

SPACEHAB INC \WA\
Form S-4/A
August 16, 2005
Table of Contents

As filed with the Securities and Exchange Commission on August 16, 2005

Registration No. 333-126772

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

Amendment

No. 1

to

FORM S-4

REGISTRATION STATEMENT

UNDER

THE SECURITIES ACT OF 1933

SPACEHAB, Incorporated

(Exact name of registrant as specified in its charter)

Washington
(State or other jurisdiction of
incorporation or organization)

3760
(Primary standard industrial
classification code number)
12130 State Highway 3, Building 1

91-1273737
(I.R.S. Employer
Identification No.)

Edgar Filing: SPACEHAB INC \WA\ - Form S-4/A

Webster, Texas 77598-1504

(713) 558-5000

(Address, including zip code, and telephone number, including area code, of registrant's principal executive offices)

Michael E. Kearney

12130 State Highway 3, Building 1

Webster, TX 77598

(713) 558-5000

(Name, address, including zip code, and telephone number, including area code, of agent for service)

Copies to:

Arthur S. Berner

Haynes and Boone, LLP

1221 McKinney Street, Suite 2100

Houston, Texas 77010

Telephone: (713) 547-2526

Facsimile: (713) 236-5652

Rick C. Madden

Skadden, Arps, Slate, Meagher & Flom LLP

300 South Grand Avenue, Suite 3400

Los Angeles, California 90071

Telephone: (213) 687-5000

Approximate date of commencement of proposed sale of the securities to the public: As soon as practicable after the Registration Statement becomes effective.

If the securities being registered on this form are being offered in connection with the formation of a holding company and there is compliance with General Instruction G, check the following box. "

If this form is filed to register additional securities for an offering pursuant to Rule 462(b) under the Securities Act, check the following box and list the Securities Act registration statement number of the earlier effective registration statement for the same offering. " _____

If this form is a post-effective amendment filed pursuant to Rule 462(d) under the Securities Act, check the following box and list the Securities Act registration statement number of the earlier effective registration statement for the same offering. " _____

The registrant hereby amends this registration statement on such date or dates as may be necessary to delay its effective date until the registrant shall file a further amendment which specifically states that this registration statement shall thereafter become effective in accordance with Section 8(a) of the Securities Act of 1933 or until the registration statement shall become effective on such date as the Commission, acting pursuant to said Section 8(a), may determine.

Table of Contents

The information in this prospectus is not complete and may be changed. We may not complete the exchange offer and issue these securities until the registration statement filed with the Securities and Exchange Commission is effective. This prospectus is not an offer to sell these securities and it is not soliciting an offer to buy these securities in any state where the offer or sale is not permitted.

Subject to completion, dated August 16, 2005

SPACEHAB, Incorporated

Offer to Exchange and Consent Solicitation

in Respect of 5.5% Senior Convertible Notes due 2010

for

Any and All Outstanding 8% Convertible Subordinated Notes due 2007

(\$63,250,000 in principal amount outstanding)

The Exchange Offer and Consent Solicitation

Expiration Date. The exchange offer and consent solicitation expires at 5:00 p.m., New York City time, on [•], 2005, unless extended.

Exchange Offer and Consent Solicitation. If you decide to participate in the exchange offer, for each \$1,000 principal amount of our outstanding 8% Convertible Subordinated Notes due 2007 that you validly tender in accordance with the procedures in this prospectus before the exchange offer expires, you will receive \$1,000 principal amount of our new 5.5% Senior Convertible Notes due 2010, plus accrued and unpaid interest on the tendered outstanding notes. The exchange offer is open to all holders of our outstanding notes. Concurrently with this exchange offer, we are also soliciting consents to amend the indenture that governs the outstanding notes.

Conditions. The exchange offer is conditioned upon the satisfaction of several conditions, including, but not limited to, a minimum of \$60,087,500 aggregate principal amount of outstanding notes being tendered and the approval by the holders of our common stock of an increase in the number of authorized shares of our common stock and the issuance of our common stock upon exercise of the exchange notes. SMH Capital Advisors, Inc., the investment advisor to holders of \$40,366,000 in principal amount of the outstanding notes, has expressed its intent to tender the outstanding notes held by its clients in the exchange offer. SMH is not obligated to tender the outstanding notes under its management and its ability to tender such notes is subject to certain limitations, including any specific directions of any beneficial owner relating to those outstanding notes or the transfer of such outstanding notes out of the account managed by SMH. If you tender your outstanding notes, you are obligated to consent to the proposed amendments to the indenture governing the outstanding notes. You may not consent to the proposed amendments without tendering your outstanding notes.

Withdrawal. You may validly withdraw outstanding notes that you tender at any time until the exchange offer and consent solicitation expires.

Effect of Not Tendering. If you do not exchange your outstanding notes and the proposed amendments are adopted, you will continue to hold those notes, but the indenture governing those outstanding notes will be amended to remove the occurrence of a default on our other indebtedness as an event of default under the outstanding notes. In addition, the exchange notes being issued pursuant to this exchange offer will be senior in right of payment to any outstanding notes that you continue to hold.

The Exchange Notes

Maturity. The exchange notes will mature on October 15, 2010.

Interest. Interest on the exchange notes will accrue from the issue date at the rate of 5.5% per year. We will pay interest on the exchange notes semi-annually on each April 15 and October 15, commencing October 15, 2005.

Ranking. The exchange notes will be our general senior unsecured obligations ranking equally with our other senior unsecured debt, but will be effectively subordinated to all our secured debt, to the extent of the value of the assets securing such debt, and to all debt incurred by our subsidiaries.

Edgar Filing: SPACEHAB INC \WA\ - Form S-4/A

Conversion. The exchange notes are convertible into shares of our common stock at a conversion price ranging from \$2.12 to \$2.44 from the date of issuance until October 14, 2008. On and after October 15, 2008, the conversion price for the exchange notes will be \$2.50 per share. The exchange notes will be automatically converted into shares of our common stock at a conversion price of \$2.50 per share if the closing price of our common stock exceeds \$3.25 per share for 20 consecutive trading days at any time prior to the maturity date of the exchange notes. Our common stock is traded on The NASDAQ National Market under the symbol SPAB. On August 15, 2005, the last reported sale price of our common stock on The NASDAQ National Market was \$1.35.

Redemption and Repurchase. We may redeem some or all of the exchange notes at any time at 100% of the principal amount of the exchange notes being redeemed, plus accrued interest to the date of redemption and, if redeemed prior to [•], 2008, the payment of the premium described in this prospectus. If we experience a change of control, we must offer to purchase the exchange notes for 100% of their aggregate principal amount, plus accrued interest, payable, at our option, in cash or in shares of our common stock.

See **Risk Factors** beginning on page 14 for a discussion of certain risks that you should consider before participating in the exchange offer and consent solicitation.

Neither the Securities and Exchange Commission nor any state securities commission has approved or disapproved of these securities or determined if this prospectus is truthful or complete. Any representation to the contrary is a criminal offense.

The Co-Dealer Managers for the Exchange Offer and the Solicitation Agents for the Consent Solicitation are:

Jefferies & Company, Inc.

**Sanders Morris
Harris Inc.**

The date of this prospectus is [•], 2005

Table of Contents

TABLE OF CONTENTS

	Page
<u>Where You Can Find More Information</u>	ii
<u>Forward-Looking Statements</u>	iii
<u>Prospectus Summary</u>	1
<u>Risk Factors</u>	14
<u>Use of Proceeds</u>	29
<u>Capitalization</u>	29
<u>Ratio of Earnings to Fixed Charges</u>	30
<u>Industry Overview</u>	31
<u>Business</u>	32
<u>Selected Consolidated Financial Data</u>	42
<u>Management's Discussion and Analysis of Financial Condition and Results of Operations</u>	44
<u>Market for Our Common Stock and Related Stockholder Matters</u>	66
<u>Security Ownership of Certain Beneficial Owners and Management</u>	67
<u>Description of Other Indebtedness and Financing Arrangements</u>	70
<u>The Exchange Offer and Consent Solicitation</u>	71
<u>Material U.S. Federal Income Tax Considerations</u>	83
<u>Description of the Exchange Notes</u>	91
<u>Description of Our Capital Stock</u>	117
<u>Legal Matters</u>	120
<u>Independent Registered Public Accountants</u>	120
<u>Index to Financial Statements</u>	F-1

This exchange offer and consent solicitation is not being made to, nor will we accept tenders of outstanding notes from, holders of outstanding notes in any jurisdiction in which this exchange offer or the acceptance of outstanding notes would not be in compliance with the securities or blue sky laws of such jurisdiction.

Table of Contents

WHERE YOU CAN FIND MORE INFORMATION

This prospectus is part of a registration statement that we have filed with the SEC. You should read this prospectus and the information incorporated by reference, including the exhibits to the registration statement.

We file annual, quarterly, and current reports; proxy statements; and other information with the SEC. Our SEC filings are available to the public over the Internet at the SEC's web site at <http://www.sec.gov>. Our filings are located in the EDGAR database on that website. You may also read and copy any document we file at the SEC's public reference room at 100 F Street, N.E., Washington, D.C. 20549. You may obtain information on the operation of the SEC's public reference room in Washington, D.C. by calling the SEC at 1-800-SEC-0330.

All of our annual reports on Form 10-K, quarterly reports on Form 10-Q, current reports on Form 8-K, and amendments to such reports as well as other filings we make pursuant to Section 13(a) and 15(d) of the Securities Exchange Act of 1934 are also available free of charge through our Internet website. The address of our Internet website is www.spacehab.com. Our SEC filings are available through our website as soon as reasonably practicable after they are electronically filed or furnished to the SEC. However, information on our website is not incorporated by reference.

We incorporate by reference the information we file with the SEC, which means that we can disclose important information to you by referring you to those documents. The information incorporated by reference is considered to be part of this prospectus. Information that was filed prior to the date of this prospectus that is updated or superseded by information contained in this prospectus is considered a part of this prospectus only as so updated or superseded. Information that we later file with the SEC will automatically update and supersede the information contained in this prospectus and the documents incorporated by reference. We incorporate by reference the documents listed below and any future filings we make with the SEC under Sections 13(a), 13(c), 14, or 15(d) of the Securities Exchange Act of 1934 until we terminate this offering:

Our Annual Report on Form 10-K for the fiscal year ended June 30, 2004, as amended by our Form 10-K/A filed on July 20, 2005;

Our Quarterly Reports on Form 10-Q for the periods ended September 30, 2004, December 31, 2004, and March 31, 2005, as amended by our Form 10-Q/A filed on July 20, 2005;

Our Current Reports on Form 8-K filed on September 10, 2004, October 12, 2004, May 3, 2005, May 19, 2005, May 26, 2005, June 2, 2005, July 1, 2005, July 14, 2005, July 20, 2005 and August 16, 2005 (to the extent these items were filed with the SEC and not furnished);

Our Proxy Statement on Schedule 14A for our 2004 Annual Meeting filed on October 28, 2004; and

The description of our common stock, no par value per share, contained in our Registration Statement on Form S-1 filed on October 5, 1995.

This prospectus incorporates important business and financial information about us that is not included in or delivered with this document. You may request a copy of this information at no cost by writing or telephoning us at the following address and telephone number: Attention: Investor Relations, SPACEHAB, Incorporated, 12130 State Highway 3, Building 1, Webster, Texas 77598, telephone: (713) 558-5000.

The exchange offer and consent solicitation is expected to expire at 5:00 p.m., New York City time, on [•], 2005 and you must make your exchange decision by this expiration date. To obtain timely delivery of the requested information, you must request this information by [•], 2005 or the date that is no later than five business days before the expiration date.

In making your decision regarding participation in the exchange offer and consent solicitation, you should rely only on the information contained or incorporated by reference in this prospectus. We have not authorized anyone to provide you with any other information. We are not making an offer of these securities in places where offers and sales are not permitted. You should not assume that the information contained in this prospectus is accurate as of any date other than the date on the front cover of this prospectus, or that information incorporated by reference into this prospectus is accurate as of any date other than the date such information was filed with the SEC. Our business, financial condition, results of operations, and prospectus may have changed since that date.

Table of Contents

FORWARD-LOOKING STATEMENTS

This prospectus contains forward-looking statements within the meaning of Section 27A of the Securities Act of 1933 and Section 21E of the Securities Exchange Act of 1934. All statements, other than statements of historical fact or statements relating to the exchange offer and consent solicitation, are forward-looking statements for purposes of federal and state securities laws. Forward-looking statements may include the words may, will, plans, believes, estimates, expects, intends and other similar expressions. Such statements are subject to risks and uncertainties that could cause our actual results to differ materially from those projected in the statements. Such risks and uncertainties include, but are not limited to:

whether we will fully realize the economic benefits under our NASA and other customer contracts;

continued utilization by NASA and others of our habitat and logistics modules and related commercial space assets and services;

completion of the International Space Station, and the continued availability and use of the U.S. space shuttle;

technological difficulties and potential legal claims arising from any technological difficulties;

product demand and market acceptance risks, including our ability to develop and sell products and services to be used by the manned and unmanned space programs that replace the space shuttle program;

the effect of economic conditions in the U.S. or other space faring nations that could impact our ability to support or gain customers;

uncertainty in government funding and support for key space programs;

the impact of competition on our ability to win new contracts;

delays and uncertainties in future space shuttle and International Space Station programs;

the U.S. Government's commitment to President Bush's Vision for Space Exploration;

delays in the timing of performance of other contracts;

resolution of our claims against NASA relating to the loss of our research double module on the *Columbia* orbiter; and

risks described in the Risk Factors section of this prospectus.

Edgar Filing: SPACEHAB INC \WA\ - Form S-4/A

Although we believe that the assumptions underlying our forward-looking statements are reasonable, any of the assumptions could be inaccurate, and, therefore, we cannot assure you that the forward-looking statements included in this prospectus will prove to be accurate. In light of the significant uncertainties inherent in our forward-looking statements, the inclusion of such information should not be regarded as a representation by us or any other person that our objectives and plans will be achieved. Some of these and other risks and uncertainties that could cause actual results to differ materially from such forward-looking statements are more fully described under the heading Risk Factors beginning on page 14 of this prospectus and elsewhere in this prospectus, or in the documents incorporated by reference herein. Except as may be required by applicable law, we undertake no obligation to publicly update or advise of any change in any forward-looking statement, whether as a result of new information, future events or otherwise. In making these statements, we disclaim any obligation to address or update each factor in future filings with the SEC or communications regarding our business or results, and we do not undertake to address how any of these factors may have caused changes to discussions or information contained in previous filings or communications. In addition, any of the matters discussed above may have affected our past results and may affect future results, so that our actual results may differ materially from those expressed in this prospectus and in prior or subsequent communications.

Table of Contents

PROSPECTUS SUMMARY

This summary highlights information from this prospectus, but does not contain a complete description of our business or all material features of the exchange offer and consent solicitation. To understand all of the terms of the exchange offer and consent solicitation and for a more complete understanding of our business, you should carefully read the entire prospectus, particularly the section entitled "Risk Factors," and the materials to which we have referred you. You should also consult with your own legal and tax advisors.

In this prospectus, SPACEHAB, the Company, we, us, our and ours refer to SPACEHAB, Incorporated and its subsidiaries, unless the context otherwise requires. In this prospectus, we use the term "outstanding notes" to refer to the 8% Convertible Subordinated Notes due 2007 that we issued in October 1997 and the term "exchange notes" to refer to the 5.5% Senior Convertible Notes due 2010 that we have registered under the Securities Act of 1933 and are offering in exchange for the outstanding notes as described in this prospectus.

Our Company

Overview

We provide services that focus on the needs of organizations requiring access to the unique environment of space for commercial, scientific and other reasons. We are a leading provider of services that facilitate commercial access to space, and were the first company to commercially develop, own and operate pressurized space habitat modules. Serving the international community, we have experience supporting both manned and unmanned missions to space. We offer many levels of products and services by providing:

access to space through the use of our research and logistics modules and unpressurized integrated cargo carriers;

expertise on the habitability and occupational challenges of space;

facilities and support services needed to prepare satellites and payloads for launch;

engineering, analysis, and payload operations services;

program integration and control;

product design and development; and

space media, education, and retail goods.

Edgar Filing: SPACEHAB INC \WA\ - Form S-4/A

As an enabler of access to space, we provide these products and services to the space industry through the following three primary business units:

SPACEHAB Flight Services. Our Flight Services business unit provides research and logistics expertise and hardware, including a habitat module and unpressurized integrated cargo carriers provided to NASA for use on the U.S. space shuttle fleet.

Astrotech Space Operations. Our Astrotech spacecraft processing business unit provides facilities and support for the preparation of satellites and payloads for launch on expendable launch vehicles.

SPACEHAB Government Services. Our Government Services business unit provides project management and specialized engineering analysis, products, and services to NASA and other customers.

SPACEHAB Flight Services. The primary goal of our Flight Services business unit is to enable government and commercial enterprises to overcome the habitability and occupational challenges of space. Through the provision of experts, specialized hardware, and established processes, we help our customers access the resources of space. We offer a range of engineering, integration, operations, and ground support services that we tailor to meet our clients' specific requirements. Our Flight Services business unit provides a habitat module and unpressurized integrated cargo carriers to NASA for use on the U.S. space shuttle fleet and the International Space Station. We sell research and logistics services to NASA and commercial customers who want to use our

Table of Contents

modules and unpressurized carriers for specific space applications. Our modules provide space-based research facilities and pressurized cargo services for use aboard the space shuttle. Our single module, when installed in the payload bay of a space shuttle, more than doubles the space available to astronauts for research, habitation, and storage, while still leaving space in the shuttle bay for unpressurized cargo. We also have a second module that can be attached to our single module and used in the space shuttle in a double configuration. We outfit each module for research, logistics, or a combination of both depending on customer needs. Our unpressurized integrated cargo carrier systems are used to ferry equipment, supplies, and tools to the International Space Station onboard the space shuttle. As of August 12, 2005, our modules and integrated cargo carriers have flown on 19 missions on the space shuttle, including 13 logistics missions (six to the International Space Station and seven to the Russian space station *Mir*). For the July 2005 return-to-flight mission, we provided an integrated cargo carrier that was permanently attached to the International Space Station. Following the launch of the Space Shuttle *Discovery* in July 2005, NASA announced that the space shuttle fleet will be grounded for an indefinite period of time until loss of foam from the shuttle's external fuel tank can be remedied. In addition to our flight assets, we offer a full range of ground-based pre- and post-flight experiment and payload processing services and in-flight operations support.

Astrotech Space Operations. Our Astrotech spacecraft processing business unit provides government and commercial customers with a commercial alternative to using government-owned facilities to prepare their satellites for launch in the United States. We believe that growing wireless telecommunication demands, such as direct-broadcast radio and television, cellular telephones, and broadband internet services, as well as the continued need for video and long-distance telephone transmissions, will provide us with opportunities to expand our customer base. Our modern facilities are used by payload customers launching on a wide range of expendable launch vehicles, including Atlas, Delta, Pegasus, Sea Launch, and Taurus, as well as secondary payloads flown on the space shuttle. Our largest facility, which we own, supports spacecraft processing for launches in Cape Canaveral and is capable of processing larger five meter class satellites and payload fairings for Lockheed Martin's and Boeing's Evolved Expendable Launch Vehicle Programs. The satellite and payload fairings for the Evolved Expendable Launch Vehicle Programs are significantly larger than other launch vehicles currently in use and require larger facilities for processing. We also lease facilities located on Vandenberg Air Force Base to support launches on the west coast. In addition, we manage the facilities at the Port of Long Beach that are used to process satellites and payloads being launched from an equatorial sea-based platform by Sea Launch Company, LLC. As of June 30, 2005, we had supported the processing of more than 225 satellites and payloads.

SPACEHAB Government Services. Our Government Services business unit has provided specialized engineering support services for the U.S. Government, including NASA, and various commercial industries for over 30 years. Specifically, we have supported the Government in the areas of:

large-scale configuration and data management programs, including for the construction of the International Space Station;

specialized design, development, and fabrication of flight hardware;

low- to high-fidelity mockup design and construction; and

safety and quality support services.

Space Media, Inc. In addition to our three primary business units, we also have a majority-owned subsidiary that creates proprietary space-themed content for education and commerce. By leveraging our access to engineers, marketing and industry professionals, and aerospace subcontractors, we are able to provide the space enthusiast with a variety of services and products. These services range from outfitting a comprehensive space exhibit to providing astronaut appearances and product endorsements. This business unit owns and operates an online retailing outlet, TheSpaceStore.com, and a retail store adjacent to NASA's Johnson Space Center in Houston. Our website and retail store offer hundreds of products, providing distinctive and personalized gifts, clothing, mission patches, space collectibles, and more. Through the STARS Program, we provide educational and outreach services to schools around the globe through which we help students develop and fly their own experiments in space.

Table of Contents

Strategy

Our strategic vision is to be a recognized market leader in providing services to support space operations and utilization with consistent growth, high employee morale, and a realistic shareholder return on investment. Extracted from that vision, our strategies encompass the following:

deliver excellence on current work;

leverage our mission/program support expertise;

provide technical support on space programs;

expand and enhance existing payload-processing facilities;

design solutions that encourage private commercial investment in space;

develop space-related hardware;

support alignment of domestic and foreign resource sharing; and

identify new applications for our technology and expertise.

We believe that our business units are tactically aligned with our overriding corporate strategy in a manner that is poised to achieve our operational and financial goals. Our units are focused on three areas in the near term:

utilizing the expertise of our Flight Services business unit to provide support for the space shuttle's return-to-flight and subsequent missions, assembly and utilization of the International Space Station, and the evolution of NASA's exploration initiatives;

expanding our Astrotech spacecraft processing business unit's revenue base through new markets and services in an effort to increase utilization of our modern, commercially-operated facilities and extensive payload processing expertise; and

supporting the International Space Station Program Office through our Government Services business unit under cost reimbursable government contracts, further defining ourselves as a principal in configuration and data management services.

We are continuing to identify new business opportunities within our core competencies to maintain and expand our role as a NASA team member and commercial space access facilitator. For example, we recently completed a six-month NASA study contract valued at approximately \$1.0 million to support the space agency's new exploration initiatives. The purpose of this contract was to design a technical solution to accomplish the agency's objectives for lunar exploration and to identify systems that could also be used on missions to Mars and other

destinations. Our winning proposal documented our approach for designing an architecture that takes advantage of commercial efficiencies; specifically, how private industry can benefit from investing in transporting people to the moon and elsewhere. We believe that our approach results in lower program costs and provides the additional benefit of applying existing capabilities and mature technology. Following our initial six-month effort, NASA awarded us an additional six-month contract, also valued at approximately \$1.0 million, to continue and expand upon our initial work.

Our NASA study contract involves us in President Bush's space exploration vision at the onset, allowing us to promote the value of commercial solutions and private enterprise in NASA's growing initiatives. NASA is now in the process of defining the next steps for the national vision and will be issuing multiple proposals for the development of a crew exploration vehicle and a lunar vehicle, and the use of mature technologies that will assist in the process of exploring the moon and beyond. We believe that our expertise in the areas of logistics services, crew habitability, payload integration, and ground processing positions us to benefit from NASA's new initiatives.

In order to meet the evolving needs of NASA's exploration program and potential commercial customers, we are in the process of developing a commercial payload service. We believe that retirement of the shuttle eliminates a significant payload transport capability both to and from space for which NASA has not identified a

Table of Contents

replacement. Additionally, the retirement of the shuttle results in the loss of an orbiting platform that can host short duration technology maturation experiments. Our goal is to enable the smooth transition of a portion of space shuttle based International Space Station payload transport capabilities to commercial payload transport services. We are designing our proposed commercial payload service so that it can evolve with minimal redesign efforts as NASA migrates from International Space Station operations in low Earth orbit to lunar operations and beyond. Our proposed commercial payload service would consist of a variety of spacecraft that could be launched using existing expendable, unmanned launch vehicles, from smaller rockets to Boeing's Delta IV and Lockheed Martin's Atlas V Evolved Expendable Launch Vehicle Programs. We believe that we will have a payload transport carrier by 2008.

Recent Developments

In April 2005, we consummated the sale and lease back of our 58,000 square-foot payload processing facility in Cape Canaveral, Florida in a transaction with Tamir Silvers LLC for \$4.8 million. This payload processing facility hosts payload integration activities for our modules and integrated cargo carriers. This lease offers the flexibility to respond to new opportunities and re-evaluate our facility requirements for both our nearby Cape Canaveral and Titusville, Florida locations upon the proposed retirement of the space shuttle in 2010. The contract terms provide for a lease by us of 100% of the facility for an initial period of five years, with an option period for an additional five years. Currently, we have subleases in place that occupy approximately 20% of the available space with another 20% available for prospective tenants.

On May 26, 2005, we exercised a right of first refusal contained in the lease for our 90,000 square foot corporate administrative facility and an adjacent three acres of land in Webster, Texas. We purchased the building and the adjacent three acres of land from American National Insurance Corporation for \$2.0 million. We sold the building, excluding the three acres of adjacent undeveloped land for \$3.25 million pursuant to a sale-leaseback arrangement. We have leased back 100% of the facility for an initial period of ten years, with two five-year options. We retained the adjacent three acres parcel for future development or sale.

In January 2004, Lloyd's of London, our insurer for the research double module, filed a complaint in the United States District Court for the Western District of Washington seeking the return of the \$17.7 million Lloyd's had paid to us under the research double module insurance policy. On May 12, 2005 we and Lloyd's agreed to jointly pursue recovery against NASA with us in full control of the appeals process. Lloyd's will participate in any recovery both pursuant to our administrative claim and our tort claim against NASA, net of legal costs, in accordance with a pre-agreed schedule under which our liability to Lloyd's ranges from a minimum of \$500,000 if we do not recover any additional amounts to approximately \$17.7 million if we recover over \$70.0 million from NASA. Also in accordance with the agreement, Lloyd's dismissed its complaint against us with prejudice. We will record a charge in our fourth quarter financial statements of \$500,000 pending a final resolution of our actions against NASA. For a discussion of our claims against NASA see Business Legal Proceedings.

On July 20, 2005, we restated our statements of cash flows for the year ended June 30, 2003 and the nine months ended March 31, 2005 to revise the classification of insurance and contractual indemnification proceeds that we received in connection with the loss of our research double module. We originally classified these proceeds, which totaled \$17.7 million in insurance proceeds and \$8.2 million in indemnification proceeds, as cash flows from operating activities; however, such proceeds should have been classified as cash flows from investing activities. Our restatement properly classifies such amounts.

The address of our principal executive offices is 12130 State Highway 3, Building 1, Webster, Texas 77598. Our telephone number is (713) 558-5000. Our Internet website address is www.spacehab.com. Information contained in or connected to our Internet website is not a part of this prospectus.

Table of Contents

The Exchange Offer and Consent Solicitation

The material terms of this exchange offer and consent solicitation are summarized below. However, in addition, we encourage you to read the detailed descriptions in the sections entitled **The Exchange Offer and Consent Solicitation** and **Summary Comparison of Key Differences Between the Outstanding Notes and the Exchange Notes** for further information about the exchange offer and the consent solicitation.

We are making this exchange offer and consent solicitation in order to increase our liquidity by reducing our interest expense, extend the maturity of the outstanding notes since we do not believe that we would be able to make the required principal payment on the outstanding notes in 2007, and modify the terms of the notes, including the conversion price, so that they more closely resemble current market terms for convertible notes.

We believe that the corporate restructuring and refinancing steps taken to date are inadequate to provide sufficient cash flow to fund research and development efforts necessary to develop new space assets that we believe will be required to ensure our long term viability and competitiveness. Furthermore, if the outstanding notes remain outstanding, we do not believe that we will have the financial flexibility necessary to obtain future financing to fund needed research and development efforts. In addition to limiting our ability to fund research and development, if the exchange offer is not completed, we will be required to direct substantial available cash flows during the next two years to the repayment of the outstanding notes by 2007. Since we do not believe that these cash flows will be sufficient to repay the outstanding notes in 2007, we may also be required to divest core assets to generate sufficient funds to repay the outstanding notes at maturity and, if such divestitures are not successful, to seek a restructuring of our debt.

We believe that the actions that would need to be taken to repay the outstanding notes in 2007 would substantially narrow our future prospects. The cash flows redirected to the repayment of, and any divestiture of assets to repay, the outstanding notes may not generate sufficient funds to fully repay the outstanding notes. Due to the adverse effects that the outstanding notes will have on our future liquidity and ability to restructure and refocus our business at a time when our largest market is changing dramatically, we are proposing to exchange the outstanding notes for exchange notes pursuant to the terms of the exchange offer described below.

The Exchange Offer

We are making this exchange offer for all of our outstanding 8% Convertible Subordinated Notes due 2007. For every \$1,000 in principal amount of outstanding notes that you validly tender prior to the expiration of the exchange offer, you will receive \$1,000 in principal amount of 5.5% Senior Convertible Notes due 2010, plus accrued and unpaid interest on the outstanding notes that you tender. The exchange notes will bear a different CUSIP number from the outstanding notes.

Consent Solicitation

In addition to the exchange offer, we are soliciting consents to amend provisions of the indenture governing the outstanding notes. If you tender your outstanding notes in the exchange offer and they are accepted, you will be consenting to amend the indenture that governs the outstanding notes to remove the occurrence of a default on our other indebtedness as an event of default under the outstanding notes. Duly executed consents to the proposed amendment from holders representing at least a majority of the principal amount of the outstanding notes are required to amend the indenture governing the outstanding notes.

Table of Contents

Exchange Offer and Consent Solicitation Expiration Date The expiration date for the exchange offer and consent solicitation is 5:00 p.m., New York City time, on [●], 2005, unless we extend the expiration date. It is possible that we will extend the exchange offer. See The Exchange Offer and Consent Solicitation Expiration Date; Extensions; Amendments.

Withdrawal Rights You may withdraw outstanding notes you tendered by furnishing a notice of withdrawal to the exchange agent or by complying with applicable ATOP procedures at any time before 5:00 p.m., New York City time, on the expiration date or at any time after midnight, New York city time, on [●], 2005 if the outstanding notes have not been accepted for exchange. See The Exchange Offer and Consent Solicitation Withdrawal of Tenders.

Accrued Interest on the Exchange Notes and the Outstanding Notes You will receive accrued and unpaid interest on any outstanding notes accepted in the exchange offer, calculated from the last interest payment date up to but excluding the issue date of the exchange notes. The exchange notes will bear interest from the issue date at a rate of 5.5% per year. We will pay interest on the exchange notes in cash semi-annually on each April 15 and October 15, commencing October 15, 2005.

Conditions to the Exchange Offer The exchange offer is conditioned upon the satisfaction of several conditions, including, but not limited to, a minimum of \$60,087,500 aggregate principal amount of outstanding notes being tendered and the approval by the holders of our common stock of an increase in the number of authorized shares of our common stock and the issuance of common stock upon exercise of the exchange notes. See The Exchange Offer and Consent Solicitation Conditions. SMH Capital Advisors, Inc. is a registered investment advisor who has been granted discretionary authority to sell, tender, or exchange an aggregate principal amount of \$40,366,000 of the outstanding notes by the beneficial owners of those outstanding notes. While SMH Capital Advisors' ability to tender the outstanding notes under its management is subject to certain limitations, including any specific directions of any beneficial owner relating to those outstanding notes or the transfer of such outstanding notes out of the account managed by SMH Capital Advisors, SMH Capital Advisors has expressed its intent to tender all outstanding notes under its management at the time of the closing of the exchange offer. SMH Capital Advisors is under no obligation to tender any of the outstanding notes under its management and we cannot make any assurances that it will tender the outstanding notes that it holds. In addition, an affiliate of SMH Capital Advisors, Sanders Morris Harris Inc., is acting as a co-dealer manager in connection with this transaction and will receive compensation for serving in such capacity. See The Exchange Offer and Consent Solicitation Co-Dealer Managers and Soliciting Dealer Fees.

Table of Contents

Consent to Amendments	If you tender your outstanding notes for exchange, you are obligated to consent to the proposed amendments. You may not consent to the proposed amendments without tendering your outstanding notes.
Dissenter s Rights	Holders of the outstanding notes do not have any appraisal or dissenters rights under the Washington Business Corporation Act or the indenture in connection with the exchange offer and consent solicitation.
Governmental Approvals	No governmental approvals or consents must be received to consummate the exchange offer and consent solicitation.
Procedures for Tendering Outstanding Notes Held in the Form of Book-Entry Interests	<p>The outstanding notes were issued as global securities and were deposited with Wachovia Bank, National Association who holds the outstanding notes as the custodian for the Depository Trust Company (DTC). Beneficial interests in the outstanding notes are held by participants in DTC on behalf of the beneficial owners of the outstanding notes. We refer to beneficial interests in notes held by participants in DTC as notes held in book-entry form. Beneficial interests in notes held in book-entry form are shown on, and transfers of the notes can be made only through, records maintained in book-entry form by DTC and its participants.</p> <p>If you are a holder of an outstanding note held in the form of a book-entry interest and you wish to tender your book-entry interest for exchange in the exchange offer, you must transmit to Wachovia Bank, National Association, as exchange agent, on or prior to the expiration date of the exchange offer, the following:</p> <ul style="list-style-type: none">a computer-generated message transmitted by means of DTC s Automated Tender Offer Program (ATOP) system that, when received by the exchange agent will form a part of a confirmation of book-entry transfer in which you acknowledge and agree to be bound by the terms of the letter of transmittal; anda timely confirmation of book-entry transfer of your outstanding notes into the exchange agent s account at DTC, according to the procedure for book-entry transfers described in this prospectus under the heading The Exchange Offer and Consent Solicitation Procedures for Tendering Outstanding Notes Held in Book-Entry Form.
Procedures for Tendering Outstanding Notes Held in Certificated Form	If you hold your outstanding notes in certificated form and wish to accept the exchange offer, sign and date the letter of transmittal, and deliver the letter of transmittal, along with certificates for the outstanding notes and any other required documentation, to the exchange agent on or before the expiration date in accordance with the instructions contained in this prospectus and the letter of transmittal.

Table of Contents

Special Procedures for Beneficial Owners	If you are a beneficial owner whose outstanding notes are registered in the name of a broker, dealer, commercial bank, trust company or other nominee and wish to tender those outstanding notes in the exchange offer, please contact the registered holder as soon as possible and instruct them to tender on your behalf and comply with the instructions in this prospectus and the letter of transmittal.
Guaranteed Delivery Procedures	If you are unable to deliver the outstanding notes, the letter of transmittal or any other required documents to the exchange agent or comply with the applicable ATOP procedures prior to the expiration date, you may tender your outstanding notes according to the guaranteed delivery procedures described in this prospectus under the heading "The Exchange Offer and Consent Solicitation - Guaranteed Delivery Procedures."
Acceptance of Outstanding Notes and Delivery of Exchange Notes	If the conditions described under "The Exchange Offer and Consent Solicitation - Conditions" are satisfied, we will accept for exchange any and all outstanding notes that are properly tendered and not withdrawn before the expiration date. See "The Exchange Offer and Consent Solicitation - Procedures for Tendering." If we close the exchange offer, the exchange notes will be delivered promptly following the expiration date. Otherwise, we will promptly return any outstanding notes that are not accepted.
Consequences of Failure to Exchange	If you do not exchange your outstanding notes and the proposed amendments are adopted, you will continue to hold those notes, but the indenture governing those outstanding notes will have been amended to remove the occurrence of a default on our other indebtedness as an event of default under the outstanding notes. In addition, the exchange notes being issued pursuant to this exchange offer will be senior in right of payment to any outstanding notes that you continue to hold. See "Material U.S. Federal Income Tax Considerations" for a discussion of U.S. federal income tax considerations of the failure to exchange your outstanding notes.
Federal Income Tax Considerations	We intend to take the position that the exchange of outstanding notes for exchange notes as a tax-free recapitalization for purposes of United States federal income taxation. If the exchange qualifies as a recapitalization, you generally will not recognize taxable gain or loss as a result of the exchange. See "Material U.S. Federal Income Tax Considerations" for a discussion of U.S. federal income tax considerations you should consider before tendering outstanding notes in the exchange offer. You should also consult your own tax advisor as to the consequences to you of participating in the exchange offer or your decision not to participate in the exchange offer.
Co-Dealer Managers	Jefferies & Company, Inc. and Sanders Morris Harris Inc.

Table of Contents

Soliciting Dealer Fees

If you validly tender, and we accept from you, \$500,000 or less in aggregate principal amount of the outstanding notes, we will pay your broker a soliciting dealer fee of an amount equal to 1.5% of those tendered and accepted outstanding notes. For more information, please see [The Exchange Offer and Consent Solicitation Soliciting Dealer Fees](#).

Information Agent

CapitalBridge is serving as information agent for the exchange offer and consent solicitation. The address for the information agent is listed under [The Exchange Offer and Consent Solicitation Information Agent](#). If you would like more information about the exchange offer and consent solicitation, you should call the information agent at (877) 746-3583 (toll-free). The facsimile number for the information agent is (201) 499-3600.

Exchange Agent

Wachovia Bank, National Association is serving as exchange agent for the exchange offer and consent solicitation. The address for the exchange agent is listed under [The Exchange Offer and Consent Solicitation Exchange Agent](#). If you would like more information about the exchange offer, you should call the exchange agent at (704) 590-7413. The facsimile number for the exchange agent is (704) 590-7628.

See [The Exchange Offer and Consent Solicitation](#) for more detailed information concerning the terms of the exchange offer and consent solicitation.

Table of Contents**Summary Comparison of Key Differences Between the Outstanding Notes and the Exchange Notes**

The following is a summary of the key differences between the provisions of our outstanding 8% Convertible Subordinated Notes due 2007 and our new 5.5% Senior Convertible Notes due 2010 that are being offered in exchange for the outstanding notes and the reasons we believe these changes will help us to implement our strategic restructuring plan. This summary only describes the material differences between the indenture governing the outstanding notes and the indenture governing the exchange notes. We urge you to review each of these indentures to review additional changes that may be important to you.

Outstanding 8% Convertible	New 5.5% Senior Convertible
Subordinated Notes due 2007 Indenture	Notes due 2010 Indenture
<p>Interest Rate. The outstanding notes bear interest at 8% per year.</p> <p>Maturity Date. The maturity date for the outstanding notes is October 15, 2007.</p> <p>Ranking. The outstanding notes are subordinated to all of our senior indebtedness.</p> <p>Conversion Price. The conversion price for the outstanding notes is \$13.625 per share of common stock.</p> <p>Mandatory Conversion. The outstanding notes do not have any mandatory conversion provisions.</p> <p>Redemption. The outstanding notes can currently be redeemed at a redemption price equal to 101.7778% of the principal amount. From October 15, 2005 until October 14, 2006 the outstanding notes will be redeemable at a price equal to 100.8889% of the principal amount. On and after October 15, 2006, the outstanding notes are redeemable at a redemption price equal to 100% of the principal amount. In connection with any redemption, accrued and unpaid interest to the redemption date is also payable to the holders of the outstanding notes.</p> <p>Limitation on Senior Secured Indebtedness and Acquired Indebtedness. The indenture governing the outstanding notes does not limit the incurrence of additional indebtedness.</p>	<p>Interest Rate. The exchange notes bear interest at 5.5% per year.</p> <p>Maturity Date. The maturity date for the exchange notes is October 15, 2010.</p> <p>Ranking. The exchange notes will be senior indebtedness.</p> <p>Conversion Price. The conversion price for the exchange notes will initially be \$2.12 and will increase semi-annually until October 15, 2008, when the conversion price will be set at \$2.50.</p> <p>Mandatory Conversion. If our stock price exceeds \$3.25 for 20 consecutive trading days, the exchange notes will be automatically converted into shares of our common stock.</p> <p>Redemption. The exchange notes can be redeemed at a redemption price equal to 100% of the principal amount, plus accrued and unpaid interest to the date of redemption. In addition, if the exchange notes are redeemed prior to [•], 2008 we will be required to pay a make-whole premium equal to the present value of interest payments remaining from the date of redemption until [•], 2008, discounted using the treasury rate on the date of redemption plus 1%.</p> <p>Limitation on Senior Secured Indebtedness and Acquired Indebtedness. The indenture governing the exchange notes prohibits us from incurring more than \$20 million in additional senior secured indebtedness and, unless a leverage ratio test is met, from assuming or incurring indebtedness in connection with acquisitions. For a description of this covenant see Description of the Exchange Notes Certain Covenants Limitation on Incurrence of Senior Secured Indebtedness and Assumption of Acquired Indebtedness</p>

Table of Contents

Outstanding 8% Convertible

Subordinated Notes due 2007 Indenture

Limitation on Dividends. The indenture governing the outstanding notes does not limit the payment of dividends.

Change of Control. In the event of a change of control, holders of the outstanding notes have the right to require us to repurchase their outstanding notes at a price equal to 100% of the principal amount of such notes, plus accrued and unpaid interest. The provisions in the indenture governing the outstanding notes regarding a change of control can not be amended without the consent of all affected holders.

New 5.5% Senior Convertible

Notes due 2010 Indenture

Limitation on Dividends. The indenture governing the exchange notes prohibits us from paying dividends on our common stock unless the dividends are paid in shares of our non-redeemable capital stock or common stock of any of our subsidiaries. The indenture governing the exchange notes will not limit our ability to repurchase or redeem our common stock.

Change of Control. The indenture governing the exchange notes contains provisions substantially similar to the provisions in the indenture for the outstanding notes that permits holders of the exchange notes to require us to repurchase their exchange notes at a price equal to 100% of the principal amount of such notes, plus accrued and unpaid interest. Unlike the indenture for the outstanding notes, we are permitted to repurchase exchange notes upon a change of control in cash or in shares of our common stock, valued at the average closing price of our common stock for the 15 trading days immediately preceding the second trading day before we give notice of a change of control. The provisions in the indenture governing the exchange notes regarding a change of control can be amended with the approval of the holders of at least a majority in principal amount of the outstanding exchange notes.

Table of Contents

The Exchange Notes

The following is a summary of the terms of the exchange notes. For a more complete description of the differences between the outstanding notes and the exchange notes, see Summary Comparison of Key Differences Between the Outstanding Notes and the Exchange Notes.

Issuer	SPACEHAB, Incorporated.
Title	5.5% Senior Convertible Notes due 2010.
Maturity Date	October 15, 2010
Interest Payment Dates	Interest will be payable semi-annually on April 15 th and October 15 th , commencing October 15, 2005.
Ranking	The exchange notes will be the unsecured and unsubordinated debt of SPACEHAB, Incorporated. Accordingly, they will rank:

equally with all of our existing and future unsecured and unsubordinated debt;

effectively subordinated to any future secured debt to the extent of the assets securing such debt, including our senior credit facility;

effectively subordinated to all debt of our subsidiaries, including the \$3.7 million term loan of Astrotech Florida Holdings, which we have also guaranteed; and

ahead of any of our future subordinated debt.

As of June 30, 2005, we and our subsidiaries had \$67.0 million in principal amount of indebtedness outstanding, which consists of \$63.3 million in aggregate principal amount of the outstanding notes and \$3.7 million in aggregate principal amount of indebtedness of our subsidiary Astrotech Florida Holdings.

Guarantees	The exchange notes will not be guaranteed by any of our current or future subsidiaries.
-------------------	---

Optional Conversion	The exchange notes are convertible into shares of our common stock at a conversion price that increases semi-annually as follows:
----------------------------	---

Period

Conversion Price

Per Share

Issue Date	April 14, 2006	\$	2.12
	April 15, 2006 - October 14, 2006	\$	2.19
	October 15, 2006 - April 14, 2007	\$	2.25
	April 15, 2007 - October 14, 2007	\$	2.32
	October 15, 2007 - April 14, 2008	\$	2.38
	April 15, 2008 - October 14, 2008	\$	2.44
	October 15, 2008 and thereafter	\$	2.50

Table of Contents

Mandatory Conversion

The exchange notes will be automatically converted into shares of our common stock at a conversion price of \$2.50 per share if the closing price of our common stock exceeds \$3.25 per share for 20 consecutive trading days at any time prior to the maturity date of the exchange notes.

Optional Redemption

We may redeem some or all of the exchange notes at any time at 100% of the principal amount of the exchange notes being redeemed, plus accrued interest to the date of redemption. If we redeem the exchange notes prior to October 15, 2008, we will be required to pay a make-whole premium equal to the present value of the interest payments due on the exchange notes being redeemed to October 15, 2008, computed using a discount rate equal to the treasury rate on such date plus 1%.

Change of Control

Upon the occurrence of a change of control (as described under [Description of the Exchange Notes - Repurchase at the Option of Holders upon Change of Control](#)), we must offer to repurchase the exchange notes at 100% of the principal amount of the exchange notes, plus accrued interest to the date of repurchase. At our option, we may pay this amount in cash or in shares of our common stock valued at the average closing price of our common stock for the 15 trading days immediately preceding the second trading day before we give notice of a change of control. We may not be able to repurchase the exchange notes upon a change of control. See [Risk Factors - Risks Related to the Exchange Notes](#) We may be unable to make a change of control offer required by the indenture governing the exchange notes, which would cause defaults under the indenture governing the exchange notes, our revolving credit facility and other financing arrangements.

Certain Covenants

The indenture under which the exchange notes will be issued contains covenants that will, among other things, limit our ability to incur additional senior secured indebtedness, assume or incur indebtedness in connection with acquisitions, and sell assets or merge with other companies. These covenants are subject to a number of important qualifications and exceptions as described in this prospectus under the caption [Description of the Exchange Notes - Certain Covenants](#).

See [Description of the Exchange Notes](#) for more detailed information about the terms of exchange notes.

Risk Factors

See [Risk Factors](#) for a discussion of factors you should carefully consider before deciding to participate in the exchange offer and consent solicitation and invest in the exchange notes.

Table of Contents

RISK FACTORS

You should carefully consider the following risks and other information contained or incorporated by reference in this prospectus before deciding to participate in the exchange offer and consent solicitation. The risks and uncertainties described below are not the only risks facing us or applicable to your investment in our exchange notes. Additional risks not presently known to us or which we consider immaterial based on information currently available to us may also materially adversely affect us. If any of the following risks or uncertainties actually occur, our business, financial condition and results of operations could be materially adversely affected.

Risks Related to Our Business

In 2004, our Flight Services business unit derived over 80% of its revenues, which represented approximately 50% of our fiscal year 2004 consolidated revenues, from the use of our modules and integrated cargo carriers by the space shuttle fleet, which is currently expected to be retired by 2010.

Our modules and integrated cargo carriers have been specifically designed to enhance the capabilities of the space shuttle and, therefore, our current Flight Services business is highly dependent on the availability of the space shuttle fleet. President Bush's vision for U.S. space exploration envisions that the United States will fulfill its commitments to international partners and complete its work on the International Space Station by 2010. The shuttle is currently scheduled to be retired after its work on the station is complete. Our single module is currently scheduled to fly on two space shuttle missions. Since the shuttle's chief purpose is anticipated to be assisting in the completion of the assembly of the station, our modules may not be used for many additional missions, if any. We currently own one single module and a second module that can be added to our single module in order for it to be configured as a double module. We invested approximately \$72.5 million in the design and construction of these two modules. We do not anticipate being able to sell or use these two modules or use our integrated cargo carriers following the retirement of the space shuttle fleet. If our Flight Services business is unable to develop projects or services that will be used by the crew exploration vehicle and other spacecraft that will replace the shuttle fleet, our financial condition and results of operations will be materially adversely affected.

Our Flight Services business unit depends on regular space shuttle flights.

In addition to the scheduled retirement of the space shuttle fleet, the space shuttle fleet has been grounded for extended periods numerous times. The space shuttle fleet was grounded until July 2005 following the loss of the Space Shuttle *Columbia* on re-entry in February 2003. Following the launch of the Space Shuttle *Discovery* in July 2005, NASA announced that the space shuttle fleet will be grounded for an indefinite period of time until loss of foam from the shuttle's external fuel tank can be remedied. All missions aboard the space shuttle were previously suspended from January 1986 to September 1988, pending the redesign of certain of its subcomponents which had caused the loss of the Space Shuttle *Challenger*. The space shuttle fleet has also been temporarily grounded for shorter periods of time on several occasions. No assurances can be made as to when NASA will lift the current grounding of the space shuttle fleet, that future missions of the space shuttle will not be delayed, or that NASA will launch the number of space shuttle missions currently scheduled. There are three space shuttles in operation. Failure to have access to the space shuttle, either through technical difficulties affecting the entire fleet or the loss of an individual space shuttle, would have a material adverse effect on our financial condition and results of operations.

We have incurred, and expect in the future to incur, significant legal costs related to the loss of our research double module in the Columbia tragedy.

On February 1, 2003 we lost our research double module in the *Columbia* tragedy. We sought indemnification from NASA in the amount of \$87.7 million for the value of our research double module and related equipment that was destroyed. We received insurance proceeds of \$17.7 million and \$8.0 million in indemnification from NASA in connection with the loss of this module. We have filed an appeal of NASA's decision to deny our claim for indemnification in excess of \$8.0 million with the Armed Services Board of

Table of Contents

Contract Appeals and a tort claim against NASA seeking damages of \$79.7 million for the loss of the research double module. Since NASA did not respond to our claim for six months from the date on which we made the claim, NASA is deemed to have denied our claim. As a result of our administrative claim being deemed denied due to NASA's failure to respond, we have the right to, and intend to, pursue our tort claim in federal district court. In pursuing our appeal and tort claims, we will be required to expend material amounts on legal fees, but may not recover any additional amounts from NASA. Lloyd's will participate in any recovery both pursuant to our administrative claim and our tort claim against NASA, net of legal costs, in accordance with a pre-agreed schedule under which our liability to Lloyd's ranges from a minimum of \$500,000 if we do not recover any additional amounts to approximately \$17.7 million if we recover over \$70.0 million from NASA.

Since we do not intend to build any more modules, if our single module is lost, our net income from operations associated with space shuttle missions would be materially reduced and our insurance coverages may not be adequate.

Our second module is designed to convert our single module into a double module configuration. It can only be used in connection with our remaining single module. If our single module is lost as a result of another shuttle accident, we will not have any modules available for future shuttle missions. If we only lost our single module, we could not recover insurance proceeds for the second module, which is not usable without the single module. Although our modules are insured for replacement value if they are lost, we currently do not intend to build any additional modules due to the planned retirement of the space shuttle fleet in 2010 and the inability of our modules to be used on other spacecraft. As a result, the loss of one or both of our modules would materially reduce the amount of income we could potentially generate from the remaining shuttle missions. In addition, the loss of another space shuttle could result in the termination of the shuttle program earlier than is currently expected. In the event of another catastrophic space tragedy in which our modules or carriers cause damage to third parties, our liability may exceed the limits of our liability coverage. The loss of one or both of our modules will materially reduce our net income from operations associated with shuttle missions and will have a material adverse affect on our financial condition and results of operations.

Since we are dependent on NASA as a customer, if the products and services we are currently developing for use by NASA's successor to the space shuttle program are not used, our financial condition and results of operations will be materially adversely affected.

Approximately 54% of our fiscal 2004 revenue was generated from seven contracts supporting NASA. We anticipate that revenue from NASA-related projects will continue to account for a material amount of our revenue in the future. We currently are providing services supporting NASA under five primary contracts. There are no assurances, however, that NASA will require our module or integrated cargo carrier services in the future. We currently anticipate that NASA will not use our modules as much as they have in the past. Even if NASA continues to use our modules and integrated cargo carriers to the same extent that it did prior to the suspension of shuttle flights following the *Columbia* disaster, these products will become obsolete when the space shuttle is retired. See In 2004, our Flight Services business unit derived over 80% of its revenues, which represented approximately 50% of our fiscal year 2004 consolidated revenues, from the use of our modules and integrated cargo carriers by the space shuttle fleet, which is currently expected to be retired by 2010. Our failure to execute new contracts supporting NASA for use of our modules and integrated cargo carriers could have a material adverse effect on our financial condition and results of operations.

In the past, we have developed products without any firm commitments from NASA. Although we may invest substantial amounts developing products for the shuttle's replacement program without any contracts with NASA, we cannot provide any assurances that such products will be used. Since the final program that will be chosen by NASA is not currently known, we can not provide any assurances that the products and services we may develop will be suitable for such replacement programs. If NASA or its contractors do not purchase the products and services we are developing for the shuttle's replacement programs, our financial condition and results of operations will be adversely affected.

Termination of our backlog of orders could negatively impact our revenues.

As of March 31, 2005, we had a firm backlog of approximately \$17 million and total backlog of approximately \$81.9 million. Firm backlog consists of aggregate contract values, excluding the portion previously

Table of Contents

recognized as revenues, and our estimate of potential award fees. Total backlog includes firm backlog in addition to unexercised options under existing contracts, expected indefinite-quantity indefinite delivery task orders under existing contracts and undefinitized orders under existing contracts, which may not result in definitized contracts or orders. Backlog as of March 31, 2005 does not give effect to new orders received or any terminations or cancellations since that date. Approximately 86% of our contract backlog as of March 31, 2005 was derived from contracts with the U.S. Government and its agencies or from subcontracts with the U.S. Government's prime contractors. Since our government contracts are contingent upon Congressional appropriations and are terminable for convenience, we cannot assure you that our backlog will ultimately result in revenues.

Our existing NASA contracts are subject to continued appropriations by Congress and may be terminated if future funding is not made available, which would have a material adverse effect on our business.

Our financial performance is substantially dependent on the revenue generated from our contracts supporting NASA which, similar to contracts with other agencies of the U.S. government, are conditioned upon the continuing availability of Congressional appropriations. The U.S. Congress usually appropriates funds for a given program on a fiscal year basis even though contract performance may extend over many years. Failure to receive sufficient funds from Congress or a withdrawal by Congress of prior appropriations would permit NASA to terminate its contracts with us for convenience. Therefore, no assurances can be made that Congress will continue to fund NASA at levels which will permit space shuttle missions to continue on their current schedules or that Congress will appropriate the funds necessary for NASA to fulfill its obligations under its contracts with us. Any substantial reduction in Congressional funding for space shuttle missions or annual appropriations to NASA to fulfill, among other things, NASA's contracts with us or the U.S. commitment to the International Space Station, would have a material adverse effect on our financial condition and results of operations. In addition, termination of large programs or multiple contracts affecting our Flight Services business unit could require us to evaluate the continued viability of operating that business.

As a U.S. Government contractor, we are subject to a number of rules and regulations the violation of which could result in us being barred from future NASA contracts.

We must comply with and are affected by laws and regulations relating to the award, administration and performance of U.S. Government contracts. These laws and regulations, among other things:

require certification and disclosure of all cost or pricing data in connection with certain contract negotiations;

impose acquisition regulations that define allowable and unallowable costs and otherwise govern our right to reimbursement under certain cost-based U.S. Government contracts; and

restrict the use and dissemination of information classified for national security purposes and the exportation of certain products and technical data.

A violation of specific laws and regulations could result in the imposition of fines and penalties, the termination of our contracts or debarment from bidding on U.S. Government contracts. In some instances, these laws and regulations impose terms or rights that are more favorable to the government than those typically available to commercial parties in negotiated transactions. For example, the U.S. Government may terminate any of our government contracts for convenience, as well as for default based on performance. In addition, U.S. Government contracts generally contain provisions that allow the U.S. Government to unilaterally suspend us from receiving new contracts pending resolution of alleged violations of certain federal laws or regulations, reduce the value of existing contracts, issue modifications to a contract and control and potentially prohibit the export of our services and associated materials. Since a majority of our revenues are currently, and a material portion of

future revenues are expected to be, derived from contracts supporting NASA, material modifications to our existing contracts or a prohibition against bidding on future U.S. Government contracts would have a material adverse affect on our financial condition and results of operations.

Table of Contents

Our business could be adversely affected by a negative audit by the U.S. Government.

U.S. Government agencies, including NASA, routinely audit and investigate government contractors. These agencies review a contractor's performance under its contracts, cost structure and compliance with applicable laws, regulations and standards. The U.S. Government also may review the adequacy of, and a contractor's compliance with, its internal control systems and policies, including the contractor's purchasing, property, estimating, compensation and management information systems. Any costs found to be improperly allocated to a specific contract will not be reimbursed, while such costs already reimbursed must be refunded. If an audit uncovers improper or illegal activities, we may be subject to civil and criminal penalties and administrative sanctions, including termination of contracts, forfeiture of profits, suspension of payments, fines, and suspension or prohibition from doing business with the U.S. Government. In addition, we could suffer serious reputational harm that affects our non-governmental business if allegations of impropriety were made against us.

Most of our competitors, including NASA which is also our largest customer, have much greater financial resources than we do.

The U.S. Government, the governments of other countries, and private companies participate in the highly competitive space industry often as both suppliers and end-users of space services. Our long-term strategy for growth is to provide research, logistics, infrastructure and payload processing services to NASA and others during the International Space Station era and for the manned and unmanned programs that will replace the space shuttle program. This strategy could require us to compete with commercial companies such as Boeing, Lockheed Martin and other large aerospace companies, many of which have existing NASA support contracts, substantially greater financial resources and manufacturing capabilities, more established and larger marketing and sales organizations, and larger technical staffs than we have.

Pursuant to a treaty between the United States and Italian governments, the Italian government has provided three multi-purpose logistics modules to NASA for use in the construction and operation of the International Space Station. These NASA-owned and operated modules are capable of carrying pressurized logistics and other payloads in the cargo bay of the space shuttle to and from the International Space Station. These NASA owned modules are our most direct competitor for pressurized logistics resupply to the International Space Station. Russia also operates *Progress* unmanned, expendable logistics resupply vehicles, which were the sole means of re-supplying the International Space Station while shuttle flights were suspended. Japan and certain European countries are also currently working on their own expendable, automated docking modules for logistics resupply missions. The NASA owned modules might, and successful implementation of the proposed expendable docking modules could further, reduce the demand for our modules, which would have a material adverse effect on our future financial performance.

Prior to January 2004, Boeing was our subcontractor for processing payloads for our modules. We now perform all of our payload processing services using our employees. Boeing and United Space Alliance currently perform payload processing services for NASA's multi-purpose logistics modules. In addition, there are several other space shuttle payload processing contractors currently performing flight and ground operations work for NASA, including but not limited to: United Space Alliance, The Boeing Company, Lockheed Martin Corporation, and Teledyne Technologies Incorporated. All of these companies are larger and have greater resources than us in space shuttle payload processing.

United Space Alliance, which is equally owned by The Boeing Company and Lockheed Martin Corporation, is the prime contractor for NASA's space shuttle program. United Space Alliance is responsible for the day-to-day operation and management of the U.S. space shuttle fleet. United Space Alliance is currently the primary contractor in the market for civil ground operations and payload processing services. We believe that the privatization of space station operations and successor programs will continue to result in intense competitive pressure among contractors to retain their current contracts and/or capture new payload processing work from other contractors. To the extent that these contractors are able to retain or enlarge their roles in payload

Table of Contents

processing operations, our ability to successfully compete for a share in this market could be impeded, which could have a material adverse effect on our future financial performance.

At present, competition in the United States for our Astrotech spacecraft launch processing services is limited to the California (Vandenberg) launch site, where a competing company called California Commercial Spaceport Systems International is located. California Commercial Spaceport Systems International does not have payload processing facilities in Florida, where the majority of U.S. commercial satellite launches occur. However, if California Commercial Spaceport Systems International or another satellite launch processing service provider were to build, or NASA were to expand its facilities in Florida, our financial performance could be adversely affected.

Our earnings and margins may vary based on the mix of our cost reimbursable and fixed-price contracts.

As of June 30, 2005, we had one significant cost reimbursable and five significant fixed-price contracts. Cost reimbursable contracts generally have lower profit margins than fixed-price contracts. Our Flight Services and Astrotech spacecraft processing business units' contracts are mainly fixed-price contracts, while our Government Services business unit contracts are generally cost reimbursable contracts. Our earnings and margins may vary materially depending on the types of contracts undertaken, the costs incurred in their performance, the achievement of other performance objectives and the stage of performance at which the right to receive fees, particularly under incentive and award fee contracts, is finally determined.

Under fixed-price contracts, we receive a fixed price irrespective of the actual costs we incur and, consequently, any costs in excess of the fixed price are absorbed by us. Under cost reimbursable contracts, subject to a contract-ceiling amount in certain cases, we are reimbursed for allowable costs and paid a fee, which may be fixed or performance based. However, if our costs exceed the contract ceiling or are not allowable under the provisions of the contract or applicable regulations, we may not be able to obtain reimbursement for all such costs and may have our fees reduced or eliminated. The failure to perform to customer expectations and contract requirements can result in reduced fees and may affect our financial performance for the affected period. Cost over-runs also may adversely affect our ability to sustain existing programs and obtain future contract awards. Under each type of contract, if we are unable to control costs we incur in performing under the contract, our financial condition and operating results could be materially adversely affected.

Our financial results could be affected if the estimates that we use in accounting for contracts are incorrect and need to be changed.

Contract accounting requires judgment relative to assessing risks, estimating contract revenues and costs and making assumptions for schedule and technical issues. The estimation of total revenues and cost at completion for many of our contracts is complicated and subject to many variables. Assumptions have to be made regarding the length of time to complete the contract because costs also include expected increases in wages and prices for materials. Incentives or penalties related to performance on contracts are considered in estimating revenue and profit rates, and are recorded when there is sufficient information for us to assess anticipated performance. Estimates of award and incentive fees are also used in billing customers and estimating revenue and profit rates based on actual and anticipated awards. If our performance under a cost reimbursable contract results in an award fee that is lower than we have estimated, we would be required to refund previously billed fee amounts and would have to adjust our revenue recognition accordingly. If our performance was determined to be significantly deficient, we may be required to reimburse our customer for the entire amount of previously billed awards.

Because of the significance of the judgments and estimation processes described above, it is likely that materially different amounts could be recorded if we used different assumptions or if the underlying circumstances were to change. Changes in underlying assumptions, circumstances or estimates may adversely affect future period financial performance.

Table of Contents

Most of the costs for our Astrotech business unit are fixed regardless of the number of satellites that are processed at our facility.

The primary costs related to our Astrotech business unit are associated with operating and running our three satellite launch processing facilities and our Flight Services facility for our modules. These costs remain relatively unchanged regardless of whether or not customers are using the facilities. As a result, if we do not properly estimate the number of satellites that will be processed when calculating our price structure for our satellite launch processing services, our financial results could be adversely affected.

In developing the products we will offer in connection with the manned and unmanned programs that will replace the space shuttle, we will depend heavily on our relationships with our partners and subcontractors.

We depended significantly on other companies for the development and manufacture of our modules and integrated cargo carriers that are material to our business. Boeing designed our modules and integrated cargo carriers, Alenia Spazio constructed the shell for our modules, and RSC Energia built the pallets and the European Aeronautic Defense and Space Company (EADS) built the keel yokes for our integrated cargo carriers. EADS also performs the integration work on our integrated cargo carriers as a subcontractor. Future products that we develop to be offered to NASA for use in the space program, including the successors to the space shuttle program, will probably be designed and manufactured by other companies and future services that we offer may include the use by us of subcontractors to provide some or all of these services. In addition, we may partner with other companies to provide future product and service offerings to NASA. These arrangements with other companies may involve us acting as a subcontractor to other companies that are the prime contractor with NASA. These companies may also compete with us to offer their own products and services to our target market, which could place us at a competitive disadvantage.

There is a risk that we may have disputes with our current or future subcontractors, including disputes regarding the ownership of the intellectual property underlying the deliverables produced under the contract, the quality and timeliness of work performed by the subcontractor, customer concerns about the subcontractor, our failure to extend existing task orders or issue new task orders under a subcontract or our hiring of personnel of a subcontractor. In addition, a prime contractor may have similar disputes with us in situations where we are serving as a subcontractor. A failure by one or more of our subcontractors to satisfactorily provide on a timely basis the agreed-upon products or perform the agreed-upon services may materially and adversely impact our ability to perform our obligations as the prime contractor. Subcontractor performance deficiencies could result in a customer terminating our contract for default which could have a material adverse effect on our financial condition and results of operations.

If we do not receive additional contracts to use our modules or cargo carriers, or if we are unable to find users of future products we develop without a contract for such product, we will have to write off the value of such assets.

We have in the past, and expect to continue in the future, to fund development of certain projects prior to being awarded a contract for such projects. No assurances can be made that any funds we may spend in the future in connection with the development of new products will lead to the award of a contract or that any such contract will be awarded on terms that are economically favorable to us. In addition, we depreciate space hardware, and intend to depreciate our modules and cargo carriers and other future capital assets that are dedicated to supporting the space shuttle over a period that approximates the useful life of the space shuttles. In the event we are not awarded additional contracts for the use of our modules, cargo carriers, or future products or services, we could be required to write-off the remaining value of our modules, cargo carriers and any future capital assets, and/or costs of prepaid services performed, which could have a material adverse effect on our financial condition and results of operations.

Table of Contents

Our spacecraft payload processing facilities that are specifically designed to process satellite and other payloads and our modules and integrated cargo carriers would lose a substantial portion of their value if we no longer provided these services.

Our Astrotech spacecraft processing facilities and the payload processing facilities for our Flight Services business unit were built specifically to process satellites and our modules and integrated cargo carriers. These facilities are not well suited for other uses. Currently, our Astrotech facilities in Titusville, Florida are depreciated using the straight-line method over their remaining useful lives which range from 32 to 37 years. If we were required to terminate our satellite or module processing businesses, the value of these facilities would be significantly impaired. In addition to having to take a substantial write-down of the value of our Titusville, Florida facility on our books, if we attempted to sell this facility we do not think that we would be able to recover the amounts we have invested. If we were able to sublease our leased facilities, we do not think such subleases would be sufficient to cover our current rental payments. Due to our substantial capital expenditures for our spacecraft processing facilities and the limited uses of these facilities, the termination of operations at our Titusville, Florida facility that we own or one or more of our other leased facilities could have a material adverse effect on our financial condition and results of operations.

We incur substantial costs in preparing proposals to bid on contracts that we may not be awarded.

Preparing a proposal to bid on a contract competition is generally a three to six month process. This process is time consuming and results in the incurrence of substantial costs that are generally not reimbursable even if the contract is awarded. We have prepared proposals for and bid on contracts that were not awarded to us in the past and anticipate that we could incur substantial costs related to contracts that are not ultimately awarded to us in the future. In addition, even if we are awarded a contract, we generally do not begin performing work for several months after the bidding process is complete. If funding problems by the party awarding the contract or other matters further delay our commencement of work on the contract, these delays may sufficiently lower the value of the contract to us, even rendering it unprofitable.

Because our operating results are highly dependent on the timing of space shuttle missions and satellite launches, they may fluctuate significantly from quarter to quarter.

For contracts for which the capability to successfully complete the contract can be demonstrated at contract inception, we recognize revenue using the percentage-of-completion method based on costs incurred over the period of the contract. The timing of space shuttle missions which carry our modules, the number and types of missions flown, the number and timing of satellite launches that use our Astrotech spacecraft processing facilities, and other factors can cause our results of operations to fluctuate significantly from quarter to quarter. The grounding of the space shuttle fleet following the problems encountered during the July 26, 2005 launch will impact the schedule for future launches and, as a result, may affect our results of operations. Revenue recognition on cost reimbursable contracts that our Government Services business unit enters into is based on reimbursable costs incurred plus an award fee.

Most obligations under our contracts, including contract-related engineering, research and development, and selling, general and administrative expenses, are recorded in the periods in which they are incurred. Accordingly, we may report routine operating losses in quarters in which no space shuttle missions are in process.

Although we achieved profitability in fiscal year 2004, our profitability was primarily attributable to our receipt of extraordinary income relating to Boeing's termination of their spacecraft processing contract with us. In addition, we have incurred significant losses in the past and, as such, we believe that period-to-period comparisons of our results of operations are not necessarily meaningful and should not be relied upon as indications of future performance.

If we are unable to anticipate technological advances and customer requirements, including NASA's requirements for products and services following the retirement of the space shuttle fleet, our business and financial condition will be adversely affected.

Our growth and future financial performance depend in part upon our ability to anticipate technological advances and customer requirements, particularly NASA's post-shuttle needs. There can be no assurance that we

Table of Contents

will be able to achieve the technological advances that may be necessary for us to remain competitive. Our failure to anticipate or respond adequately to changes in technology and NASA requirements, or delays in additional product development or introduction, could have a material adverse effect on our business and financial performance.

Compliance with environmental and other government regulations could be costly and could negatively affect our financial condition.

Our business, particularly our Astrotech spacecraft processing business unit, is subject to numerous laws and regulations governing the operation and maintenance of our facilities and the release or discharge of hazardous or toxic substances, including spacecraft fuels and oxidizers, into the environment or otherwise relating to environmental protection. Under these laws and regulations, we could be liable for personal injury and clean-up costs and other environmental and property damages, as well as administrative, civil and criminal penalties in the event of a violation of these laws, or a release of a hazardous substances at or from our facilities, and such liabilities could have a material adverse effect on our business, financial condition and results of operations.

Our failure to comply with U.S. export control laws and regulations could adversely affect our business.

We are obligated by law and under our NASA contracts to comply, and to ensure that our subcontractors comply, with all U.S. export control laws and regulations, including the International Traffic in Arms Regulations and the Export Administration Regulations. We are responsible for obtaining all necessary licenses or other approvals, if required, for exports of hardware, technical data, and software, or for the provision of technical assistance. We are also required to obtain export licenses, if required, before utilizing foreign persons in the performance of our NASA contracts if the foreign person will have access to export-controlled technical data or software. The violation of any of the applicable export control laws and regulations, whether by us or any of our subcontractors, could subject us to administrative, civil and criminal penalties.

Our facilities located in Florida and California are particularly susceptible to damage caused by hurricanes, earthquakes or other natural disasters.

Our largest Astrotech satellite launch processing facility, which we own, and our leased Flight Services facility on the east coast of Florida are particularly susceptible to damage caused by hurricanes or other natural disasters. In addition, our leased launch processing facilities at Vandenberg Air Force Base and the facilities we operate at the Port of Long Beach are subject to damage caused by earthquakes. The extent to which the buildings located at these facilities are designed to sustain natural disasters varies. Although we insure our properties and maintain business interruption insurance, there can be no assurance that such insurance would be sufficient. If a severe hurricane, earthquake or other natural disaster materially affected any of these facilities, our financial condition and results of operations could be adversely affected.

The loss of key management and other employees could have a material adverse effect on our business.

We are dependent on the personal efforts and abilities of our senior management and our success will also depend on our ability to attract and retain additional qualified employees. We do not maintain key man insurance with any of these employees. Failure to attract personnel sufficiently qualified to execute our strategy, or to retain existing key personnel, could have a material adverse effect on our business.

If we fail to comply with Section 404 of the Sarbanes-Oxley Act of 2002, our reputation, financial condition and the value of our notes and common stock may be adversely affected.

Beginning with our report for the fiscal year ending June 30, 2006, Section 404 of the Sarbanes-Oxley Act of 2002 will require us to include an internal control report of management with our annual report on Form 10-K, which is to include management's assessment of the effectiveness of our internal control over financial reporting

Table of Contents

as of the end of the fiscal year. The report will also be required to include a statement that our independent auditors have issued an attestation report on management's assessment of our internal control over financial reporting.

In order to achieve compliance with Section 404 within the prescribed period, management is interviewing outside consultants to aid us in the adoption of a detailed project work plan that assesses the adequacy of our internal control over financial reporting, remediate any control weaknesses that may be identified, validate through testing that controls are functioning as documented and implement a continuous reporting and improvement process for internal control over financial reporting. However, we may not be able to complete the work necessary for our management to issue its management report in a timely manner, or any work that will be required for our management to be able to report that our internal control over financial reporting is effective. In addition, our independent auditors may not be able to issue an attestation report on management's assessment. Our failure to comply with Section 404, including issuing the management report and obtaining the attestation report, may materially adversely affect our reputation, our financial condition and the value of our securities, including our outstanding notes, exchange notes and common stock. Furthermore, our costs of compliance with Section 404, including the cost of remedying any identified weaknesses, could be material and could adversely affect our financial condition and results of operations.

We may face risks related to our recent restatement of our financial statements.

We recently restated our statements of cash flows for the fiscal year ended June 30, 2003 and the nine months ended March 31, 2005 to revise the classification of insurance and indemnification proceeds that we received in connection with the loss of our research double module. We originally classified these proceeds, which totaled \$17.7 million in insurance proceeds and \$8.2 million in indemnification proceeds, as cash flows from operating activities; however, such proceeds should have been classified as cash flows from investing activities. Our restatement properly classifies such amounts. In the past, some companies that have restated their financial statements have been subject to securities class action lawsuits and shareholder derivative actions and have experienced a decline in the value of their securities. Either of these events could adversely affect the value of your exchange notes or the common stock into which they are convertible.

Risks Related to Retaining the Outstanding Notes

If you do not elect to exchange the outstanding notes that you hold in this exchange offer, and the exchange offer and consent solicitation described in this prospectus is successful, your rights as a holder of those notes, including your priority with respect to repayment, will be adversely affected.

If this exchange offer and consent solicitation is completed, the indenture governing the outstanding notes will be amended to eliminate the occurrence of a default on our other indebtedness as an event of default on the outstanding notes, and the remaining holders of the outstanding notes who do not tender their notes for exchange will no longer benefit from the protection to their credit interest afforded by that event of default. See "The Exchange Offer and Consent Solicitation Proposed Amendments to Indenture for the Outstanding Notes." In addition, any of our outstanding notes that are not tendered and therefore remain outstanding after this exchange offer will be subordinated to all of our senior indebtedness, including the exchange notes. As a result, if we were to undergo a bankruptcy, liquidation, dissolution, reorganization or similar proceeding, our assets would be available to repay the outstanding notes only after all of our senior indebtedness, including the exchange notes, have been paid. In such an event, we may not have sufficient assets remaining to pay amounts due on the outstanding notes.

If you do not exchange the outstanding notes that you hold in this exchange offer, the liquidity of the outstanding notes in the secondary market may be significantly reduced.

Any outstanding notes tendered and exchanged in this exchange offer will significantly reduce the aggregate principal amount of the outstanding notes. As a result, the trading market for outstanding notes that remain outstanding after the exchange offer is likely to be significantly more limited than it is at present. A debt security with a smaller outstanding principal amount available for trading may command a lower price than would a comparable debt security with a larger principle amount available for trading. A reduced principle amount available for trading may also make the trading price of outstanding notes that are not exchanged in the exchange offer and consent solicitation more volatile.

Table of Contents

Risks Related to the Exchange Notes

Our substantial levels of debt, even following the exchange offer, will limit our operations and could have a material adverse effect on our business and prevent us from fulfilling our obligations under the exchange notes.

As of June 30, 2005, we had approximately \$67.0 million in total debt, including capital leases. We may incur additional indebtedness after the exchange offer as we execute our business strategy. Our ability to make payments on our debt, operate our business, and to fund capital expenditures will depend on our ability to generate cash in the future. The level of our outstanding indebtedness has several important consequences for our future operations, including the following:

a substantial portion of our cash flow from operations will be dedicated to the payment of interest on, and principal of, our indebtedness and will not be available for other purposes;

our revolving credit facility contains financial tests that we must satisfy in order to continue to borrow funds under the facility, and a failure to meet these tests may also be a default under our facility;

covenants contained in the indenture limiting the amount of additional senior secured indebtedness that we may incur or additional indebtedness that we may assume or incur in connection with acquisitions may have the effect of limiting our flexibility in reacting to changes in our business and our ability to fund future operations and acquisitions;

our ability to refinance existing debt or obtain additional financing in the future for capital expenditures, acquisitions, general corporate purposes or other purposes may be impaired; and

our ability to withstand competitive pressures, adverse economic conditions and adverse changes in governmental regulations, and to make acquisitions, react to changes in our industry or take advantage of significant business opportunities that may arise could be negatively impacted.

These consequences could make us more vulnerable to a downturn in our business or general economic conditions than a less leveraged competitor.

To service our debt, we will require a significant amount of cash, which may not be available to us.

Our ability to make payments on, or repay or refinance, our debt, including the debt under the outstanding notes and exchange notes, and to fund capital expenditures will depend largely upon our future operating performance. Our future performance, to a certain extent, is subject to general economic, financial, competitive, legislative, regulatory and other factors that are beyond our control. In particular, a substantial portion of our revenues are derived from services that we provide to support space shuttle missions. If the space shuttle fleet is retired as expected in 2010, which is the same year in which the exchange notes mature, and we have not successfully diversified our business, then our ability to repay the exchange notes may be materially adversely affected.

Edgar Filing: SPACEHAB INC \WA\ - Form S-4/A

In addition, our ability to borrow funds in the future will depend on the satisfaction of the covenants in our revolving credit facility and other debt agreements, including the indenture governing the exchange notes and other agreements we may enter into in the future. Specifically, we will need to maintain certain financial ratios. We cannot assure you that our business will generate sufficient cash flow from operations or that future borrowings will be available to us under our revolving credit facility or from other sources in an amount sufficient to enable us to pay our debt, including the exchange notes, or to fund our other liquidity needs.

The indenture governing the exchange notes permits us to use funds that would otherwise be available to make interest and principal payments on the exchange notes to repurchase shares of our common stock.

The indenture governing the exchange notes contains a restrictive covenant prohibiting us from paying dividends on shares of our common stock. One of the reasons for this covenant is to provide additional liquidity

Table of Contents

to make interest payments on, and repay the principal amount of, the exchange notes. The indenture does not contain any prohibitions against us repurchasing shares of our common stock. Subject to compliance with the restrictive covenants contained in our revolving credit facility, we would be able to use funds that would otherwise be available to make principal and interest payments on the exchange notes to repurchase shares of our common stock. Accordingly, there may not be sufficient funds remaining to pay interest and principal due on the exchange notes.

Despite the restrictive covenants in the new indenture that will govern the exchange notes, we and our subsidiaries may still incur substantial additional indebtedness, which could further exacerbate the risks associated with our substantial leverage.

The covenant in the indenture for the exchange notes that restricts our incurrence of senior secured indebtedness and assumption or incurrence of indebtedness in connection with acquisitions does not place any limits on our ability to incur additional debt that would be equal in right of payment or subordinate to the exchange notes. In addition, the covenant does not place any restrictions on the ability of our subsidiaries to incur any additional debt. The exchange notes are effectively subordinated to the debt of our subsidiaries. If we, or our subsidiaries incur additional indebtedness, the leverage-related risks that we face would be exacerbated. In addition, if our subsidiaries incur any new indebtedness and that indebtedness restricts the ability of our subsidiaries to distribute funds to us, then our ability to meet our other obligations, including our obligations with respect to the exchange notes, could be materially adversely affected.

Although the exchange notes are referred to as senior convertible notes, they are effectively subordinated to our secured debt to the extent of the value of the collateral securing such debt, and are effectively subordinated to the debt and other liabilities of our subsidiaries.

The exchange notes are unsecured and therefore will be effectively subordinated to any secured debt we may incur to the extent of the assets securing such debt. In the event of a bankruptcy or similar proceeding involving us, the assets which serve as collateral for any secured debt will be available to satisfy the obligations under the secured debt before any payments are made on the exchange notes. As of June 30, 2005, we had \$67.0 million of total debt outstanding, and up to \$5.0 million of additional availability under our revolving credit facility which would be effectively senior to the exchange notes. The terms of the indenture governing the exchange notes allows us to incur up to \$20.0 million of additional senior secured debt.

In addition, the exchange notes are effectively subordinated to the debt and other liabilities of our subsidiaries. The creditors of our subsidiaries are entitled to be paid what is due to them before the assets of our subsidiaries become available to our creditors, including holders of the exchange notes. Further, certain revenues of our Astrotech business unit under our payload processing contract with Lockheed Martin are paid into a lock box for the benefit of the lender for our mortgage loan and therefore are not available to repay any other indebtedness. See Description of Other Indebtedness and Financing Arrangements Mortgage Loan Agreement. Our total debt outstanding of \$67.0 million as of June 30, 2005 includes approximately \$3.7 million of indebtedness of our subsidiaries, all of which we have guaranteed and which is effectively senior in right of payment to the exchange notes.

Borrowings under our revolving credit facility are secured by a security interest in substantially all of our and our subsidiaries accounts receivable, and borrowings under our 5.5% term loan due 2007 are secured by our payload processing contract with Lockheed Martin and our spacecraft processing facility. In the event of a liquidation, dissolution, reorganization, bankruptcy or any similar proceeding, or if our debt under our revolving credit facility is accelerated, the lenders under such facility and the term loan would be entitled to exercise the remedies available to secured lenders under applicable law. In such event, our assets will be available to pay obligations on the exchange notes only after holders of our secured indebtedness have been paid the value of the assets securing such debt. Accordingly, there may not be sufficient funds remaining to pay amounts due on all or any of the exchange notes.

Table of Contents

Our debt instruments include restrictive and financial covenants that limit our operating flexibility.

Our revolving credit facility requires us to maintain certain financial ratios, and our credit facility and the indenture governing the exchange notes contain covenants that, among other things, restrict our ability to take specific actions, even if we believe such actions are in our best interest. The indenture governing the exchange notes contains restrictions on our ability to incur additional senior secured indebtedness, assume or incur indebtedness in connection with acquisitions, and sell assets or merge with other companies. The covenants in our revolving credit facility contain, among other things, restrictions on our ability to:

incur additional debt;

create liens or pledges with respect to our assets;

merge, consolidate or sell our assets;

pay dividends or distributions on, or redeem or repurchase, our capital stock;

make investments, loans or advances or other purchases of securities;

enter into transactions with affiliates;

enter into sale and leaseback agreements;

prepay or defease specified indebtedness, including the exchange notes; or

enter new lines of business.

Any failure to comply with the restrictions of our revolving credit facility or the indenture governing the exchange notes or existing and any subsequent financing agreements may result in an event of default. Such default may allow our creditors to accelerate the related debt and may result in the acceleration of any other debt to which a cross-acceleration or cross-default provision applies. In addition, these creditors may be able to terminate any commitments they had made to provide us with further funds. See Description of the Exchange Notes Certain Covenants for more information on the restrictive and financial covenants of the exchange notes.

A single beneficial owner will own more than a majority of the exchange notes. The exchange notes controlled by this owner will be convertible into greater than 50% of our common stock.

SMH Capital Advisors, Inc., is a registered investment advisor who has been granted discretionary authority to sell, tender, or exchange an aggregate principal amount of \$40,366,000 of the outstanding notes by the beneficial owners of those outstanding notes. While SMH Capital

Advisors' ability to control the outstanding notes under its management is subject to certain limitations, including any specific directions of any beneficial owner relating to those outstanding notes or the transfer of such outstanding notes out of the account managed by SMH Capital Advisors. SMH Capital Advisors has expressed its intent to tender all outstanding notes under its management at the time of the closing of the exchange offer. If all outstanding notes are tendered and validly accepted, then SMH Capital Advisors will beneficially own, on behalf of its clients, approximately 63.8% of the then outstanding exchange notes and, as such, would be able to control the outcome of matters submitted to the holders of exchange notes for approval that do not require the approval of all holders, including certain amendments to the terms of the notes or waivers of certain defaults.

Furthermore, if all of the exchange notes were converted into our common stock at a conversion price of \$2.50 per share, including those under management by SMH Capital Advisors, then SMH Capital Advisors would have the ability, on behalf of its clients and subject to certain limitations, to vote approximately 42.5% of our shares of common stock and, as such, would have the ability, to a significant extent, to affect the outcome of all matters required to be submitted to our shareholders for approval, including decisions relating to the election of directors and our ability to be acquired and other significant corporate transactions.

We cannot assure you that the value of the exchange notes that you will receive will be equal to or greater than the outstanding notes that you tender for exchange.

We have not undertaken a valuation with respect to the exchange ratios for the exchange offer of the outstanding notes. Our board of directors has made no determination that the exchange ratios represent a fair

Table of Contents

valuation of either series of the outstanding notes. We have not obtained a fairness opinion from any financial advisor about the fairness of the exchange ratios to you or to us. We cannot assure you that if you tender your outstanding notes you will receive the same or greater value than if you choose to keep them.

We may be unable to make a change of control offer required by the indenture governing the exchange notes, which would cause defaults under the indenture governing the exchange notes, our revolving credit facility and other financing arrangements.

The terms of the exchange notes require us to make an offer to repurchase the exchange notes upon the occurrence of a change of control at a purchase price equal to 100% of the principal amount of the exchange notes, plus accrued and unpaid interest, if any, to the date of the purchase. Accrued and unpaid interest is payable, at our option, in cash or shares of our common stock. The terms of our revolving credit facility require, and future financing and other arrangements may require, repayment of amounts outstanding in the event of a change of control and prohibit us from repurchasing your exchange notes while commitments or amounts are outstanding under the revolving credit facility. It is possible that we will not have sufficient funds at the time of the change of control to make any required repurchase of exchange notes or that restrictions in our revolving credit facility, and other financing agreements will not allow the repurchases. In the event that we do not have sufficient funds, we may elect to offer to repurchase your notes in exchange for shares of our common stock, or shares of such other person into which our common stock is converted. See Description of the Exchange Notes Repurchase at the Option of Holders upon Change of Control.

In addition, it is not certain whether we would be required to make a change in control offer to repurchase the exchange notes upon certain asset sales, because the meaning of substantially all assets, the sale of which would constitute a change of control, is not established under applicable law. Although there is a limited body of case law interpreting the phrase substantially all, there is no precise established definition of the phrase under applicable law. Accordingly, the ability of a holder of exchange notes to require us to repurchase such exchange notes as a result of a sale, lease, transfer, conveyance or other disposition of less than all of our and our subsidiaries assets taken as a whole to another person or group may be uncertain. See Description of the Exchange Notes Certain Covenants Asset Sales.

If a change in control occurs and we do not offer to repurchase the exchange notes or if we do not repurchase the exchange notes when we are required to do so, an event of default will occur under the indenture governing the exchange notes, which would also be a default under our revolving credit facility. Each of these defaults could have a material adverse effect on us and our ability to repay the exchange notes.

Holder of our exchange notes will not be entitled to any rights with respect to our common stock, but will be subject to all changes made with respect to our common stock.

Holder of exchange notes, which are convertible into our common stock, will not be entitled to any rights with respect to our common stock, including voting rights and rights to receive any dividends or other distributions on our common stock, but will be subject to all changes affecting our common stock. Holder of exchange notes will have rights with respect to our common stock only if and when we deliver shares of common stock upon conversion of such exchange notes and, in limited cases, under the conversion rate adjustments applicable to the exchange notes. For example, in the event that an amendment is proposed to our certificate of incorporation or by-laws requiring stockholder approval and the record date for determining the stockholders of record entitled to vote on the amendment occurs prior to delivery of common stock to a holder of exchange notes following conversion, such holder will not be entitled to vote on the amendment, although the holder will nevertheless be subject to any changes in the powers, preferences or special rights of our common stock.

There is no public market for the exchange notes.

The exchange notes are new securities for which there currently is no market. A market for the exchange notes may not develop, and any market that develops may not last. In addition, SMH Capital Advisors currently

Table of Contents

has over \$40 million of our outstanding notes under its management. As long as SMH Capital Advisors continues to control such a substantial amount of our notes, we believe that it will be difficult for an active market in our notes to form. We do not intend to apply for listing of the exchange notes on any securities exchange or other stock market. Historically, the market for non-investment grade debt has been subject to disruptions that have caused volatility in prices. It is possible that any market for the exchange notes will be subject to disruptions. Any such disruptions may have a negative effect on you, as a holder of the exchange notes, regardless of our prospects and financial performance.

The trading prices for the exchange notes could be directly affected by the trading prices for our common stock, which are impossible to predict.

The price of our common stock could be affected by possible sales of our common stock by investors who view the exchange notes as a more attractive means of equity participation in our company and by hedging or arbitrage trading activity that may develop involving our common stock. The hedging or arbitrage could, in turn, affect the trading prices of the exchange notes to the extent the exchange notes are traded.

The price at which our common stock trades has fluctuated significantly and may continue to be highly volatile. Since July 1, 2002 through August 10, 2005, the sale price of our common stock, as reported on the NASDAQ National Market, has ranged from a low of \$0.54 to a high of \$4.81 per share. In addition, the stock market in general has from time to time experienced significant price and volume fluctuations that have affected the market prices for companies like ours.

Conversion of the exchange notes will dilute the ownership interest of existing shareholders.

The conversion of the exchange notes into common stock will dilute the ownership interests of existing shareholders. As of August 10, 2005, we had 12,661,179 shares of our common stock outstanding while, as of the issue date, the exchange notes would be convertible into approximately 29,834,906 shares of our common stock. Any sales in the public market of the common stock issuable upon conversion of the exchange notes could adversely affect prevailing market prices of our common stock. The mandatory conversion feature of the exchange notes could limit the ability of our common stock to achieve the mandatory conversion price due to the fact that a mandatory conversion would cause substantial dilution of existing shareholders. In addition, the existence of the exchange notes may encourage short selling by market participants due to this dilution or facilitate trading strategies involving the exchange notes and our common stock, all of which could have an adverse impact on the market price of the exchange notes and the shares of common stock issuable upon conversion of the exchange notes.

The conversion rate of the exchange notes may not be adjusted for all dilutive events.

The conversion rate of the exchange notes is subject to adjustment for certain events, including, but not limited to, the issuance of stock dividends on our common stock, the issuance of certain rights or warrants, subdivisions or combinations of our common stock, certain distributions of assets, debt securities, capital stock or cash to holders of our common stock and certain issuer tender or exchange offers as described under [Description of the Exchange Notes](#) [Conversion Rights](#) [Conversion Procedures](#). The conversion rate will not be adjusted for other events, such as an issuance of common stock for cash, that may adversely affect the trading price of the exchange notes or our common stock. We cannot assure you that an event that adversely affects the value of the exchange notes or our common stock, but does not result in an adjustment to the conversion rate, will not occur.

Edgar Filing: SPACEHAB INC \WA\ - Form S-4/A

Future sales of our common stock in the public market or the issuance of securities senior to our common stock could adversely affect the trading price of our common stock, the value of the exchange notes and our ability to raise funds in new stock offerings.

We are not restricted from issuing additional common stock during the life of the notes and have no obligation to consider your interests for any reason. Future sales of substantial amounts of our common stock or

Table of Contents

equity-related securities in the public market, or the perception that such sales could occur, could adversely affect prevailing trading prices of our common stock and the value of the exchange notes and could impair our ability to raise capital through future offerings of equity or equity-related securities. No prediction can be made as to the effect, if any, that future sales of shares of common stock or the availability of shares of common stock for future sale will have on the trading price of our common stock or the value of the exchange notes.

We may incur an income tax liability as a result of the exchange offer.

If the outstanding notes or the exchange notes are publicly traded for U.S. income tax purposes, we may recognize cancellation of indebtedness income for tax purposes which may be subject to reduction, including by offset against available net operating loss deductions. No assurances can be given, however, that net operating losses will be available to us, and, we may incur a U.S. federal and/or state income or alternative minimum tax liability arising from cancellation of indebtedness income, if any, recognized in the exchange. In addition, to the extent that available net operating losses are used to offset cancellation of indebtedness income, if any, such net operating losses will be unavailable as a potential offset to future income. See Material U.S. Federal Income Tax Considerations Tax Consequences to the Company Cancellation of Indebtedness Income.

We may be unable to deduct for tax purposes the interest or original issue discount, if any, paid or accrued on the exchange notes.

No deduction is allowed for U.S. federal income tax purposes for interest paid on a disqualified debt instrument. A disqualified debt instrument generally includes any indebtedness of a corporation which is payable in equity of the issuer. Although we believe and intend to take the position that the exchange notes are not disqualified debt instruments, the exchange notes may be treated as disqualified debt instruments, and we may be prohibited from deducting the interest due on the exchange notes. Consequently, we may have less cash available with which to satisfy our obligations.

The conversion, including a mandatory conversion, of the exchange notes into our common stock may limit our ability to use our net operating losses to offset future taxable income.

An ownership change occurs for purposes of Section 382 of the Internal Revenue Code of 1986 if, under certain circumstances, there is a cumulative change of more than 50% of our common stock, as determined under tax rules, within a three year period. If we undergo an ownership change, we believe that the amount of net operating losses that will be able to use to offset our taxable income for taxable periods, or portions thereof, beginning after the ownership change will be limited under Section 382 of the Internal Revenue Code of 1986. The conversion, including a mandatory conversion, of the exchange notes, future equity issuances or transactions among shareholders may trigger an ownership change for U.S. federal income tax purposes. If we undergo an ownership change, we may have less cash available with which to satisfy our obligations.

Holders of the exchange notes may be required to include interest income or original issue discount in an amount greater than the actual cash interest payments.

We believe and intend to take the position that the exchange notes will not be subject to the contingent payment debt instruments rules for U.S. federal income tax purposes. However, it is possible that the exchange notes will be subject to these rules. If the exchange notes are treated as contingent payment debt instruments under such regulations, you will be required to include interest income in taxable income in each year

Edgar Filing: SPACEHAB INC \WA\ - Form S-4/A

significantly in excess of the amounts of stated interest on the exchange notes actually received by you in that year. Any gain that you recognize upon a sale, exchange, conversion, redemption, or retirement of the exchange notes would generally be treated as ordinary income and any loss will be ordinary loss to the extent of interest on the exchange notes previously included in income and, thereafter, as capital loss. For a summary of these potential adverse tax consequences, see [Material U.S. Federal Income Tax Considerations U.S. Holders Original Issue Discount on Exchange Notes](#).

Table of Contents**USE OF PROCEEDS**

We will not receive any cash proceeds from the issuance of the exchange notes in this exchange offer and consent solicitation.

CAPITALIZATION

The following table sets forth our unaudited historical consolidated indebtedness and capitalization as of March 31, 2005 and our pro forma consolidated indebtedness and capitalization as of March 31, 2005 assuming the exchange of all outstanding notes for exchange notes. You should read this information in conjunction with Management's Discussion and Analysis of Financial Condition and Results of Operations and our consolidated financial statements and notes thereto included in this prospectus.

	As of March 31, 2005	
	Actual	As Adjusted
	(in thousands)	
Cash, cash equivalents and restricted cash	\$ 5,994	\$ 5,994
Indebtedness		
Mortgage loan payable, current	1,946	1,946
Mortgage loan payable, net of current portion	2,244	2,244
8% Convertible Subordinated Notes due 2007	63,250	
5.5% Senior Convertible Notes due 2010		63,250
Total indebtedness	67,440	67,440
Stockholders' equity:		
Preferred stock, no par value, convertible, 2,500,000 shares authorized, 1,333,334 shares issued and outstanding, (liquidation preference of \$9.00 per share)	11,892	11,892
Common stock, no par value, 30,000,000 shares authorized, 12,760,227 shares issued	83,857	83,857
Treasury stock, 116,100 shares, at cost	(117)	(117)
Additional paid-in capital	16	16
Accumulated deficit	(80,963)	(80,963)
Total stockholders' equity	14,685	14,685
Total capitalization	\$ 82,125	\$ 82,125

Table of Contents**RATIO OF EARNINGS TO FIXED CHARGES**

The following table sets forth our consolidated ratio of earnings to fixed charges for each of the periods indicated. For purposes of computing the ratio of earnings to fixed charges, earnings consist of the sum of our pre-tax income from continuing operations, amortization of capitalized interest and fixed charges minus capitalized interest. Fixed charges consist of interest expense, including amounts capitalized, amortization of capitalized expenses related to indebtedness, and one third of rent expense, which we estimate represents the interest associated with rental expense.

	<u>Years Ended June 30,</u>					Nine Month
						Period Ended
	2000	2001	2002	2003	2004	March 31,
	<u>2000</u>	<u>2001</u>	<u>2002</u>	<u>2003</u>	<u>2004</u>	<u>2005</u>
Ratio of Earnings to Fixed Charges ⁽¹⁾					1.27	2.12

- (1) Earnings did not cover fixed charges by \$5.6 million, \$13.6 million, \$4.4 million, and \$82.6 million for the years ended June 30, 2000, 2001, 2002 and 2003, respectively.

Table of Contents

INDUSTRY OVERVIEW

With the space shuttle fleet's two-and-a-half year hiatus and a NASA budget that had previously seen only inflationary adjustment annually over the past several fiscal years, the aerospace industry has experienced some significant challenges. Additionally, the 54 orbital launches recorded in 2004 were the lowest total since 1961.

In January 2004, President George W. Bush announced an initiative for space exploration, not only declaring his support of the United States space program but setting a goal for further exploration. The President committed the United States to a long-term human and robotic program to explore the solar system, starting with a return to the Moon that is intended to enable future exploration of Mars and other destinations. This initiative is expected to provide rewards for many of the leading aerospace companies and reverse the steady or shrinking NASA budget.

The President's fiscal year 2006 budget request of \$16.5 billion identifies what is needed to continue transforming the U.S. civil space program. The request, which represents a 2.4% increase from 2005, supports critical national needs and technologies, including investments in next generation earth observing satellites, vehicle systems and educational programs for the next generation of explorers. The budget assumes an ongoing effort to retool NASA's institution based on best achieving its priorities for the Vision for Space Exploration. This will require adjustments to work-force skill distribution, physical capital, facilities and innovations in management structure.

The main beneficiary of the 2006 budget is NASA's Exploration Systems, with funding up from \$2.7 billion to \$3.2 billion, representing a 17.9% increase. The role of Exploration Systems is to develop a set of new capabilities, supporting technologies and foundational research that enables sustained and affordable human and robotic exploration. The budget proposal also maintains the return-to-flight of the space shuttle fleet as a top priority and includes \$1.9 billion for the International Space Station with funding support for an enhanced crew size of up to six prior to completion of assembly. This level of funding should allow NASA to meet obligations for international partners as well. We believe that the 2006 budget reaffirms the President's commitment and provides NASA the next step in implementing its strategic vision. Based on NASA's estimates, the budget is expected to increase to over \$18 billion by fiscal year 2010.

In June 2004 the President's Commission on Implementation of United States Space Exploration Policy issued its final report of conclusions and recommendations gathered from public testimony of 96 individuals and over 6,000 written inputs. The commission's objective was to examine and make recommendations on implementing the new national vision. The commission found overwhelming public support (public comments supporting the vision compared to those against the program by 7 to 1) for this new National Vision for Space Exploration. Throughout the report, the commission found and emphasized the need for a greater role of commercial enterprise in the space exploration program.

Futron study statistics for the global space industry reflect strong government spending and consumer demand for satellite services, producing growing revenues of \$78.6 billion in 2001, \$86.1 billion for 2002 and \$91.0 billion in 2003. Global space industry revenues have continued to increase, growing at a rate of approximately 7.6% annually over the two years from 2001 to 2003, even though some markets, such as the commercial satellite sector, have experienced a significant decline in recent years. Satellite services and ground equipment manufacturing have shown the greatest growth, while satellite manufacturing and the launch industry have shown the greatest declines. Government spending and strong consumer demands for satellite video services were responsible for almost all of this growth. Although industry revenues have been positive, other indicators, such as prices, profit margins, stock prices and new orders, have experienced negative trends and reflect significant financial stress in the industry.

Table of Contents

BUSINESS

We were incorporated as a Washington corporation in 1984 and made our initial public offering of our common stock in 1995. We flew our first module on a space shuttle mission in 1993 and have continued to grow our customer base and services offerings since then. With approximately \$75 million in annual revenue and over \$100 million in flight and payload processing assets in 2004, we are a leading provider of commercial space services.

After the completion of several space shuttle science missions using our research module, we expanded our services into the logistics arena, developing new flight assets to support the growing transportation needs of space station users. The logistics module, which is attached to the research module in order to transform our module into a double module configuration, enables delivery of up to 4,500 kilograms (10,000 pounds) of supplies while our unpressurized integrated cargo carriers permit delivery of 2,700 kilograms (6,000 pounds) of cargo.

In February 1997 we acquired Astrotech Space Operations, the leading commercial supplier of launch processing services in the United States. Expanding our core business of supporting people living and working in space, we acquired Johnson Engineering, now named SPACEHAB Government Services, in 1998 to include specialized engineering support services for the U.S. Government. Space Media, Inc. was formed in 2000 to develop space-related media and education and entertainment services to space enthusiasts around the world.

Core Business Operations

Our business segments provide a range of products and services to the aerospace and commercial markets. Our four business units consist of:

SPACEHAB Flight Services. Our Flight Services business unit provides research and logistics expertise and hardware.

Astrotech Spacecraft Operations. Our Astrotech spacecraft processing business unit provides facilities and support for the preparation of satellites and payloads for launch on expendable launch vehicles.

SPACEHAB Government Services. Our Government Services business unit provides project management and specialized engineering analysis, products and services to NASA and other customers.

Space Media, Inc. Our Space Media business unit provides space-themed educational and retail products and services.

SPACEHAB Flight Services

The primary goal of our Flight Services business unit is to enable government and commercial enterprise to overcome the habitability and occupational challenges of space. Through the provision of experts, specialized hardware and established processes, we help provide access to the resources of space. We offer a range of engineering, integration, operations and ground support services that we tailor to meet our clients specific requirements. Our Flight Services business unit also provides habitat and logistics modules and unpressurized integrated cargo carriers

Edgar Filing: SPACEHAB INC \WA\ - Form S-4/A

to NASA for use on the U.S. space shuttle fleet and the International Space Station. We sell research and logistics services to NASA and commercial customers who want to use our modules and unpressurized carriers for specific space applications.

Modules. Our modules provide space-based research facilities and pressurized cargo services for use aboard the space shuttle. Our single module is an aluminum cylinder, measuring 10 feet in length by 13.5 feet in diameter, that provides resources such as power, data management, thermal control, and vacuum venting. Our single module, which has a payload capacity of 5,400 pounds, is employed primarily for research and logistics missions. We also have a second logistics module that cannot be used alone but can be attached to our single module and used in the space shuttle in a double configuration. When used in a doubled configuration the payload capacity of our modules increases to 10,000 pounds and optimizes the resupply capability for NASA by

Table of Contents

carrying vital supplies to cosmonauts and astronauts onboard the International Space Station. Our single and double module configuration, when installed in the payload bay of a space shuttle, doubles or quadruples the space available to astronauts for research, habitation, and storage, while still leaving space in the shuttle bay for unpressurized cargo. As of August 12, 2005 NASA had utilized our modules, including our research double module that we lost in the *Columbia* tragedy, on 16 space shuttle missions for research and logistics purposes in both single and double module configurations.

In April 2004 we successfully completed the transition of our module systems integration and operations work from our subcontractor, The Boeing Company, to an in-house capability. Our personnel now perform mission integration, hardware development, and sustaining engineering required to support the flight of our two modules. This move reduced operating costs, increased flexibility in responding quickly to changing customer requirements, and built upon our existing core capabilities needed to support future logistics and research missions to the International Space Station.

Unpressurized Carriers. In addition to our two modules, we have developed with RSC Energia an integrated cargo carrier system of unpressurized payload carriers to transport cargo that does not require a pressurized environment in space. Cargo suitable for transport on our integrated cargo carriers includes International Space Station assembly components and spares, astronaut tools, and unpressurized experiments. Our integrated cargo carriers fly in what is ordinarily unused volume in the front or rear of the space shuttle's cargo bay. Integrated cargo carriers can be used alone or in combination with our single or double module to provide the optimum mix of pressurized and unpressurized cargo capacity on a single mission to the International Space Station. In addition, depending upon NASA's mission requirements, our integrated cargo carriers can be removed from the shuttle bay and attached to the International Space Station. By expanding the capabilities of the space shuttle and offering flexibility in the mix of pressurized and unpressurized cargo carried on each mission, the integrated cargo carrier is a cost-effective solution for International Space Station logistics.

Our integrated cargo carrier initially flew on NASA's first supply mission to the International Space Station, space shuttle flight STS-96 in May 1999, and has flown on five subsequent missions with more flights scheduled on the NASA manifest. In fiscal year 2001, we sold our integrated cargo carriers to EADS and entered into an agreement with them to lease back these assets for a period of four years with two additional four-year options.

To meet particular NASA requirements for unpressurized cargo transport, we also developed a vertical integrated cargo carrier, designed and built for us by RSC Energia. In fiscal year 2002, we received the vertical integrated cargo carrier and also sold this asset to EADS for inclusion in the lease back arrangements discussed above. The integrated cargo carrier system, including the vertical integrated cargo carrier, is a flexible and adaptable payload transport option.

Other Services. In addition to our flight assets, we offer a full range of ground-based pre- and post-flight experiment and payload processing services and in-flight operations support. NASA and other users of the space shuttle and International Space Station must follow a complex set of procedures to prepare payloads for launch, operate them in space, and process them upon return. Our carrier development and operations team offers these users turn-key, fixed-price payload services using our modules and unpressurized integrated cargo carriers. These services include payload scheduling, mission planning, safety analysis and certification, physical integration with a module or integrated cargo carrier, integration of these carriers with the space shuttle, flight operations, data gathering and synthesis, and launch and landing site activities.

We are also providing research access on the International Space Station to the Japan Aerospace Exploration Agency (JAXA) through RSC Energia. We contracted with V.J.F. Russian Consulting Inc. for the construction of certain space research equipment, access to launch vehicles, and research space aboard the Russian *Progress* carrier when the originally-scheduled services on the space shuttle were suspended due to the *Columbia* tragedy.

We also have an advanced programs team chartered to investigate and develop new technologies and concepts that support the vision of the President's stated "Moon, Mars, and Beyond" goals. See "Industry

Table of Contents

Overview for a discussion of this initiative. We recently completed a six-month NASA study contract valued at approximately \$1.0 million to support the space agency's new exploration initiatives. The purpose of this contract was to design a technical solution to accomplish the agency's objectives for lunar exploration and to identify systems that could also be used on missions to Mars and other destinations. Our winning proposal documented our approach for designing an architecture that takes advantage of commercial efficiencies; specifically, how private industry can contribute to the investment in getting people to the moon and elsewhere. We believe that our approach results in lower program costs and provides the additional benefit of applying existing capabilities and mature technology. Following the six-month effort, NASA awarded us an additional six-month contract, also valued at approximately \$1.0 million, to continue and expand upon our initial work.

Astrotech Space Operations

Our spacecraft processing services business unit provides government and commercial customers with a commercial alternative to using government-owned facilities to prepare their satellites for launch in the United States. This business unit began operations at our Titusville, Florida facility in 1985. We believe that growing wireless telecommunication demands, such as direct-broadcast radio and television, cellular telephones, and broadband internet services, as well as the continued need for video and long-distance telephone transmissions, will provide us with opportunities to expand our customer base. As of June 30, 2005, we had supported the processing of more than 225 spacecraft. Our standard package of services provides all support necessary for the customer to successfully process its spaceflight hardware for launch, including:

cleanroom facilities for hardware processing and encapsulation operations;

communications network for spacecraft command/control through launch;

storage and transportation of liquid propellants;

facilities for solid-rocket motor preparation;

life safety support for propellant loading operations;

program security to include convoy escorts to and from launch facilities;

sampling and analysis of propellants and gases;

emergency fire and medical assistance;

coordination with NASA and the Air Force for government-supplied support; and

safety oversight of all hazardous operations.

Edgar Filing: SPACEHAB INC \WA\ - Form S-4/A

Astrotech-processed payloads have launched from Florida's NASA Kennedy Space Center/Cape Canaveral Air Force Station, Vandenberg Air Force Base, California, and via the equatorial platform of Sea Launch. Customers have used our facilities to prepare payloads for launch on a wide range of expendable launch vehicles including Atlas, Delta, Pegasus, Sea Launch, and Taurus, as well as secondary payloads flown on the space shuttle. Our modern facilities are specifically sized and outfitted to accommodate a wide range of customer payloads as well as the payload fairings and payload adapter assemblies of the launch service providers. We believe that this approach allows for maximum flexibility in the processing of parallel missions and accommodating schedule changes. Our goal is to make our facilities a seamless extension of the customer's factory environment.

Our largest facility in Titusville, Florida, which we own, supports spacecraft processing for launches in Cape Canaveral and is capable of processing larger five meter class satellites and payload fairings for Lockheed Martin's and Boeing's Evolved Expandable Launch Vehicle Programs. The satellite and payload fairings for the Evolved Expandable Launch Vehicle Programs are significantly bigger than other launch vehicles currently in use, with weights in excess of 25,000 pounds and payload fairings up to 75 feet long, and require larger facilities for processing. Our facility is the only satellite processing facility at Florida's Kennedy Space Center/ Cape Canaveral Air Force Station launch complex with the capability to accommodate these larger five meter class

Table of Contents

satellite and payload fairings. Our Titusville, Florida spacecraft processing facility supports all planned configurations of the Boeing Delta IV and Lockheed Martin Atlas V Evolved Expendable Launch Vehicle systems. We also lease facilities located on Vandenberg Air Force Base to support launches on the west coast. In addition, we manage the facilities at the Port of Long Beach that are used to process satellites and payloads being launched by Sea Launch Company, LLC.

SPACEHAB Government Services

Our Government Services business unit has provided specialized engineering support services for the U.S. Government, including NASA, and various commercial industries for over 30 years. Specifically, we have supported the U.S. Government in the areas of:

large-scale configuration and data management programs such as the International Space Station;

specialized design, development, and fabrication of flight hardware;

low- to high-fidelity mockup design and construction; and

safety and quality support services.

We offer a wide array of products and services in these varied fields and bring advanced ideas and solid execution of these innovations to our customers.

Currently, our Government Services business unit derives most of its revenue from our contract to provide configuration and data management services within NASA's Program Integration & Control contract for the International Space Station as a subcontractor to ARES Corporation. This contract expires in 2008. Using our skill and expertise, we are an integral part of the total NASA team responsible for final acceptance of International Space Station hardware and software that includes both the development contractors and the 16 international partners. Configuration management focuses on the approved design and the configuration of the thousands of hardware and software parts and components for the International Space Station by constant review of development processes and the status of progressing and constantly-changing activities. Specifically, the configuration management functions we currently provide to the customer include:

planning and management of International Space Station Partners configuration management policies, procedures and requirements;

identification of configurations and processes;

change management;

status accounting; and

verifications and audits.

Our Government Services business unit also has the ability to support customer data management requirements by:

ensuring data validity;

providing deliverables tracking support;

creating data management programs;

providing data directories; and

developing documentation trees.

Space Media

Space Media, Inc., a majority-owned subsidiary, creates proprietary space-themed content for education and commerce. By leveraging our access to engineers, marketing and industry professionals, and aerospace

Table of Contents

subcontractors, we are able to provide the space enthusiast with a variety of services and products. These services range from outfitting a comprehensive space exhibit to providing astronaut appearances and product endorsements. Two of the most successful ventures within Space Media are the STARS Program and The Space Store, both of which we believe are unique in their focus on inspiring our youth through space exploration.

The STARS Program is our commercial education initiative developed as a hands-on, interactive, scientific and cultural exchange lesson primarily designed for students aged 11-21 to promote interest in engineering, mathematical, and scientific careers. Through the STARS Program, which is funded by participating schools, students design an actual experiment for flight on the space shuttle or International Space Station. During the design and flight of their experiments, students worldwide work directly with space scientists, engineers, and managers to gain comprehensive knowledge of the flight and scientific method process. Three STARS Program missions have been flown to date, with experiments launched on NASA's STS-93 mission, an International Space Station mission via a Russian Soyuz rocket, and on STS-107.

We believe The SpaceStore.com is the largest on-line retailer of space-themed merchandise. Started in May 1997, we believe this outlet has been in operation longer than any other space e-commerce website, including NASA's on-line store. The Space Store also maintains a physical storefront located directly across the street from NASA's Johnson Space Center and Space Center Houston. The store is frequented by NASA employees, numerous astronauts, and tourists visiting Houston's official visitor's center at Johnson Space Center. Our website and retail store offer a large variety of specialized space toys, clothes, and memorabilia and host astronaut book signings and children's story time, space collector appraisals, and media events geared towards spreading the excitement of space.

Competition

Our competition and the barriers to entry vary amongst our business units. We believe that, generally, barriers to entry for new competitors for our Flight Services and Astrotech business units remain high. The modules, facilities, and other assets that we own represent a capital investment that many new entrants into the market would have difficulty matching. We estimate that it would take another organization three to five years to develop, and certify for use by NASA, a module service similar to that operated by our Flight Services business unit. We are not aware of any company that is currently making such an effort and, given the proposed retirement of the space shuttle fleet in 2010, would not expect any company to commence such an effort. For our logistics module and unpressurized integrated cargo carriers there are similar assets currently owned and periodically used by NASA (i.e. the Italian Space Agency-built Multi Purpose Logistics Module, the Multi Purpose Experiment Support Structure carrier, and the Spacelab pallet). However, we believe our assets provide more utility in supporting powered experiments and are able to carry more weight and volume than the other solutions available to NASA.

Our Astrotech spacecraft and payload processing facilities are located in Florida and California and serves satellites constructed in the United States. Due to the costs of transporting internationally, our Astrotech business unit generally does not compete with launch services based in other countries. At present, our Astrotech business unit's commercial U.S. competition is limited to the California launch site at Vandenberg Air Force Base where California Commercial Spaceport Systems International is located. California Commercial Spaceport Systems International acquired surplus United States Air Force (USAF) facilities through a lease agreement with the USAF at Vandenberg Air Force Base before we established our facilities there. California Commercial Spaceport Systems International does not have payload processing facilities in Florida, where the majority of U.S. commercial satellite launches occur. In addition, as the commercial space industry continues to evolve, we expect to face increasing competition from new companies.

Our Government Services business unit competes with companies that provide operations support, configuration management, and engineering and fabrication services to NASA. These competitors include aerospace contractors such as Boeing, Lockheed Martin, United Space Alliance, ARES Corporation, Barrios Technologies Inc., Hernandez Engineering Inc., Cimarron, and Oceaneering Space Systems. However, for this business unit's primary source of revenue, we are currently operating under a subcontract through at least 2008.

Table of Contents

Space Media competes with various suppliers of space education and retail goods. This includes internet sites and retailers with space-related toys, food, games, clothing, and patches; builders of space museum exhibits, mockups, and displays; and some providers of space-based education curriculum.

Dependence on a Single Customer

Approximately half of our revenue in fiscal year 2004 was generated by various NASA contracts or subcontracts. While other contracts with commercial customers provide revenue from varying sources, we anticipate that contracts servicing NASA will continue to account for a significant amount of our revenue in the near future. Although we cannot make any assurances that NASA will require our services in the future, we are under firm contracts with NASA to support a variety of activities for the next several years. We continue to work on diversifying our customer base to include foreign space agencies, aerospace partners, and private companies.

Similar to contracts with other agencies of the U.S. Government, our contracts servicing NASA contain provisions pursuant to which NASA or the prime contractor may terminate the contract for convenience. Our contracts servicing NASA depend upon NASA's receipt of adequate annual appropriations from the U.S. Congress, and failure to receive adequate funds could prompt NASA to terminate its contracts with us or the prime contractor for convenience. There is no assurance that future funding will be adequate for NASA to complete all of its initiatives including those relating to contracts with us. In light of the problems with the July 26, 2005 launch, NASA has currently grounded the space shuttle fleet. If space shuttle flights are not resumed or currently planned flights are cancelled, then our contracts that are dependent on such flights may be cancelled in full or in part. We anticipate that a portion of our revenue for our next fiscal year will be derived from contracts with entities other than agencies of the U.S. Government that will not be subject to federal contract regulations such as termination for convenience or government funding restrictions.

Our Astrotech business unit serves the satellite launch industry, which is dominated domestically by Lockheed Martin and Boeing. We have a contract in place with Lockheed Martin to support payload processing for the Atlas launch vehicle program and we also provide payload processing services for Boeing's Delta launch vehicle program. Our Lockheed Martin contract guarantees us a minimum of four launches annually through December 2006. Certain launches on Boeing's launch vehicles count towards this minimum. We have other current contracts in place with NASA, Boeing, and Orbital Sciences Corp. for support of spacecraft processing activities in both Florida and California. Our Astrotech business unit manages the Sea Launch facility under a long-term contract with Sea Launch Company, LLC which expires in 2011.

Backlog

As of March 31, 2005, our contract backlog was approximately \$81.9 million, of which \$70.3 million represented U.S. Government backlog and \$11.6 million represented non-U.S. Government contracts. We estimate that \$13.5 million of our current contract backlog will not be filled during fiscal 2006. Our contract backlog was approximately \$107.2 million as of March 31, 2004, of which \$91.9 million represented U.S. Government backlog. See Risk Factors Termination of our backlog orders could negatively impact our revenues for additional discussion of our backlog.

Contract History

Edgar Filing: SPACEHAB INC \WA\ - Form S-4/A

Our business strategy focuses on anticipating customer requirements, investing capital to develop space flight assets, contracting with established aerospace companies for engineering and asset production, and retaining control of these assets.

For our Flight Services business unit, we have obtained four significant space Flight Services contracts with NASA to date that utilize our privately-developed modules and unpressurized integrated cargo carriers. This includes the original Commercial Middeck Augmentation Module contract for four space shuttle research missions, which we completed in May, 1996; a contract for four logistics missions and three option missions (all of which were exercised) to the Russian space station *Mir*, which we completed in June, 1998; a Research and Logistics Mission Support contract initially for four missions, followed by six additional missions in support of the International Space Station and microgravity science requirements; and the current Cargo Mission Contract

Table of Contents

subcontract in support of NASA's International Space Station logistics requirements served through Lockheed Martin.

For the first half of fiscal 2004, the Research and Logistics Mission Support contract was the vehicle used by NASA to obtain the use of our modules and unpressurized integrated cargo carriers. Upon the restructuring of NASA's various International Space Station contracts, Lockheed Martin became the Cargo Mission Contract prime contractor, and we now provide our logistics services and assets as a subcontractor. The new contract calls for our single and double modules as well as integrated cargo carriers to support research payloads and outfitting of the International Space Station. We are currently supporting three missions under this contract, STS-121, STS-116, and STS-118. Additionally, we had a contract with Boeing for integrated cargo carrier services on the STS-114 mission that was completed in August 2005. We are paid an equitable adjustment for delays in launching missions under contract. The equitable adjustment is a cost-based contract price adjustment to cover any periods during which a scheduled space shuttle flight for which we are under contract is delayed.

Our Astrotech spacecraft processing business unit has successfully supported the processing of over 225 spacecraft since beginning operations in 1985. In fiscal year 2000, we completed negotiations of long-term extensions to payload processing contracts with our two largest customers, Boeing and Lockheed Martin. The total projected revenue under these contracts was approximately \$85 million. Additionally, we also have payload processing contracts in place with NASA and Orbital Sciences Corp. Our Astrotech business unit also operates and maintains the payload processing infrastructure of, and provides operational support, to Sea Launch Company, LLC.

On October 1, 2003, we were notified by Boeing that it was exercising its termination rights with regards to its financial guarantees under its contract with us for payload processing support services for the Delta launch vehicle program. Boeing indicated that the decision to terminate its guarantees for future services was based on the downturn of the commercial expendable launch market rather than performance related considerations. We believe that we were in compliance with the contract terms at the time of the termination. Under the contract provision related to termination of its financial guarantees, Boeing paid us \$17.5 million representing consideration for future contract payments guaranteed under the contract. Since this time, Boeing has contracted with us for payload processing support on a mission-by-mission basis.

In fiscal year 2004 our Government Services business unit operated primarily under two contracts. For the first half of the year, we were the prime contractor for International Space Station Configuration Management, a contract that was completed. We are now supporting the International Space Station Program Integration & Control contract as a subcontractor to ARES Corporation through a NASA contract awarded at the completion of the original International Space Station Configuration Management contract.

Research and Development

We incurred \$0.2 million, \$0.1 million, and \$0.4 million in research and development expense during fiscal years 2004, 2003, and 2002, respectively. We spent \$0.2 million in 2004 and \$0.1 million in 2003 on miscellaneous research and development projects, including the design of a new commercial payload service. Research and development in fiscal year 2005 has been directed towards development of commercial responses to the National Vision for Space Exploration.

Most of our research and development expenditures for fiscal year 2004 were spent on the development of the *Enterprise* module, a commercial space station habitat module, which is no longer under development, but much of the technological and structural design from that effort is being used to develop the new commercial payload service system. The remainder of the \$0.2 million was spent on miscellaneous research and development projects in 2004.

Certain Regulatory Matters

We are subject to federal, state, and local laws and regulations designed to protect the environment and to regulate the discharge of materials into the environment. We believe that our policies, practices, and procedures

Table of Contents

are properly designed to prevent unreasonable risk of environmental damage and consequential financial liability to us. Compliance with environmental laws and regulations and technology export requirements has not had in the past, and, we believe, will not have in the future, material effects on our capital expenditures, earnings or competitive position. Our operations are subject to various regulations under federal laws relative to the international transfer of technology as well as to various federal and state laws relative to business operations. In addition, we are subject to federal contracting procedures, audit, and oversight under Federal Acquisition Regulations.

Significant federal regulations impacting our operations include the following:

Federal Regulation of International Business. We are subject to various federal regulations relative to the export of certain goods, services, and technology. These regulations, which include the Export Administration Act of 1979 administered by the Commerce Department and the Arms Export Control Act administered by the State Department, impose substantial restrictions on the sharing or transfer of technology to foreign entities. Our activities in the development of space technology and in the processing of commercial satellites deal with technology of the type subject to these regulations. Our operations are conducted pursuant to a comprehensive export compliance policy that provides close review and documentation of activities subject to these laws and regulations.

Foreign Corrupt Practices Act. The Foreign Corrupt Practices Act establishes rules for U.S. companies doing business internationally. Compliance with these rules is achieved through established and enforced corporate policies and documented procedures in our internal procedures and financial controls.

Iran Nonproliferation Act of 2000. This act includes specific prohibitions on commercial activities with certain specified Russian entities engaged in providing goods or services to the International Space Station. Our activities with RSC Energia of Russia are not subject to this act.

Federal Acquisition Regulations. Goods and services provided by us to NASA and other U.S. Government agencies are subject to Federal Acquisition Regulations. These regulations provide rules and procedures for invoicing, documenting, and conducting business under contract with such entities. The Federal Acquisition Regulations also subject us to audit by federal auditors to confirm such compliance.

Truth in Negotiations Act. The Truth in Negotiations Act was enacted for the purpose of providing for full and fair disclosure by contractors in the conduct of negotiations with the U.S. Government. The most significant provision included in the Truth in Negotiations Act is the requirement that contractors submit certified cost and pricing data for negotiated procurements above a defined threshold.

Regulatory Compliance and Risk Management

We maintain compliance with regulatory requirements and manage our risks through a program of compliance, awareness, and insurance which includes the following:

Safety. We place a continual emphasis on safety throughout our organization. At the corporate level, safety programs and training are monitored by a corporate safety manager. A staff of senior safety professionals within our Flight Services business unit provides safety as a component of

our space flight operations and augments the safety awareness and oversight available at the corporate level.

Export Control Compliance. We have a designated senior officer responsible for export control issues and the procedures detailed in our export control policy. This officer and the designated export compliance administrator monitor training and compliance with regulations relative to foreign business activities. Employees are provided comprehensive training in compliance with regulations relative to export and foreign activities through our interactive training program and are certified as proficient in such regulations as are relative to their job responsibilities.

Table of Contents

Insurance. Our operations are subject to the hazards associated with operating assets in the severe environment of space. These hazards include the risk of loss or damage to the assets during storage, preparation for launch, in transit to the launch site, and during the space mission itself. We maintain insurance coverage against these hazards with reputable insurance underwriters. Although we did not fully insure our flight assets in the past, we intend to insure our flight assets at replacement value for risk of loss during future space flight missions.

Legal Proceedings

Contract Claim. In January 2004 we filed a formal proceeding with NASA seeking indemnification under our Research and Logistics Mission Support contract in the amount of \$87.7 million for the value of our research double module and related equipment that was destroyed during the Space Shuttle *Columbia* tragedy. NASA responded to this contract claim on October 5, 2004. NASA's determination states that its liability is limited under the Research and Logistics Mission Support contract to \$8.0 million. We received payment of \$8.2 million, which included \$0.2 million of interest, from NASA in October 2004. In January 2005, we filed an appeal of NASA's decision to deny its claim for indemnification in excess of \$8.0 million with the Armed Services Board of Contract Appeals. On May 5, 2005 NASA filed its answer to our complaint with the Armed Services Board of Contract Appeals. We are now proceeding with discovery.

Lloyd's Complaint. In January 2004, Lloyd's of London, our insurer for the research double module, filed a complaint in the United States District Court for the Western District of Washington seeking the return of the \$17.7 million Lloyd's had paid to us under the research double module insurance policy. On May 12, 2005 we and Lloyd's agreed to jointly pursue recovery against NASA with us in full control of the appeals process. Lloyd's will participate in any recovery, both pursuant to our administrative claim and our tort claim against NASA, net of legal costs, in accordance with a pre-agreed schedule under which our liability to Lloyd's ranges from a minimum of \$500,000 if we do not recover any additional amounts to approximately \$17.7 million if we recover over \$70.0 million from NASA. Also in accordance with the agreement, Lloyd's dismissed its complaint against us with prejudice. We will record a charge in our fourth quarter financial statements of \$500,000 pending a final resolution of our actions against NASA.

Tort Claim. On November 8, 2004, we filed a second claim with NASA seeking damages of \$79.7 million under the federal tort claims act for the loss of our research double module resulting from NASA's alleged negligence leading to the destruction of the space shuttle *Columbia* and the loss of our research double module. The claim represents our loss of \$87.7 million less the \$8.0 million recovered from NASA. Since NASA did not respond to our claim for six months from the date on which we made the claim, NASA is deemed to have denied our claim. As a result of our administrative claim being deemed denied due to NASA's failure to respond, we have the right to, and intend to, pursue the claim in federal district court.

Changes in Certifying Accountant

On May 17, 2004, Ernst & Young LLP was dismissed as our independent registered public accounting firm. On May 18, 2004, Grant Thornton LLP was appointed as our new independent registered public accounting firm to replace Ernst & Young for the fiscal year ending June 30, 2004. The decision to dismiss Ernst & Young LLP and to appoint Grant Thornton LLP was recommended by the Audit Committee of our Board of Directors and was approved by our Board of Directors. The decision to dismiss Ernst & Young was the result of our and Ernst & Young's conclusion to discontinue the client-auditor relationship.

Ernst & Young's reports on our financial statements for the past two fiscal years did not contain an adverse opinion or disclaimer of opinion, nor were they qualified or modified as to uncertainty, audit scope or accounting principles.

During our two most recent fiscal years prior to the engagement of Grant Thornton and the period from June 30, 2003 through May 17, 2004, there were no disagreements with Ernst & Young on any matter of accounting

Table of Contents

principles or practices, financial statement disclosure, or auditing scope or procedure, which disagreements, if not resolved to the satisfaction of Ernst & Young, would have caused it to make reference to the subject matter of the disagreements in connection with its report; and there were no reportable events as defined in Item 304(a)(1)(v) of Regulation S-K.

We provided Ernst & Young with a copy of prior disclosure regarding its dismissal in a Current Report on Form 8-K dated May 17, 2004 and Ernst & Young furnished us with a letter addressed to the Commission stating whether it agrees with the statements by us in the current report. A letter from Ernst & Young to such effect is filed as an exhibit to our Current Report on Form 8-K dated May 19, 2004.

During our two most recent fiscal years prior to the engagement of Grant Thornton LLP and through May 17, 2004, we did not consult Grant Thornton LLP with respect to the application of accounting principles to a specified transaction, either completed or proposed, or the type of audit opinion that might be rendered on our consolidated financial statements, or any other matters or reportable events listed in Item 304(a)(2) of Regulation S-K.

Table of Contents**SELECTED CONSOLIDATED FINANCIAL DATA**

The following table sets forth our selected consolidated financial data as of and for the years ended June 30, 2000, 2001, 2002, 2003, and 2004. Such data has been derived from our consolidated financial statements audited by Grant Thornton LLP for the fiscal year ended June 30, 2004, by Ernst & Young LLP for the fiscal years ended June 30, 2001, 2002, and 2003, and by KPMG for fiscal year ended June 30, 2000. The summary financial data for the nine-month periods ended March 31, 2004 and 2005 has been derived from our unaudited condensed consolidated financial statements for these periods. The data set forth below should be read in conjunction with Management's Discussion and Analysis of Financial Condition and Results of Operations, Risk Factors and our Consolidated Financial Statements and Notes thereto included in this prospectus. All amounts, except per share amounts, are in thousands.

	Years Ended June 30,					Nine Months Ended March 31,	
	2000	2001	2002	2003	2004	2004	2005
				Restated			Restated
Statement of Operations Data:							
Revenue from operations	\$ 105,708	\$ 105,254	\$ 102,773	\$ 94,963	\$ 77,606 ⁽⁷⁾	\$ 66,466 ⁽⁷⁾	\$ 40,443
Costs of revenue	87,931	92,243	81,767	78,791	45,678	36,172	32,592
Gross profit	17,777	13,011	21,006	16,172	31,928	30,294	7,851
Selling, general and administrative expenses	17,832 ⁽¹⁾	21,796	19,507 ⁽⁴⁾	91,434 ⁽⁵⁾	20,982 ⁽⁸⁾	18,954 ⁽⁹⁾	(1,688) ⁽¹⁰⁾
Research and development expenses	2,440 ⁽²⁾	393	383	118	223	9	37
Income (loss) from operations	(2,495)	(9,178)	1,116	(75,380)	10,723	11,331	9,502
Interest expense, net of capitalized amounts and interest and other income	3,773	4,804	5,533	7,252	8,142	6,679	4,178
Net income (loss)	(3,844)	(12,785) ⁽³⁾	(2,367)	(81,775)	2,075	4,401	5,169
Net income (loss) per common share basic	\$ (0.34)	\$ (1.12)	\$ (0.20)	\$ (6.66)	\$ 0.17	\$ 0.35	\$ 0.41
Net income (loss) per common share diluted	\$ (0.34)	\$ (1.12)	\$ (0.20)	\$ (6.66)	\$ 0.15	\$ 0.31	\$ 0.36
Shares used in computing net income (loss) per common share basic	11,273	11,400	11,884	12,285	12,450	12,416	12,603
Shares used in computing net income (loss) per common share diluted	11,273	11,400	11,884	12,285	14,142	14,040	14,204
Cash dividends declared per common share							
Other Data:							
Cash provided by (used in) operating activities	\$ 1,424	\$ 17,124	\$ 8,592	\$ 2,114	\$ 5,273	\$ 7,287	\$ (6,243)
Cash provided by (used in) investing activities	(29,794)	(23,076)	(13,167)	3,037 ⁽⁶⁾	5,019	6,171	13,646 ⁽¹⁰⁾
Balance Sheet Data (at period end):							
Working capital (deficit) surplus	\$ (1,601)	\$ (41,424)	\$ (22,022)	\$ (4,750)	\$ (6,351)	\$ (4,277)	\$ 1,057
Total assets	225,109	222,477	220,826	121,356	99,925	99,967	95,725
Long-term debt, excluding current portion	75,901	64,589	83,426	80,056	66,942	67,427	65,494
Stockholders' equity	102,702	90,356	87,670	5,090	9,410	11,704	14,685

Edgar Filing: SPACEHAB INC \WA\ - Form S-4/A

Book value per common share (11)	8.06	6.88	6.38	(0.55)	(0.20)	(0.02)	0.22
----------------------------------	------	------	------	--------	--------	--------	------

- (1) Includes approximately \$1.8 million of expenses associated with the startup of Space Media.
- (2) Includes approximately \$0.5 million of expenses associated with our discontinued *Enterprise* module.
- (3) Includes approximately \$3.3 million of non-cash expense to record a full valuation allowance on our deferred tax asset.

Table of Contents

- (4) Includes approximately \$0.8 million of non-cash expenses related to subleasing of excess facilities.
- (5) Includes approximately \$78.3 million of non-cash write downs related to the loss of our research double module, goodwill impairment at our Government Services business unit, and asset impairment.
- (6) Includes approximately \$17.7 million of insurance proceeds related to the loss of our research double module.
- (7) Includes approximately \$17.5 million due to Boeing's termination of its spacecraft processing contract with us.
- (8) Includes approximately \$0.3 million of non-cash expenses related to subleasing of excess facilities, \$8.3 million of goodwill impairment at our Government Services and Astrotech Space Operations business units, and a \$1.8 million non-cash write-down of an investment in Guignè.
- (9) Includes approximately \$8.3 million of goodwill impairment at our Government Services and Astrotech Space Operations business units and a \$1.8 million non-cash writedown of an investment in Guignè.
- (10) Includes approximately \$8.2 million of recovery related to indemnification payments for the loss of our research double module.
- (11) Excludes common stock issuable upon conversion of our Series B convertible preferred stock.

Table of Contents

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

The following discussion should be read in conjunction with, and is qualified in its entirety by reference to, our audited consolidated financial statements and notes thereto included elsewhere in this prospectus.

Overview

We are pleased that the White House issued a new vision for U.S. space leadership. We view the President's commitment to space exploration, the human spaceflight program, and the plan for missions to the Moon, Mars, and beyond as positive indicators that will reinvigorate the space program, likely yielding benefits to the aerospace and space commerce industries. We believe that this vision provides NASA with a clear focus, will stabilize the NASA program, and will increase funding for the new pursuits.

We believe the impacts of this vision will materialize over time, and we will continue to align our business direction to remain a constructive force in the human spaceflight program. In the long term, we believe that our core competencies offer opportunities to continue to provide services as well as to design, build, and operate assets that could support initiatives beyond low Earth orbit. We plan to pursue these new opportunities. In the near term, our primary objective is to continue providing services to NASA and the space community in support of the space shuttle and the International Space Station programs. Even with the renewed vision, we expect that the space shuttle and International Space Station will remain an integral part of the human spaceflight program through at least 2010. We supported the return to flight mission in July 2005 and are currently supporting three of the next five scheduled space shuttle flights. We are pursuing additional missions that will be important for completing the final assembly of the International Space Station. In January 2005 we received authorization to proceed on integration and operations activities for the STS-116 shuttle mission currently scheduled for February 2006. In addition, we received authorization for new contract work to add a deployable stowage platform to the STS-118 shuttle mission scheduled to launch in July 2006. This deployable storage platform will be permanently affixed to the International Space Station. Following the launch of the Space Shuttle *Discovery* in July 2005, NASA announced that the space shuttle fleet will be grounded for an indefinite period of time until loss of foam from the shuttle's external fuel tank can be remedied. Our contractual arrangements provide for the payment to us of a periodic asset maintenance fee when we are making available and maintaining our space assets pending launch.

We are actively engaged in defining commercial payload service solutions capable of meeting the International Space Station on-orbit re-supply and return requirements more efficiently than the space shuttle. These activities, some of which leverage our international strategic partnerships and intellectual property rights, include the development of an affordable cargo transportation system based on existing commercial launch vehicles and our modular payload integration architecture to transport pressurized and unpressurized cargo to and from the International Space Station. We further believe that our experience and expertise in the conceptual design, development, ground processing, and on-orbit operations support of payload and crew accommodations position us well for a role in the development of NASA's space exploration systems, the envisioned next phase in human exploration of space.

In September 2004, our Flight Services business unit was awarded a six-month NASA study contract valued at approximately \$1.0 million to support the space agency's new exploration initiatives. We defined concepts for accomplishing human lunar exploration with a focus on innovative solutions and commercial approaches that could be reapplied to missions to Mars and beyond. In March 2005, we were awarded a contract option for an additional six-month effort valued at nearly \$1.0 million.

Edgar Filing: SPACEHAB INC \WA\ - Form S-4/A

We operate in three main areas generally related to space flight activities within the aerospace industry: space assets and mission support services for manned and unmanned space exploration and research missions; commercial and exploratory satellite pre-launch services; and engineering services in support of government space operations. We also operate a retail space merchandise business and provide space-related educational services. Because of the diversity among the operations of our activities, we report the results of each business as

Table of Contents

a separate segment in our consolidated financial statements. Our consolidated financial results also reflect corporate-level expenses such as general and administrative, interest, and depreciation and amortization, but because of their nature, these items are not reported as a separate segment.

Business Segments

Following is a brief discussion of each of our four business segments, including a list of key factors that have affected, and are expected to continue to affect, their respective earnings and cash flows. We also present a brief discussion of our corporate-level expenses along with a summary of our current liquidity position and items that could impact our liquidity position in fiscal year 2005 and beyond.

SPACEHAB Flight Services. This business unit generates revenue by providing space shuttle-based, turnkey services that include customer access to space via our pressurized modules and unpressurized integrated cargo carriers; integration and operations support to logistics suppliers transporting their cargo aboard our modules and integrated cargo carriers to and from the orbiting International Space Station; and/or integration and operations support to scientists and technologists responsible for experiments performed aboard module and integrated cargo carrier research platforms.

We also offer on a space-available basis for each mission, access to space on board the space shuttle, Russian *Progress*, and European Space Agency ATV cargo vehicles under commercial contracts with non-NASA customers, including both government and private customers. Commercial contracts with non-NASA customers will continue to be established directly between us and our commercial customers.

Additionally, during the space shuttle stand-down period, we provided cargo shipment coordination services to NASA for all U.S. cargo shipped to the International Space Station via the Russian *Progress* space vehicle. These services are provided under contract to Lockheed Martin, the prime Cargo Mission Contract contractor to NASA. We are also providing research access to space and on the International Space Station to the Japanese Aerospace Exploration Agency through RSC-Energia, a major Russian aerospace enterprise. We contracted through V.J.F. Russian Consulting with RSC-Energia for construction of certain space research equipment, access to Russian *Progress* launch vehicles, and research space aboard the International Space Station when the originally-scheduled services on the space shuttle were suspended due to the *Columbia* tragedy.

The primary factors impacting our Flight Services business unit earnings and cash flows are the number of space shuttle missions flown and the configuration of the cargo handling and research logistics required for each mission. Our revenues and earnings, if any, from each mission are dependent upon the space assets required in the cargo or research logistics configuration and the mission support services required to employ those assets. Other factors that have impacted, and are expected to continue to impact, earnings and cash flows for this business unit include:

Congress funding for NASA and the allocation of that funding to International Space Station operations and space shuttle cargo missions;

the return to flight of the U.S. space shuttle;

the role of international space research projects flying on future space shuttle and Russian and European Space Agency missions;

Edgar Filing: SPACEHAB INC \WA\ - Form S-4/A

the growth of space exploration programs within NASA and NASA's commitment to the President's Vision for Space Exploration regarding enhancement of the role of commercial enterprise in space exploration programs; and

our ability to control our capital expenditures, particularly those for spare or replacement parts for space assets.

Astrotech Space Operations. Revenue is generated from various fixed-price contracts with launch service providers in both the commercial and government markets. The services and facilities we provide to our customers support the final assembly, checkout, and countdown functions associated with preparing a satellite for launch.

Table of Contents

The earnings and cash flows generated from our Astrotech operations are related to the number of commercial satellite launches, which reflects the growth in the satellite-based communication industries, and the requirement to replace aging satellites. Other factors that have impacted, and are expected to continue to impact, earnings and cash flows for this business include:

our ability to control our capital expenditures, which primarily are limited to modifications to accommodate payload processing for new launch vehicles, maintenance and safety, environmental and reliability projects, and other costs, through disciplined management and safe, efficient operations; and

the continuing limited availability of competing facilities at the major domestic launch sites that can offer compatible services, leading to an increase in government use of our services.

SPACEHAB Government Services. Our Government Services business unit generates revenue by providing support to the U.S. Government in the areas of large-scale configuration and data management programs such as the International Space Station; specialized hardware design, development, and fabrication; low-to high-fidelity mockup design and construction; and safety and quality support services. This business unit offers a wide array of products and services in these varied fields. Our Government Services business unit currently provides configuration management services as a subcontractor of ARES under ARES Program Integration and Control contract with NASA.

Earnings from our Government Services business unit operations are dependent on our ability to continue to win contracts with NASA or other government entities through the competitive bidding process and our performance under those contracts in achieving performance bonuses. Other factors that have impacted, and are expected to continue to impact, earnings and cash flows for this business include:

continuation through 2008 of our Program Integration and Control contract with the International Space Station program;

our ability to maintain small business qualification for our Government Services business unit under NASA contracting rules; and

our ability to control costs within our budget commitments.

Space Media. Our space media business unit operates a retail store and internet store offering space-themed products and is engaged in space-related educational programs and other space-themed activities. Revenue and earnings in our retail operations are dependent upon general enthusiasm for the space exploration program, advertising and promotion, and competition.

Corporate and Other. Significant items impacting future earnings and cash flows include:

interest expense, which has decreased in the first nine months of fiscal year 2005 as compared to the first nine months of fiscal year 2004, due to the repayment of a substantial portion of our mortgage debt during fiscal year 2004 using proceeds from Boeing's early termination of their satellite preparation contract with our Astrotech business unit;

general and administrative costs, which were reduced in fiscal year 2004 due to staff reductions and the closing of our Washington D.C. corporate office, and our ability to continue to manage future overhead costs;

Edgar Filing: SPACEHAB INC \WA\ - Form S-4/A

the ultimate settlement of our claim against NASA for indemnification of our losses on the Space Shuttle *Columbia* mission and/or our tort claim; and

income taxes, with respect to which we currently only pay alternative minimum tax and minimal state income taxes; income taxes will also be impacted by our ability to realize our significant deferred tax assets, including loss carry forwards.

Table of Contents**Liquidity and Capital Resources**

As of March 31, 2005 we had cash on hand and in short-term investments of \$6.0 million, including \$0.9 million in restricted cash. Our \$5.0 million revolving credit facility had no outstanding borrowings as of March 31, 2005. Our primary source of liquidity is cash flow from operations and short-term investments. The principal uses of cash flow that affect our liquidity position include both operational expenditures and debt service payments. We are focused on increasing cash flow and on managing cash effectively through limiting cash investments in long-term assets. Our ability to maintain sufficient liquidity in the future will depend on a number of factors, including our ability to acquire future business, control our costs and manage capital expenditures, the return to flight of the space shuttle, and the continued activity in the commercial and governmental satellite launch industry.

We expect that our operating cash flows through fiscal year 2006 will be sufficient to satisfy our capital expenditures, debt maturities, interest expenses, and operating commitments. In February 2005, we entered into a new \$5.0 million revolving credit facility, replacing our previous revolving credit facility. This new revolving credit facility is secured by our accounts receivable and funds available under the facility are limited to 80% of eligible accounts receivable. Under the credit facility, we are subject to various financial and other covenants, including a minimum tangible net worth covenant, a cash flow covenant, and a secured debt coverage covenant. As of March 31, 2005, there was \$5.0 million available for borrowings under this credit facility and restricted cash of \$0.3 million. If we do not satisfy the minimum tangible net worth covenant in our credit facility, we are required to maintain a restricted cash balance. We were required to maintain a restricted cash balance of \$0.3 million and \$0.4 million as of March 31, 2005 and June 30, 2005, respectively, because we did not satisfy the minimum tangible net worth covenant in our credit facility.

Over the longer term we believe that the space shuttle return to flight and the President's Vision for Space Exploration will lead to increased activity and related cash flows from operations for our Flight Services business unit. We expect additions to our contract with Lockheed Martin for International Space Station configuration hardware and contract additions in our satellite processing business, reflecting increased activity in the space exploration and commercial satellite industries. However, there can be no assurance that we will be able to win future contracts with NASA, other national space agencies, or commercial space enterprises, or to successfully exploit other business opportunities.

Cash Flows From Operating Activities. Cash provided by (used in) operations for the nine months ended March 31, 2005 (restated) and 2004 was \$(6.2) million and \$7.3 million, respectively. The significant items affecting the differences in cash flows from operating activities for the nine months ended March 31, 2005 as compared to the nine months ended March 31, 2004 are discussed below:

Net income for the nine months ended March 31, 2005 was \$5.2 million as compared to net income for the nine months ended March 31, 2004 of \$4.4 million. Previously, net income for the nine months ended March 31, 2005 included \$8.2 million recognized as recovery of a previously reported non-recurring loss of our research double module. The \$8.2 million in proceeds is being reclassified to Investing Cash Flows out of Operating Cash Flows.

For the nine months ended March 31, 2004, we received \$17.5 million due to the Boeing termination. In addition, we recorded a non-cash charge of \$8.3 million for impairment of goodwill at our Astrotech and Government Services business units. We recorded a non-cash valuation allowance charge of \$1.8 million for our investment in Guigne. We also recorded a non-cash charge of approximately \$0.7 million due to the loan repayment.

Depreciation and amortization for the nine months ended March 31, 2005 was \$4.0 million as compared to \$4.2 million for the nine months ended March 31, 2004.

Edgar Filing: SPACEHAB INC \WA\ - Form S-4/A

Changes in assets for the nine months ended March 31, 2005 used cash from operations of \$0.6 million. This change is primarily due to an increase in accounts receivable of \$1.6 million and an increase in prepaid expenses of \$0.4 million, which were partially offset by a decrease in other assets of \$1.4 million. The increase in accounts receivable is primarily due to increased billings on the Cargo Mission contract due to contract billable milestones being delivered. The decrease in other assets is primarily due

Table of Contents

to a decrease in deferred mission costs for the Japanese Experiment Thermal Incubator Service contract due to the launch of the first mission in July, 2004 and the subsequent on-orbit operations. For the nine months ended March 31, 2004 change in assets provided cash from operations of \$0.6 million primarily from a decrease in accounts receivable.

Changes in liabilities for the nine months ended March 31, 2005 used cash from operations of \$6.6 million. This change is due primarily to the decreases in accounts payable and accrued expenses of \$1.8 million and the decrease in deferred revenue of \$4.8 million. The decrease in deferred revenue is primarily due to the first launch for the Japanese Experiment Thermal Incubator Service contract during the nine months ended March 31, 2005 and subsequent on-orbit operations. For the nine months ended March 31, 2004 changes in liabilities used cash in operations of \$13.0 million, primarily due to a decrease in accounts payable to EADS of \$4.4 million and a decrease in deferred revenue of approximately \$8.6 million primarily due to revenue recognition for STS-116 and NASA's planned dedicated research mission that was previously scheduled to follow STS-107.

Cash Flows From Investing Activities. For the nine months ended March 31, 2005 (restated) and 2004, cash flows provided by investing activities were \$13.6 million and \$6.1 million, respectively. The significant items affecting the differences in cash flows from investing activities for the nine months ended March 31, 2005 as compared to the nine months ended March 31, 2004 are discussed below:

There were property and equipment purchases of \$0.8 million for the nine months ended March 31, 2005 as compared to \$1.3 million for the nine months ended March 31, 2004.

For the nine months ended March 31, 2005, cash flows from investing activities were primarily generated from the sale of short-term investments of \$6.6 million as compared to sales of such short-term investments of \$7.4 million for the nine months ended March 31, 2004.

The increase in investing cash flows was offset by an increase in restricted cash of \$0.4 million as compared to no change for the nine months ended March 31, 2004.

For the nine months ended March 31, 2005, cash flows from investing activities included \$8.2 million received from NASA under the Research and Logistics Mission Support contract indemnification clause for the loss of our research double module.

Cash Flows From Financing Activities. For the nine months ended March 31, 2005 and 2004, cash flows used in financing activities were \$2.8 million and \$12.7 million, respectively. The significant items affecting the differences in cash flows from financing activities for the nine months ended March 31, 2005 as compared to the nine months ended March 31, 2004 are discussed below:

For the nine months ended March 31, 2005, we had net repayments of \$1.4 million in principal under the revolving credit facility as compared to no net borrowings for the nine months ended March 31, 2004.

For the nine months ended March 31, 2005, we paid \$1.4 million under various credit agreements as compared to \$13.0 million for the nine months ended March 31, 2004. This reduction is primarily due to the payment of \$11.0 million on our mortgage loan due to the Boeing termination and the final payment to Alenia Spazio S.P.A during the nine months ended March 31, 2004.

For the nine months ended March 31, 2005, we had proceeds from the issuance of common stock upon the exercise of employee stock options of \$0.1 million as compared to \$0.3 million for the nine months ended March 31, 2004.

Edgar Filing: SPACEHAB INC \WA\ - Form S-4/A

On March 25, 2003 the Board of Directors authorized us to repurchase up to \$1.0 million of our outstanding common stock at market prices. Any purchases under our stock repurchase program may be made from time to time, in the open market, through block trades or otherwise in accordance with applicable regulations of the SEC. As of March 31, 2005, we had repurchased 116,100 shares at a cost of \$117,320 under the program. We will continue to evaluate the stock repurchase program and the funds authorized for the program.

We continue to focus our efforts on improving our overall liquidity through identifying new business opportunities within the areas of our core competencies, reducing operating expenses, and limiting cash commitments for future capital investments and new asset development. On November 5, 2003, NASA notified us

Table of Contents

that we were not awarded the International Space Station Mission Integration Contract. Additionally, the Boeing team's bid for the Cargo Mission Contract with NASA, of which our Government Services business unit was a subcontractor, was not selected for contract award. As a result of the loss of these contract awards, we made significant adjustments to our staffing and cost base structure during 2004. We reduced staffing by 67 employees in the quarter ended March 31, 2004 as a result of NASA's award decisions. On October 1, 2003 we announced that we would close our corporate office in Washington, D.C. by March 31, 2004 and consolidate those operations into our headquarters in Houston, Texas. We took these actions as part of our continuing efforts to further reduce operating expenses and improve profitability. To offset a portion of our remaining lease commitment, we subleased our Washington, D.C. facility for the remaining lease period which is under lease through May 31, 2006. We have continued to restrict new capital investment and new asset development, limiting projects to those required to support current contracts and facility maintenance. Additionally, we continue to evaluate operating expenses in an effort to reduce or eliminate costs not required for us to operate effectively.

On April 28, 2005 we consummated the sale and simultaneous lease back of our Cape Canaveral, Florida payload processing facility. The sale resulted in net cash to us of approximately \$3.8 million. We leased back the facility for an initial period of five years, with an option period of an additional five years. The annual rental for the first five years of this lease is approximately \$0.45 million. On May 26, 2005 we consummated the sale and lease back of our corporate offices in Webster (Houston), Texas. The sale resulted in net cash to us of approximately \$0.9 million. We leased back 100% of the facility for an initial period of ten years, with two five-year options. We also retained the adjacent 3.0 acres parcel for future development or sale. The annual rental for the first year of this lease is approximately \$0.32 million and gradually increases through the tenth year of the lease to approximately \$0.4 million.

Our cash and short-term investments were approximately \$6.0 million, including \$0.9 million in restricted cash, as of March 31, 2005. We believe that we have sufficient liquidity, including cash and short-term investments, advances available under our revolving credit facility, and cash anticipated or expected to be generated from operations to fund ongoing operations beyond the remainder of this fiscal year. We also expect to utilize existing cash and cash anticipated from future operations to support strategies for new business initiatives and to reduce long-term debt.

Our contractual obligations as of March 31, 2005 are as follows (in thousands):

	At March 31, 2005	Remaining in Fiscal Year 2005	Fiscal Year 2006	Fiscal Year 2007	Fiscal Year 2008	Fiscal Year 2009	Thereafter
Contractual Obligations							
Long-term Debt	\$ 63,250	\$	\$	\$	\$ 63,250	\$	\$
Mortgage Loan Payable	4,190	497	2,057	1,636			
V.J.F. Russian Consultant Agreement	210	45	165				
V.J.F. Russian Subcontract	1,003	603	400				
Operating leases ⁽¹⁾⁽²⁾	21,826	960	4,918	4,507	4,372	4,217	2,852
Total Contractual Cash Obligations⁽³⁾	\$ 90,479	\$ 2,105	\$ 7,540	\$ 6,143	\$ 67,622	\$ 4,217	\$ 2,852

- (1) For the remainder of fiscal year 2005, we expect to receive net payments of \$0.2 million for subleases. For fiscal years 2006, 2007, and 2008, we expect to receive net payments of approximately \$0.7 million, \$0.5 million, and \$0.3 million, respectively, for subleases. Additionally, we exercised a four year option on our leases with EADS Space Transportation.
- (2) Does not include amounts for sale leaseback of our Payload Processing Facility on April 28, 2005 or our corporate administrative offices on May 26, 2005.
- (3) Does not include commitment to Dayna Justiz for compensation that can be earned as a result of the agreement dated June 19, 2000. The agreement states that Dayna Justiz can earn up to \$375,000 as additional compensation if she meets certain financial goals in the management of The Space Store. The yearly amount is equal to five percent of The Space Store's net after-tax operating income during

Edgar Filing: SPACEHAB INC \WA\ - Form S-4/A

each fiscal year until such time an aggregate amount of \$375,000 has been earned. At this time, we have recorded no liability for this obligation due to the uncertainty of the obligation being met.

Table of Contents**Critical Accounting Policies**

Revenue Recognition. Our business units' revenue is derived primarily from long-term contracts with the U.S. Government and commercial customers. Revenues under these contracts are recognized using the methods described below. Estimating future costs and, therefore, revenues and profits, is a process requiring a high degree of management judgment. See Risk Factors Risks Related to Our Business Our financial results could be affected if the estimates that we use in accounting for contracts are incorrect and need to be changed. We base our estimate on historical experience and on various assumptions that are believed to be reasonable under the circumstances including the negotiation of an equitable adjustment on the Research and Logistics Mission Support contract which was added to the contract as a pricing amendment due to the delay in the return to flight. Costs to complete include, when appropriate, material, labor, subcontracting costs, lease costs, commissions, insurance and depreciation. Our business units' personnel perform periodic contract status and performance reviews. In the event of a change in total estimated contract cost or profit, the cumulative effect of such change is recorded in the period that the change in estimate occurs.

A Summary of Revenue Recognition Methods Follows:

Business Unit	Services/Products		Method of Revenue
	Provided	Contract Type	Recognition
Flight Services	Commercial Space Habitat Modules, Integration & Operations Support Services	Firm Fixed Price	Percentage-of-completion based on costs incurred
Government Services	Configuration Management, Engineering Services	Cost Reimbursable Award/Fixed Fee	Reimbursable costs incurred plus award/fixed fee
Astrotech	Payload Processing Facilities	Firm Fixed Price - Mission Specific Firm Fixed Price - Guaranteed Number of Missions	Ratably, over the occupancy period of a satellite within the facility from arrival through launch For multi-year contract payments recognized ratably over the contract period
Space Media	Space-Themed Commercial Products/Activities	Retail	Internet and retail sales recognized when goods are shipped

Goodwill. In assessing the recoverability of goodwill and other intangibles, we must make assumptions regarding the estimated future cash flows and other factors to determine the fair value of the respective assets. If and when these circumstances or their related assumptions change in the future, we may be required to record impairment charges for these assets. We adopted SFAS No. 142, Goodwill and Other Intangible Assets, on July 1, 2002, under which we ceased to amortize goodwill and instead analyze goodwill at least annually for impairment issues. The remaining goodwill on the balance sheet as of December 2003 was tested for impairment and was written off in fiscal year 2004.

Long-Lived Assets. In assessing the recoverability of long-lived assets, fixed assets, assets under construction and intangible assets, we evaluate the recoverability of those assets in accordance with the provisions of the Statement of Financial Accounting Standards No. 144, Accounting for the Impairment or

Table of Contents

Disposal of Long-Lived Assets. This Statement requires that certain of our long-lived fixed assets be reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. Recoverability of assets to be held and used is measured by a comparison of the carrying amount of an asset to future net cash flows expected to be generated by the asset. If such assets are considered to be impaired, the impairment to be recognized is measured by the amount by which the carrying amount of the asset exceeds the fair value of the asset. Assets to be disposed of are reported at the lower of the carrying amount or fair value less costs to sell.

Revenue

Our revenue for the nine months ended March 31, 2005 and 2004 was generated primarily from the Research and Logistics Mission Support contract, the Lockheed Martin letter contract, and contracts with related commercial customers in the Flight Services business unit; the remaining contracts under the Flight Crew Systems Development contract and the Program Integration and Control contract in our Government Services business unit; and our contracts with Lockheed Martin and other commercial satellite providers in our Astrotech business unit. Revenue for our Space Media business unit was immaterial for the nine months ended March 31, 2005 and 2004. During the period, there were launch delays that affected planned revenue that is expected to materialize in the upcoming months in our Astrotech business unit.

Our Flight Services business unit supported NASA's return-to-flight mission in July 2005 and is continuing operations in preparation for shuttle missions, including STS-121, 116, and 118 (in order of their anticipated flight sequence). We contracted directly with NASA's prime International Space Station contractor, Boeing, for the July 2005 mission during which a cargo carrier provided by us was deployed and permanently mounted to the International Space Station. Our Flight Services business unit is preparing another cargo carriers for shuttle mission STS-118, the External Stowage Platform 3, that will be deployed and permanently mounted to the International Space Station. For STS-121, we are scheduled to provide our non-deployable integrated cargo carrier to NASA under our Cargo Mission Contract subcontract with Lockheed Martin for transport of several critical International Space Station orbital replacement unit spares. For both STS-116 and 118, missions also under the Cargo Mission contract, we are scheduled to provide our pressurized single module and an unpressurized non-deployable integrated cargo carrier for transport of critical cargo and orbital replacement units to and from the International Space Station. We have successfully completed negotiations with Boeing and Lockheed Martin for the respective contract equitable adjustments required to continue uninterrupted support to ongoing STS-121, 116 and 118 mission preparation activities during any shuttle down periods. Support for missions STS-121, 116 and 118 is continuing under a subcontract agreement with Lockheed Martin, effective February 1, 2004. We are currently providing these services under a letter contract, have completed final contract negotiations with Lockheed Martin, and are awaiting issuance of this new contract. Additionally, after approximately April 15, 2004, our Flight Services business unit no longer is subcontracting its module mission integration, operations and sustaining engineering technical support to Boeing. Most module mission tasks previously performed by Boeing personnel are now being performed by our Flight Services business unit personnel, and selected NASA cargo integration tasks on our module missions are now being performed by Lockheed Martin as a part of their Cargo Mission Contract with NASA. This decision enables our Flight Services business unit to continue to provide services to NASA and is consistent with the direction of the International Space Station program office.

In January 2004 we initiated activity under the Japanese Experiment Thermal Incubator Service contract with the Mitsubishi Corporation, representing the Japanese Aerospace Exploration Agency, that was entered into in 2000 and originally scheduled to fly aboard our research double module. Subsequent to the suspension of the space shuttle flights and destruction of our research double module, we contracted for construction of certain space research equipment, research space aboard the International Space Station and up to three Russian *Progress* cargo missions with V.J.F. Russian Consulting, representing RSC Energia, a major Russian aerospace manufacturer and mission operator. The first experiment was successfully launched on the Russian *Progress* spacecraft on August 11, 2004.

Table of Contents

During the three and nine months ended March 31, 2005, deferred revenue decreased by \$0.2 million and \$4.8 million, respectively, as we recognized revenue on contracts where milestone payments had been received in prior periods. We expect further reduction of deferred revenue through the next twelve months which will result in revenue recognition on contracts for which the related cash was received in a prior period.

Costs of Revenue

We have several types of costs of revenue in our business segments. Costs of revenue for our Flight Services business unit include integration and operations expenses associated with the performance of two types of efforts, sustaining engineering in support of all missions under a contract and mission specific support. Costs associated with the performance of the contracts using the percentage-of-completion method of revenue recognition are expensed as incurred. Costs associated with the cost-reimbursable award and fixed-fee contracts are expensed as incurred by our Government Services business unit. Other costs of revenue include depreciation expense and costs associated with the Astrotech payload processing facilities. Flight related insurance covering transportation of our modules from our payload processing facility to the space shuttle, in-flight insurance, and third-party liability insurance are also included in costs of revenue and are recorded as incurred. Selling, general and administrative and interest and other expenses are recognized when incurred.

Non Recurring Charge

On February 1, 2003 our research double module was lost in the *Columbia* tragedy. The net book value of the research double module was \$67.9 million, which, net of insurance proceeds of \$17.7 million, was recognized as a loss in the third quarter of fiscal year 2003. The \$8.0 million plus interest of \$0.2 million paid by NASA as indemnification for our loss of the research double module is recognized as a recovery of previously recognized loss in the quarter ended September 30, 2004. At this time, we do not plan to replace the research double module. Our Flight Services business unit has two additional modules and other flight assets available to support current NASA requirements. We believe that these modules and assets can also be used to support future NASA requirements during the remaining life of the space shuttle fleet. Following the launch of the Space Shuttle *Discovery* in July 2005, NASA announced that the space shuttle fleet will be grounded for an indefinite period of time until loss of foam from the shuttle's external fuel tank can be remedied.

Results of Operations for the Three and Nine Month Periods Ended March 31, 2005 and 2004***Three Months Ended March 31, 2005 as Compared to the Three Months Ended March 31, 2004***

Revenue. Revenue decreased approximately 4% to \$14.3 million as compared to \$14.8 million for the three months ended March 31, 2005 and 2004, respectively (in millions).

	Three Months Ended		Dollar	Percent
	March 31,			
	2005	2004	Change	Change
Flight Services	\$ 10.0	\$ 10.3	\$ (0.3)	(3)%

Edgar Filing: SPACEHAB INC \WA\ - Form S-4/A

Astrotech Space Operations	2.5	2.5		
Government Services	1.6	1.8	(0.2)	(11)%
Space Media	0.2	0.2	0.0	
	<u> </u>	<u> </u>	<u> </u>	<u> </u>
	\$ 14.3	\$ 14.8	\$ (0.5)	(4)%
	<u> </u>	<u> </u>	<u> </u>	<u> </u>

Revenue from our Flight Services business unit has been adversely affected by the temporary grounding of the shuttle fleet due to the *Columbia* tragedy in February 2003, partially offset by revenue from the Lockheed Martin letter contract, and other contract revenue. The following summarizes the significant changes for the three months ended March 31, 2005 as compared to the comparable period in fiscal year 2004:

a decrease in the Research and Logistics Mission Support contract revenue of \$4.2 million in the three months ended March 31, 2005 compared to the three months ended March 31, 2004 due to the termination of the Research and Logistics Mission Support contract in January 2004;

Table of Contents

an increase in Lockheed Martin contract revenue of \$4.4 million in the three months ended March 31, 2005 compared to the three months ended March 31, 2004 due to the startup of the contract in February 2004;

a decrease in revenue from the Japanese Experiment Thermal Incubator Service contract of \$1.2 million due to the timing of the mission operations;

an increase in revenue attributable to our Concept Exploration and Refinement contract with NASA of \$0.6 million that was started in the first quarter of fiscal year 2005; and

other contract revenue increase of \$0.1 million.

Revenue from our Astrotech business unit was generally unchanged in the quarter ending March 31, 2005 as compared to the comparable quarter in 2004.

The decrease in revenue at our Government Services business unit is primarily due to the closeout of the Stowage, Engineering and Decal contract and Configuration Management contract in December 2004. The following summarizes the significant changes for the three months ended March 31, 2005 as compared to the comparable period in fiscal year 2004:

a revenue decrease of \$0.4 million due to the closeout of the Stowage, Engineering and Decal contract and Configuration Management contract in December 2004; and

other contract revenue increase of \$0.2 million.

Costs of Revenue. Costs of revenue for the three months ended March 31, 2005 increased by 13% to approximately \$11.1 million, as compared to \$9.8 million for the prior fiscal year's comparable quarter (in millions):

	Three Months Ended March 31,		Dollar Change	Percent Change
	2005	2004		
Flight Services	\$ 7.9	\$ 6.2	\$ 1.7	27%
Astrotech Space Operations	2.0	2.0		0%
Government Services	1.1	1.5	0.4	(27)%
Space Media	0.1	0.1		
	<u>\$ 11.1</u>	<u>\$ 9.8</u>	<u>\$ 1.3</u>	<u>13%</u>

Costs of revenue from our Flight Services business unit have primarily increased due to costs of revenue attributable to our performance under the Lockheed Martin letter contract, the termination of Boeing as a subcontractor for module services, and other contract costs of revenue, partially offset by reduced costs as a result of the temporary grounding of the shuttle fleet due to the *Columbia* tragedy in February 2003. The

Edgar Filing: SPACEHAB INC \WA\ - Form S-4/A

following summarizes the significant changes for our Flight Services business unit for the three months ended March 31, 2005 as compared to the comparable period in fiscal year 2004:

a decrease in costs of revenue for shuttle related mission work performed by Boeing of \$0.9 million due to subcontract termination;

an increase in costs of revenue for shuttle related mission work performed by EADS of \$1.4 million due to the scheduled launch of the STS-114 shuttle mission in July 2005;

an increase in costs of revenue for shuttle related missions for in-house engineering labor of \$1.2 million; and

other costs of revenue decreases of \$0.4 million, offset by Concept Exploration and Refinement contract costs of \$0.3 million.

Table of Contents

Cost of revenue from our Astrotech business unit were generally unchanged in the quarter ending March 31, 2005 as compared to the comparable quarter in 2004.

The decrease in costs of revenue at our Government Services business unit is primarily due to the closeout of the Stowage, Engineering and Decal contract in December 2004. The following summarizes the significant changes for our Government Services business unit for the three months ended March 31, 2005 as compared to the comparable period in fiscal year 2004:

costs of revenue decrease of \$0.3 million due to the closeout of the Stowage, Engineering and Decal contract in December 2004; and

other costs of revenue decreases of \$0.1 million due to less contract activities in the third quarter of 2005 as compared to third quarter of fiscal year 2004.

Operating Expenses. Operating expenses decreased to \$2.3 million for the three months ended March 31, 2005 as compared to approximately \$2.6 million for the three months ended March 31, 2004. Operating expenses are lower in the quarter ended March 31, 2005 compared to the last fiscal year's comparable quarter due to our ongoing cost reduction efforts and staffing and reductions in selling, general and administrative expenses. Research and development expenses were immaterial for the three months ended March 31, 2005 and 2004, although we expect these costs to increase in future periods. In the three months ended March 31, 2005, we recognized legal expenses of \$0.3 million relating to our claims against NASA for the loss of the research double module and response to Lloyd's complaint regarding its payment of insurance proceeds on the accident.

Interest Expense. Interest expense was approximately \$1.4 million for the three months ended March 31, 2005 as compared to approximately \$2.2 million for the three months ended March 31, 2004. The decrease in interest expense is primarily due to the loss of hedge accounting in 2004 as a result of the termination of our interest rate swap for our mortgage loan payable, resulting in expense of \$0.5 million on a portion of the interest rate swap. Additionally, there was an acceleration of \$0.2 million of debt placement costs in 2004 associated with the repayment of the mortgage loan and decreasing interest expense on the amended mortgage loan.

Interest and Other Income. Interest and other income was immaterial for the three months ended March 31, 2005 and March 31, 2004. Interest income is earned on our short-term investments.

Income Taxes. Based on our projected effective tax rate for fiscal year 2005, we recorded minimal tax expense for the three months ended March 31, 2005 as compared to a minimal tax expense for the three months ended March 31, 2004.

Net Income (Loss). Net loss for the three months ended March 31, 2005 was approximately \$0.5 million or \$0.04 per share basic and diluted on 12,626,130 shares as compared to net income of approximately \$0.3 million or \$0.02 per share basic and \$0.02 per share diluted on 12,476,342 and 14,264,818 shares, respectively, for the three months ended March 31, 2004.

Nine Months Ended March 31, 2005 as Compared to the Nine Months Ended March 31, 2004.

Edgar Filing: SPACEHAB INC \WA\ - Form S-4/A

Revenue. Revenue decreased approximately 39% to \$40.4 million for the nine months ended March 31, 2005 as compared to \$66.5 million for the nine months ended March 31, 2004 (in millions):

	Nine Months Ended March 31,		Dollar Change	Percent Change
	2005	2004		
Flight Services	\$ 28.4	\$ 32.6	\$ (4.2)	(13)%
Astrotech Space Operations	6.7	24.7	(18.0)	(73)%
Government Services	4.7	8.6	(3.9)	(45)%
Space Media	0.6	0.6		
	<u>\$ 40.4</u>	<u>\$ 66.5</u>	<u>\$ (26.1)</u>	<u>(39)%</u>

Table of Contents

Revenue from our Flight Services business unit has been adversely affected by the temporary grounding of the shuttle fleet due to the *Columbia* tragedy in February 2003. Even though the shuttle fleet was grounded for both the nine months ended March 31, 2005 and nine months ended March 31, 2004, there is a significant difference in revenue due to how NASA proceeded with the grounding of the shuttle fleet. For the nine months ended March 31, 2004, we were operating as if the shuttle would return to flight in the near term which resulted in higher revenue due to the products and services that were being required to be delivered to NASA in preparation for the return to flight. For the period ended March 31, 2005, we were required to deliver fewer products and services to NASA due to a more defined return to flight schedule. The following summarizes the significant changes for our Flight Services business unit for the nine months ended March 31, 2005 as compared to the comparable period in fiscal year 2004:

a decrease in the Research and Logistics Mission Support contract revenue of \$23.3 million in the nine months ended March 31, 2005 compared to the nine months ended March 31, 2004 due to the termination of the Research and Logistics Mission Support contract in January 2004;

an increase in revenue from the Lockheed Martin contract, which replaced the Research and Logistics Mission Support contract in February 2004, of \$16.0 million in the nine months ended March 31, 2004;

an increase in the External Stowage Platform 2 contract revenue of \$3.6 million in the nine months ended March 31, 2005 compared to the nine months ended March 31, 2004 due to the anticipated launch in July 2005;

an increase in revenue from the Japanese Experiment Thermal Incubator Service contract of \$0.8 million that was started in the third quarter of fiscal year 2004;

an increase in revenue from the Concept Exploration and Refinement contract of \$1.0 million that was started in the first quarter of fiscal year 2005; and

other contract revenue decrease of \$2.3 million, mainly due to the cancellation of the research double module's planned second mission under the Research and Logistics Mission Support contract during the nine months ended March 31, 2004.

The decrease in revenue at our Astrotech business unit is primarily due to Boeing's termination in October 2003 of its contractually fixed guarantee payments, which was partially offset by the one time termination payment in the amount of \$17.5 million that we received from Boeing in the nine months ended March 31, 2004 and by the additional services that we supply to Boeing. During the nine months ended March 31, 2005, our Astrotech business unit underwent scheduled downtime between launches and recognized contractually guaranteed revenues of \$2.5 million and \$0.6 million from missions that began in the fourth quarter of fiscal year 2004 and were completed in the first quarter of fiscal year 2005, contract revenue from five missions that began in the second and third quarters of fiscal year 2005 of \$2.9 million and other revenue of \$0.7 million.

The decrease in revenue at our Government Services business unit is primarily due to the closeout of the Stowage, Engineering and Decal contract and the Configuration Management contract in December 2004 partially offset by the Program Integration & Control contract which started in January 2004. The following summarizes the significant changes for our Government Services business unit for the nine months ended March 31, 2005 as compared to the comparable period in fiscal year 2004:

a revenue decrease of \$6.3 million due to the closeout of the Stowage, Engineering and Decal contract and the Configuration Management contract in December 2004;

other contract revenue decrease of \$0.3 million due to less contract activity; and

a revenue increase of \$2.7 million due to the Program Integration & Control contract.

Table of Contents

Costs of Revenue. Costs of revenue for the nine months ended March 31, 2005 decreased by 10% to approximately \$32.6 million, as compared to \$36.2 million for the nine months ended March 31, 2004 (in millions):

	Nine Months Ended March 31,		Dollar	Percent
	2005	2004	Change	Change
Flight Services	22.8	23.0	(0.2)	(1)%
Astrotech	5.9	5.7	0.2	4%
Government Services	3.6	7.2	(3.6)	50%
Space Media	0.3	0.3		
	<u>32.6</u>	<u>36.2</u>	<u>(3.6)</u>	<u>10%</u>

Costs of revenue from the Flight Services business unit has been affected by the temporary grounding of the shuttle fleet due to the *Columbia* tragedy in February 2003, partially offset by costs of revenue from the Lockheed Martin letter contract, the termination of Boeing as a subcontractor for module services, and other contract costs of revenue. The following summarizes the significant changes for our Flight Services business unit for the nine months ended March 31, 2005 as compared to the comparable period in fiscal year 2004:

a decrease in the Research and Logistics Mission Support contract costs of revenue of \$13.0 million from March 31, 2004 to March 31, 2005 due to the Research and Logistics Mission Support contract closeout;

costs of revenue from Lockheed Martin letter contract of \$9.7 million that started in the third quarter of fiscal year 2004;

an increase in the External Stowage Platform 2 costs of revenue of \$3.1 million due to the expected launch in July 2005;

costs of revenue of \$0.2 million from Japanese Experiment Thermal Incubator Service that was started in the third quarter of fiscal year 2004;

costs of revenue of \$0.8 million from the Concept Exploration and Refinement contract that was started in the first quarter of fiscal year 2005; and

other costs of revenue decreases of \$1.0 million, primarily resulting from the termination of Boeing as a subcontractor for module services, offset by in-house engineering labor and related costs.

Our Astrotech business unit's increase in costs of revenue is due primarily to increased mission support costs and increase in the costs of operations at the satellite processing facilities, including increased utility costs.

The decrease in costs of revenue at our Government Services business unit is primarily due to the closeout of the Stowage, Engineering and Decal contract and the Configuration Management contract in December 2004 partially offset by the Program Integration & Control contract.

Edgar Filing: SPACEHAB INC \WA\ - Form S-4/A

The following summarizes the significant changes for our Government Services business unit for the nine months ended March 31, 2005 as compared to the comparable period in fiscal year 2004:

a cost of revenue decrease of \$3.8 million due to the closeout of the Stowage, Engineering and Decal contract in December 2004;

a cost of revenue decrease of \$2.3 million due to the closeout of the Configuration Management contract in December 2004;

a cost of revenue increase of \$3.1 million due to the startup of the Program Integration & Control contract in January 2004; and

other costs of revenue decreases of \$0.6 million due to less contract activity.

Table of Contents

Operating Expenses. Operating expenses, other than the \$8.2 million recovery of a non-recurring charge for the loss of the research double module that was recorded for the period ended September 30, 2004, and the goodwill and Guignè impairments totaling \$10.1 million that were recorded for the period ended March 31, 2004, decreased to \$6.6 million for the nine months ended March 31, 2005 as compared to approximately \$8.9 million for the nine months ended March 31, 2004. The primary factors causing this decrease are our on-going reductions in staff and facilities. Research and development expenses were immaterial for the nine months ended March 31, 2005 and 2004, although we expect these costs to increase in future periods. For the nine months ended March 31, 2005, our expenses for bid and proposal efforts were less than \$0.1 million. In the nine months ended March 31, 2004, we incurred bid and proposal costs of \$0.2 million primarily relating to the Mission Integration Contract proposal. During the nine months ended March 31, 2005, we recognized legal expenses of \$0.8 million relating to our claims against NASA for loss of our research double module and response to Lloyd's complaint regarding its payment of insurance proceeds on the accident.

Interest Expense. Interest expense was approximately \$4.3 million for the nine months ended March 31, 2005 as compared to approximately \$6.8 million for the nine months ended March 31, 2004. The decrease in interest expense is primarily due to the loss of hedge accounting on a portion of the interest rate swap for the mortgage loan in 2004 resulting in the expensing of \$1.3 million of unrealized losses previously in other comprehensive loss upon repayment of \$9.5 million of the mortgage loan, as well as the acceleration of \$0.7 million of debt placement costs associated with the repayment for the nine months ended March 31, 2004. Due to the \$9.5 million payment on the mortgage loan and the subsequent lower interest rate (5.5%), the interest expense on our mortgage loan was \$0.8 million less in the nine months ended March 31, 2005 compared to the nine months ended March 31, 2004.

Interest and Other Income. Interest and other income was immaterial for the nine months ended March 31, 2005 and March 31, 2004. Interest income is earned on our short-term investments.

Income Taxes. Based on our projected effective tax rate for fiscal year 2005, we recorded a tax expense of \$0.2 million for the nine months ended March 31, 2005 as compared to a tax expense of \$0.3 million during the nine months ended March 31, 2004.

Net Income. Net income for the nine months ended March 31, 2005 was approximately \$5.2 million or \$0.41 per share basic and \$0.36 per share diluted on 12,603,240 and 14,203,597 shares, respectively, as compared to net income of approximately \$4.4 million or \$0.35 per share basic and \$0.31 per share diluted on 12,415,997 and 14,039,798 shares, respectively, for the nine months ended March 31, 2004.

Results of Operations for the Years Ended June 30, 2004, 2003 and 2002

Overview. In this section we discuss our results of operations, both on a consolidated basis and, where appropriate, by business unit for our fiscal years ended June 30, 2004, 2003, and 2002. Where we report earnings or loss on a per share basis, we have done so on a diluted earnings per share basis. The weighted average number of common shares applicable to diluted earnings for 2004, 2003, and 2002 were 14,141,949, and 12,285,467, and 11,884,309, respectively.

We had net income (loss) of \$2,075,000 or \$0.15 per diluted share on revenues of \$77,606,000 for our 2004 fiscal year compared to (\$81,775,000) or (\$6.66) per diluted share on revenues of \$94,963,000 for 2003 and (\$2,367,000) or (\$0.20) per diluted share on revenues of \$102,773,000 for 2002. For our 2002 fiscal year, net earnings and earnings per share included \$0.09 per share of goodwill amortization expense. Amortization of goodwill ceased January 1, 2002 as a result of the adoption of Statement of Financial Accounting Standards No. 142.

Non-GAAP Financial Measures. We use income from operations before charges as one measure of financial performance. Income from operations before charges is a non-GAAP financial measure and consists of operating

Table of Contents

income before unusual and infrequent events such as: goodwill impairments, asset impairments, investment impairments and the loss of the research double module. Income from operations before charges also does not include interest expense or income taxes, each of which is evaluated on a consolidated basis. Because we do not allocate interest expense and income taxes by unit, we believe that income from operations is a useful measure of our units' operating performance for investors. Income from operations before charges should not be considered an alternative to, or more meaningful than, net income or cash flows from operations as determined in accordance with GAAP. The *Other* column in the presentation below is our corporate selling, general and administrative expenses that are incurred for our overall operations that are not allocable to any specific business unit.

The following tables provide summary financial data regarding our consolidated and segmented results of operations for our 2004, 2003, and 2002 fiscal years, respectively (in millions):

Fiscal Year Ended June 30, 2004

	Government					Total
	Astrotech		Services	Space Media		
	Flight Services Business Unit	Business Unit	Business Unit	Business Unit	Other	
Income (loss) from operations before charges	\$ 8.9	\$ 20.0	\$ 0.3	\$ (0.1)	\$ (8.4)	\$ 20.7
Goodwill impairment		(2.5)	(5.7)			(8.2)
Investment impairment charge					(1.8)	(1.8)
Operating income (loss)	8.9	17.5	(5.4)	(0.1)	(10.2)	10.7
Other income/expense					0.1	0.1
Interest expense					(8.2)	(8.2)
Pre-tax income (loss)	8.9	17.5	(5.4)	(0.1)	(18.3)	2.6
Income tax expense					(0.5)	(0.5)
Net income (loss)	\$ 8.9	\$ 17.5	\$ (5.4)	\$ (0.1)	\$ (18.8)	\$ 2.1

Fiscal Year Ended June 30, 2003

	Government					Total
	Astrotech		Services	Space Media		
	Flight Services Business Unit	Business Unit	Business Unit	Business Unit	Other	
Income (loss) from operations before charges	\$ 6.8	\$ 4.5	\$ 1.9	\$ (0.3)	\$ (10.0)	\$ 2.9
Loss on <i>Columbia</i> accident	(50.3)					(50.3)
Goodwill impairment			(11.9)			(11.9)
Asset impairment charge	(7.9)				(8.2)	(16.1)

Edgar Filing: SPACEHAB INC \WA\ - Form S-4/A

Operating income (loss)	(51.4)	4.5	(10.0)	(0.3)	(18.2)	(75.4)
Interest expense					(7.2)	(7.2)
	<u> </u>	<u> </u>	<u> </u>	<u> </u>	<u> </u>	<u> </u>
Pre-tax income (loss)	(51.4)	4.5	(10.0)	(0.3)	(25.4)	(82.6)
Income tax expense					0.9	0.9
	<u> </u>	<u> </u>	<u> </u>	<u> </u>	<u> </u>	<u> </u>
Net income (loss)	\$ (51.4)	\$ 4.5	\$ (10.0)	\$ (0.3)	\$ (24.5)	\$ (81.7)

Table of Contents**Fiscal Year Ended June 30, 2002**

	Government					
		Astrotech	Services	Space Media		
	Flight Services Business Unit	Business Unit	Business Unit	Business Unit	Other	Total
Operating income (loss)	\$ 12.9	\$ 3.8	\$ 2.0	\$ (1.6)	\$ (16.0)	\$ 1.1
Other income					1.2	1.2
Interest expense					(6.7)	(6.7)
Pre-tax income (loss)	12.9	3.8	2.0	(1.6)	(21.5)	(4.4)
Income tax expense					2.1	2.1
Net income (loss)	\$ 12.9	\$ 3.8	\$ 2.0	\$ (1.6)	\$ (19.4)	\$ (2.3)

Operating Income (Loss). Operating income (loss) was \$10.7 million in fiscal year 2004, compared to (\$75.4) million and \$1.1 million for fiscal years 2003 and 2002, respectively. The following summarizes the activity in each of our operating segments:

SPACEHAB Flight Services

Operating income (loss) for our flights services business unit was \$8.9 million for fiscal year 2004, compared to (\$51.4) million and \$12.9 million for fiscal years 2003 and 2002, respectively. Operating income for 2004 included general and administrative expense of \$0.7 million and depreciation and amortization expense of \$2.8 million as compared to general and administrative expenses of \$0.1 million and \$0.1 million and depreciation and amortization expense of \$5.0 million and \$8.6 million for fiscal years 2003 and 2002, respectively. Please see Results of Operations for the Years Ended June 30, 2004, 2003 and 2002 Other for a consolidated discussion of general and administrative expense and depreciation and amortization expense.

Flight Service Business Unit Results of Operations before Charges for the Fiscal Year Ended June 30, 2004 as Compared to the Fiscal Year Ended June 30, 2003

The Flight Services business unit's operating income before charges increased by \$2.1 million from fiscal year 2003 to fiscal year 2004. The following summarizes significant changes for our fiscal year ended June 30, 2004 as compared to our fiscal year ended June 30, 2003:

Revenue decreases of \$8.4 million, consisting of the following:

Research and Logistics Mission Support contract revenue decreased by \$14.4 million as it was terminated in January 2004;

Edgar Filing: SPACEHAB INC \WA\ - Form S-4/A

New revenue from the Lockheed Martin letter contract of \$7.8 million that replaced the Research and Logistics Mission Support contract;

The External Stowage Platform 2 contract revenue decreased by \$4.5 million;

The various other contract revenue decreased \$0.1 million; and

Recognized revenue from the Japanese Experiment Thermal Incubator Service of \$2.8 million.

Cost of Revenue decrease of \$10.5 million, consisting of the following:

Termination of Boeing's subcontract decreased cost of revenue by \$7.0 million;

Reduced EADS subcontract costs in 2004 of \$3.6 million due to no missions in 2004;

Decrease in asset depreciation in 2004 of \$1.8 million due to the loss of the research double module in fiscal year 2003;

Decrease in other cost of revenue of \$0.3 million;

Increase in internal labor costs of \$1.6 million due to bringing the integrations and operations of our modules in-house; and

Increase in selling, general and administrative expenses of \$0.6 million.

Table of Contents

All space shuttle missions were suspended following the space shuttle *Columbia* accident in February 2003 until the July 2005 shuttle mission, affecting revenues and operating income of our Flight Services business unit for fiscal year 2004. Pending the return to flight of the space shuttle program, we operated under equitable adjustments and subsequently in preparation for the return to flight under the contractual arrangements in place prior to the accident. The equitable adjustment provided compensation for space flight assets committed for future contracted missions and for personnel and services in place to maintain those assets and support the return-to-flight activities.

Our Flight Services business unit supported NASA's return-to-flight mission in July 2005 and is continuing its operations in preparation for shuttle missions STS-121, 116, and 118 (in order of their anticipated flight sequence). Our Flight Services business unit prepared an integrated cargo carrier for the July 2005 shuttle mission, the External Stowage Platform 2, that was deployed and permanently mounted to the International Space Station. We contracted directly with NASA's prime International Space Station contractor, Boeing, for the space shuttle's July 2005 mission. For the space shuttle STS-121 mission, we are scheduled to provide our non-deployable integrated cargo carrier to NASA for transport of several critical International Space Station orbital replacement unit spares. For both shuttle missions STS-116 and 118, missions previously placed under the Research and Logistics Mission Support contract, we are scheduled to provide our pressurized single module and our unpressurized integrated cargo carrier for transport of critical cargo and orbital replacement units to and from the International Space Station. We have completed negotiations with Boeing and NASA for the respective contract equitable adjustments required to continue uninterrupted support to ongoing mission preparation activities during any shuttle down periods. As previously described, the Research and Logistics Mission Support contract expired January 31, 2004 and support for shuttle missions STS-121, 116 and 118 is continuing under a subcontract agreement to Lockheed Martin, effective February 1, 2004. We are currently providing these services under letter agreement and we are in contract negotiations with Lockheed Martin for a new contract. Additionally, after April 15, 2004 our Flight Services business unit is no longer subcontracting its module mission integration, operations, and sustaining engineering technical support to Boeing. Most module mission tasks previously performed by Boeing personnel will now be performed by our Flight Services business unit personnel and selected NASA cargo integration tasks on our module missions will now be performed by Lockheed Martin as a part of the Cargo Mission contract with NASA. This action enables our Flight Services business unit to continue providing services to NASA and is consistent with the direction of the International Space Station program office.

In January 2004, we initiated activity under the Japanese Experiment Thermal Incubator Service contract with Mitsubishi Corporation, representing the Japanese Aeronautics Exploration Agency, that was entered into in 2000 and originally scheduled to fly aboard our research double module. Subsequent to the suspension of the space shuttle flights and destruction of our research double module, we contracted for construction of certain space research equipment, for research space aboard the International Space Station and up to three Russian *Progress* cargo missions with V.J.F. Russian Consulting, representing RSC Energia, a major Russian aerospace manufacturer and mission operator.

Flight Services Business Unit Operating Results before Charges for Fiscal Year Ended June 30, 2003 as Compared to the Fiscal Year Ended June 30, 2002

Our Flight Services business unit's operating income before charges decreased by \$6.1 million from fiscal year 2002 to fiscal year 2003. The following summarizes significant changes for our fiscal year ended June 30, 2003 as compared to our fiscal year ended June 30, 2002:

Revenue decreases of \$4.7 million consisted of the following:

Research and Logistics Mission Support contract revenue decreased by \$8.8 million due to the completion of STS-107 and the grounding of the space shuttle fleet due to the *Columbia* accident; and

Edgar Filing: SPACEHAB INC \WA\ - Form S-4/A

The External Storage Platform 2 revenue increased by \$4.1 million due to the increased work on the project during fiscal year 2003 as compared to fiscal year 2002.

Table of Contents

Cost of Revenue increases of \$2.8 million consisted of the following:

The External Storage Platform 2 cost of revenue increased by \$3.6 million due to the increased work on the project during fiscal year 2003 as compared to fiscal year 2002;

Research and Logistics Mission Support contract cost of revenue decreased by \$3.3 million primarily due to the closeout of the *Columbia* mission;

Increase of \$1.5 million in integrated cargo carrier lease costs in fiscal year 2003 as compared to fiscal year 2002 primarily due to a full year of lease costs related to our vertical integrated cargo carrier in fiscal year 2003; and

Increase in indirect costs of \$1.0 million due to recording certain costs that had been previously recorded as corporate costs as our Flight Services business unit's indirect costs, such as, depreciation, insurance, and benefits.

Our fiscal year 2003 operating income included a charge of approximately \$50.3 million, net of insurance proceeds of \$17.7 million on our loss of the research double module in the *Columbia* tragedy. Also, due to the uncertainties in the human space flight programs following the *Columbia* accident, we decided to no longer fund certain work in process in development of future flight assets and recorded an impairment charge of \$7.9 million. During fiscal year 2003, we contracted for the research double module on shuttle mission STS-107, the integrated cargo carrier on shuttle mission STS-114, and the logistics single module and integrated cargo carrier on shuttle missions STS-116 and 118.

We participated in one space shuttle mission in fiscal year 2002 that included the integrated cargo carrier. In fiscal year 2003 we participated in one space shuttle mission that included our research double module. There were no space shuttle missions in fiscal year 2004.

Astrotech Space Operations

Operating income for our Astrotech business unit was \$17.5 million for fiscal year 2004, compared to \$4.5 million and \$3.8 million for fiscal years 2003 and 2002, respectively. Operating income for 2004 included selling, general and administrative expense of \$0.4 million and depreciation and amortization expense of \$2.0 million as compared to selling, general and administrative expense of \$0.5 million and \$0.9 million and depreciation and amortization expense of \$1.9 million and \$1.3 million for fiscal years 2003 and 2002, respectively. Please see

Results of Operations for the Years Ended June 30, 2004, 2003 and 2002 Other for a consolidated discussion of selling, general and administrative expense and depreciation and amortization expense.

Astrotech Business Unit Operating Results before Charges for Fiscal Year ended June 30, 2004 as Compared to the Fiscal Year Ended June 30, 2003

Our Astrotech business unit's operating income before charges increased by \$15.5 million from fiscal year 2003 to fiscal year 2004. The following summarizes significant changes for our fiscal year ended June 30, 2004 as compared to our fiscal year ended June 30, 2003:

Edgar Filing: SPACEHAB INC \WA\ - Form S-4/A

Revenue increased by \$15.8 million as a result of a \$17.5 million early payment from Boeing's termination of their financial guarantees partially offset by decreased Boeing missions in fiscal year 2004.

Cost of Revenue increase of \$0.3 million, consisting of:

Astrotech business unit's support for 12 missions in 2004 versus 9 missions in 2003 which resulted in higher labor and benefit costs of \$0.2 million;

Additional depreciation expense of \$0.2 million in 2004; and

Decrease in selling, general and administrative expense of \$0.1 million.

Table of Contents

Fiscal year 2004 operating income for our Astrotech business unit included a contract early termination payment of \$17.5 million by Boeing with regards to its financial guarantees under the contract agreement with Boeing for payload processing support services for the Delta launch vehicle program. Boeing indicated that the decision to terminate its guarantees for future services was based on the downturn of the commercial expendable launch market rather than performance-related considerations. We believe we were in compliance with the contract terms at the time of the termination. We recognized the early termination payment as revenue in the quarter ended December 31, 2003. The termination of the Boeing contract guarantees had a significant impact on the Astrotech business unit's future guaranteed revenue stream. As a result of this event, we performed a goodwill impairment test in accordance with Statement of Financial Accounting Standards No. 142, "Goodwill and Intangible Assets." The impairment test indicated an impairment of the Astrotech business unit's remaining goodwill of approximately \$2.5 million. This impairment was recorded in the period ended December 31, 2003. We utilized market valuation techniques to calculate the fair value of the Astrotech business unit.

Astrotech Business Unit Results of Operations before Charges for Fiscal Year ended June 30, 2003 as Compared to the Fiscal Year Ended June 30, 2002

Astrotech business unit's operating income before charges increased by \$0.7 million from fiscal year 2002 to fiscal year 2003. The following summarizes significant changes for our fiscal year ended June 30, 2003 as compared to our fiscal year ended June 30, 2002:

Revenue increased by \$2.5 million from fiscal year 2002 to fiscal year 2003 due to nine launches in fiscal year 2003 as compared to seven launches for fiscal year 2002. Cost of revenue increased by \$1.8 million primarily due to increased facilities costs, as a result of our Astrotech business unit's new building being in full operation for the entire fiscal year. Our Astrotech business unit's operating expenses decreased \$0.4 million due to no longer recording amortization of goodwill of \$0.2 million and a reduction of \$0.2 million in financing fees that occurred in fiscal year 2002.

SPACEHAB Government Services

Operating income (loss) for our Government Services business unit was (\$5.4) million for fiscal year 2004, compared to (\$10.0) million and \$2.0 million for fiscal years 2003 and 2002, respectively. Operating loss for 2004 included selling, general and administrative expense of \$1.3 million and depreciation and amortization expense of \$0.1 million as compared to selling, general and administrative expense of \$1.9 and \$2.0 and depreciation and amortization expense of \$0.7 million and \$1.6 million for fiscal years 2003 and 2002, respectively. Please see "Results of Operations for the Years Ended June 30, 2004, 2003 and 2002 - Other" for a consolidated discussion of selling, general and administrative expense and depreciation and amortization expense.

Government Services Business Unit Results of Operations before Charges for Fiscal year ended June 30, 2004 as Compared to the Fiscal Year Ended June 30, 2003

Our Government Services business unit's operating income before charges decreased by \$1.6 million from fiscal year 2003 to fiscal year 2004. The following summarizes significant changes for our fiscal year ended June 30, 2004 as compared to our fiscal year ended June 30, 2003:

Revenue decreased by \$24.5 million for our fiscal year ended June 30, 2004 as compared to our fiscal year ended June 30, 2003 primarily as a result of:

The completion of the Flight Crew Systems Development contract on April 30, 2003, which resulted in no revenue in fiscal year 2004 versus \$25.8 million in fiscal year 2003;

Revenue recorded under the Stowage, Engineering And Decal contract increased by \$1.3 million in fiscal year 2004 as compared to fiscal year 2003 due to increased project work in fiscal year 2004;

The Configuration Management contract revenue decreased by \$2.4 million from fiscal year 2003 to fiscal year 2004 due to completion of the contract;

Table of Contents

The Program Integration & Control contract which was awarded in January 2004 recognized revenue of \$2.8 million in fiscal year 2004; and

A decrease in other contract revenue of \$0.4 million.

Cost of revenue decreased by \$22.9 million for our fiscal year ended June 30, 2004 as compared to our fiscal year ended June 30, 2003, primarily due to:

The completion of the Flight Crew Systems Development contract on April 30, 2003, which resulted in a reduction in our cost of revenue of \$23.9 million in fiscal year 2004 as compared to fiscal year 2003;

Cost of revenue increasing under the Stowage, Engineering And Decal contract by \$1.5 million in fiscal year 2004 as compared to fiscal year 2003 due to increased project work in fiscal year 2004;

The Configuration Management contract cost of revenue decreased by \$1.9 million from fiscal year 2003 to fiscal year 2004 due to the completion of the contract;

The award in January 2004 of the Program Integration and Control contract which increased our cost of revenue for fiscal year 2004 by \$2.8 million;

Decreases in the Shanghai Scienceland project cost of revenue of \$0.3 million;

Decreases in the cost of revenue for the Destiny module of \$0.7 million in fiscal year 2004 as compared to fiscal year 2003 due to the completion of the project in fiscal year 2003; and

Decreases in other cost of revenue of \$0.4 million.

On November 5, 2003, NASA notified us that we were not awarded the International Space Station Mission Integration Contract. Additionally, the Boeing team's bid for the Cargo Mission contract with NASA, of which our Government Services business unit was a subcontractor, was not selected for contract award. As a result of these events, we performed a goodwill impairment test at our Government Services business unit in accordance with SFAS No. 142, Goodwill and Intangible Assets. The test indicated an impairment of the Government Services business unit's remaining goodwill of approximately \$5.7 million which was recorded in the period ended December 31, 2003. We utilized market valuation techniques to calculate the fair value of the Government Services business unit.

Government Services Business Unit Operating Results before Charges for Fiscal year ended June 30, 2003 as Compared to the Fiscal Year Ended June 30, 2002

Our Government Services business unit's operating income before charges decreased by \$0.2 million from fiscal year 2002 to fiscal year 2003. The following summarizes significant changes for our fiscal year ended June 30, 2003 as compared to our fiscal year ended June 30, 2002:

Edgar Filing: SPACEHAB INC \WA\ - Form S-4/A

Revenue decreases of \$6.0 million from fiscal year 2002 to fiscal year 2003, consisting of:

The Flight Crew Systems Development contract being completed on April 30, 2003, which resulted in \$8.8 million less revenue in fiscal year 2003 as compared to fiscal year 2002;

Revenue recorded under the Stowage, Engineering and Decal contract, which was awarded in fiscal year 2003, was \$2.5 million;

The Configuration Management contract revenue decreased by \$0.5 million from fiscal year 2002 to fiscal year 2003 due to a decrease in project work; and

Other revenue increased by \$0.8 million.

Cost of revenue decreases of \$6.2 million from fiscal year 2002 to fiscal year 2003, consisting of:

The Flight Crew Systems Development contract being completed on April 30, 2003, which resulted in \$8.0 million less cost of revenue in fiscal year 2003 as compared to fiscal year 2002;

Table of Contents

Cost of revenue recorded under the Stowage, Engineering and Decal contract, which was awarded in fiscal year 2003, was \$2.4 million;

The Configuration Management contract cost of revenue decreased by \$0.4 million from fiscal year 2002 to fiscal year 2003 due to a decrease in project work;

In fiscal year 2002, there was \$1.0 million of cost of revenue for a project with Shanghai Scienceland that was completed in fiscal year 2002 with only minimum trailing costs in fiscal year 2003; and

Increases in other cost of revenue of \$0.8 million.

As a result of the loss of the recomplete of the Flight Crew Systems Development contract by our Government Services business unit in fiscal year 2003, a goodwill impairment test was performed. The impairment test indicated that the goodwill at our Government Services business unit was impaired and a \$11.9 million impairment charge of goodwill was recorded.

Space Media

Operating loss before charges for our Space Media business unit was (\$0.1) million for fiscal year 2004, compared to (\$0.3) million and (\$1.6) million for fiscal years 2003 and 2002, respectively. Operating loss for 2004 included selling, general and administrative expense of \$0.3 million and minimal depreciation and amortization expense as compared to selling, general and administrative expense of \$0.8 million and \$1.7 million and depreciation and amortization expense of \$0.3 million and \$0.3 million for fiscal years 2003 and 2002, respectively. Please see Results of Operations for the Years Ended June 30, 2004, 2003 and 2002 Other below for a consolidated discussion of selling, general and administrative expense and depreciation and amortization expense.

Other

Other operating loss was (\$10.2) million for fiscal year 2004, compared to (\$18.2) million and (\$16.0) million for fiscal years 2003 and 2002 respectively. The \$10.2 million loss for fiscal year 2004 relates primarily to selling, general and administrative expenses and depreciation and amortization expenses that were incurred at the corporate level and an impairment charge of \$1.8 million attributable to our write-down of our investment in Guignè. The (\$18.2) million loss for fiscal year 2003 includes a \$8.2 million charge for asset impairments.

Consolidated selling, general and administrative expenses and research and development were \$11.1 million in fiscal year 2004, compared to \$13.2 million and \$19.9 million in 2003 and 2002, respectively. The \$2.1 million decrease for fiscal year 2004 to 2003 is principally the result of our ongoing cost reduction efforts and staffing reductions. In addition, for the year ended June 30, 2004, we recorded a charge of approximately \$0.3 million related to the closing of our Washington, D.C. office.

The \$6.7 million decrease in selling, general and administrative expenses and research and development for fiscal year 2002 to 2003 was primarily due to our company-wide cost reduction actions. The decrease in our Space Media business unit's expenses by \$1.0 million was associated with the downsizing of its operations during the year ended June 2002. Selling, general and administrative expenses were reduced by \$0.6 million in facilities, and \$0.5 million in depreciation and other expense. Our Astrotech business unit's selling, general and administrative

Edgar Filing: SPACEHAB INC \WA\ - Form S-4/A

expenses decreased \$0.4 million due to no longer recording amortization of goodwill of \$0.2 million and reduction of \$0.2 million in financing that occurred in fiscal year 2002. Our selling, general and administrative expenses decreased due to the closing of the Huntsville operations partially offset by increased bid and proposal efforts.

Consolidated depreciation and amortization expenses were \$5.4 million in fiscal year 2004 compared to \$8.9 million and \$12.7 million in 2003 and 2002, respectively. The \$3.5 million decrease in fiscal year 2004 compared to 2003 is primarily due to the write-off of the research double module lost in the space shuttle

Table of Contents

Columbia accident, offset by the increased depreciation on the completion of the new spacecraft processing facility at our Astrotech business unit's Titusville, Florida facility. The decrease in depreciation of \$3.8 million for fiscal year 2003 as compared to 2002 resulted from the research double module having 12 months of depreciation in fiscal year 2002 as compared to seven months of depreciation in fiscal year 2003.

Interest Expense. Interest expense totaled \$8.2 million for fiscal year 2004, compared with \$7.2 million and \$8.0 million for 2003 and 2002, respectively. The \$1.0 million increase for 2004 as compared to 2003 resulted primarily from the termination of the interest rate swap upon restructuring our mortgage financing for our Astrotech spacecraft processing facility, partially offset by the lower interest payments on the lower mortgage amount after the restructuring.

The decrease of interest expense from 2002 to 2003 was primarily due to the fact that no interest expense was capitalized in 2003 as compared to \$1.3 million of capitalized interest in 2002. In addition, fiscal year 2003 includes a full year of interest on the mortgage loan payable. Interest was capitalized on the in-progress construction of our modules and payload processing facilities in 2002.

Income Tax Provision (Benefit). For fiscal year 2004 we recorded an income tax provision of \$0.5 million, applying our net operating loss carry-forwards to the extent allowable. The income tax provision is a result of the alternative minimum tax limiting our ability to use all of our net operating loss carry forwards. We recorded an income tax benefit for fiscal years 2003 and 2002 of (\$0.9) million and (\$2.1) million, respectively. As of June 30, 2004, we had approximately \$22.0 million of available net operating loss carry-forwards expiring between 2008 and 2023 to offset future regular taxable income.

Inflation. The effects of inflation and changing prices had no material effect on our revenue or income from continuing operations during the years ended June 30, 2004 and 2003.

Market Risk

Our primary exposure to market risk relates to interest rates. Our only financial instrument that is subject to interest rate risk is our revolving loan payable that has interest at prime plus one percent. We do not currently use any interest rate swaps or derivative financial instruments to manage our exposure to fluctuations in interest rates. A one percent change in variable interest rates will not have a material impact on our financial condition.

Off Balance Sheet Arrangements

We did not have any off-balance sheet arrangements as of March 31, 2005.

Table of Contents**MARKET FOR OUR COMMON STOCK AND RELATED STOCKHOLDER MATTERS**

Our common stock trades on the NASDAQ National market System under the symbol SPAB. The following table sets forth the quarterly high and low intra-day bid prices for the periods indicated.

<u>Fiscal 2006</u>	<u>High</u>	<u>Low</u>
First Quarter (through August 15, 2005)	\$ 2.04	\$ 1.30
<u>Fiscal 2005</u>	<u>High</u>	<u>Low</u>
First Quarter	\$ 3.89	\$ 2.16
Second Quarter	\$ 2.75	\$ 0.88
Third Quarter	\$ 2.20	\$ 1.50
Fourth Quarter	\$ 2.00	\$ 1.20
<u>Fiscal 2004</u>	<u>High</u>	<u>Low</u>
First Quarter	\$ 1.17	\$ 0.75
Second Quarter	\$ 1.83	\$ 0.90
Third Quarter	\$ 4.74	\$ 1.40
Fourth Quarter	\$ 4.81	\$ 3.00
<u>Fiscal 2003</u>	<u>High</u>	<u>Low</u>
First Quarter	\$ 1.24	\$ 0.60
Second Quarter	\$ 1.10	\$ 0.54
Third Quarter	\$ 1.12	\$ 0.61
Fourth Quarter	\$ 1.19	\$ 0.69

We have never paid cash dividends. It is our present policy to retain earnings to finance the growth and development of our business and, therefore, we do not anticipate paying cash dividends on our common stock in the foreseeable future. Our revolving credit facility prohibits, and the indenture for the exchange notes will prohibit, the payment of cash dividends.

We have 30,000,000 shares of common stock authorized for issuance. As of August 10, 2005 we had 12,661,179 shares of common stock outstanding. We had approximately 232 shareholders of record of our common stock on August 10, 2005.

Table of Contents**SECURITY OWNERSHIP OF CERTAIN BENEFICIAL OWNERS AND MANAGEMENT**

The following table sets forth as of August 10, 2005, certain information regarding the beneficial ownership of our outstanding common stock and Series B senior convertible preferred stock held by:

each person known to us to be a beneficial owner of more than five percent of any outstanding class of our capital stock;

each of our directors, our chief executive officer and four most highly-compensated executive officers, and all of our directors and executive officers as a group.

Unless otherwise indicated below, each of the parties listed in the table below has sole voting and investment power over the shares indicated as owned by such party.

Name and Address of Beneficial Owners:	Amount and Nature of Beneficial Ownership	Percentage of Class⁽¹⁾
<i>Series B Senior Convertible Preferred Stock</i>		
EADS Space Transportation GmbH	1,333,334 ⁽²⁾	100%
<i>Common Stock</i>		
EADS Space Transportation GmbH	1,437,499 ⁽²⁾	10.27%
SMH Capital Advisors, Inc.	2,962,642 ⁽³⁾	18.96%
SPACEHAB Taiwan, Inc.	791,666 ⁽⁴⁾	6.25%
Tejas Incorporated	692,732 ⁽⁵⁾	5.47%
Austin W. Marxe and David M. Greenhouse	1,816,600 ⁽⁶⁾	14.34%
Ore Hill Hub Fund Ltd.	674,714 ⁽⁷⁾	5.33%
Non-Employee Directors:		
Richard S. Bodman	20,000 ⁽⁸⁾	*
Dr. Edward E. David, Jr	16,000 ⁽⁹⁾	*
Richard M. Fairbanks	115,000 ⁽¹⁰⁾	*
Dr. Stefan-Fritz Graul		*
Dr. Shelley A. Harrison	394,000 ⁽¹¹⁾	3.02%
James R. Thompson	35,000 ⁽¹²⁾	*
Roscoe Michael Moore, III	5,000	*
Thomas Boone Pickens, III		*
Barry A. Williamson		*
Named Executive Officers:		
Daniel A. Bland	11,239 ⁽¹³⁾	*
Brian K. Harrington	20,000 ⁽¹⁴⁾	*
Michael E. Kearney	229,950 ⁽¹⁵⁾	1.79%
John B. Satrom	36,000 ⁽¹⁶⁾	*
Michael Chewning	59,020 ⁽¹⁷⁾	*
All Directors and Executive Officers as a Group (14 persons)	1,014,573⁽¹⁸⁾	7.50%

-
- (*) Indicates beneficial ownership of less than 1% of the outstanding shares of common stock.
- (1) Calculated pursuant to Rule 13d-3(d) of the Securities Exchange Act of 1934. Under Rule 13d-3(d), shares not outstanding which are subject to options, warrants, rights or conversion privileges exercisable within 60 days are deemed outstanding for the purpose of calculating the number and percentage owned by a

Table of Contents

- person, but not deemed outstanding for the purpose of calculating the number and percentage owned by any other person listed. As of August 10, 2005, we had 12,661,179 shares of common stock outstanding.
- (2) EADS Space Transportation GmbH beneficially owns 1,333,334 shares of our Series B convertible preferred stock that are convertible at the holder's option into common stock on the basis of one share of preferred stock for one share of common stock. EADS Space Transportation GmbH's address is Postfach 80 11 69, 81663 Munich, Germany. The preceding information is based on a Schedule 13D/A, filed with the Securities and Exchange Commission on October 27, 1999.
 - (3) Represents \$40,366,000 principal amount of our 8% Convertible Subordinated Notes due 2007 that may be converted into common stock at a rate of \$13.625 per share held by SMH Capital Advisors, Inc. in discretionary accounts for the benefit of its clients. SMH Capital Advisors has shared voting power and sole investment power with respect to these shares. This holder disclaims beneficial ownership of all shares of common stock it holds. This holder's address is 600 Travis, Suite 3100, Houston, Texas 77002. The preceding information is based on Amendment No. 3 to a Schedule 13G filed with the Securities and Exchange Commission on July 22, 2005 by SMH Capital Advisors, Inc.
 - (4) Except for the ownership of 791,666 shares of our common stock, SPACEHAB Taiwan has no other affiliation with us. SPACEHAB Taiwan's address is 14th Floor No. 180, Chang-Shiao E. Road, Sec. 4, Taipei, Taiwan, R.O.C.
 - (5) Tejas Incorporated and Tejas Securities Group, Inc., a wholly-owned subsidiary of Tejas Incorporated, share voting and investment power with respect to 541,332 shares, which are held in a proprietary trading account of Tejas Securities Group, Inc. Tejas Incorporated has sole voting and investment power with respect to 151,400 shares of common stock. The address for Tejas Incorporated and Tejas Securities Group, Inc. is 8226 Bee Caves Road, Austin, Texas 78746. The preceding information is based on Amendment No. 3 to a Schedule 13D, filed with the Securities and Exchange Commission on August 2, 2005.
 - (6) Austin W. Marx and David M. Greenhouse share voting and investment power over 971,600 shares of common stock held by Special Situations Fund III, L.P., 91,780 shares of common stock held by Special Situations Technology Fund, L.P., 467,970 shares of common stock held by Special Situations Technology Fund II, L.P. and 285,300 shares of common stock held by Special Situations Cayman Fund, L.P. Austin W. Marx and David M. Greenhouse are the controlling principals of AWM Investment Company, Inc., the general partner and investment adviser to Special Situations Cayman Fund, L.P. AWM Investment Company, Inc. also serves as general partner of MGP Advisors Limited Partnership, the general partner of and investment adviser to Special Situations Fund III, L.P. Mr. Marx and Mr. Greenhouse are also members of SST Advisers, L.L.C., the general partner and investment adviser to Special Situations Technology Fund, L.P. and Special Situations Technology Fund II, L.P. The principal business address for Mr. Marx and Mr. Greenhouse is East 53rd Street, 55th Floor, New York, New York 10022. The preceding information is based on Amendment No. 4 to Schedule 13G filed with the Securities and Exchange Commission on February 11, 2005.
 - (7) Ore Hill Partners LLC, a Delaware LLC, is the investment manager of Ore Hill Hub Fund, Ltd. The two entities share voting and investment power over these shares. The principal business address of Ore Hill Partners LLC is 444 Madison Avenue, 12th Floor, New York, New York 10022. The principal business address of Ore Hill Hub Fund, Ltd. is c/o Bank of Butterfield International (Cayman) Ltd., P.O. Box 705 GT, Butterfield House, 68 Front Street, Grand Cayman, Cayman Islands. The preceding information is based on a Schedule 13G filed with the Securities and Exchange Commission on May 19, 2005.
 - (8) Includes options to purchase 10,000 shares of common stock.
 - (9) Includes options to purchase 15,000 shares of common stock.
 - (10) Includes options to purchase 35,000 shares of common stock.
 - (11) Includes options to purchase 393,000 shares of common stock.
 - (12) Includes options to purchase 30,000 shares of common stock.
 - (13) Includes 954 shares of common stock held in our 1997 Employee Stock Purchase Plan. Mr. Bland resigned on July 1, 2005.
 - (14) Includes options to purchase 10,000 shares of common stock.

Table of Contents

- (15) Includes 2,006 shares of common stock held in our 1997 Employee Stock Purchase Plan, and options to purchase 195,304 shares of common stock.
- (16) Represents options to purchase 36,000 shares of common stock. Mr. Satrom resigned on August 12, 2005.
- (17) Includes options to purchase 49,020 shares of common stock.
- (18) Includes options to purchase 794,361 shares of common stock and 65,572 shares of common stock held in our 1997 Employee Stock Purchase Plan.

Table of Contents

DESCRIPTION OF OTHER INDEBTEDNESS AND FINANCING ARRANGEMENTS

Revolving Loan Agreement

On February 11, 2005, we entered into a \$5.0 million loan agreement with First American Bank, SSB, a Texas financial institution. The agreement provides for a revolving line of credit of up to \$5.0 million for 12 months. Funds borrowed under the revolving senior credit facility will be used for general working capital, capital expenditures and corporate purposes. The agreement provides for an unused facility fee incurred on the unused portion of the facility. Contemporaneously with the loan agreement, we entered into a security agreement with First American Bank, SSB. The loans under the revolving credit facility are secured by our accounts, general intangibles, chattel paper and instruments, deposit accounts, and all proceeds of the foregoing. If we do not satisfy the minimum tangible net worth covenant in our credit facility, we are required to maintain a restricted cash balance. We were required to maintain a restricted cash balance of \$0.3 million and \$.04 million, as of March 31, 2005 and June 30, 2005, respectively, because we did not satisfy the minimum tangible net worth covenant in our credit facility. As of June 30, 2005, no borrowings were outstanding under the credit facility.

Mortgage Loan Agreement

On August 30, 2001, our Astrotech business unit entered into a credit agreement with Southtrust Bank, an Alabama banking corporation, providing for a \$20.0 million financing of our spacecraft processing facility expansion project in Titusville, Florida. The proceeds of this financing were used to complete the construction of a new spacecraft processing facility and supporting infrastructure. The term loan was collateralized primarily by the multi-year payload processing contracts with The Boeing Company and Lockheed Martin and by the new building. The net book value of the building as of December 31, 2004 was \$37.4 million. As a result of Boeing's termination of its financial guarantees related to its use of our payload processing support services, we repaid \$9.5 million of principal on the term loan on December 31, 2003. The term loan agreement was amended on January 29, 2004, whereby the maturity date was shortened to January 2007, the interest rate was fixed at 5.5% and the hedge requirement was eliminated. Pursuant to the terms of the term loan agreement, the quarterly payments that we receive from Lockheed Martin under our payload processing contract in the amount of \$0.6 million are paid into a lock box for the benefit of Southtrust Bank. As of June 30, 2005, the outstanding balance under this loan was \$3.7 million.

Table of Contents

THE EXCHANGE OFFER AND CONSENT SOLICITATION

We are making this exchange offer for all of our outstanding 8% Convertible Subordinated Notes due 2007. Concurrently with the exchange offer, we are soliciting consents to amend provisions of the indenture governing the outstanding notes. If you tender any of your outstanding notes in the exchange offer and they are accepted before the exchange offer and consent solicitation expires, you will automatically be consenting to amend the indenture that governs the outstanding notes to eliminate the event of default relating to cross defaults.

Purpose and Effect of the Exchange Offer and Consent Solicitation

We are making this exchange offer and consent solicitation as a part of our overall strategic plan to enhance cash flow from operations, improve our liquidity and working capital position, and provide balance sheet and cash flow capacity for potential future investments in space commerce assets. The consummation of the exchange offer and consent solicitation to restructure our long term debt is the next step in our plan. We believe that the corporate restructuring and refinancing steps taken to date are inadequate to provide sufficient cash flow to fund research and development efforts necessary to develop new space assets that we believe will be required to ensure our long term viability and competitiveness. If we are unable to reduce our current debt obligations and extend debt maturities on the outstanding notes through the exchange offer and thus improve our liquidity and financial stability, we may be unable to replace our shuttle based assets with rocket based launch systems as the space shuttle is phased out of operation. If the exchange offer is not successful, we do not believe that we will have the financial flexibility necessary to obtain future financing to fund needed research and development efforts.

In addition to limiting our ability to fund research and development, if the exchange offer is not completed, we will be required to direct substantial available cash flows during the next two years to the repayment of the outstanding notes by 2007. Since we do not believe that these cash flows will be sufficient to repay the outstanding notes in 2007, we may also be required to divest core assets to generate sufficient funds to repay the outstanding notes at maturity and, if such divestitures are not successful, to seek a restructuring of our debt. We believe that the actions that would need to be taken to repay the outstanding notes in 2007 would substantially narrow our future prospects. The cash flows redirected to the repayment of, and any divestiture of assets to repay, the outstanding notes may not generate sufficient funds to fully repay the outstanding notes and owners of the outstanding notes may only receive repayments of little or none of the principal amount of their outstanding notes. Due to the adverse effects that the outstanding notes will have on our future liquidity and ability to restructure and refocus our business at a time when our largest market is changing dramatically, we are proposing to exchange the outstanding notes for exchange notes pursuant to the terms of the exchange offer described below.

Terms of the Exchange Offer and Consent Solicitation

Upon the terms and subject to the conditions stated in this prospectus and in the letter of transmittal, we will accept all outstanding notes properly tendered and not withdrawn prior to 5:00 p.m. New York City time, on [●], 2005. After authentication of the exchange notes by the trustee or an authenticating agent, we will issue \$1,000 principal amount of exchange notes in exchange for each \$1,000 principal amount of outstanding notes accepted in the exchange offer. Holders may tender some or all of their outstanding notes in denominations of \$1,000 or any integral multiple of \$1,000.

We will pay the accrued interest on the validly tendered outstanding notes on the settlement date, which will be promptly after the expiration date. We will make all payments by the deposit of immediately available funds with the exchange agent. The exchange agent will act as agent for tendering holders for the purpose of receiving payments from us and transmitting payments to the holders. The exchange agent will pay DTC the aggregate amount of accrued interest we owe holders of outstanding notes held in global form and tendered and accepted in the exchange

offer, and such holders will receive the applicable portion of such accrued interest payment pursuant to the applicable procedures established by DTC and its participants.

Table of Contents

This prospectus, together with the accompanying letter of transmittal, is initially being sent to all registered holders as of the close of business on [●]. We intend to conduct the exchange offer as required by the Exchange Act, and the rules and regulations of the SEC under the Exchange Act, including Rule 14e-1, to the extent applicable.

Holders of the outstanding notes do not have any appraisal or dissenters' rights under the Washington Business Corporation Act or under the indenture in connection with the exchange offer. No governmental approvals or consents must be received to consummate the exchange offer. We shall be considered to have accepted outstanding notes tendered according to the procedures in this prospectus when, as and if we have given oral or written notice of acceptance to the exchange agent. See Exchange Agent. The exchange agent will act as agent for the tendering holders for the purpose of receiving exchange notes from us and delivering exchange notes to those holders.

Neither we nor our board of directors makes any recommendation to holders of outstanding notes as to whether to tender or refrain from tendering all or any portion of their outstanding notes pursuant to the exchange offer. Moreover, no one has been authorized to make any recommendation. Holders of outstanding notes must make their own decision whether to tender in the exchange offer and, if so, the amount of outstanding notes to tender after reading this prospectus and the letter of transmittal and consulting with their advisors, if any, based on their own financial position and requirements.

Certain Consequences to Holders of Outstanding Notes Not Tendering in the Exchange Offer

See the section of this prospectus entitled Risk Factors Risks Related to Retaining the Outstanding Notes for a discussion of the consequences to holders of outstanding notes who elect not to tender their outstanding notes in the exchange offer.

Acceptance of Outstandin