use for our shore bases is for drilling fluids manufacturers to manufacture and sell drilling fluids to the offshore drilling industry. Offshore drilling companies may also set up service facilities at these terminals to support their offshore operations. Customers are primarily oil and gas exploration and production companies, and oilfield service companies such as drilling fluids companies, marine transportation companies, and offshore construction companies.

The following is a summary description of our eight full service terminals:

Terminal	Location	Acres	Tanks	Aggregate Capacity
Pelican Island	Galveston, Texas	51.3	16	87,200 Bbls.
Harbor Island(1)	Harbor Island, Texas	25.5	12	32,500 Bbls.
Freeport	Freeport, Texas	17.8	1	8,300 Bbls.
Port O Connor(2)	Port O Connor, Texas	22.8	8	7,000 Bbls.
Sabine Pass(3)	Sabine Pass, Texas	23.1	11	17,000 Bbls.
Cameron East (4)	Cameron, Louisiana	34.3	12	34,000 Bbls.
Cameron West (5)	Cameron, Louisiana	16.9	5	16,500 Bbls.
Venice (6)	Venice, Louisiana	2.8	2	15,000 Bbls.

(1) A portion of this terminal is located on land owned by a third party and leased under a lease that expires in January 2010 and can be extended by us through January 2015.

(2) This terminal is located on land owned by a third

party and leased under a lease that expires in March 2014.

(3) A portion of this terminal is located on land owned by a third party and leased under a lease that expires in September 2036.

(4) This terminal is located on land owned by third parties and leased under a lease that expires in March 2012 and can be extended by us through March 2022.

(5) This terminal is located on land owned by a third party and leased under a lease that expires in February 2013.

(6) This terminal is located on land owned by a third party and leased under a sublease agreement that expires in August 2009 and can be extended by us through August 2024.

Fuel and Lubricant Terminals. We own or operate four lubricant and fuel oil terminals located in the Gulf Coast region that provide storage and handling service for lubricants and fuel oil. We also distribute and market lubricants at these terminals.

The following is a summary description of our fuel and lubricant terminals:

Terminal	Location	Tanks	Aggregate Capacity
Amelia	Amelia, Louisiana	17	14,900 Bbls.

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Berwick(1)	Berwick, Louisiana	2	25,000 Bbls.
Intracoastal City(2)(3)	Intracoastal City, Louisiana	16	39,000 Bbls.
Fourchon(4)	Fourchon, Louisiana	11	80,000 Bbls.

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- (1) This terminal is located on land owned by third parties and leased under a lease that expires in September 2012 and can be extended by us through September 2017.
- (2) A portion of this terminal is located on land owned by a third party at which we throughput fuel oil pursuant to an agreement that expires in January 2010.
- (3) A portion of this terminal is located on land owned by third parties and leased under a lease that expires in April 2014.
- (4) This terminal is located on land owned by a third party at which we throughput lubricants and fuel oil pursuant to an agreement that expires in January 2017.

Specialty Petroleum Terminals. We own or operate five terminal facilities providing storage and handling services for some or all of the following: anhydrous ammonia, asphalt, sulfur, sulfuric acid, fuel oil, crude oil and other petroleum products and by-products. Our specialty terminals have an aggregate storage capacity of approximately 1.90 million barrels. Each of these terminals has storage capacity for petroleum products and by-products and has assets to handle products transported by vessel, barge and truck. Our Tampa terminal is located on approximately 10 acres of land owned by the Tampa Port Authority that was leased to us under a 10-year lease that

commenced on December 16, 2006 with two five year options. Our Stanolind terminal is located on approximately 11 acres of land owned by us located on the Neches River in Beaumont. Our Neches terminal is a deep water marine terminal located near Beaumont, Texas on approximately 50 acres of land owned by us. Our Ouachita County terminal is located on approximately six acres of land owned by us on the Ouachita River in southern Arkansas. Our Corpus Christi terminal is located on approximately 25 acres of land owned by us and has access to the waterfront via marine docks owned by the Port of Corpus Christi.

At our Tampa, Neches, Stanolind and Corpus Christi terminals, our customers are primarily large oil refining and natural gas processing companies. We charge either a fixed monthly fee or a throughput fee for the use of our facilities, based on the capacity of the applicable tank. We conduct a substantial portion of our terminalling and storage operations under long-term contracts, which enhances the stability and predictability of our operations and cash flow. We attempt to balance our short term and long term terminalling contracts in order to allow us to maintain a consistent level of cash flow while maintaining flexibility to earn higher storage revenues when demand for storage space increases. At our Ouachita County terminal, Cross Oil Refining & Marketing, Inc., a related party owned by Martin Resource Management, operates the terminal under a long-term terminalling agreement whereby we receive a throughput fee. We also continually evaluate opportunities to add services and increase access to our terminals to attract more customers and create additional revenues. The following is a summary description of our specialty marine terminals:

Terminal	Location	Tanks	Aggregate Capacity	Products	Description
Tampa(1)	Tampa, Florida	8	779,000 Bbls.	Asphalt, sulfur and fuel oil	Marine terminal, loading/unloading for vessels, barges and trucks
Stanolind	Beaumont, Texas	8	555,000 Bbls.	Asphalt, crude oil, sulfur, sulfuric acid and fuel oil	Marine terminal, marine dock for loading/unloading of vessels, barges, railcars and trucks
Neches	Beaumont, Texas	7	500,400 Bbls.	Ammonia, asphalt, fuel oil, crude oil and sulfur-based fertilizer	Marine terminal, loading/unloading for vessels, barges, railcars and trucks
Ouachita County	Ouachita County, Arkansas	2	77,500 Bbls.	Crude oil	Marine terminal, loading/unloading for barges and trucks
Corpus Christi	Corpus Christi, Texas	4	330,000 Bbls.	Fuel oil and diesel	Marine Terminal, loading/unloading barges and vessels and unloading trucks

(1) This terminal is located on land owned by the Tampa Port Authority that was leased to us under a 10-year lease that expires in December 2016

with two five
year extension
options.

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Inland Terminals. We own or operate six inland terminals.

At Mont Belvieu, Texas, we own a rail unloading terminal where we unload and measure NGLs and transport these products via a half-mile pipeline to Enterprise Products Texas Operating L.P.'s NGL fractionator facility. Our fees for the use of this facility are based on the number of gallons unloaded at the terminal.

In Beaumont, Texas we own Spindletop Terminal where we receive natural gasoline via pipeline and then ship the product to our customers via other pipelines to which the facility is connected. Our fees for the use of this facility are based on the number of barrels shipped from the terminal.

In Channelview, Texas, we operate an inland terminal used for lubricant storage, packaging and distribution. This terminal is used as our central hub for lubricant distribution where we receive, package, and ship our lubricants to our terminals or directly to customers.

In Houston, Texas, we own an asphalt terminal whose use is dedicated to an affiliate of Martin Resource Management through a terminalling service agreement based on throughput rates.

In Port Neches, Texas, we own an asphalt terminal whose use is dedicated to an affiliate of Martin Resource Management through a terminalling service agreement based upon throughput rates.

In Omaha, Nebraska, we own an asphalt terminal whose use is dedicated to an affiliate of Martin Resource Management through a terminalling service agreement based on throughput rates.

The following is a summary description our inland terminals:

Terminal	Location	Aggregate Capacity	Products	Description
Channelview	Houston, Texas	34,000 sq. ft. Warehouse/29,000 Bbls	Lubricants	Lubricants blending and truck loading/unloading
Mont Belvieu	Mont Belvieu, Texas	20 rail car spaces	Propane-propylene mix	Rail car unloading
South Houston Asphalt	Houston, Texas	71,000 Bbls	Asphalt	Asphalt Processing and storage
Port Neches Asphalt	Port Neches, Texas	31,250 Bbls	Asphalt	Asphalt Processing and storage
Omaha Asphalt	Omaha, Nebraska	114,225 Bbls	Asphalt	Asphalt Processing and storage
Spindletop	Beaumont, Texas	90,000 Bbls	Natural Gasoline	Pipeline receipts and shipments

Competition. We compete with independent terminal operators and major energy and chemical companies that own their own terminalling and storage facilities. We believe many customers prefer to contract with independent terminal operators rather than terminal operators owned by integrated energy and chemical companies that may have refining or marketing interests that compete with the customers.

Independent terminal owners generally compete on the basis of the location and versatility of terminals, service and price. A favorably-located terminal has access to various cost effective transportation modes, both to and from the terminal, such as waterways, railroads, roadways and pipelines. Terminal versatility depends upon the operator's ability to handle diverse products, some of which have complex or specialized handling and storage requirements. The service function of a terminal includes, among other things, the safe storage of product at specified temperature, moisture and other conditions, and receiving and delivering product to and from the terminal. All of these services must be in compliance with applicable environmental and other regulations.

We believe we successfully compete for terminal customers because of the strategic location of our terminals along the Gulf Coast, our integrated transportation services, our reputation, the prices we charge for our services and the quality and versatility of our services.

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Additionally, while some companies have significantly more terminalling and storage capacity than us, not all terminalling and storage facilities located in the markets we serve are equipped to properly handle specialty products such as asphalt, sulfur and sulfuric acid. As a result, our facilities typically command higher terminal fees when compared to fees charged for terminalling and storage of other petroleum products.

The principal competitive factors affecting our terminals which provide lubricant distribution and marketing as well as shore bases at certain terminals, are the locations of the facilities, availability of competing logistical support services, and the experience of personnel and dependability of service. The distribution and marketing of our lubricant products is brand sensitive, and we encounter brand loyalty competition. Shore base rental contracts are generally long-term contracts and provide more protection from competition. Our primary competitors for both lubricants and shore bases include several independent operations as well as major companies that maintain their own similarly equipped marine terminals, shore bases and lubricant supply sources.

Natural Gas Services Segment

NGL Industry Overview. NGLs are produced through natural gas processing. They are also a by-product of crude oil refining. NGL consists of hydrocarbons that are vapors at atmospheric temperatures and pressures but change to liquid phase under pressure. NGLs include ethane, propane, normal butane, iso butane and natural gasoline.

Ethane is almost entirely used as a petrochemical feedstock in the production of ethylene and propylene. Propane is used as a petrochemical feedstock in the production of ethylene and propylene, as a fuel for heating, for industrial applications, as motor fuel and as a refrigerant. Normal butane is used as a petrochemical feedstock, as a blend stock for motor gasoline and as a component in aerosol propellants. Normal butane can also be made into iso butane through isomerization. Iso butane is used in the production of motor gasoline, petrochemical feedstock and as a component in aerosol propellants. Natural gasoline is used as a component of motor gasoline and as a petrochemical feedstock.

NGL Facilities. We purchase NGLs primarily from natural gas processors and, to a lesser extent, major domestic oil refiners. We transport NGLs using Martin Resource Management's land transportation fleet or by contracting with common carriers, owner-operators and railroad tank cars. We typically enter into annual contracts with independent retail propane distributors to deliver their estimated annual volume requirements based on prevailing market prices. We believe dependable delivery is very important to these customers and in some cases may be more important than price. We ensure adequate supply of NGLs through:

storage of NGLs purchased in off-peak months;

efficient use of the transportation fleet of vehicles owned by Martin Resource Management; and

product management expertise to obtain supplies when needed.

The following is a summary description of our owned and leased NGL facilities:

NGL Facility	Location	Capacity	Description
Wholesale terminals	Arcadia, Louisiana(1)	2,000,000 barrels	Underground storage
	Hattiesburg, Mississippi(2)	100,000 barrels	Underground storage
	Mt. Belvieu, Texas(3)(2)	40,000 barrels	Underground storage
Retail terminals	Kilgore, Texas	90,000 gallons	Retail propane distribution
	Longview, Texas	30,000 gallons	Retail propane distribution
	Henderson, Texas	12,000 gallons	Retail propane distribution

(1) We lease our underground storage at Arcadia, Louisiana from Martin Resource

Management under a three-year product storage agreement, which is renewable on a yearly basis thereafter subject to a re-determination of the lease rate for each subsequent year.

(2) We lease our underground storage at Hattiesburg, Mississippi and Mont Belvieu, Texas from third parties under one-year lease agreements, which have been renewed annually for more than 20 years.

(3) In addition, under a throughput agreement, we are entitled to the sole access to and use of a truck loading and unloading and pipeline distribution terminal owned by Martin Resource Management and located at Mont Belvieu, Texas. Effective each January 1, this agreement

automatically
renews for
consecutive
one-year periods
unless either
party terminates
the agreement by
giving written
notice to the
other party at
least 30 days
prior to the
expiration of the
then-applicable
term. This
terminal facility
has a storage
capacity of 8,000
barrels.

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Our NGL customers that utilize these assets consist of retail propane distributors, industrial processors and refiners. For the year ended December 31, 2008, we sold approximately 34% of our NGL volume to independent retail propane distributors located in Texas and the southeastern United States and approximately 66% of our NGL volume to refiners and industrial processors.

NGL Competition. We compete with large integrated NGL producers and marketers, as well as small local independent marketers. NGLs compete primarily with natural gas, electricity and fuel oil as an energy source, principally on the basis of price, availability and portability.

NGL Seasonality. The level of NGL supply and demand is subject to changes in domestic production, weather, inventory levels and other factors. While production is not seasonal, residential and wholesale demand is highly seasonal. This imbalance causes increases in inventories during summer months when consumption is low and decreases in inventories during winter months when consumption is high. If inventories are low at the start of the winter, higher prices are more likely to occur during the winter. Additionally, abnormally cold weather can put extra upward pressure on prices during the winter because there are less readily available sources of additional supply except for imports which are less accessible and may take several weeks to arrive. General economic conditions and inventory levels have a greater impact on industrial and refinery use of NGLs than the weather.

We generally maintain consistent margins in our natural gas services business because we attempt to pass increases and decreases in the cost of NGLs directly to our customers. We generally try to coordinate our sales and purchases of NGLs based on the same daily price index of NGLs in order to decrease the impact of NGL price volatility on our profitability.

Prism Gas. Prism Gas is operated and reported as part of our natural gas services business segment, which has been expanded to include natural gas gathering and processing as well as the NGL services business described herein.

Prism Gas has ownership interests in over 669 miles of gathering pipelines located in the natural gas producing regions of North Central Texas and East Texas, Northwest Louisiana, the Texas Gulf Coast and offshore Texas and federal waters in the Gulf of Mexico as well as a 265 MMcfd natural gas processing plant located in East Texas. The underlying assets are in two operating areas:

North Central Texas and East Texas

The North Central Texas and East Texas area assets consist of the Waskom Processing Plant, Woodlawn Pipeline Co., the McLeod Gathering System, the Hallsville Gathering System, the Marshall Line, Bosque County Pipeline (BCP), the East Texas Gathering System and the Prism Liquids Pipeline.

Waskom Processing Plant The Waskom Processing Plant, located in Harrison County in East Texas, currently has 265 MMcfd of processing capacity with full fractionation facilities. Expansions to the processing plant were completed in March and June of 2007, and July of 2008 increasing the capacity from 150 MMcfd to 265 MMcfd. In January 2007, the Waskom fractionator was expanded to a capacity of 12,500 barrels per day (bpd). In addition, an increase in the processing capacity of the plant to 285 MMcfd and fractionation capacity to 14,500 bpd is expected to be completed by the end of the second quarter of 2009. For the years ended December 31, 2008 and 2007, inlet throughput and NGL fractionation averaged approximately 257 and 229 MMcfd and 10,542 and 8,725 bpd, respectively. Prism Gas owns an unconsolidated 50% operating interest in the Waskom Processing Plant with CenterPoint Energy Gas Processing, Inc. owning the remaining 50% non-operating interest. We reflect the results of operations from this facility using the equity method of accounting

Woodlawn Plant and Gathering System On May 2, 2007, we, through our subsidiary Prism Gas acquired 100% of the outstanding stock of Woodlawn. The results of Woodlawn's operations have been included in our consolidated financial statements beginning May 2, 2007. Woodlawn is a natural gas gathering and processing company which owns integrated gathering and processing assets in East Texas. Woodlawn's system consists of approximately 135 miles of natural gas gathering pipe, approximately 36 miles of condensate transport pipe and a 30 MMcfd processing plant. Prism Gas acquired a nine-mile pipeline, from a Woodlawn related party, that delivers residue gas from the Woodlawn plant to the Texas Eastern Transmission pipeline system.

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McLeod Gathering System The McLeod Gathering System, located in East Texas and Northwest Louisiana, is a low pressure gathering system connected to the Waskom Processing Plant, providing processing and blending services for natural gas with high nitrogen and high liquids content gathered by the system. For both years ended December 31, 2008 and 2007, the McLeod Gathering System gathered approximately 5 MMcfd of natural gas. Prism Gas owns a consolidated 100% interest in this system.

Hallsville Gathering System The Hallsville Gathering System, which Prism Gas constructed in 2006 in Harrison County, Texas, provides gathering and centralized compression for producers in the Oak Hill Field of East Texas. The system operates at low pressure and redelivers gas to two interstate and three intrastate markets via the Oakhill Gathering System. For the years ended December 31, 2008 and 2007, the Hallsville Gathering System gathered approximately 21 and 17 MMcfd of natural gas, respectively. Prism Gas owns a consolidated 100% interest in this system.

The Marshall Line The Marshall Line is a 10 gathering line that Prism Gas began leasing from Kinder Morgan Texas in 2006. It is located in Harrison County, Texas. The Marshall Line gathers gas at intermediate pressure and feeds the Waskom Processing Plant. Prism Gas owns a consolidated 100% interest in the lease.

Bosque County Pipeline The Bosque County Pipeline, gathers gas in four North Central Texas counties centered around Bosque County. Prism Gas owns an unconsolidated 20% non-operating interest in a partnership that owns the lease rights to the assets of the Bosque County Pipeline, with Panther Pipeline Ltd. owning a 42.5% operating interest and two unrelated parties owning the remaining 37.5% interest. The lease contract provides for termination in June 2009 and an extension of the lease is not currently contemplated.

East Texas Gathering System The East Texas Gathering System, located in Panola County, Texas, is comprised of gathering systems built to gather gas produced in this area to market outlets. Prism Gas owns a consolidated 100% interest in these systems.

The natural gas supply for the Waskom Processing Plant, the Woodlawn Plant and Gathering System, the McLeod Gathering System, the Hallsville Gathering System, the Marshall Line and the East Texas Gathering System is derived primarily from natural gas wells located in the Cotton Valley formation of East Texas and Northwest Louisiana. The Cotton Valley formation is one of the largest tight gas plays in the U.S. and extends over fourteen counties in East Texas and into Northwest Louisiana. Prism Gas East Texas Operating Area includes assets that provide gathering and processing services to producers in Cass, Gregg, Harrison, Panola, and Rusk Counties, Texas and Caddo Parish, Louisiana. The total number of wells permitted in Prism Gas East Texas Operating Area was 2,323 and 2,290 in calendar years 2008 and 2007, respectively. These annual permit numbers include 261 permits for horizontal wells in 2008 and 83 permits for horizontal wells in 2007. Improved technology and drilling applications have enhanced the economics of drilling in the Cotton Valley formation. This increase in drilling activity has provided us with access to newly developed natural gas supplies. However, we anticipate that drilling activity in 2009 will be negatively impacted by low commodity prices and capital constraints. In addition, emphasis in the area will shift from predominantly Cotton Valley drilling to a blend of Cotton Valley and Haynesville formation drilling.

Our primary suppliers of natural gas to the Waskom Processing Plant include BP America Production Company, Centerpoint Energy Gas Transmission Company and Devon Energy Corporation, which collectively represented approximately 72% of the 229 MMcfd of natural gas supplied in 2007 and approximately 70% of the 257 MMcfd of natural gas supplied for the year ended December 31, 2008. A substantial portion (approximately 27%) of the Waskom Processing Plant's inlet volumes are derived from production at BP's Blocker, East Mountain, Carthage and Woodlawn fields in East Texas. Production from these fields is dedicated to the Waskom Processing Plant under a contract with BP for the life of the Waskom partnership. We receive natural gas at the Waskom Processing Plant from our McLeod Gathering System. We also receive a significant amount of trucked-in NGLs that are fractionated, treated and stabilized at the Waskom Processing Plant. The tightening of pipeline dew point specifications and access to local

markets with high NGL demand has resulted in increased trucked-in NGL volumes at the Waskom Processing Plant.

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In October 2006, we began construction to expand the fractionator to 12,500 bpd to provide additional capacity for both the increase in NGL volumes from the plant expansions that were underway and this increase in trucked-in NGL volumes. This expansion was completed in late January 2007. The processing plant was expanded to 265 MMcfd in three phases with the first expansion of 30 MMcfd being completed in March 2007, the second expansion of 70 MMcfd being completed in June 2007 and the third phase of 15 Mmcfd being completed in July 2008.

There are currently six processing plants that compete with Waskom for natural gas supplies. Drilling activity in the Cotton Valley trend is moving north from the Panola-Harrison County line further into Harrison County. Our plant is the preferred gas plant for much of this new production due to its proximity to the increased drilling activity. In addition, the Waskom Processing Plant is the only plant in this area that has full fractionation capability with access to strong local markets for NGLs. Purchasers of NGLs fractionated at Waskom include various chemical companies and other industrial distributors.

The processing contracts for the Waskom Processing Plant are primarily percent-of-liquids (POL) contracts, in which we retain a portion of the NGLs recovered as a processing fee, percent-of-proceeds (POP) contracts in which we retain a portion of both the residue gas and the NGLs as payment for services and straight fee contracts in which we receive a fee for every Mcf of gas delivered to the plant. Currently, approximately 50% of the contracts are POL, 30% of the contracts are fee and 20% of the contracts are POP. In addition, there is one minor contract for processing on a keep-whole basis.

Woodlawn provides gathering and processing services. The Woodlawn gathering system provides both low and intermediate pressure gathering services. The gas is gathered to a 30 MMcfd refrigerated gas processing plant. The NGL s that are recovered at Woodlawn are trucked to the Waskom Processing Plant for fractionation. In 2007, after acquiring Woodlawn, the system gathered and processed 21 MMcfd and recovered 223 bpd of NGL s. For the year ended December 31, 2008, the system gathered and processed 24 MMcfd and recovered 247 bpd of NGL s. The contracts on the Woodlawn system are primarily wellhead purchase with some POP contracts.

The McLeod Gathering System is a low-pressure gathering system that provides an outlet for high nitrogen and high liquids content gas. In June 2003, Prism Gas constructed a pipeline to tie the McLeod Gathering System to the Waskom Processing Plant to provide an outlet for high nitrogen gas. As a result, the majority of gas gathered on the McLeod Gathering System is transported to the Waskom Processing Plant for processing and blending. Revenue from the McLeod Gathering System is earned through gathering and compression fees and processing revenue. The processing revenue results from the difference in the processing agreements with the producers and the agreement that we have with the Waskom partnership. The processing contracts in the McLeod Gathering System are predominately POP contracts. Natural gas gathered in the region surrounding the McLeod Gathering System has two primary outlets, including the Waskom Processing Plant.

Cotton Valley wells are now being drilled in the southern area served by the McLeod Gathering System. The new Cotton Valley wells that have recently been tied into the system are POL contracts with a small gathering fee. These contracts are typically lower margin, higher volume contracts. In this area, competition is geographic based with the McLeod Gathering System capturing wells that are located near the system and the competitor capturing wells that are near its system.

The Hallsville Gathering System was constructed in 2005 and 2006 to gather low pressure gas. The wells tied into the system are fee based gathering contracts.

The Marshall Line was leased from Kinder Morgan to provide additional sources of gas for the Waskom Processing Plant. The gas on the system is from Cotton Valley production and is tied into the system under percent of index based contracts.

The BCP is an approximate 67 mile pipeline located in the Barnett Shale extension.

The East Texas Gathering System was constructed in 2004 to tie producers into DCP Midstream s gathering system in Panola County, Texas. These lines are sized to handle volumes that are expected to increase as producers continue to develop Cotton Valley sands in areas that were traditionally marginal. The existing East Texas Gathering System contracts are all fee-for-service contracts dependent on volumes gathered.

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The Prism Liquids Pipeline condensate system was formed from the condensate pipeline system obtained in the Woodlawn acquisition. The system was subsequently extended approximately 10 miles using lateral lines to gather condensate from additional locations. The pipeline is a common carrier under the Rules and Regulations of the Railroad Commission of Texas, Oil and Gas Division and, as such, operates under a tariff filed with the Railroad Commission of Texas. The system gathers and transports condensate for producers along the main line which extends south from the Woodlawn Plant to the Carthage Plant operated by DCP Midstream.

Gulf Coast

The Gulf Coast area assets consist of the Fishhook Gathering System and the Matagorda Offshore Gathering System (Matagorda) located offshore and onshore of the Texas Gulf Coast.

Fishhook Gathering System The Fishhook Gathering System, located in Jefferson County, Texas and offshore federal waters, gathers and transports gas in both offshore and onshore areas. For the year ended December 31, 2007, the Fishhook Gathering System gathered and transported approximately 32 MMcfd of natural gas. In September 2008, Hurricane Ike caused extensive damage to an offshore platform on the system. Repairs were completed in February 2009. Prior to the hurricane damage approximately 15 MMcfd of natural gas was gathered and transported for the year ended December 31, 2008. Prism Gas owns an unconsolidated 50% non-operating interest in Panther Interstate Pipeline Energy, LLC (PIPE), the owner of the Fishhook Gathering System, with Panther Pipeline Ltd owning the remaining 50% operating interest. We reflect the results of operations from this system using the equity method of accounting.

Matagorda Offshore Gathering System The Matagorda Offshore Gathering System, located in Matagorda County, Texas and offshore Texas State waters, gathers gas in both the offshore and onshore areas. For the years ended December 31, 2008 and 2007, the Matagorda Offshore Gathering System gathered approximately 15 and 7 MMcfd of natural gas, respectively. Prism Gas owns an unconsolidated 50% non-operating interest in the Matagorda Offshore Gathering System, with Panther Pipeline Ltd. owning the remaining 50% operating interest. We reflect the results of operations from this system using the equity method of accounting.

The Fishhook Gathering System and the Matagorda Offshore Gathering System gather and transport natural gas from Texas and federal waters of the Gulf of Mexico to onshore pipelines. The Fishhook Pipeline gathers and transports natural gas principally from the eastern portion of the High Island Area which is further offshore. The offshore natural gas supply for the Matagorda Offshore Gathering System is produced primarily from the Brazos Area blocks, which are near shore in the Texas State waters. Additionally, the Matagorda Offshore Gathering System includes onshore gathering in Matagorda, Wharton and Brazoria Counties.

The Fishhook Gathering System is located in federal waters offshore from Beaumont, Texas and gathers gas from producers. This area is characterized by strong drilling activity with traditionally high volume, high decline wells. Typically, two to four of these traditional wells are drilled near the Fishhook Gathering System each year. Contracts on this system are 100% fee-for-service contracts with both the gathering fee and the maximum transmission fee stated in PIPE 's FERC Gas Tariff, on file with the Federal Energy Regulatory Commission. There are currently two competing pipelines in the area which limit our ability to increase margins on this system. However, we believe that our existing relationships with active producers will enable us to capture additional volumes from new production in this area.

The Matagorda Offshore Gathering System gathers gas from producers. Contracts for the offshore portion of the Matagorda Offshore Gathering System are a combination of fixed transportation fees plus a fixed margin. The contracts for the onshore portion of the Matagorda Offshore Gathering System are under either a fixed margin or a fixed transportation fee. There is limited competition for the offshore portion of the pipeline. There are currently two pipelines situated in the offshore area but they primarily gather natural gas from wells further offshore than the Matagorda Offshore Gathering System. There are several pipelines that compete with the onshore portion of the system. These competing pipelines result in lower margins for the onshore portion of this system.

Marine Transportation Segment

Industry Overview. The United States inland waterway system is a vast and heavily used transportation system. This inland waterway system is composed of a network of interconnected rivers and canals that serve as water highways and is used to transport vast quantities of products annually. This waterway system extends approximately 26,000 miles, of which 12,000 miles are generally considered significant for domestic commerce.

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The Gulf Coast region is a major hub for petroleum refining. Approximately two-thirds of United States refining capacity expansion in the 1990s occurred in this region. The hydrocarbon refining process generates products and by-products that require transportation in large quantities from the refinery or processor. Convenient access to and use of this waterway system by the petroleum and petrochemical industry is a major reason for the current location of United States refineries and petrochemical facilities. Recent growth in refining and natural gas processing capacity has increased the volume of petroleum products and by-products transported within the Gulf Coast region, which consequently has increased the need for transportation, storage and distribution facilities.

The marine transportation industry uses push boats and tugboats as power sources and tank barges for freight capacity. The combination of the power source and tank barge freight capacity is called a tow.

Marine Fleet. We own a fleet of inland and offshore tows that provide marine transportation of petroleum products and by-products produced in oil refining and natural gas processing. Our marine transportation system operates coastwise along the Gulf of Mexico and on the United States inland waterway system, primarily between domestic ports along the Gulf of Mexico Intracoastal Waterway, the Mississippi River system and the Tennessee-Tombigbee Waterway system. Our inland tows generally consist of one push boat and one to three tank barges, depending upon the horsepower of the push boat, the river or canal capacity and conditions, and customer requirements. Each of our offshore tows consist of one tugboat, with much greater horsepower than an inland push boat, and one large tank barge.

We transport asphalt, fuel oil, gasoline, sulfur and other bulk liquids. The following is a summary description of the marine vessels we use in our marine transportation business:

Class of Equipment	Number in Class	Capacity/Horsepower	Description of Products Carried
Inland tank barges	14	20,000 bbl and under	Asphalt, crude oil, fuel oil, gasoline and sulfur(1)
Inland tank barges	26	20,000 30,000 bbl	Asphalt, crude oil, fuel oil and gasoline(1)
Inland push boats	17	800 3,800 horsepower	N/A
Offshore tank barges	4	40,000 bbl and 95,000 bbl	Asphalt, fuel oil and NGLs
Offshore tugboats	4	3,200 7,200 horsepower	N/A

(1) One of our 14 inland tank barges with capacity of up to 20,000 bbl, and 13 of our 26 inland tank barges with capacity of 20,000 to 30,000 bbl, are specialized and equipped to transport asphalt.

Our largest marine transportation customers include major and independent oil and gas refining companies, petroleum marketing companies and Martin Resource Management. We conduct our marine transportation services under spot contracts and under term contracts that typically range from one to 12 months in length.

In order to maintain a balance of pricing flexibility and stable cash flow, we strive to maintain an appropriate mix of spot versus term contracts, based on current market conditions.

We are a party to a marine transportation agreement effective January 1, 2006 under which we provide marine transportation services to Martin Resource Management on a spot contract basis at applicable market rates. This agreement replaced a prior agreement between us and Martin Resource Management covering marine transportation services which expired in November 2005. Effective each January 1, this agreement automatically renews for consecutive one-year periods unless either party terminates the agreement by giving written notice to the other party at least 60 days prior to the expiration of the then-applicable term. The fees we charge Martin Resource Management are based on applicable market rates.

Competition. We compete primarily with other marine transportation companies. The marine barging industry has experienced significant consolidation in the past few years. The total number of tank barges and push boats that operate in the inland waters of the United States declined from approximately 4,200 in 1982 to approximately 2,900 in 1993 and has reduced to approximately 2,800 since 1993. We believe the earlier decrease primarily resulted from:

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the increasing age of the domestic tank barge fleet, resulting in retirements;

a reduction in tax incentives, which previously encouraged speculative construction of new equipment;