

PHI INC  
Form 10-Q  
November 07, 2011

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**UNITED STATES  
SECURITIES AND EXCHANGE COMMISSION  
Washington, D. C. 20549  
FORM 10-Q**

☒ **Quarterly Report Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934**  
**For the quarterly period ended: September 30, 2011**

**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: 0-9827**

**PHI, Inc.**

(Exact name of registrant as specified in its charter)

**Louisiana**

(State or other jurisdiction of incorporation or  
organization)

**72-0395707**

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

**2001 SE Evangeline Thruway**

**Lafayette, Louisiana**

(Address of principal executive offices)

**70508**

(Zip Code)

Registrant's telephone number, including area code: **(337) 235-2452**

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days.

Yes: ☒ No: ☐

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulations S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files).

Yes: ☒ No: ☐

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

Large accelerated filer: ☐

Accelerated filer: ☒

Non-accelerated filer: ☐  
(Do not check if a smaller  
reporting company)

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: ☒

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

Class

Outstanding at October 28, 2011

Voting Common Stock

2,852,616 shares

Non-Voting Common Stock

12,458,992 shares

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**PHI, INC. AND SUBSIDIARIES**  
**CONDENSED CONSOLIDATED BALANCE SHEETS**  
**(Thousand of dollars)**  
**(Unaudited)**

|  | <b>September<br/>30,<br/>2011</b> | <b>December<br/>31,<br/>2010</b> |
|--|-----------------------------------|----------------------------------|
| <b>ASSETS</b>  |                                   |                                  |
| Current Assets:  |                                   |                                  |
| Cash   | \$ 3,462                          | \$ 3,628                         |
| Short-term investments   | 99,896                            | 150,072                          |
| Accounts receivable net  |                                   |                                  |
| Trade  | 107,326                           | 84,768                           |
| Other  | 761                               | 4,891                            |
| Inventories of spare parts net   | 57,139                            | 59,336                           |
| Other current assets   | 12,968                            | 16,233                           |
| Income taxes receivable  | 926                               | 558                              |
| Total current assets   | 282,478                           | 319,486                          |
| Other  | 33,128                            | 29,120                           |
| Property and equipment net   | 665,219                           | 596,533                          |
| Total assets   | \$ 980,825                        | \$ 945,139                       |
| <b>LIABILITIES AND SHAREHOLDERS EQUITY</b>   |                                   |                                  |
| Current Liabilities:   |                                   |                                  |
| Accounts payable   | \$ 20,757                         | \$ 22,404                        |
| Accrued liabilities  | 37,206                            | 28,319                           |
| Other current liabilities  | 22,900                            |                                  |
| Total current liabilities  | 80,863                            | 50,723                           |
| Long-term debt   | 335,368                           | 331,074                          |
| Deferred income taxes  | 83,110                            | 81,988                           |
| Other long-term liabilities  | 7,383                             | 8,938                            |
| Total liabilities  | 506,724                           | 472,723                          |
| Commitments and contingencies (Note 3)   |                                   |                                  |
| Shareholders Equity:   |                                   |                                  |
| Voting common stock par value of \$0.10: 12,500,000 shares authorized,<br>2,852,616 issued and outstanding | 285<br>1,246                      | 285<br>1,246                     |

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Non-voting common stock par value of \$0.10: 25,000,000 shares authorized,  
12,458,992 issued and outstanding

|                                      |            |            |
|--------------------------------------|------------|------------|
| Additional paid-in capital           | 291,403    | 291,403    |
| Accumulated other comprehensive loss | (111)      | (162)      |
| Retained earnings                    | 181,278    | 179,644    |
| Total shareholders' equity           | 474,101    | 472,416    |
| Total liabilities and equity         | \$ 980,825 | \$ 945,139 |

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

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**PHI, INC. AND SUBSIDIARIES**  
**CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS**  
(Thousands of dollars and shares, except per share data)  
(Unaudited)

|  | <b>Quarter Ended<br/>September 30,</b> |             | <b>Nine Months Ended<br/>September 30,</b> |             |
|--|--|-------------|--|-------------|
|  | <b>2011</b>                            | <b>2010</b> | <b>2011</b>                                | <b>2010</b> |
| Operating revenues, net                      | \$ 145,576                             | \$ 135,669  | \$ 401,192                                 | \$ 396,875  |
| Gain (loss) on dispositions of assets, net   | (638)                                  | 98          | (415)                                      | 221         |
| Other, principally interest income           | 50                                     | 22          | 686  | 58          |
|  | 144,988                                | 135,789     | 401,463                                    | 397,154     |
| Expenses:                                    |  |             |  |             |
| Direct expenses                              | 123,622                                | 115,812     | 352,271                                    | 336,120     |
| Selling, general and administrative expenses | 8,400                                  | 7,688       | 25,679                                     | 22,091      |
| Interest expense                             | 6,997                                  | 4,208       | 20,790                                     | 12,387      |
| Loss on debt restructuring                   |  | 9,521       |  | 9,521       |
|  | 139,019                                | 137,229     | 398,740                                    | 380,119     |
| Earnings (loss) before income taxes          | 5,969                                  | (1,440)     | 2,723                                      | 17,035      |
| Income tax expense                           | 2,387                                  | 1,003       | 1,089                                      | 8,393       |
| Net earnings (loss)                          | \$ 3,582                               | \$ (2,443)  | \$ 1,634                                   | \$ 8,642    |
| Weighted average shares<br>outstanding:      |  |             |  |             |
| Basic  | 15,312                                 | 15,312      | 15,312                                     | 15,312      |
| Diluted                                      | 15,474                                 | 15,312      | 15,474                                     | 15,312      |
| Net earnings (loss) per share:               |  |             |  |             |
| Basic  | \$ 0.23                                | \$ (0.16)   | \$ 0.11                                    | \$ 0.56     |
| Diluted                                      | \$ 0.23                                | \$ (0.16)   | \$ 0.11                                    | \$ 0.56     |

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

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**PHI, INC. AND SUBSIDIARIES**  
**CONDENSED CONSOLIDATED STATEMENTS OF SHAREHOLDERS' EQUITY**  
(Thousands of dollars and shares)  
(Unaudited)

|  | Voting<br>Common Stock |        | Non-Voting<br>Common Stock |          | Additional<br>Paid-in | Accumulated<br>Other<br>Com-<br>prehensive<br>Income<br>(Loss) | Retained<br>Earnings | Total<br>Share-<br>Holders<br>Equity |
|--|------------------------|--------|----------------------------|----------|-----------------------|--|----------------------|--------------------------------------|
|  | Shares                 | Amount | Shares                     | Amount   | Capital               |  |                      |                                      |
| Balance at<br>December 31, 2010                              | 2,853                  | \$ 285 | 12,459                     | \$ 1,246 | \$ 291,403            | \$ (162)   | \$ 179,644           | \$ 472,416                           |
| Net earnings   |                        |        |                            |          |                       |  | 1,634                | 1,634                                |
| Unrealized gain on<br>short-term<br>investments              |                        |        |                            |          |                       | 61   |                      | 61                                   |
| Changes in pension<br>plan assets and<br>benefit obligations |                        |        |                            |          |                       | (10)   |                      | (10)                                 |
| Total<br>comprehensive<br>income                             |                        |        |                            |          |                       |  |                      | 1,685                                |
| Balance at<br>September 30, 2011                             | 2,853                  | \$ 285 | 12,459                     | \$ 1,246 | \$ 291,403            | \$ (111)   | \$ 181,278           | \$ 474,101                           |

**CONDENSED CONSOLIDATED STATEMENTS OF SHAREHOLDERS' EQUITY**

|  | Voting<br>Common Stock |        | Non-Voting<br>Common Stock |          | Additional<br>Paid-in | Accumulated<br>Other<br>Com-<br>prehensive<br>Income<br>(Loss) | Retained<br>Earnings | Total<br>Share-<br>Holders<br>Equity |
|--|------------------------|--------|----------------------------|----------|-----------------------|--|----------------------|--------------------------------------|
|  | Shares                 | Amount | Shares                     | Amount   | Capital               |  |                      |                                      |
| Balance at<br>December 31, 2009                              | 2,853                  | \$ 285 | 12,459                     | \$ 1,246 | \$ 291,403            | \$ (13)  | \$ 172,527           | \$ 465,448                           |
| Net earnings   |                        |        |                            |          |                       |  | 8,642                | 8,642                                |
| Changes in pension<br>plan assets and<br>benefit obligations |                        |        |                            |          |                       | (7)  |                      | (7)                                  |
| Total<br>comprehensive<br>income, net of<br>income taxes     |                        |        |                            |          |                       |  |                      | 8,635                                |

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|                    |       |    |     |        |    |       |    |         |                               |
|--------------------|-------|----|-----|--------|----|-------|----|---------|-------------------------------|
| Balance at         |       |    |     |        |    |       |    |         |                               |
| September 30, 2010 | 2,853 | \$ | 285 | 12,459 | \$ | 1,246 | \$ | 291,403 | \$ (20) \$ 181,169 \$ 474,083 |

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

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**PHI, INC. AND SUBSIDIARIES**  
**CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS**  
(Thousands of dollars)  
(Unaudited)

|   | <b>Nine Months Ended<br/>September 30,</b> |             |
|---|--|-------------|
|   | <b>2011</b>                                | <b>2010</b> |
| <b>Operating activities:</b>  |  |             |
| Net earnings  | \$ 1,634                                   | \$ 8,642    |
| Adjustments to reconcile net earnings to net cash provided by operating activities: |  |             |
| Depreciation  | 23,186                                     | 20,587      |
| Deferred income taxes   | 1,122                                      | 8,058       |
| Gain (loss) on asset dispositions, net  | 415  | (221)       |
| Other   | 832  | 747         |
| Loss on debt restructuring  |  | 9,521       |
| Changes in operating assets and liabilities   | (5,129)                                    | 4,169       |
| Net cash provided by operating activities   | 22,060                                     | 51,503      |
| <b>Investing activities:</b>  |  |             |
| Purchase of property and equipment  | (66,747)                                   | (39,739)    |
| Proceeds from asset dispositions  | 3,804                                      | 1,171       |
| Purchase of short-term investments  | (193,557)                                  | (102,710)   |
| Proceeds from sale of short-term investments  | 241,989                                    | 24,260      |
| Payment on deposits on aircraft   | (13,009)                                   | (3,660)     |
| Refund on deposits on aircraft  | 1,000                                      |             |
| Net cash used in investing activities   | (26,520)                                   | (120,678)   |
| <b>Financing activities:</b>  |  |             |
| Proceeds from issuance of Senior Notes due 2018                                     |  | 300,000     |
| Premium and costs to retire debt early  |  | (7,293)     |
| Repayment of Senior Notes due 2013  |  | (189,490)   |
| Debt issuance costs   |  | (4,982)     |
| Payments on line of credit  | (40,323)                                   | (37,518)    |
| Proceeds from line of credit  | 44,617                                     | 37,500      |
| Net cash provided by financing activities   | 4,294                                      | 98,217      |
| (Decrease) increase in cash   | (166)                                      | 29,042      |
| Cash, beginning of period   | 3,628                                      | 2,501       |
| Cash, end of period   | \$ 3,462                                   | \$ 31,543   |

**Supplemental Disclosures of Cash Flow Information**

Cash paid during the period for:

|          |           |           |
|----------|-----------|-----------|
| Interest | \$ 15,186 | \$ 13,863 |
|----------|-----------|-----------|

|              |        |        |
|--------------|--------|--------|
| Income taxes | \$ 508 | \$ 614 |
|--------------|--------|--------|

Non-cash investing activities:

|  |        |          |
|--|--------|----------|
| Other current liabilities and accrued payables related to purchase of property and equipment | \$ 326 | \$ 1,065 |
|--|--------|----------|

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

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**NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS  
(Unaudited)**

**1. General**

The accompanying unaudited condensed consolidated financial statements include the accounts of PHI, Inc. and subsidiaries ( PHI or the Company or we or our ). In the opinion of management, these condensed consolidated financial statements reflect all adjustments, consisting of only normal, recurring adjustments, necessary to present fairly the financial results for the interim periods presented. These condensed consolidated financial statements should be read in conjunction with the consolidated financial statements contained in the Company's Annual Report on Form 10-K for the year ended December 31, 2010 and the accompanying notes.

The Company's financial results, particularly as they relate to the Company's Oil and Gas operations, are influenced by seasonal fluctuations as discussed in the Company's Annual Report on Form 10-K for the year ended December 31, 2010. Therefore, the results of operations for interim periods are not necessarily indicative of the operating results that may be expected for a full fiscal year.

**2. Segment Information**

PHI is primarily a provider of helicopter services, including helicopter maintenance and repair services. We use a combination of factors to identify reportable segments as required by Accounting Standards Codification 280,

Segment Reporting. The overriding determination of our segments is based on how the chief operating decision maker of our Company evaluates our results of operations. The underlying factors include customer bases, types of service, operational management, physical locations, and underlying economic characteristics of the types of work we perform.

A segment's operating profit is its operating revenues less its direct expenses and selling, general and administrative expenses. Each segment has a portion of selling, general and administrative expenses that are charged directly to the segment and a portion that is allocated. Direct charges represent the vast majority of the segment's selling, general and administrative expenses. Allocated selling, general and administrative expenses are based primarily on total segment direct expenses as a percentage of total direct expenses. Unallocated overhead consists primarily of corporate selling, general, and administrative expenses that we do not allocate to the reportable segments.

Effective June 30, 2011, the Company made changes to the presentation of reportable segments to reflect changes in the way its chief operating decision maker evaluates the performance of its operations, develops strategy and allocates capital resources. These changes resulted from how our chief operating decision maker views the roles of certain corporate departments whose duties had previously been considered company-wide but now are considered to focus solely on our Oil & Gas segment's operations. The change resulted in the reclassification of certain selling, general and administrative expenses from within the Company's unallocated selling, general and administrative expenses to the Oil & Gas segment's selling, general, and administrative expenses. The total amount of the reclassification was \$0.7 million for the three months ended September 30, 2010, and \$2.9 million for the nine months ended September 30, 2010. The Company's historical segment disclosures have been recast to be consistent with the current presentation.

*Oil and Gas Segment.* Our Oil and Gas segment, headquartered in Lafayette, Louisiana, provides helicopter services primarily for the major integrated and independent oil and gas production companies transporting personnel and/or equipment to offshore platforms in the Gulf of Mexico. Our customers include Shell Oil Company, BP America Production Company and ConocoPhillips Company, with whom we have worked for 30 or more years, and ExxonMobil Production Co. and ENI Petroleum, with whom we have worked for more than 15 years. We currently operate 164 aircraft in this segment.

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Operating revenue from the Oil and Gas segment is derived mainly from contracts that include a fixed monthly rate for a particular model of aircraft, plus a variable rate for flight time. Operating costs for the Oil and Gas operations are primarily aircraft operations costs, including costs for pilots and maintenance personnel. Total fuel cost is included in direct expense and reimbursement of a portion of these costs above a contracted per-gallon amount is included in revenue. Our Oil and Gas operations generated approximately 66% of our total operating revenue for the quarters ended September 30, 2011 and 2010, and approximately 66% and 68% of our total operating revenue for the nine months ended September 30, 2011 and 2010, respectively.

*Air Medical Segment.* Air Medical operations are headquartered in Phoenix, Arizona, where we maintain significant separate facilities and administrative staff dedicated to this segment. Those costs are charged directly to the Air Medical segment.

We provide air medical transportation services for hospitals and emergency service agencies in 17 states using approximately 88 aircraft at 64 separate locations. Our Air Medical segment operates primarily under the independent provider model and, to a lesser extent, under the hospital-based model. Under the independent provider model, we have no contracts and no fixed revenue stream, and compete for transport referrals on a daily basis with other independent operators in the area. Under the hospital-based model, we contract directly with the hospital to provide their transportation services, with the contracts typically awarded on a competitive bid basis. For the quarters ended September 30, 2011 and 2010, approximately 32% and 33% of our total operating revenues were generated by our Air Medical operations, respectively. For the nine months ended September 30, 2011 and 2010, approximately 32% and 30% of our total operating revenues were generated by our Air Medical operations, respectively.

As an independent provider, we bill for our services on the basis of a flat rate plus a variable charge per loaded mile, regardless of aircraft model. Revenues are recorded net of contractual allowances under agreements with third party payors and estimated uncompensated care when the services are provided. Contractual allowances and uncompensated care are estimated based on historical collection experience by payor category. The main payor categories are Medicaid, Medicare, Insurance, and Self-Pay. Payor mix and changes in reimbursement rates are the factors most subject to sensitivity and variability in calculating our allowances. We compute a historical payment analysis of accounts fully closed, by category. The allowance percentages calculated are applied to the payor categories, and the necessary adjustments are made to the revenue allowance. The allowance for contractual discounts was \$43.6 million and \$42.2 million as of September 30, 2011 and September 30, 2010, respectively. The allowance for uncompensated care was \$38.4 million and \$36.0 million as of September 30, 2011 and September 30, 2010, respectively.

Provisions for contractual discounts and estimated uncompensated care for Air Medical operations as a percentage of gross billings are as follows:

|                                     | Revenue                        |      |                                    |      |
|-------------------------------------|--------------------------------|------|------------------------------------|------|
|                                     | Quarter Ended<br>September 30, |      | Nine Months Ended<br>September 30, |      |
|                                     | 2011                           | 2010 | 2011                               | 2010 |
| Gross billings                      | 100%                           | 100% | 100%                               | 100% |
| Provision for contractual discounts | 54%                            | 50%  | 54%                                | 52%  |
| Provision for uncompensated care    | 13%                            | 13%  | 10%                                | 11%  |

Net reimbursement per transport from commercial payors generally increases when a rate increase is implemented.

Net reimbursement from certain commercial payors, as well as Medicare and Medicaid, does not increase proportionately with rate increases.

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Net revenue attributable to Medicaid, Medicare, Insurance, and Self-Pay as a percentage of net Air Medical revenues are as follows:

|           | Quarter Ended<br>September 30, |      | Nine Months Ended<br>September 30, |      |
|-----------|--------------------------------|------|------------------------------------|------|
|           | 2011                           | 2010 | 2011                               | 2010 |
| Medicaid  | 15%                            | 15%  | 15%                                | 16%  |
| Medicare  | 24%                            | 22%  | 24%                                | 21%  |
| Insurance | 60%                            | 62%  | 60%                                | 62%  |
| Self-Pay  | 1%                             | 1%   | 1%                                 | 1%   |

We also have a limited number of contracts with hospitals under which we receive a fixed monthly rate for aircraft availability and an hourly rate for flight time. Those contracts generated approximately 19% and 14% of the segment's revenues for the quarters ended September 30, 2011 and 2010, respectively, and approximately 19% and 16% of the segment's revenues for the nine months ended September 30, 2011 and 2010, respectively.

*Technical Services Segment.* The Technical Services segment provides helicopter repair and overhaul services for customer owned aircraft. Costs associated with these services are primarily labor, and customers are generally billed at a percentage above cost. We currently operate five aircraft for the National Science Foundation in Antarctica under this segment.

Approximately 1% of our total operating revenues were generated by our Technical Services operations for the quarters ended September 30, 2011 and September 30, 2010. Approximately 2% of our total operating revenues were generated by our Technical Services operations for the nine months ended September 30, 2011 and September 30, 2010.

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Summarized financial information concerning our reportable operating segments for the quarters and nine months ended September 30, 2011 and 2010 is as follows:

Certain reclassifications have been made to prior fiscal year amounts to conform with the current fiscal year presentation, as discussed above. These changes had no impact on consolidated net sales or operating income.

|  | <b>Quarter Ended<br/>September 30,</b> |             | <b>Nine Months Ended<br/>September 30,</b> |             |
|--|--|-------------|--|-------------|
|  | <b>2011</b>                            | <b>2010</b> | <b>2011</b>                                | <b>2010</b> |
|  | (Thousands of dollars)                 |             | (Thousands of dollars)                     |             |
| Segment operating revenues   |  |             |  |             |
| Oil and Gas  | \$ 96,611                              | \$ 89,797   | \$ 264,292                                 | \$ 269,471  |
| Air Medical  | 46,894                                 | 44,254      | 129,490                                    | 120,924     |
| Technical Services   | 2,071                                  | 1,618       | 7,410                                      | 6,480       |
| Total operating revenues   | 145,576                                | 135,669     | 401,192                                    | 396,875     |
| Segment direct expenses <sup>(1)</sup>                               |  |             |  |             |
| Oil and Gas  | 82,196                                 | 75,679      | 231,573                                    | 221,777     |
| Air Medical  | 39,673                                 | 38,689      | 115,093                                    | 108,700     |
| Technical Services   | 1,753                                  | 1,444       | 5,605                                      | 5,643       |
| Total direct expenses  | 123,622                                | 115,812     | 352,271                                    | 336,120     |
| Segment selling, general and administrative expenses                 |  |             |  |             |
| Oil and Gas  | 905                                    | 814         | 2,670                                      | 3,410       |
| Air Medical  | 1,109                                  | 954         | 2,896                                      | 3,253       |
| Technical Services   | 8                                      | 5           | 27   | 19          |
| Total selling, general and administrative expenses                   | 2,022                                  | 1,773       | 5,593                                      | 6,682       |
| Total direct and selling, general and administrative expenses        | 125,644                                | 117,585     | 357,864                                    | 342,802     |
| Net segment profit   |  |             |  |             |
| Oil and Gas  | 13,510                                 | 13,304      | 30,049                                     | 44,284      |
| Air Medical  | 6,112                                  | 4,611       | 11,501                                     | 8,971       |
| Technical Services   | 310                                    | 169         | 1,778                                      | 818         |
| Total  | 19,932                                 | 18,084      | 43,328                                     | 54,073      |
| Other, net <sup>(2)</sup>  | (588)                                  | 120         | 271  | 279         |
| Unallocated selling, general and administrative costs <sup>(1)</sup> | (6,378)                                | (5,915)     | (20,086)                                   | (15,409)    |
| Interest expense   | (6,997)                                | (4,208)     | (20,790)                                   | (12,387)    |
| Loss on debt restructuring   |  | (9,521)     |  | (9,521)     |

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|                              |          |            |          |           |
|------------------------------|----------|------------|----------|-----------|
| Earnings before income taxes | \$ 5,969 | \$ (1,440) | \$ 2,723 | \$ 17,035 |
|------------------------------|----------|------------|----------|-----------|

(1) Included in direct expenses and unallocated selling, general, and administrative costs are the depreciation expense amounts below:

|                    | <b>Quarter Ended<br/>September 30,</b> |             | <b>Nine Months Ended<br/>September 30,</b> |             |
|--------------------|--|-------------|--|-------------|
|                    | <b>2011</b>                            | <b>2010</b> | <b>2011</b>                                | <b>2010</b> |
| Oil and Gas        | \$ 5,473                               | \$ 4,814    | \$ 15,798                                  | \$ 13,521   |
| Air Medical        | 2,095                                  | 1,990       | 6,354                                      | 5,941       |
| Technical Services | (1)                                    | 8           | 95   | 153         |
| Total              | \$ 7,567                               | \$ 6,812    | \$ 22,247                                  | \$ 19,615   |
| Unallocated SG&A   | \$ 303                                 | \$ 333      | \$ 940                                     | \$ 972      |

(2) Consists of gains (losses) on dispositions of property and equipment, and other income.

**Table of Contents****3. Commitments and Contingencies**

*Commitments* In 2010, we executed a contract to acquire ten new medium aircraft related to our new contract with a major customer. Four of these aircraft have been delivered. The remaining six are scheduled for delivery in late 2011 and through late 2012, with an aggregate acquisition cost of approximately \$73.6 million. We have traded in two aircraft in exchange for a credit of approximately \$20.3 million towards these acquisition costs, of which a credit of \$13.5 million remained as of September 30, 2011.

During the second quarter of 2011, we entered into a contract to acquire six new heavy transport aircraft for an aggregate purchase price of approximately \$148.0 million. In June 2011, we took initial delivery of the first two baseline aircraft and title passed to PHI. The aircraft will be finally delivered in November 2011 when completion services are finished. In conjunction with the initial delivery of the baseline aircraft, we obtained short-term financing for the \$45.8 million initial delivery payment, which was recorded in other current liabilities. In September, we obtained an operating lease for one aircraft for \$22.9 million. We intend to fund the second aircraft with an operating lease with a commercial bank at final delivery in November. Two of the remaining aircraft have an initial delivery date in late 2011, and the balance of the deliveries will occur in 2012. These aircraft will be utilized in our Oil and Gas segment.

Due to anticipated increases in accelerated tax depreciation from our planned purchases of aircraft, net operating losses for tax purposes will increase in future years. Because of the net operating loss increases, certain foreign tax credits and certain net operating losses available in three states will not be used and will expire due to the time limit on the carry-forward of those credits. This resulted in a charge to tax expense of \$1.5 million during the quarter ended September 30, 2010. The \$1.5 million charge resulted in a variation in the customary relationship between the Company's loss before income taxes and income tax expense for that period. For the quarter and nine months ended September 30, 2011, our income tax expense was computed at our estimated annual effective tax rate of forty percent. Total aircraft deposits of \$24.2 million are included in Other Assets. This amount represents deposits for the medium and heavy transport aircraft contracts.

*Environmental Matters* We have recorded an aggregate estimated probable liability of \$0.2 million as of September 30, 2011 for environmental response costs. The Company has conducted environmental surveys of its former Lafayette facility located at the Lafayette Regional Airport, which it vacated in 2001, and has determined that limited soil and groundwater contamination exists at the facility. The Company has installed groundwater monitoring wells at the facility and periodically monitors and reports on the contamination to the Louisiana Department of Environmental Quality ( LDEQ ). The Company previously submitted a Risk Evaluation Corrective Action Plan (RECAP) Standard Site Assessment Report to the LDEQ fully delineating the extent and type of contamination and updated the Report to include additional analytical data in April 2006. LDEQ reviewed the Assessment Report and requested a Corrective Action Plan from the Company. LDEQ approved the Corrective Action Plan ( CAP ) for the remediation of the former PHI Plant I location on August 23, 2010. All Louisiana Department of Natural Resources ( DNR ) approvals were received and the project began on May 16, 2011. Sampling will be performed on a quarterly basis over the next year to evaluate the effectiveness of remedial actions. Based upon the May 2003 Site Assessment Report, the April 2006 update, ongoing monitoring, and the August 2010 CAP, the Company believes the ultimate remediation costs for the former Lafayette facility will not be material to its consolidated financial position, results of operations, or cash flows.

*Legal Matters* The Company is named as a defendant in various legal actions that have arisen in the ordinary course of business and have not been finally adjudicated. In the opinion of management, the amount of the liability with respect to these actions will not have a material effect on the Company's consolidated financial position, results of operations, or cash flows.

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Superior Offshore International Inc. v. Bristow Group Inc., ERA Helicopters, LLC, Seacor Holdings Inc., ERA Group Inc., ERA Aviation, Inc., and PHI, Inc., Civil Action No. 1:09-cv-00438 on the docket of the United States District Court for the District of Delaware. This purported class action was filed on June 12, 2009, on behalf of a class defined to include all direct purchasers of offshore helicopter services in the Gulf of Mexico from the defendants at any time from January 1, 2001 through December 31, 2005. The suit alleged that the defendants acted jointly to fix, maintain, or stabilize prices for offshore helicopter services during the above time frame in violation of the federal antitrust laws. The plaintiff sought unspecified treble damages, injunctive relief, costs, and attorneys' fees. On September 14, 2010, the Court granted defendants' motion to dismiss (filed on September 4, 2009) and dismissed the complaint. On November 30, 2010, the court granted plaintiff leave to amend the complaint, limited discovery to the new allegations, and established a schedule for briefing dispositive motions. The defendants filed a motion for summary judgment on February 11, 2011. On June 23, 2011, the court granted the defendants' motion for summary judgment, entered final judgment in favor of the defendants, and dismissed all of the plaintiff's claims. On July 22, 2011, the plaintiff filed a notice of appeal with the U.S. Court of Appeals, Third Circuit, and on October 11, 2011 filed its appeal brief. Given that plaintiff has not succeeded in advancing its claim beyond dispositive motions, management currently believes that the likelihood of loss to the Company from the litigation is remote.

As previously reported, the Company has been involved in Federal Court litigation in the Western District of Louisiana and the Fifth Circuit Court of Appeals with the Office and Professional Employees International Union (OPEIU), the union representing the Company's domestic pilots. This litigation involves claims of bad faith bargaining, compensation of striking pilots both at the time of the strike and upon their return to work under both the Railway Labor Act (RLA) and Louisiana state law, and the terms of employment for the Company's pilots since the strike ended including non-payment of retention bonuses. After approximately two years of bargaining between the Company and OPEIU for a second collective bargaining agreement, including negotiations mediated by the National Mediation Board, both parties entered a self-help period as defined by the applicable labor law, the RLA. At that time the pilots commenced a strike in September 2006 and immediately prior to that strike the Company implemented its own terms and conditions of employment for the pilots. The strike ended in November 2006 and a court-approved return to work process began in January 2007 for those pilots who had not already returned to work or left the Company's employment. This process was essentially completed in April 2007. The Company's pilots continue to work under the terms and conditions of employment determined by the Company since the strike began. By Order dated July 9, 2010, the Court dismissed both the Company's and OPEIU's claims that the other had violated the RLA by bargaining in bad faith before exercising self-help. By Order dated July 30, 2010, the Court dismissed all claims that the Company violated the RLA in the manner in which it returned pilots to work following the strike. Also, the Court dismissed all but claims by 47 pilots under Louisiana state law. On August 27, 2010, the OPEIU and the individual pilot plaintiffs filed a notice of appeal with the Fifth Circuit Court of Appeals. Then, by Order entered September 27, 2010, the district court dismissed the Louisiana-law claims of the remaining 47 individual pilots. On October 22, 2010, the unions and the individual pilots filed a second notice of appeal to the Fifth Circuit Court of Appeals, by which they appeal the district court's dismissal of all their RLA and Louisiana-law wage payment claims against PHI. On November 5, 2010, PHI filed a cross-appeal of the district court's dismissal of PHI's bad-faith bargaining claim against the unions. By orders dated September 12, 2011, the Fifth Circuit Court of Appeals affirmed the dismissal of all claims brought against PHI by the OPEIU and the individual pilots, whether under the RLA or Louisiana law. That Court also remanded the Return-to-Work case to the district court for the sole purpose of calculating court costs payable to PHI. The OPEIU and individual pilots did not seek rehearing of the Fifth Circuit's judgment within the time permitted by the rules of appellate procedure. However, they have until approximately December 2, 2011 to file a petition for a writ of certiorari from the United States Supreme Court.

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On December 31, 2009, the OPEIU filed another case against the Company in the Western District of Louisiana in which the OPEIU asserts that its acceptance in 2009 of the terms and conditions of employment for the Company's pilots initially implemented by the Company prior to the strike has created a binding collective bargaining agreement and that the Company has inappropriately made unilateral revisions to those terms including failing to pay a retention bonus. The Court administratively stayed this case pending the completion of appellate briefing in the consolidated cases, which briefing concluded on April 15, 2011. The Court further administratively stayed this case pending the appellate court's decision in the consolidated cases described above, which cases have now been resolved by the September 12 judgments of the Fifth Circuit Court of Appeals described above. We therefore expect the district court to lift the administrative stay of this case at any time (the Court has not yet done so) and for discovery and/or motion practice to commence in this case. Management does not expect the outcome of this litigation to have a material effect on our consolidated financial position, results of operations or cash flows.

**Operating Leases** We lease certain aircraft, facilities, and equipment used in our operations. The related lease agreements, which include both non-cancelable and month-to-month terms, generally provide for fixed monthly rentals, and certain real estate leases also include renewal options. We generally pay all insurance, taxes, and maintenance expenses associated with these leases. Some of the facility leases contain renewal options. Aircraft leases contain purchase options exercisable at certain dates in the lease agreements.

At September 30, 2011, we had approximately \$156.9 million in aggregate commitments under operating leases of which approximately \$7.2 million is payable through December 31, 2011, and a total of \$28.3 million is payable over the twelve months ending September 30, 2012. The total lease commitments include \$142.3 million for aircraft and \$14.6 million for facility lease commitments.

As of September 30, 2011, we had options to purchase aircraft under lease becoming exercisable in 2012 through 2014 for the following aggregate purchase prices, respectively: \$45.0 million, \$38.8 million and \$114.4 million. Subject to market conditions, we intend to exercise these options as they become exercisable. There are no other lease purchase options in 2011.

**4. Long-term Debt**

As of September 30, 2011, our total long-term indebtedness was \$335.4 million, consisting of \$300 million of our 8.625% Senior Notes due 2018 (the 8.625% Senior Notes), and \$35.4 million borrowed under our revolving credit facility.

On September 23, 2010, we issued \$300 million of 8.625% Senior Notes that mature in 2018. Interest is payable semi-annually in arrears on April 15 and October 15 of each year. Net proceeds of \$295.5 million were used to repurchase \$189.5 million of our \$200 million outstanding 7.125% Senior Notes due 2013 (the 7.125% Senior Notes) pursuant to a tender offer and consent solicitation that also settled on September 23, 2010. Our total cost to repurchase those notes was \$9.5 million, including the tender offer premium of \$7.6 million and \$1.9 million of unamortized issuance costs. We called for redemption on October 25, 2010 the remaining \$10.5 million of 7.125% Senior Notes outstanding, at a redemption price of 103.563% of their face amount plus accrued interest.

Mr. Al A. Gonsoulin, our Chairman and CEO and the Matzke Family Trust, of which Richard Matzke, one of our directors, is trustee, purchased \$2 million and \$1 million of the 8.625% Senior Notes, respectively.

The 8.625% Senior Notes are unconditionally guaranteed on a senior basis by our domestic subsidiaries, and are general, unsecured obligations of ours and the subsidiary guarantors. We have the option to redeem some or all of the notes at any time on or after October 15, 2014 at specified redemption prices, and prior to that time pursuant to certain make-whole provisions.

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The 8.625% Senior Notes contain restrictive covenants, including limitations on incurring indebtedness, creating liens, selling assets and entering into certain transactions with affiliates. The covenants limit our ability to pay cash dividends on common stock, repurchase or redeem common or preferred equity, prepay subordinated debt and make certain investments. There are no restrictions on dividends from a subsidiary to the parent company, nor any restrictions on contributions from the parent company to a subsidiary. Upon the occurrence of a Change in Control (as defined in the indenture governing the notes), each holder of the notes will have the right to require us purchase that holder's notes for a cash price equal to 101% of their principal amount. Upon the occurrence of an Event of Default (as defined in the indenture), the trustee or the holders of the notes may declare all of the outstanding notes to be due and payable immediately. We were in compliance with the covenants applicable to the notes as of September 30, 2011. On September 26, 2011, we amended our senior secured revolving credit facility to extend the maturity date from September 1, 2012 to September 1, 2013. The facility permits borrowings up to \$75 million, contains a borrowing base of 80% of eligible receivables (as defined in the credit agreement) and 50% of the value of parts. The interest rate is the prime rate plus 100 basis points. We may prepay the revolving credit facility at any time in whole or in part without premium or penalty. All obligations under the revolving credit facility are secured by a perfected first priority security interest in all of our eligible receivables and parts, and are guaranteed by certain of our domestic subsidiaries. As of September 30, 2011, we had \$35.4 million in borrowings under the facility. As of December 31, 2010, we had \$31.1 million in borrowings under the facility. We maintain a separate letter of credit facility that had \$5.5 million in letters of credit outstanding as of September 30, 2011 and December 31, 2010. During the nine months ended September 30, 2011 and 2010, the weighted average effective interest rate on amounts borrowed under the revolving credit facility was 4.25%. We reviewed interest expense for the quarters ended September 30, 2011 and 2010 that could be capitalized for certain projects and any such amounts were immaterial.

The revolving credit facility includes financial covenants related to working capital, funded debt to consolidated net worth, and consolidated net worth, and other covenants including restrictions on additional debt, liens and a change of control. Events of default include a change of control, a default in any other material credit agreement, including the 8.625% Senior Notes, and customary events of default. As of September 30, 2011, we were in compliance with all of the covenants under the revolving credit facility.

Our \$300 million outstanding 8.625% Senior Notes bear interest at a fixed rate of 8.625% and therefore changes in market interest rates do not affect our interest payment obligations on the notes. The fair market value of our 8.625% Senior Notes will vary as changes occur to general market interest rates, the remaining maturity of the notes, and our credit worthiness. At September 30, 2011, the market value of the notes was approximately \$300.3 million, based on quoted market indications.

**5. Valuation Accounts**

We have established an allowance for doubtful accounts based upon factors surrounding the credit risk of specific customers, current market conditions, and other information. The allowance for doubtful accounts was approximately \$0.1 million at September 30, 2011 and December 31, 2010.

Revenues related to emergency flights generated by the Company's Air Medical segment are recorded net of contractual allowances under agreements with third party payors and estimated uncompensated care when the services are provided. The allowance for contractual discounts was \$43.6 million and \$34.7 million as of September 30, 2011 and December 31, 2010, respectively. The allowance for uncompensated care was \$38.4 million and \$39.3 million as of September 30, 2011 and December 31, 2010, respectively.

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The allowance for contractual discounts and estimated uncompensated care as a percentage of gross accounts receivable are as follows:

|                                     | September<br>30,<br>2011 | December<br>31,<br>2010 |
|-------------------------------------|--------------------------|-------------------------|
| Gross Accounts Receivable           | 100%                     | 100%                    |
| Allowance for Contractual Discounts | 37%                      | 33%                     |
| Allowance for Uncompensated Care    | 33%                      | 37%                     |

We have also established valuation reserves related to obsolete and excess inventory. The inventory valuation reserves were \$12.4 million at September 30, 2011 and \$11.4 million at December 31, 2010.

**6. Employee Compensation**

*Employee Incentive Compensation* Pursuant to our incentive compensation plans, we accrued \$0.5 million for the quarter and nine months ended September 30, 2011. We accrued \$1.0 million and \$2.3 million incentive compensation expense for the quarter and nine months ended September 30, 2010, respectively.

We also have a Safety Incentive Plan related to Occupational Safety and Health Administration recordable incidents, for which we expensed \$0.1 million and \$0.5 million for the quarter and nine months ended September 30, 2011, respectively. For the quarter and nine months ended September 30, 2010, we expensed \$0.2 million and \$0.5 million, respectively.

**7. Fair Value Measurements**

Accounting standards require that assets and liabilities carried at fair value will be classified and disclosed in one of the following three categories:

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

Level 2: Observable market based inputs or unobservable inputs that are corroborated by market data.

Level 3: Unobservable inputs that are not corroborated by market data.

The following table summarizes the valuation of our short-term investments and financial instruments by the above pricing levels as of the valuation dates listed:

|                             | <b>Total</b>           | September 30, 2011<br>(Level 1) | (Level 2) |
|-----------------------------|------------------------|---------------------------------|-----------|
|                             | (Thousands of dollars) |                                 |           |
| Short-term investments:     |                        |                                 |           |
| Money Market Mutual Funds   | \$ 59,695              | \$ 59,695                       | \$        |
| Commercial Paper            | 2,989                  |                                 | 2,989     |
| Corporate bonds and notes   | 37,212                 |                                 | 37,212    |
|                             | 99,896                 | 59,695                          | 40,201    |
| Investments in other assets | 2,699                  | 2,699                           |           |
| Total                       | \$ 102,595             | \$ 62,394                       | \$ 40,201 |

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|                             |              | December 31, 2010<br>(Level 1) (Level 2)<br>(Thousands of dollars) |            |
|-----------------------------|--------------|--|------------|
|                             | <b>Total</b> |  |            |
| Short-term investments:     |              |  |            |
| Money Market Mutual Funds   | \$ 33,968    | \$ 33,968  | \$         |
| Commercial Paper            | 42,455       |  | 42,455     |
| U.S. Government Agencies    | 8,013        |  | 8,013      |
| Corporate bonds and notes   | 65,636       |  | 65,636     |
|                             | 150,072      | 33,968   | 116,104    |
| Investments in other assets | 3,547        | 3,547  |            |
| Total                       | \$ 153,619   | \$ 37,515  | \$ 116,104 |

The Company holds its short-term investments in an investment fund consisting of high quality money market instruments of governmental and private issuers, which is classified as short-term investments. Level 1 inputs are quoted prices (unadjusted) for identical assets or liabilities in active markets. These items are traded with sufficient frequency and volume to provide pricing on an ongoing basis. The fair values of the shares of these funds are based on observable market prices, and therefore, have been categorized in Level 1 in the fair value hierarchy. Level 2 inputs reflect quoted prices for identical assets or liabilities that are not active. These items may not be traded daily; examples include corporate bonds and U.S. government agencies. Assets are valued based on prices derived by independent third parties that use inputs such as benchmark yields, reported trades, broker/dealer quotes, and issuer spreads. Prices are reviewed and can be challenged with the independent parties and/or overridden by the Company, if it is believed such would be more reflective of fair value. Investments included in other assets, which relate to the liability for the Officers' Deferred Compensation Plan, consist mainly of multiple investment funds that are highly liquid and diversified.

Cash, accounts receivable, accounts payable and accrued liabilities all had fair values approximating their carrying amounts at September 30, 2011 and December 31, 2010.

**8. Investments**

We classify all of our short-term investments as available-for-sale. We carry these at fair value and report unrealized gains and losses, net of taxes, in other comprehensive income until realized. These gains and losses are reflected as a separate component of shareholders' equity in our consolidated balance sheets and our consolidated statements of shareholders' equity. Cost, gains, and losses are determined using the specific identification method.

Investments consisted of the following as of September 30, 2011:

|                             | Cost      | Unrealized<br>Gains<br>(Thousands of dollars) | Unrealized<br>Losses | Fair<br>Value |
|-----------------------------|-----------|---|----------------------|---------------|
| Short-term investments:     |           |   |                      |               |
| Money Market Mutual Funds   | \$ 59,695 | \$  | \$                   | \$ 59,695     |
| Commercial Paper            | 2,996     |   | (7)                  | 2,989         |
| Corporate bonds and notes   | 37,340    | 14  | (142)                | 37,212        |
| Subtotal                    | 100,031   | 14  | (149)                | 99,896        |
| Investments in other assets | 2,699     |   |                      | 2,699         |

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|       |            |       |          |            |
|-------|------------|-------|----------|------------|
| Total | \$ 102,730 | \$ 14 | \$ (149) | \$ 102,595 |
|-------|------------|-------|----------|------------|

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Investments consisted of the following as of December 31, 2010:

|                             | Cost       | Unrealized<br>Gains<br>(Thousands of dollars) | Unrealized<br>Losses<br>(Thousands of dollars) | Fair<br>Value |
|-----------------------------|------------|---|--|---------------|
| Short-term investments:     |            |   |  |               |
| Money Market Mutual Funds   | \$ 33,968  | \$  | \$   | \$ 33,968     |
| Commercial Paper            | 42,471     |   | (16)   | 42,455        |
| U.S. Government Agencies    | 8,022      |   | (10)   | 8,012         |
| Corporate bonds and notes   | 65,847     | 4   | (214)  | 65,637        |
| Subtotal                    | 150,308    | 4   | (240)  | 150,072       |
| Investments in other assets | 3,547      |   |  | 3,547         |
| Total                       | \$ 153,855 | \$ 4  | \$ (240)                                       | \$ 153,619    |

The following table presents the cost and fair value of our debt investments based on maturities as of September 30, 2011.

|                         | Amortized<br>Cost<br>(Thousands of dollars) | Fair<br>Value |
|-------------------------|---|---------------|
| Due in one year or less | \$ 28,589                                   | \$ 28,493     |
| Due within two years    | 11,747                                      | 11,708        |
| Total                   | \$ 40,336                                   | \$ 40,201     |

The following table presents the cost and fair value of our debt investments based on maturities as of December 31, 2010.

|                         | Amortized<br>Cost<br>(Thousands of dollars) | Fair<br>Value |
|-------------------------|---|---------------|
| Due in one year or less | \$ 58,740                                   | \$ 58,704     |
| Due within two years    | 57,600                                      | 57,400        |
| Total                   | \$ 116,340                                  | \$ 116,104    |

The following table presents the average coupon rate percentage and the average days to maturity of our debt investments as of September 30, 2011.

|                           | Average<br>Coupon<br>Rate (%) | Average<br>Days To<br>Maturity |
|---------------------------|-------------------------------|--------------------------------|
| Commercial Paper          | 0.260                         | 172                            |
| Corporate bonds and notes | 5.215                         | 273                            |

The following table presents the fair value and unrealized losses related to our investments that have been in a continuous unrealized loss position for less than twelve months as of September 30, 2011.

|                           | Fair<br>Value<br>(Thousands of dollars) | Unrealized<br>Losses |
|---------------------------|---|----------------------|
| Commercial Paper          | \$ 2,996                                | \$ (7)               |
| Corporate bonds and notes | 31,420                                  | (142)                |
|                           | \$ 34,416                               | \$ (149)             |

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The following table presents the fair value and unrealized losses related to our investments that have been in a continuous unrealized loss position for less than twelve months as of December 31, 2010.

|                           | Fair<br>Value<br>(Thousands of dollars) | Unrealized<br>Losses |
|---------------------------|---|----------------------|
| Commercial Paper          | \$ 42,471                               | \$ (16)              |
| U.S. Government Agencies  | 3,993                                   | (10)                 |
| Corporate bonds and notes | 60,501                                  | (214)                |
|                           | \$ 106,965                              | \$ (240)             |

As of September 30, 2011 and December 31, 2010, we had no investments in a continuous unrealized loss position for more than twelve months.

We consider the decline in market value to be due to market conditions, and we do not plan to sell these investments prior to a recovery of cost. For these reasons, we do not consider any of our investments to be other than temporarily impaired at September 30, 2011. The assessment of whether an investment in a debt security has suffered an other-than-temporary impairment is based on whether the Company has the intent to sell or more likely than not will be required to sell the debt security before recovery of its amortized costs. Further, if the Company does not expect to recover the entire amortized cost basis of the debt security, an other-than-temporary impairment is considered to have occurred and it is measured by the present value of cash flows expected to be collected less the amortized cost basis (credit loss). The Company did not have any other-than-temporary impairments relating to credit losses on debt securities for the nine months ended September 30, 2011.

**9. Shareholders' Equity**

We had an average of 15.3 million common shares outstanding for the quarters ended September 30, 2011 and 2010. Accumulated other comprehensive loss is included in the shareholders' equity section of the condensed consolidated balance sheets of the Company. Accumulated other comprehensive loss in the condensed consolidated balance sheets included the following components:

|  | September<br>30,<br>2011 | December<br>31,<br>2010 |
|--|--------------------------|-------------------------|
| Unrealized gain (loss) on short-term investments       | \$ (81)                  | \$ (142)                |
| Changes in pension plan assets and benefit obligations | (30)                     | (20)                    |
|  | \$ (111)                 | \$ (162)                |

**10. Condensed Consolidating Financial Information**

PHI, Inc. issued 8.625% Senior Notes that are fully and unconditionally guaranteed on a joint and several, senior basis by all of our domestic subsidiaries. All of our domestic subsidiaries are 100% owned.

The following supplemental condensed financial information sets forth, on a consolidated basis, the balance sheet, statement of operations, and statement of cash flows information for PHI, Inc. ( Parent Company Only ) and the guarantor subsidiaries. The eliminating entries eliminate investments in subsidiaries, intercompany balances, and intercompany revenues and expenses. The condensed consolidating financial statements have been prepared on the same basis as the consolidated financial statements of PHI, Inc. The equity method is followed by the parent company within these financials.

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**PHI, INC. AND SUBSIDIARIES**  
**CONDENSED CONSOLIDATING BALANCE SHEETS**  
(Thousands of dollars)  
(Unaudited)

|   | <b>September 30, 2011</b>          |   |                     |                     |
|---|------------------------------------|---|---------------------|---------------------|
|   | <b>Parent<br/>Company<br/>Only</b> | <b>Guarantor<br/>Subsidiaries<sup>(1)</sup></b> | <b>Eliminations</b> | <b>Consolidated</b> |
| <b>ASSETS</b>   |                                    |   |                     |                     |
| Current Assets:                                       |                                    |   |                     |                     |
| Cash  | \$ 2,799                           | \$ 663  | \$                  | \$ 3,462            |
| Short-term investments                                | 99,896                             |   |                     | 99,896              |
| Accounts receivable net                               | 97,968                             | 10,119  |                     | 108,087             |
| Intercompany receivable                               |                                    | 90,245  | (90,245)            |                     |
| Inventories of spare parts net                        | 57,139                             |   |                     | 57,139              |
| Other current assets                                  | 12,958                             | 10  |                     | 12,968              |
| Income taxes receivable                               | 926                                |   |                     | 926                 |
| Total current assets                                  | 271,686                            | 101,037   | (90,245)            | 282,478             |
| Investment in subsidiaries and other                  | 79,798                             |   | (79,798)            |                     |
| Other assets  | 33,106                             | 22  |                     | 33,128              |
| Property and equipment net                            | 654,497                            | 10,722  |                     | 665,219             |
| Total assets  | \$ 1,039,087                       | \$ 111,781                                      | \$ (170,043)        | \$ 980,825          |
| <b>LIABILITIES AND SHAREHOLDERS<br/>EQUITY</b>        |                                    |   |                     |                     |
| Current Liabilities:                                  |                                    |   |                     |                     |
| Accounts payable                                      | \$ 19,134                          | \$ 1,623  | \$                  | \$ 20,757           |
| Accrued liabilities                                   | 29,553                             | 7,653   |                     | 37,206              |
| Other current liabilities                             | 22,900                             |   |                     | 22,900              |
| Intercompany payable                                  | 90,245                             |   | (90,245)            |                     |
| Total current liabilities                             | 161,832                            | 9,276   | (90,245)            | 80,863              |
| Long-term debt  | 335,368                            |   |                     | 335,368             |
| Deferred income taxes and other long-term liabilities | 67,786                             | 22,707  |                     | 90,493              |
| Shareholders' Equity:                                 |                                    |   |                     |                     |
| Common stock and paid-in capital                      | 292,934                            | 2,674   | (2,674)             | 292,934             |
| Accumulated other comprehensive loss                  | (111)                              |   |                     | (111)               |
| Retained earnings                                     | 181,278                            | 77,124  | (77,124)            | 181,278             |
| Total shareholders' equity                            | 474,101                            | 79,798  | (79,798)            | 474,101             |

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|   |              |            |              |            |
|---|--------------|------------|--------------|------------|
| Total liabilities and shareholders equity | \$ 1,039,087 | \$ 111,781 | \$ (170,043) | \$ 980,825 |
|---|--------------|------------|--------------|------------|

(1) Foreign subsidiaries represent minor subsidiaries and are included in the guarantors subsidiaries amounts.

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**PHI, INC. AND SUBSIDIARIES**  
**CONDENSED CONSOLIDATING BALANCE SHEETS**  
(Thousands of dollars)

|   | <b>December 31, 2010</b>           |   |                     |                     |
|---|------------------------------------|---|---------------------|---------------------|
|   | <b>Parent<br/>Company<br/>Only</b> | <b>Guarantor<br/>Subsidiaries<sup>(1)</sup></b> | <b>Eliminations</b> | <b>Consolidated</b> |
| <b>ASSETS</b>   |                                    |   |                     |                     |
| Current Assets:                                       |                                    |   |                     |                     |
| Cash  | \$ 2,957                           | \$ 671  | \$                  | \$ 3,628            |
| Short-term investments                                | 150,072                            |   |                     | 150,072             |
| Accounts receivable net                               | 81,393                             | 8,266   |                     | 89,659              |
| Intercompany receivable                               |                                    | 79,810  | (79,810)            |                     |
| Inventories of spare parts net                        | 59,336                             |   |                     | 59,336              |
| Other current assets                                  | 16,224                             | 9   |                     | 16,233              |
| Income taxes receivable                               | 558                                |   |                     | 558                 |
| Total current assets                                  | 310,540                            | 88,756  | (79,810)            | 319,486             |
| Investment in subsidiaries and others                 | 75,114                             |   | (75,114)            |                     |
| Other assets  | 29,099                             | 21  |                     | 29,120              |
| Property and equipment, net                           | 583,091                            | 13,442  |                     | 596,533             |
| Total assets  | \$ 997,844                         | \$ 102,219                                      | \$ (154,924)        | \$ 945,139          |
| <b>LIABILITIES AND SHAREHOLDERS EQUITY</b>            |                                    |   |                     |                     |
| Current Liabilities:                                  |                                    |   |                     |                     |
| Accounts payable                                      | \$ 22,191                          | \$ 213  | \$                  | \$ 22,404           |
| Accrued liabilities                                   | 23,482                             | 4,837   |                     | 28,319              |
| Intercompany payable                                  | 79,810                             |   | (79,810)            |                     |
| Total current liabilities                             | 125,483                            | 5,050   | (79,810)            | 50,723              |
| Long-term debt  | 331,074                            |   |                     | 331,074             |
| Deferred income taxes and other long-term liabilities | 68,871                             | 22,055  |                     | 90,926              |
| Shareholders' Equity:                                 |                                    |   |                     |                     |
| Common stock and paid-in capital                      | 292,934                            | 2,674   | (2,674)             | 292,934             |
| Accumulated other comprehensive loss                  | (162)                              |   |                     | (162)               |
| Retained earnings                                     | 179,644                            | 72,440  | (72,440)            | 179,644             |
| Total shareholders' equity                            | 472,416                            | 75,114  | (75,114)            | 472,416             |
| Total liabilities and shareholders' equity            | \$ 997,844                         | \$ 102,219                                      | \$ (154,924)        | \$ 945,139          |

- (1) Foreign subsidiaries represent minor subsidiaries and are included in the guarantors' subsidiaries amounts.
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**PHI, INC. AND SUBSIDIARIES**  
**CONDENSED CONSOLIDATING STATEMENTS OF OPERATIONS**  
(Thousands of dollars)  
(Unaudited)

**For the quarter ended September 30, 2011**

|   | <b>Parent<br/>Company<br/>Only</b> | <b>Guarantor<br/>Subsidiaries<sup>(1)</sup></b> | <b>Eliminations</b> | <b>Consolidated</b> |
|---|------------------------------------|---|---------------------|---------------------|
| Operating revenues, net                           | \$ 130,180                         | \$ 15,396                                       | \$                  | \$ 145,576          |
| Management fees                                   | 616                                |   | (616)               |                     |
| Gain on dispositions of assets, net               | (638)                              |   |                     | (638)               |
| Other, principally interest income                | 50                                 |   |                     | 50                  |
|   | 130,208                            | 15,396  | (616)               | 144,988             |
| Expenses:   |                                    |   |                     |                     |
| Direct expenses                                   | 111,133                            | 12,489  |                     | 123,622             |
| Management fees                                   |                                    | 616   | (616)               |                     |
| Selling, general and administrative expenses      | 8,076                              | 324   |                     | 8,400               |
| Equity in net income of consolidated subsidiaries | (1,181)                            |   | 1,181               |                     |
| Interest expense                                  | 6,997                              |   |                     | 6,997               |
|   | 125,025                            | 13,429  | 565                 | 139,019             |
| Earnings before income taxes                      | 5,183                              | 1,967   | (1,181)             | 5,969               |
| Income tax expense                                | 1,601                              | 786   |                     | 2,387               |
| Net earnings                                      | \$ 3,582                           | \$ 1,181  | \$ (1,181)          | \$ 3,582            |

**For the quarter ended September 30, 2010**

|                                     | <b>Parent<br/>Company<br/>Only</b> | <b>Guarantor<br/>Subsidiaries<sup>(1)</sup></b> | <b>Eliminations</b> | <b>Consolidated</b> |
|-------------------------------------|------------------------------------|---|---------------------|---------------------|
| Operating revenues, net             | \$ 120,381                         | \$ 15,288                                       | \$                  | \$ 135,669          |
| Management fees                     | 611                                |   | (611)               |                     |
| Gain on dispositions of assets, net | 98                                 |   |                     | 98                  |
| Other, principally interest income  | 22                                 |   |                     | 22                  |
|                                     | 121,112                            | 15,288  | (611)               | 135,789             |

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|   |            |        |          |            |
|---|------------|--------|----------|------------|
| Expenses:   |            |        |          |            |
| Direct expenses                                   | 102,934    | 12,878 |          | 115,812    |
| Management fees                                   |            | 611    | (611)    |            |
| Selling, general and administrative expenses      | 7,371      | 317    |          | 7,688      |
| Equity in net income of consolidated subsidiaries | (889)      |        | 889      |            |
| Interest expense                                  | 4,208      |        |          | 4,208      |
| Loss on debt restructuring                        | 9,521      |        |          | 9,521      |
|   | 123,145    | 13,806 | 278      | 137,229    |
| (Loss) earnings before income taxes               | (2,033)    | 1,482  | (889)    | (1,440)    |
| Income tax expense                                | 410        | 593    |          | 1,003      |
| Net (loss) earnings                               | \$ (2,443) | \$ 889 | \$ (889) | \$ (2,443) |

(1) Foreign subsidiaries represent minor subsidiaries and are included in the guarantors subsidiaries amounts.

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**PHI, INC. AND SUBSIDIARIES**  
**CONDENSED CONSOLIDATING STATEMENTS OF OPERATIONS**  
(Thousands of dollars)  
(Unaudited)

| <b>For the nine months ended September 30, 2011</b> |                                    |   |                     |                     |
|---|------------------------------------|---|---------------------|---------------------|
|   | <b>Parent<br/>Company<br/>Only</b> | <b>Guarantor<br/>Subsidiaries<sup>(1)</sup></b> | <b>Eliminations</b> | <b>Consolidated</b> |
| Operating revenues, net                             | \$ 354,614                         | \$ 46,578                                       | \$                  | \$ 401,192          |
| Management fees                                     | 1,863                              |   | (1,863)             |                     |
| Gain on dispositions of assets, net                 | (415)                              |   |                     | (415)               |
| Other, principally interest income                  | 686                                |   |                     | 686                 |
|   | 356,748                            | 46,578  | (1,863)             | 401,463             |
| Expenses:   |                                    |   |                     |                     |
| Direct expenses                                     | 316,236                            | 36,035  |                     | 352,271             |
| Management fees                                     |                                    | 1,863   | (1,863)             |                     |
| Selling, general and administrative expenses        | 24,806                             | 873   |                     | 25,679              |
| Equity in net income of consolidated subsidiaries   | (4,684)                            |   | 4,684               |                     |
| Interest expense                                    | 20,790                             |   |                     | 20,790              |
|   | 357,148                            | 38,771  | 2,821               | 398,740             |
| Earnings before income taxes                        | (400)                              | 7,807   | (4,684)             | 2,723               |
| Income tax expense                                  | (2,034)                            | 3,123   |                     | 1,089               |
| Net earnings  | \$ 1,634                           | \$ 4,684  | \$ (4,684)          | \$ 1,634            |

| <b>For the nine months ended September 30, 2010</b> |                                    |   |                     |                     |
|---|------------------------------------|---|---------------------|---------------------|
|   | <b>Parent<br/>Company<br/>Only</b> | <b>Guarantor<br/>Subsidiaries<sup>(1)</sup></b> | <b>Eliminations</b> | <b>Consolidated</b> |
| Operating revenues, net                             | \$ 347,873                         | \$ 49,002                                       | \$                  | \$ 396,875          |
| Management fees                                     | 1,960                              |   | (1,960)             |                     |
| Gain on dispositions of assets, net                 | 221                                |   |                     | 221                 |
| Other, principally interest income                  | 58                                 |   |                     | 58                  |
|   | 350,112                            | 49,002  | (1,960)             | 397,154             |

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|   |          |          |            |          |
|---|----------|----------|------------|----------|
| Expenses:   |          |          |            |          |
| Direct expenses                                   | 296,468  | 39,652   |            | 336,120  |
| Management fees                                   |          | 1,960    | (1,960)    |          |
| Selling, general and administrative expenses      | 21,008   | 1,083    |            | 22,091   |
| Equity in net income of consolidated subsidiaries | (3,784)  |          | 3,784      |          |
| Interest expense                                  | 12,387   |          |            | 12,387   |
| Loss on debt restructuring                        | 9,521    |          |            | 9,521    |
|   | 335,600  | 42,695   | 1,824      | 380,119  |
| Earnings before income taxes                      | 14,512   | 6,307    | (3,784)    | 17,035   |
| Income tax expense                                | 5,870    | 2,523    |            | 8,393    |
| Net earnings                                      | \$ 8,642 | \$ 3,784 | \$ (3,784) | \$ 8,642 |

(1) Foreign subsidiaries represent minor subsidiaries and are included in the guarantors subsidiaries amounts.

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**PHI, INC. AND SUBSIDIARIES**  
**CONDENSED CONSOLIDATING STATEMENTS OF CASH FLOWS**  
(Thousands of dollars)  
(Unaudited)

|   | <b>For the nine months ended September 30, 2011</b> |   |                     |                     |
|---|---|---|---------------------|---------------------|
|   | <b>Parent<br/>Company<br/>Only</b>                  | <b>Guarantor<br/>Subsidiaries<sup>(1)</sup></b> | <b>Eliminations</b> | <b>Consolidated</b> |
| Net cash provided by (used in) operating activities | \$ 22,068   | \$ (8)  | \$                  | \$ 22,060           |
| Investing activities:                               |   |   |                     |                     |
| Purchase of property and equipment                  | (66,747)  |   |                     | (66,747)            |
| Proceeds from asset dispositions                    | 3,804   |   |                     | 3,804               |
| Purchase of short-term investments                  | (193,557)   |   |                     | (193,557)           |
| Proceeds from sale of short-term investments        | 241,989   |   |                     | 241,989             |
| Payments for deposits on aircraft                   | (12,009)  |   |                     | (12,009)            |
| Net cash used in investing activities               | (26,520)  |   |                     | (26,520)            |
| Financing activities:                               |   |   |                     |                     |
| Payment on line of credit, net                      | 4,294   |   |                     | 4,294               |
| Net cash provided by financing activities           | 4,294   |   |                     | 4,294               |
| Increase in cash                                    | (158)   | (8)   |                     | (166)               |
| Cash, beginning of period                           | 2,957   | 671   |                     | 3,628               |
| Cash, end of period                                 | \$ 2,799  | \$ 663  | \$                  | \$ 3,462            |

|  | <b>For the nine months ended September 30, 2010</b> |   |                     |                     |
|--|---|---|---------------------|---------------------|
|  | <b>Parent<br/>Company<br/>Only</b>                  | <b>Guarantor<br/>Subsidiaries<sup>(1)</sup></b> | <b>Eliminations</b> | <b>Consolidated</b> |
| Net cash provided by operating activities    | \$ 49,451   | \$ 2,052  | \$                  | \$ 51,503           |
| Investing activities:                        |   |   |                     |                     |
| Purchase of property and equipment           | (37,551)  | (2,188)   |                     | (39,739)            |
| Proceeds from asset dispositions             | 1,171   |   |                     | 1,171               |
| Purchase of short-term investments           | (102,710)   |   |                     | (102,710)           |
| Proceeds from sale of short-term investments | 24,260  |   |                     | 24,260              |
| Payments for deposits on aircraft            | (3,660)   |   |                     | (3,660)             |
| Net cash used in investing activities        | (118,490)   | (2,188)   |                     | (120,678)           |

Financing activities:

|   |           |        |    |           |
|---|-----------|--------|----|-----------|
| Proceeds from issuance of Senior Notes due 2018 | 300,000   |        |    | 300,000   |
| Premium and costs to retire debt early          | (7,293)   |        |    | (7,293)   |
| Repayment of Senior Notes due 2013              | (189,490) |        |    | (189,490) |
| Debt issuance costs                             | (4,982)   |        |    | (4,982)   |
| Proceeds (payment) line of credit, net          | (18)      |        |    | (18)      |
| Net cash provided by financing activities       | 98,217    |        |    | 98,217    |
|   |           |        |    |           |
| Increase in cash                                | 29,178    | (136)  |    | 29,042    |
| Cash, beginning of period                       | 1,678     | 823    |    | 2,501     |
|   |           |        |    |           |
| Cash, end of period                             | \$ 30,856 | \$ 687 | \$ | \$ 31,543 |

(1) Foreign subsidiaries represent minor subsidiaries and are included in the guarantors subsidiaries amounts.

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

This discussion and analysis should be read in conjunction with the accompanying unaudited condensed consolidated financial statements and the notes thereto as well as our audited consolidated financial statements and notes thereto contained in our Annual Report on Form 10-K for the year ended December 31, 2010, management's discussion and analysis, risk factors and other information contained therein.

**Forward-Looking Statements**

All statements other than statements of historical fact contained in this Form 10-Q and other periodic reports filed by PHI, Inc. ( PHI or the Company or we or our ) under the Securities Exchange Act of 1934 and other written or oral statements made by it or on its behalf, are forward-looking statements. When used herein, the words anticipates , expects , believes , goals , intends , plans , projects and similar words and expressions are intended to identify forward-looking statements. Forward-looking statements are based on a number of assumptions about future events and are subject to significant risks, uncertainties, and other factors that may cause the Company's actual results to differ materially from the expectations, beliefs, and estimates expressed or implied in such forward-looking statements. Although the Company believes that the assumptions underlying the forward-looking statements are reasonable, no assurance can be given that such assumptions will prove correct or even approximately correct. Factors that could cause the Company's results to differ materially from the expectations expressed in such forward-looking statements include but are not limited to the following: unexpected variances in flight hours, the effect on demand for our services caused by volatility of oil and gas prices and the level of exploration and production activity in the Gulf of Mexico, the effect on the demand for our services as a result of the Deepwater Horizon incident, the effect on our operating costs of volatile fuel prices, the availability of capital required to acquire aircraft, environmental risks, hurricanes and other adverse weather conditions, the activities of our competitors, changes in government regulation, unionization, operating hazards, risks related to operating in foreign countries, the ability to obtain adequate insurance at an acceptable cost and the ability of the Company to develop and implement successful business strategies. For a more detailed description of risks, see the Risk Factors section in Item 1.A. of our Form 10-K for the year ended December 31, 2010 and in Part II Item 1.A. of our subsequently filed quarterly reports on Form 10-Q (the SEC Filings ). All forward-looking statements in this document are expressly qualified in their entirety by the cautionary statements in this paragraph and the Risk Factors section of our SEC Filings. PHI undertakes no obligation to update publicly any forward-looking statements, whether as a result of new information, future events, or otherwise.

**Overview**

Operating revenues for the three months ended September 30, 2011 were \$145.6 million, compared to \$135.7 million for the three months ended September 30, 2010, an increase of \$9.9 million. Oil and Gas operating revenues increased \$6.8 million for the quarter ended September 30, 2011, related primarily to increased heavy aircraft flight hours and revenues, due to a slight increase in deepwater drilling activity as compared to the same period in 2010 when there was no deepwater drilling activity due to the moratorium. Also contributing to the revenue increase was increased medium aircraft ad hoc flights in the month of September for hurricane evacuations in the Gulf of Mexico. Operating revenues in the Air Medical segment increased \$2.6 million primarily due to increased revenues for hospital based contracts of \$2.5 million due to increased flight hours for those contracts.

Flight hours for the quarter ended September 30, 2011 were 39,223 compared to 39,192 for the quarter ended September 30, 2010. Oil and Gas segment's flight hours decreased 218 hours due to decreases in light and medium aircraft flight hours, partially offset by an increase in heavy aircraft flight hours. Air Medical segment flight hours increased 278 hours for the quarter ended September 30, 2011, due to increased flight activity in hospital based contracts. Individual patient transports in the Air Medical

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segment were 4,881 for the quarter ended September 30, 2011, compared to transports of 5,149 for the quarter ended September 30, 2010, a decrease of 268 transports.

Net Oil and Gas segment profit was \$13.5 million for the quarter ended September 30, 2011, compared to \$13.3 million for the quarter ended September 30, 2010. The increase of \$0.2 million was primarily due to increased revenues of \$6.8 million, partially offset by increased direct expenses of \$6.5 million, discussed further in the Segment Discussion.

Net segment profit for the Air Medical segment was \$6.1 million for the quarter ended September 30, 2011, compared to \$4.6 million for the quarter ended September 30, 2010. The increase in segment profit in the Air Medical segment was primarily due to the increased revenues.

Net income for the quarter ended September 30, 2011 was \$3.6 million, or \$0.23 per diluted share, compared to a net loss of \$2.4 million for the quarter ended September 30, 2010, or \$0.16 per diluted share. Pre-tax earnings were \$6.0 million for the quarter ended September 30, 2011, compared to a pre-tax loss of \$1.4 million for the same period in 2010. Interest expense increased \$2.8 million from \$4.2 million in the third quarter of 2010 to \$7.0 million in the third quarter of 2011, due to the issuance of the 8.625% Senior Notes. Included in the quarter ended September 30, 2010 was a pre-tax charge of \$9.5 million related to the early redemption of our 7.125% Senior Notes and a \$1.5 million charge to tax expense, primarily related to an increase in our valuation allowance for foreign tax credits, discussed in Note 3 to our financial statements included in this report.

Year to date operating revenues for September 30, 2011 were \$401.2 million, compared to \$396.9 million for the nine months ended September 30, 2010, an increase of \$4.3 million. Oil and Gas operating revenues decreased \$5.2 million for the nine months ended September 30, 2011, related primarily to decreased medium aircraft flight hours and revenues resulting mainly from the continuing impact on our business of the Deepwater Horizon incident. Operating revenues in the Air Medical segment increased \$8.6 million primarily due to increased revenues for hospital based contracts of \$5.6 million due to increased flight hours for those contracts. There was also an increase in revenues of \$3.0 million in the independent provider programs primarily due to an improved payor mix and rate increases implemented in the prior year.

Flight hours for the nine months ended September 30, 2011 were 110,395 compared to 114,061 for the nine months ended September 30, 2010. Oil and Gas segment's flight hours decreased 4,146 hours due to a decrease in deepwater drilling activity in the Gulf of Mexico. Air Medical segment flight hours increased 432 hours for the nine months ended September 30, 2011, due to increased flight activity in hospital based contracts. Individual patient transports in the Air Medical segment were 13,441 for the nine months ended September 30, 2011, compared to transports of 14,124 for the nine months ended September 30, 2010, a decrease of 683 transports.

Net Oil and Gas segment profit was \$30.0 million for the nine months ended September 30, 2011, compared to \$44.3 million for the nine months ended September 30, 2010. The decrease of \$14.3 million was primarily due to decreased revenues primarily in medium aircraft revenue related to the Deepwater Horizon impact, and increased direct expenses discussed further in the Segment Discussion.

Net segment profit for the Air Medical segment was \$11.5 million for the nine months ended September 30, 2011, compared to \$9.0 million for the nine months ended September 30, 2010. The increase in segment profit in the Air Medical segment was primarily due to the increased revenues of \$8.6 million, partially offset by increased direct expenses of \$6.4 million, discussed further in the Segment Discussion. Segment profit for the nine months ended September 30, 2010 includes a credit of \$3.1 million related to the termination of a manufacturer warranty program.

Net earnings for the nine months ended September 30, 2011 was \$1.6 million, or \$0.11 per diluted share, compared to net earnings of \$8.6 million for the nine months ended September 30, 2010, or \$0.56 per

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diluted share. Pre-tax earnings were \$2.7 million for the nine months ended September 30, 2011, compared to pre-tax earnings of \$17.0 million for the same period in 2010. The decrease in earnings is due primarily to the decrease in Oil and Gas segment profit of \$14.2 million, discussed above. In addition, the decrease is due to an increase in unallocated selling, general and administrative expense of \$4.7 million as discussed in Combined Operations for the nine months. Interest expense was \$20.8 million for the first nine months of 2011, compared to \$12.4 million for the first nine months of 2010, an increase of \$8.4 million due to the issuance of the 8.625% Senior Notes. Earnings for the nine months ended September 30, 2010 included a credit of \$4.3 million in direct expense related to termination of a manufacturer's warranty program on certain aircraft, a \$9.5 million pre-tax charge related to the early redemption of our 7.125% Senior Notes and a \$1.5 million charge to tax expense, discussed above.

**Operating Statistics**

The following tables present certain non-financial operational statistics for the quarters and nine months ended September 30, 2011 and 2010:

|  | <b>Quarter Ended<br/>September 30,</b> |             | <b>Nine Months Ended<br/>September 30,</b> |                      |
|--|--|-------------|--|----------------------|
|  | <b>2011</b>                            | <b>2010</b> | <b>2011</b>                                | <b>2010</b>          |
| <b>Flight hours:</b>                             |  |             |  |                      |
| Oil and Gas                                      | 29,901                                 | 30,119      | 84,151                                     | 88,297               |
| Air Medical <sup>(1)</sup>                       | 9,322                                  | 9,044       | 25,682                                     | 25,250               |
| Technical Services                               |  | 29          | 562  | 514                  |
| Total  | 39,223                                 | 39,192      | 110,395                                    | 114,061              |
| <br><b>Air Medical Transports <sup>(2)</sup></b> | <br>4,881                              | <br>5,149   | <br>13,441                                 | <br>14,124           |
| <br><b>Aircraft operated at period end:</b>      |  |             |  |                      |
|  |  |             | <b>September 30,</b>                       | <b>September 30,</b> |
|  |  |             | <b>2011</b>                                | <b>2010</b>          |
| Oil and Gas <sup>(3)</sup>                       |  |             | 164  | 159                  |
| Air Medical <sup>(4)</sup>                       |  |             | 88   | 87                   |
| Technical Services                               |  |             | 5  | 5                    |
| Total <sup>(3) (4)</sup>                         |  |             | 257  | 251                  |

(1) Flight hours include 2,729 flight hours associated with hospital-based contracts, compared to 2,127 flight hours in the prior year quarter, and 7,415 flight hours year-to-date, compared to 6,200 in the prior year-to-date period.

(2) Represents individual patient transports for the period.

(3) Includes nine aircraft as of September 30, 2011 and 2010 that are customer owned.

(4) Includes seven aircraft as of September 30, 2011 and 2010 that are customer owned.

**Results of Operations**

*Quarter Ended September 30, 2011 compared with Quarter Ended September 30, 2010*

**Combined Operations**

**Revenues** Operating revenues for the three months ended September 30, 2011 were \$145.6 million, compared to \$135.7 million for the three months ended September 30, 2010, an increase of \$9.9 million. Oil and Gas operating revenues increased \$6.8 million for the quarter ended September 30, 2011, related primarily to increased heavy aircraft flight hours and revenues. Also contributing to the revenue increase was increased medium aircraft ad hoc flight hours in the month of September for hurricane evacuations in the Gulf of Mexico. Operating revenues in the Air Medical segment increased \$2.6 million primarily due

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to increased revenues for hospital based contracts of \$2.5 million due to increased flight hours for those contracts. Flight hours for the quarter ended September 30, 2011 were 39,223 compared to 39,192 for the quarter ended September 30, 2010. Oil and Gas segment's flight hours decreased 218 hours due to decreases in light and medium aircraft flight hours, partially offset by an increase in heavy aircraft flight hours. Air Medical segment flight hours increased 278 hours for the quarter ended September 30, 2011, due to increased flight hours in the hospital based contracts. Individual patient transports in the Air Medical segment were 4,881 for the quarter ended September 30, 2011, compared to transports of 5,149 for the quarter ended September 30, 2010, a decrease of 268 transports.

**Other Income and Gains** During the third quarter, we recorded a loss related to the sale of certain aircraft and related inventory in the amount of \$0.8 million, resulting in losses on asset dispositions of \$0.6 million for the three months ended September 30, 2011. Gains on asset dispositions were \$0.1 million for the three months ended September 30, 2010.

**Direct Expenses** Direct operating expense was \$123.6 million for the three months ended September 30, 2011, compared to \$115.8 million for the three months ended September 30, 2010, an increase of \$7.8 million. Aircraft fuel expense increased (\$3.1 million) primarily due to increased per-gallon fuel costs. Aircraft rent decreased (\$1.7 million) due to the purchase of four heavy aircraft in 2010, and two heavy and one medium aircraft in 2011 previously under lease pursuant to purchase options. Aircraft depreciation increased (\$0.8 million) due to additional aircraft purchased, including those purchased off lease. We also experienced an increase in aircraft parts usage (\$2.0 million), component repair costs (\$1.1 million) and employee compensation expenses (\$2.3 million). Other items increased, net (\$0.2 million).

**Selling, General, and Administrative Expenses** Selling, general and administrative expenses were \$8.4 million for the three months ended September 30, 2011, compared to \$7.7 million for the three months ended September 30, 2010. The \$0.7 million increase is due to increased employee compensation costs (\$0.9 million), partially offset by decreased legal expenses (\$0.2 million).

**Interest Expense** Interest expense was \$7.0 million for the three months ended September 30, 2011, compared to \$4.2 million for the three months ended September 30, 2010. The increase is due to refinancing our \$200 million 7.125% Senior Notes due 2013 with the \$300 million 8.625% Senior Notes due 2018.

**Income Taxes** Income tax expense for the three months ended September 30, 2011 was \$2.4 million compared to income tax expense of \$1.0 million for the three months ended September 30, 2010. The effective tax rate was 40% for the three months ended September 30, 2011. Tax expense for the quarter ended September 30, 2010 includes a provision of \$1.5 million related to the expiration of foreign tax credits and state net operating loss carry-forwards, resulting from actual and scheduled purchases of aircraft. The acquisitions resulted in increased tax depreciation and net operating loss carry-forwards, which must be utilized before foreign tax credits can be utilized.

**Net Earnings** Net income for the three months ended September 30, 2011 was \$3.6 million compared to a net loss of \$2.4 million for the three months ended September 30, 2010. Earnings before income taxes for the three months ended September 30, 2011 was \$6.0 million compared to a loss before tax of \$1.4 million for the same period in 2010. Earnings per diluted share was \$0.23 for the current quarter compared to a loss per diluted share of \$0.16 for the prior year quarter. We had 15.5 million common shares outstanding during the three months ended September 30, 2011, and 15.3 million common shares outstanding during the three months ended September 30, 2010. The increase in earnings before taxes for the quarter ended September 30, 2011 is related to the pre-tax charge of \$9.5 million recorded in the quarter ended September 30, 2010 related to the early redemption of our 7.125% Senior Notes.

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### **Segment Discussion**

*Oil and Gas* Oil and Gas segment revenues were \$96.6 million for the three months ended September 30, 2011, compared to \$89.8 million for the three months ended September 30, 2010, an increase of \$6.8 million. Flight hours were 29,901 for the current quarter compared to 30,119 for the same quarter in the prior year. The increase in revenue is primarily due to increased heavy aircraft flight hours and revenues, due to a slight increase in deepwater drilling activity compared to the same period in 2010 when there was no deepwater drilling activity due to the moratorium. Also contributing to the revenue increase was increased medium aircraft ad hoc flights in the month of September for hurricane evacuations in the Gulf of Mexico.

The number of aircraft in the segment was 164 at September 30, 2011, compared to 160 aircraft at September 30, 2010. We have sold or disposed of three light aircraft in the Oil and Gas segment since September 30, 2010. We also traded in two medium aircraft related to our contract for the acquisition of medium aircraft for a customer. We added eight new aircraft to the Oil and Gas segment since September 30, 2010, consisting of two light, four medium and two heavy aircraft. Inter-segment aircraft transfers account for the remaining amount. We also purchased two heavy and one medium aircraft off lease since September 30, 2010, which does not affect the segment aircraft count. In addition, in the second quarter of 2011, we entered into a heavy transport aircraft contract, as further discussed in Note 3 to our Financial Statements included in this report.

Direct expense in our Oil and Gas segment was \$82.2 million for the three months ended September 30, 2011, compared to \$75.7 million for the three months ended September 30, 2010, an increase of \$6.5 million. Fuel expense increased (\$3.2 million) as a result of increased per-gallon fuel costs. Total fuel cost is included in direct expense and reimbursement of a portion of these costs above a contracted per-gallon amount is included in revenue. Aircraft rent expense decreased (\$1.9 million) due to the exercise of lease purchase options of four heavy aircraft, two in October 2010 and two in April 2011, and the purchase of one medium aircraft in July 2011. There was an increase in aircraft depreciation (\$0.7 million) due to additional aircraft added to the fleet, including those purchased off lease. Component repair costs increased (\$2.2 million) due to the addition of AW139 model aircraft to the fleet and a reclassification of certain engine and transmission overhaul expenses from the Air Medical segment. Employee compensation expenses increased (\$2.4 million) due to compensation rate increases and increased overtime paid during hurricane season. Other items decreased, net (\$0.1 million).

Our Oil and Gas segment profit was \$13.5 million for the quarter ended September 30, 2011, compared to \$13.3 million for the quarter ended September 30, 2010. Operating margins (segment profit divided by operating revenues) were 14% for the three months ended September 30, 2011, compared to 15% for the three months ended September 30, 2010. The increase of \$0.2 million was primarily due to increased revenues of \$6.8 million, partially offset by increased direct expenses of \$6.5 million as previously discussed. The Oil and Gas segment revenues are primarily driven by contracted aircraft and flight hours. Costs are primarily fixed and are driven by the number of aircraft. The variable portion is driven by flight hours.

*Air Medical* Air Medical segment revenues were \$46.9 million for the three months ended September 30, 2011, compared to \$44.3 million for the three months ended September 30, 2010, an increase of \$2.6 million. The increase was primarily due to increased revenue of \$2.5 million related to flight activity in hospital based contracts. Total patient transports were 4,881 for the three months ended September 30, 2011, compared to 5,149 for the three months ended September 30, 2010, a decrease of 268 transports.

Flight hours were 9,322 for the three months ended September 30, 2011, compared to 9,044 for the three months ended September 30, 2010. Since September 30, 2010, we added one medium aircraft related to a hospital contract. We also acquired two fixed wing aircraft, and sold or disposed of two fixed wing aircraft.

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Direct expense in our Air Medical segment was \$39.7 million for the three months ended September 30, 2011, compared to \$38.7 million for the three months ended September 30, 2010. There was an increase in aircraft parts usage (\$2.0 million), partially offset by a decrease in component repair costs (\$1.0 million).

Selling, general and administrative expenses were \$1.1 million for the three months ended September 30, 2011, compared to \$1.0 million for the three months ended September 30, 2010. The \$0.1 million increase is primarily due to increased employee compensation expenses.

Our Air Medical segment's operating income was \$6.1 million for the quarter ended September 30, 2011, compared to \$4.6 million for the quarter ended September 30, 2010. Operating margins were 13% for the three months ended September 30, 2011, compared to 10% for the three months ended September 30, 2010.

**Technical Services** Technical Services revenues were \$2.1 million for the three months ended September 30, 2011, compared to \$1.6 million for the three months ended September 30, 2010. Direct expenses in our Technical Services segment were \$1.8 million for the three months ended September 30, 2011, compared to \$1.4 million for the three months ended September 30, 2010. Our Technical Services segment's operating income was \$0.3 million for the three months ended September 30, 2011, compared to operating income of \$0.2 million for the three months ended September 30, 2010.

### ***Nine Months Ended September 30, 2011 compared with Nine Months Ended September 30, 2010***

#### **Combined Operations**

**Revenues** Operating revenues for the nine months ended September 30, 2011 were \$401.2 million, compared to \$396.9 million for the nine months ended September 30, 2010, an increase of \$4.3 million. Oil and Gas operating revenues decreased \$5.2 million for the nine months ended September 30, 2011, related primarily to decreased medium aircraft flight hours and revenues resulting mainly from the continuing impact on our business of the Deepwater Horizon incident. Operating revenues in the Air Medical segment increased \$8.6 million primarily due to increased revenues for hospital based contracts of \$5.6 million due to increased flight hours for those contracts. There was also an increase in revenues of \$3.0 million in the independent provider programs primarily due to an improved payor mix and rate increases implemented in the current year and prior year.

Flight hours for the nine months ended September 30, 2011 were 110,395 compared to 114,061 for the nine months ended September 30, 2010. Oil and Gas segment's flight hours decreased 4,146 hours due to a decrease in deepwater drilling activity in the Gulf of Mexico. Air Medical segment flight hours increased 432 hours for the nine months ended September 30, 2011. Individual patient transports in the Air Medical segment were 13,441 for the nine months ended September 30, 2011, compared to transports of 14,124 for the nine months ended September 30, 2010, a decrease of 683 transports.

**Other Income and Gains** During the third quarter, we recorded a loss related to the sale of certain aircraft and related inventory in the amount of \$0.8 million, resulting in losses on asset dispositions of \$0.4 million for the nine months ended September 30, 2011. For the nine months ended September 30, 2010, gain on disposition of assets was \$0.2 million.

Other income was \$0.7 million for the nine months ended September 30, 2011, compared to less than \$0.1 million for the nine months ended September 30, 2010.

**Direct Expenses** Direct operating expense was \$352.3 million for the nine months ended September 30, 2011, compared to \$336.1 million for the nine months ended September 30, 2010, an increase of \$16.2 million. Contributing to this increase was a \$4.3 million credit recorded in the prior year related to termination of a warranty program for certain aircraft. We also experienced increases in fuel expense

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(\$6.3 million) due to increased per-gallon fuel costs compared to the prior year, and increases in aircraft depreciation (\$2.7 million) and aircraft insurance (\$2.7 million) due to additional aircraft added to the fleet. Aircraft parts usage also increased (\$4.7 million). Aircraft rent decreased (\$4.8 million) due to the purchase of six heavy and one medium aircraft off lease.

**Selling, General and Administrative Expenses** Selling, general and administrative expenses were \$25.7 million for the nine months ended September 30, 2011, compared to \$22.1 million for the nine months ended September 30, 2010. The \$3.6 million increase was primarily due to increased legal and accounting fees (\$1.2 million). Of this amount, \$1.0 million is due to expenses incurred in assessing a potential acquisition for which we were unsuccessful. Other increases included expense associated with the issuance of restricted stock units in 2010 (\$1.0 million), consultants and contract services (\$0.8 million), promotional and printing expenses (\$0.4 million), and other items, net (\$0.2 million).

**Interest Expense** Interest expense was \$20.8 million for the nine months ended September 30, 2011, compared to \$12.4 million for the nine months ended September 30, 2010. This increase is due to refinancing our \$200 million 7.125% Senior Notes due 2013 with the \$300 million 8.625% Senior Notes due 2018.

**Income Taxes** Income tax expense was \$1.1 million for the nine months ended September 30, 2011, compared to \$8.4 million for the nine months ended September 30, 2010. The effective tax rate was 40% for the nine months ended September 30, 2011. Tax expense for the nine months ended September 30, 2010 includes a provision of \$1.5 million related to the expiration of foreign tax credits and state net operating loss carry-forwards, resulting from actual and scheduled purchases of aircraft. The acquisitions resulted in increased tax depreciation and net operating loss carry-forwards, which must be utilized before foreign tax credits can be utilized.

**Net Earnings** Net earnings for the nine months ended September 30, 2011 was \$1.6 million, or \$0.11 per diluted share, compared to net earnings of \$8.6 million for the nine months ended September 30, 2010, or \$0.56 per diluted share. Pre-tax earnings were \$2.7 million for the nine months ended September 30, 2011, compared to pre-tax earnings of \$17.0 million for the same period in 2010. The decrease in earnings is due primarily to the decrease in Oil and Gas segment profit of \$14.2 million, and an increase in selling, general and administrative expense of \$3.6 million. Interest expense increased \$8.4 million from \$12.4 million in the nine months of 2010 to \$20.8 million in the nine months of 2011, due to the issuance of the 8.625% Senior Notes. Earnings for the nine months ended September 30, 2010 included a credit of \$4.3 million in direct expense related to termination of a manufacturer's warranty program on certain aircraft, a \$9.5 million pre-tax charge related to the early redemption of our 7.125% Senior Notes and a \$1.5 million charge to tax expense, discussed above. We had 15.5 million common shares outstanding during the nine months ended September 30, 2011, and 15.3 million common shares outstanding during the nine months ended September 30, 2010.

**Segment Discussion**

***Oil and Gas*** Oil and Gas segment revenues were \$264.2 million for the nine months ended September 30, 2011, compared to \$269.5 million for the nine months ended September 30, 2010, a decrease of \$5.3 million. Flight hours were 84,151 for the nine months ended September 30, 2011, compared to 88,297 for the same period in 2010. The decrease in Oil and Gas revenues was related primarily to decreased medium aircraft flight hours and revenue due to decreased deepwater drilling activity in the Gulf of Mexico related to the Deepwater Horizon incident in 2010 and delays in the resumption of drilling due to the new regulatory drilling permit process.

Direct expense in our Oil and Gas segment was \$231.6 million for the nine months ended September 30, 2011, compared to \$221.8 million for the nine months ended September 30, 2010, an increase of \$9.8 million. Fuel expense increased (\$5.8 million) as a result of increased pre-gallon fuel costs. Total fuel cost is included in direct expense and reimbursement of a portion of these costs above a contracted per-

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gallon amount is included in revenue. Aircraft rent expense decreased (\$5.0 million) due to the purchase of six heavy and one medium aircraft previously under lease in 2010, and aircraft insurance increased (\$2.1 million) due to additional aircraft added to the fleet. There was an increase in aircraft depreciation (\$2.3 million) due to additional aircraft added to the fleet, including those purchased off lease. Employee compensation expenses increased (\$2.8 million) due to compensation rate increases and increased overtime paid during hurricane evacuation. Aircraft parts usage also increased (\$2.1 million), and other items decreased, net (\$0.3 million).

Selling, general and administrative expenses were \$2.7 million for the nine months ended September 30, 2011, compared to \$3.4 million for the nine months ended September 30, 2010. The decrease was primarily related to decreased employee compensation expenses related primarily to severance costs in the prior year.

Our Oil and Gas segment's operating income was \$30.1 million for the nine months ended September 30, 2011, compared to \$44.3 million for the nine months ended September 30, 2010. The \$14.2 million decrease was due to the decrease in revenue of \$5.2 million and the increase in direct expenses of \$9.8 million, partially offset by the decrease in selling, general and administrative expenses of \$0.7 million. Operating margins were 11% for the nine months ended September 30, 2011, compared to 16% for the nine months ended September 30, 2010. The decrease in operating income and margin is primarily due to decreased medium aircraft revenue due to decreased deepwater drilling activity in the Gulf of Mexico as discussed above. The Oil and Gas segment revenues are primarily driven by contracted aircraft and flight hours. Costs are primarily fixed and are driven by the number of aircraft, and a portion is variable which is driven by flight hours.

*Air Medical* Air Medical segment revenues were \$129.5 million for the nine months ended September 30, 2011, compared to \$120.9 million for the nine months ended September 30, 2010, an increase of \$8.6 million or 7%. Patient transports were 13,441 for the nine months ended September 30, 2011, compared to 14,124 for the nine months ended September 30, 2010, a decrease of 683 transports. Flight hours were 25,682 for the nine months ended September 30, 2011, compared to 25,250 for the nine months ended September 30, 2010. This increase was due to the increase in hospital based contract flight hours.

Direct expense in our Air Medical segment was \$115.1 million for the nine months ended September 30, 2011, compared to \$108.7 million for the nine months ended September 30, 2010. The \$6.4 million increase is primarily due to increased aircraft warranty costs (\$2.7 million) due to a \$3.1 million credit recorded in segment direct expense in the first quarter of 2010. All new aircraft come with a manufacturer's warranty that covers defective parts. The warranty we terminated was an additional warranty purchased from the manufacturer to cover replacement or refurbishment of aircraft parts on certain aircraft in accordance with manufacturer specifications. A monthly fee was paid to the manufacturer based on flight hours for the aircraft covered under this warranty. In return, the manufacturer provided replacement parts required for maintaining the aircraft. There were also increases in aircraft parts usage (\$2.6 million) and aircraft fuel (\$0.5 million). Aircraft depreciation also increased (\$0.4 million) due to additional aircraft added to the segment's fleet. Other items increased, net (\$0.2 million).

Selling, general and administrative expenses were \$2.9 million for the nine months ended September 30, 2011, compared to \$3.3 million for the nine months ended September 30, 2010. The \$0.4 million decrease was primarily due to decreased employee costs.

Our Air Medical segment's operating income was \$11.5 million for the nine months ended September 30, 2011, compared to \$9.0 million for the nine months ended September 30, 2010. Operating margins were 9% and 7% for the nine months ended September 30, 2011 and 2010, respectively. Operating income for the nine months ended September 30, 2010 includes a credit of \$3.1 million related to the termination of a manufacturer's warranty program. The increase in revenue and decrease in selling, general and administrative expenses contributed to the improved operating margin in the Air Medical segment.

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*Technical Services* Technical Services revenues were \$7.4 million for the nine months ended September 30, 2011, compared to \$6.5 million for the nine months ended September 30, 2010. Direct expenses in our Technical Services segment were \$5.6 million for the nine months ended September 30, 2011 and the nine months ended September 30, 2010. Our Technical Services segment's operating income was \$1.8 million for the nine months ended September 30, 2011, compared to operating income of \$0.8 million for the nine months ended September 30, 2010.

Technical Services provides maintenance and repairs performed for our existing customers that own their aircraft. These services are generally labor intensive with higher operating margins as compared to other segments. In addition, the Technical Services segment conducts flight operations for the National Science Foundation in Antarctica, which are typically conducted in the first and fourth quarters each year.

## **Liquidity and Capital Resources**

### **General**

Our ongoing liquidity requirements arise primarily from the funding of working capital needs, the purchase or leasing of aircraft, the maintenance and refurbishment of aircraft, improvement of facilities, and acquisition of equipment and inventory. Our principal sources of liquidity historically have been net cash provided by our operations and borrowings under our revolving credit facility, senior notes, and the sale of non-voting common stock in 2005 and 2006. To the extent we do not use cash, short-term investments or borrowings to finance our aircraft acquisitions, we can typically enter into operating leases to fund these acquisitions.

On September 23, 2010, we issued \$300 million of 8.625% Senior Notes due 2018 and have repurchased or redeemed all of our \$200 million 7.125% Senior Notes due 2013. These transactions are discussed in Note 4 to our financial statements included in this report, and below under Long Term Debt.

We expect our existing cash and short-term investments, cash flow from operations and borrowings under our revolving credit facility will fund our cash requirements for the next twelve months.

### **Cash Flow**

Our cash position was \$3.5 million at September 30, 2011, compared to \$3.6 million at December 31, 2010. Short-term investments were \$99.9 million at September 30, 2011, compared to \$150.1 million at December 31, 2010. Working capital was \$201.6 million at September 30, 2011, compared to \$268.8 million at December 31, 2010, a decrease of \$67.2 million. The decrease was primarily due to a decrease in short-term investments of \$50.2 million and an increase in other current liabilities of \$22.9 million. The \$22.9 million other current liability due November 1, 2011, was incurred in connection with a contract to purchase heavy transport aircraft, described in Note 3 to the financial statements, upon delivery of the baseline aircraft in June 2011. The one aircraft related to the \$22.9 million other current liability is reflected in property and equipment net, as of September 30, 2011. Proceeds from the sale of short-term investments were used primarily to purchase two aircraft off lease for \$25.6 million and to pay down the revolver balance in the first quarter, \$25.5 million.

Net cash provided by operating activities was \$22.1 million for the nine months ended September 30, 2011, compared to \$51.5 million for the same period in 2010, a decrease of \$29.4 million. This decrease is primarily due to a decrease in net earnings of \$7.0 million and an increase in accounts receivable of \$18.4 million related to increased revenues. Net cash used in investing activities was \$26.5 million for the nine months ended September 30, 2011, compared to a use of cash of \$120.7 million for the same period in 2010. Purchases and sales of short-

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term investments provided a net \$48.4 million in cash during the nine months ended September 30, 2011 compared to a net use of \$78.4 million in the comparable prior year period. The increased net proceeds from short-term investments in 2011 were used to reduce the revolving credit facility balance and purchase two heavy aircraft off lease. The increase in purchases of short-term investments results primarily from the investment of approximately \$82.0 million of net proceeds of our 8.625% Senior Notes remaining after the repurchase of our 7.125% Senior Notes and payment of related fees and costs. Capital expenditures were \$66.7 million for the nine months ended September 30, 2011, compared to \$39.7 million for the same period in 2010. Capital expenditures for 2011 included \$62.7 million for aircraft purchases, upgrades, and refurbishments. Capital expenditures for 2010 included \$32.6 million for aircraft purchases, upgrades, and refurbishments. Gross proceeds from aircraft dispositions were \$3.8 million for the nine months ended September 30, 2011, compared to \$1.2 million for the same period in 2010. Financing activities for the nine months ended September 30, 2011 include only proceeds of and payments on the revolving credit facility. In 2011, we had net borrowing of \$4.3 million, compared to net borrowing of less than \$0.1 for the same period in 2010.

**Long Term Debt**

As of September 30, 2011, our total long-term debt was \$335.4 million, consisting of our \$300 million 8.625% Senior Notes due 2018 and \$35.4 million outstanding on our revolving credit facility.

Our senior secured credit facility provides a \$75 million revolving credit facility maturing in September 2013. On September 26, 2011, we amended the facility to extend the maturity date from September 1, 2012 to September 1, 2013. The interest rate is the prime rate plus 100 basis points. At September 30, 2011, we had \$35.4 million in borrowings under the facility. During the quarter ended September 30, 2011, \$35.4 million was the highest loan balance, with a weighted average balance of \$24.8 million. During the same period for 2010, \$24.8 million was the highest loan balance, with a weighted average balance of \$16.5 million.

On September 23, 2010, we issued \$300 million of 8.625% Senior Notes that mature October 15, 2018. Net proceeds of \$295.5 million were used to repurchase \$189.5 million of our \$200 million outstanding 7.125% Senior Notes due 2013 pursuant to a tender offer and consent solicitation that also settled on September 23, 2010. The tender offer for the 7.125% Senior Notes included a tender premium and interest totaling \$7.6 million. The remaining \$10.5 million of 7.125% Senior Notes outstanding were redeemed October 25, 2010, at a redemption price of 103.563% of their face amount plus accrued interest. As a result of these transactions, we incurred a loss on debt restructuring of \$9.5 million during the quarter ended September 30, 2010.

For a description of our 8.625% Senior Notes and our senior secured revolving credit facility, see Note 4 to our financial statements included in this report.

**Table of Contents****Contractual Obligations**

The table below sets out our contractual obligations as of September 30, 2011 related to our operating lease obligations, aircraft purchase commitments, revolving credit facility, and the 8.625% Senior Notes due 2018. The operating leases are not recorded as liabilities on our balance sheet. Each contractual obligation included in the table contains various terms, conditions, and covenants that, if violated, accelerate the payment of that obligation. We were in compliance with the covenants applicable to these contractual obligations as of September 30, 2011, and expect to remain in compliance through the year ending December 31, 2011. As of September 30, 2011, we leased 19 aircraft included in the lease obligations below.

|  |            | Payment Due by Year |            |                        |           |           | Beyond     |
|--|------------|---------------------|------------|------------------------|-----------|-----------|------------|
|  | Total      | 2011                | 2012       | 2013                   | 2014      | 2015      | 2015       |
|  |            |                     |            | (Thousands of dollars) |           |           |            |
| Aircraft purchase commitments <sup>(1)</sup> | \$ 220,085 | 84,467              | \$ 128,028 | \$ 7,590               | \$        | \$        | \$         |
| Aircraft lease obligations                   | 142,316    | 6,316               | 25,695     | 26,060                 | 26,060    | 25,783    | 32,402     |
| Other lease obligations                      | 14,627     | 844                 | 2,513      | 1,891                  | 1,587     | 1,507     | 6,285      |
| Other current liabilities <sup>(1)</sup>     | 22,900     | 22,900              |            |                        |           |           |            |
| Long-term debt                               | 335,368    |                     |            | 35,368                 |           |           | 300,000    |
| Senior notes interest                        | 182,203    | 6,469               | 25,875     | 25,875                 | 25,875    | 25,875    | 72,234     |
|  | \$ 917,499 | \$ 120,996          | \$ 182,111 | \$ 96,784              | \$ 53,522 | \$ 53,165 | \$ 410,921 |

(1) For information about these aircraft purchase commitments and other current liabilities, see footnote 3 to the financial statements in this report.

As of September 30, 2011, we had options to purchase aircraft under lease becoming exercisable in 2012 through 2014 for the following aggregate purchase prices, respectively: \$45.0 million, \$38.8 million and \$114.4 million. Subject to market conditions, we intend to exercise these options as they become exercisable. There are no other lease purchase options in 2011.

**Item 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK**

Our earnings are subject to changes in short-term interest rates due to the variable interest rate on our revolving credit facility. Based on the \$35.4 million in borrowings outstanding at September 30, 2011, a 10% increase (0.425%) in the interest rate would reduce our annual pre-tax earnings approximately \$0.1 million.

Our \$300 million outstanding 8.625% Senior Notes due 2018 bear interest at a fixed rate of 8.625% and therefore changes in market interest rates do not affect our interest payment obligations on the notes. The fair market value of our 8.625% Senior Notes will vary as changes occur to general market interest rates, the remaining maturity of the notes, and our credit worthiness. At September 30, 2011, the market value of the notes was approximately \$300.3 million, based on quoted market indications.

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Market risk is the risk of changes in the value of financial instruments, or in future net income or cash flows, in response to changing market conditions. The Company holds financial instruments that are exposed to the following significant market risks: the interest rate risk associated with the Company's investments in money market funds, U.S. Government Agencies, commercial paper, and corporate bonds and notes. See Note 8 to the financial statements for details regarding our short-term investments.

**Item 4. CONTROLS AND PROCEDURES**

The Company's management, with the participation of our Chief Executive Officer and Chief Financial Officer, has evaluated the effectiveness of our disclosure controls and procedures (as defined in Rule 13a-15(e) under the Securities Exchange Act of 1934) as of the end of the period covered by this report. Based on this evaluation, our Chief Executive Officer and Chief Financial Officer have concluded that our disclosure controls and procedures were effective as of such date to ensure that information required to be disclosed by the Company in the reports that it files or submits under the Securities Exchange Act of 1934 is recorded, processed, summarized and reported within the time periods specified in the rules and forms of the Securities and Exchange Commission, including to ensure that such information is accumulated and communicated to management, including our Chief Executive Officer and Chief Financial Officer, as appropriate to allow timely decisions regarding required disclosure.

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

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**PART II OTHER INFORMATION**

**Item 1. LEGAL PROCEEDINGS**

For information regarding legal proceedings, see Legal Matters in Note 3 to our financial statements included in this report, which is incorporated herein by reference.

**Item 1. A. RISK FACTORS**

Item 1.A. Risk Factors of our Annual Report on Form 10-K for the year ended December 31, 2010 includes a discussion of our risk factors.

Except as described below, there have been no significant changes to our risk factors.

**We must obtain additional financing in order to fund our aircraft purchase and other obligations.**

As of September 30, 2011, we had obligations related to aircraft purchase commitments totaling approximately \$220.0 million due in 2011 and 2012, along with other significant contractual obligations as described in this report. As of September 30, 2011, we had approximately \$103.4 million in cash and short-term investments and \$39.6 million available under our \$75.0 million revolving credit facility. We intend to seek to obtain operating leases and/or additional debt financing to fund these obligations. We have no current commitments or arrangements with respect to such financing, and no assurances can be given that such financing will be available to us on acceptable terms. Our inability to obtain such financing could have a material adverse affect on our business, financial condition and results of operations.

**Item 2. UNREGISTERED SALES OF EQUITY SECURITIES AND USE OF PROCEEDS**

None.

**Item 3. DEFAULTS UPON SENIOR SECURITIES**

None.

**Item 4. (REMOVED AND RESERVED)**

**Item 5. OTHER INFORMATION**

On October 12, 2011, the Board of Directors of PHI, Inc. appointed Didier Keller to serve as a director on the Board of Directors of PHI, Inc., effective October 12, 2011. Mr. Keller will also serve as a member of the Audit Committee and Compensation Committee.

Mr. Keller served as Chief Executive of SBM Offshore N.V., a Dutch public company serving the offshore oil and gas industry on a global basis by supplying engineered products, vessels and systems, and offshore oil and gas production services, from 2004 until his retirement in May 2008. He joined SBM Offshore (formerly IHC Caland N.V.) in 1977, and during the next 31 years held positions of increasing responsibility in project management, business development, marketing, sales, and management, including serving as President of SBM Offshore's American subsidiary from 1991 to 1994. Since May 2008, he has been engaged as an independent consultant in the oil and gas industry, and currently serves as a Supervisory Director of Dietsmann NV, a privately-held company headquartered in the Netherlands and a leading independent provider of integrated operation and maintenance services for oil, gas, and LNG production facilities and power plants. Mr. Keller graduated from the civil engineering school ESTACA in Paris in 1969 and holds a PhD French equivalent degree in aeronautics.

On November 4, 2011, the Compensation Committee of the Board of Directors of PHI, Inc. granted the Company's Chairman and Chief Executive Officer Al A. Gonsoulin restricted stock units to acquire

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83,978 shares of the Company's voting common stock under the Company's Amended and Restated 1995 Incentive Compensation Plan. The restricted stock units will vest on January 1, 2013, if Mr. Gonsoulin continues to be employed by the Company on that vesting date. Vesting will be accelerated upon death, disability or upon a change of control of the Company. The Restricted Stock Unit Agreement with respect to the grants to Mr. Gonsoulin is included as Exhibit 10.2.

**Item 6. EXHIBITS**

(a) Exhibits

- 3.1 (i) Composite Articles of Incorporation of the Company (incorporated by reference to Exhibit 3.1 to PHI's Report on Form 10-Q filed on August 7, 2008).
- (ii) Amended and Restated By-laws of the Company (incorporated by reference to Exhibit 3(ii) to PHI's Report on Form 8-K filed October 13, 2011).
- 4.1 Amended and Restated Loan Agreement dated as of March 31, 2008 by and among PHI, Inc., Air Evac Services, Inc., PHI Tech Services, Inc. (formerly Evangeline Airmotive, Inc.), and International Helicopter Transport, Inc. and Whitney National Bank (incorporated by reference to Exhibit 4.1 to PHI's Report on Form 10-Q filed on May 8, 2008).
- 4.2 First Amendment dated as of August 5, 2009 to Amended and Restated Loan Agreement dated as of March 31, 2008 by and among PHI, Inc., Air Evac Services, Inc., PHI Tech Services, Inc. (formerly Evangeline Airmotive, Inc.), and International Helicopter Transport, Inc. and Whitney National Bank (incorporated by reference to Exhibit 4.2 to PHI's Report on Form 10-Q filed on August 10, 2009).
- 4.3 Second Amendment dated September 13, 2010 to Amended and Restated Loan Agreement dated March 31, 2008 by and among PHI, Inc., Air Evac Services, Inc., PHI Tech Services, Inc. and International Helicopter Transport, Inc., and Whitney National Bank (incorporated by reference to Exhibit 4.3 to PHI's Report on Form 10-Q filed on November 8, 2010).
- 4.4 Third Amendment dated September 26, 2011 to Amended and Restated Loan Agreement dated March 31, 2008 by and among PHI, Inc., PHI Air Medical, L.L.C., successor to Air Evac Services, Inc., PHI Tech Services, Inc. and International Helicopter Transport, Inc., and Whitney National Bank.
- 4.5 Indenture dated as of September 23, 2010 by and among PHI, Inc., the subsidiary guarantors and The Bank of New York Mellon Trust Company, N.A., as trustee (incorporated by reference to Exhibit 4.1 to PHI's Report on Form 8-K filed on September 23, 2010).
- 4.6 Form of 8.625% Senior Note due 2018 (incorporated by reference to Exhibit 4.2 to PHI's Report on Form 8-K filed on September 23, 2010).
- 10.1 Form of Indemnity Agreement dated November 4, 2011 between PHI, Inc. and each of its directors.
- 10.2 Form of Restricted Stock Unit Agreement under the Amended and Restricted Petroleum Helicopters, Inc. 1995 Incentive Compensation Plan between PHI, Inc. and Al A. Gonsoulin dated as of November 4, 2011.

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|         |   |
|---------|---|
| 31.1    | Certification pursuant to Section 302 of the Sarbanes-Oxley Act of 2002 by Al A. Gonsoulin, Chairman and Chief Executive Officer. |
| 31.2    | Certification pursuant to Section 302 of the Sarbanes-Oxley Act of 2002 by Michael J. McCann, Chief Financial Officer.            |
| 32.1    | Certification pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 by Al A. Gonsoulin, Chairman and Chief Executive Officer. |
| 32.2    | Certification pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 by Michael J. McCann, Chief Financial Officer.            |
| 101.INS | XBRL Instance Document  |
| 101.SCH | XBRL Taxonomy Extension Schema  |
| 101.CAL | XBRL Taxonomy Extension Calculation Linkbase  |
| 101.DEF | XBRL Taxonomy Extension Definition Linkbase   |
| 101.LAB | XBRL Taxonomy Extension Label Linkbase  |
| 101.PRE | XBRL Taxonomy Extension Presentation Linkbase   |

**SIGNATURES**

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

PHI, Inc.

November 7, 2011

By: /s/ Al A. Gonsoulin  
Al A. Gonsoulin  
Chairman and Chief Executive Officer

November 7, 2011

By: /s/ Michael J. McCann  
Michael J. McCann  
Chief Financial Officer