SPACEHAB INC \WA\
Form 10-K/A
February 28, 2008

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-K/A

(Amendment No. 2)

(Mark One)

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

For the fiscal year ended June 30, 2007

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

For the transition period from to

Commission File No. 0-27206

SPACEHAB, Incorporated

(Exact name of registrant as specified in this charter)

Washington	**91-1273737**
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)

12130 Highway 3, Building 1

Webster, Texas 77598-1504
(Address of principal executive offices) (Zip code)

(713) 558-5000

(Registrant s telephone number, including area code)

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

Title of each class	**Name of each exchange on which registered**
Common Stock (no par value)	**NASDAQ Capital Market**

Securities registered pursuant to Section 12(g) of the Act: None

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

YES o NO x

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

YES o NO x

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

YES x NO o

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K (229.405 of this chapter) is not contained herein, and will not be contained, to the best of registrant s knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K. o

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

Large accelerated filer o
Accelerated filer o
Non-accelerated filer x
Smaller reporting company o

(Do not check if a smaller reporting company)

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).

YES o NO x

The aggregate market value of the registrants voting and non-voting common equity held by non-affiliates of the registrant, based upon the closing price of such stock on the NASDAQ Capital Market on such date of $0.65 was approximately $8,429,242 as of December 29, 2006.

As of September 19, 2007, 13,027,196 shares of the registrant s Common Stock, no par value, were outstanding.

DOCUMENTS INCORPORATED BY REFERENCE:

Information called for in Part III of this Form 10-K is incorporated by reference to the registrant s definitive Proxy Statement to be filed within 120 days after the end of the registrant s fiscal year in connection with the registrant s annual meeting of shareholders.

EXPLANATORY NOTE

SPACEHAB, Incorporated is amending their Fiscal Year 2007 Form 10-K as a result of a reclassification of $6.3 million of restricted cash as a non current asset and the reclassification of $5.7 million of advances on a construction contract as a non current liability in accordance with ARB 43, Chapter 3, Section A, Paragraph 6 and 8. The reclassification of the $6.3 million of restricted cash included classifying the net change in restricted cash as a cash flow from operating activities in accordance with FAS 95. Amendment to this document in accordance with these standards is outlined in the subsequent pages below.

Note: There are no other changes to the original Form 10-K filing other than those outlined in this document. This Form 10-K/A does not reflect events occurring after the filing of the original Form 10-K, or modify or update the disclosures therein in any way other than as required to reflect the amendment set forth below.

PART II

Item 6. Selected Financial Data.

The following table sets forth our selected consolidated financial data as of and for the years ended June 30, 2003, 2004, 2005, 2006, and 2007 restated. Such data has been derived from our consolidated financial statements audited by Ernst & Young LLP for the fiscal year ended June 30, 2003, by Grant Thornton LLP for the fiscal years ended June 30, 2004, 2005, and 2006, and by PMB Helin Donovan, LLP for fiscal year ended June 30, 2007. 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 annual report. All amounts, except per share amounts, are in thousands.

	Years Ended June 30,				
	2003	**2004**	**2005**	**2006**	**2007 Restated**
Statement of Operations Data:					
Revenue from operations	$ 94,963	$ 77,606(3)	$ 59,401	$ 50,746	$ 52,762
Costs of revenue	78,791	45,678	47,158	46,855(7)	51,029(9)
Gross profit	16,172	31,928	12,243	3,891	1,733
Selling, general and administrative expenses	91,434(1)	20,982(4)	1,639(5)	10,672	13,762(9)
Research and development expenses	118	223	77	410	801
Income (loss) from operations	(75,380)	10,723	10,527	(7,191)	(12,830)
Interest expense, net of capitalized amounts and interest and other income	7,252	8,142	5,424	5,174(8)	3,531
Net income (loss)	(81,775)	2,075	5,249	(12,397)	(16,292)
Net income (loss) per common share basic	$ (6.66)	$ 0.17	$ 0.42	$ (0.97)	$ (1.26)
Net income (loss) per common share diluted	$ (6.66)	$ 0.15	$ 0.37	$ (0.97)	$ (1.26)
Shares used in computing net income (loss) per common share basic	12,285	12,450	12,613	12,744	12,920
Shares used in computing net income (loss) per common share diluted	12,285	14,142	14,190	12,744	12,920
Cash dividends declared per common share					
Other Data:					
Cash provided by (used in) operations	$ 2,114	$ 5,273	$ (7,153)	$ 3,984(8)	$ 6,028(10)
Cash provided by (used in) investing activities	3,037(2)	5,019	17,683(6)	(1,141)	(1,077)
Balance Sheet Data (at period end):					
Working capital (deficit) surplus	$ (4,750)	$ (6,351)	$ 5,435	$ 2,753	$ (6,105)
Total assets	121,356	99,925	101,951	85,450	72,475
Long-term debt, excluding current portion	80,056	66,942	64,885	63,250	52,944
Stockholders equity (deficit)	5,090	9,410	14,797	2,809	(13,131)

(1) 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.

(2) Includes approximately $17.7 million of insurance proceeds related to the loss of our research double module.

(3) Includes approximately $17.5 million due to Boeing s termination of its spacecraft processing contract with us.

(4) 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.

(5) Includes $7.7 million of net recovery from non-recurring transactions related to the loss of our research double module.

(6) Includes approximately $8.2 million from ReALMS contract indemnification clause related to the loss of our research double module.

(7) Includes approximately $6.3 million of non-cash write downs related to our flight unit 3 and the shuttle based flight assets.

(8) Includes approximately $0.6 million of non-cash charges related to the acceleration of debt placement fees related to the convertible subordinated notes.

(9) Includes approximately $12.5 million of non-cash write downs related to our flight unit 2 and the shuttle based flight assets and a $0.1 million non-cash write down of an investment in Applied Astronautical Corporation.

(10) Includes $3.1 million advance from customer for in-flight insurance for STS-118 that was paid in July 2007 to the insurance carrier.

Item 7. 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 report.

Historically, we have operated 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 and commercial space operations. Because of the diversity among the operations of our activities, we report the results of each business as 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.

Overview

We provide a range of products and services that focus on the needs of industry, governments and academia requiring access to, and utilization of the unique environment of space. We employ a staff of engineers and technicians who have supported approximately 250 manned and unmanned missions to space from multiple locations worldwide, including 23 space shuttle missions. We offer products and services in the following areas:

- Expertise in qualifying hardware for spaceflight and the habitability and occupational challenges of space;
- Facilities and support services necessary for the preparation of satellites and payloads for launch;
- Engineering, analysis, and payload operations services;
- Program integration and control; and
- Product design, development, and fabrication.

Our Business Units

Our company is currently comprised of three primary business segments which provide the following products and services to the government and commercial markets. Our business units include:

SPACEHAB Flight Services. The primary goal of our Flight Services business unit is to enable government and commercial enterprises to overcome the accessibility, habitability and occupational challenges of space. To meet our clients specific mission requirements, we offer a range of engineering, research, logistics, integration, operations, and ground support services. Through this business unit, we have and will continue to offer a full range of ground-based pre- and post-flight experiment, cargo, and payload processing services as well as on-orbit operations support. Additionally, we are supporting contracts for ongoing flight hardware manufacturing projects in support of NASA and international customers. Our Flight Services Business Unit generates revenue by providing turnkey services generally on a fixed price basis. We recognize revenue for mission contracts that extend over multiple financial reporting periods using the percentage of completion method which relies upon estimates of costs and time to complete, as well as other estimates. During fiscal year 2007, our Flight Services business unit accounted for 65% of our consolidated revenues.

The primary factors impacting our Flight Services business unit earnings and cash flows are the number of space shuttle missions flown, the requirements for use of our space shuttle hardware and the configuration of the cargo handling and research logistics required for each mission. Other factors that have impacted, and are expected to continue to impact earnings and cash flows for this business unit include:

- NASA s use of our space shuttle modules and related space assets that utilize our competencies in configuration and cargo handling.
- Commercial demand for access to space launch capability and need for research cargo logistics
- Space shuttle mission requirements for the manufacture of specialized cargo handling equipment.

Astrotech Space Operations. Our Astrotech business unit provides modern facilities and support for the preparation of multi-million dollar satellites and payloads for launch on expendable launch vehicles. Since 1985, our Astrotech business unit has been providing government and commercial customers with a commercial alternative to using government-owned facilities to prepare their satellites for launch in the United States. Astrotech currently has long-term contracts in place with NASA, United Launch Alliance, National Reconnaissance Office and Sea Launch, LLC. During fiscal year 2007, Astrotech accounted for 23% of our consolidated revenues.

Revenue for our Astrotech business unit is generated from various fixed-priced 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 spacecraft for launch. The earnings and cash flows generated from our Astrotech operations are related to the number of commercial spacecraft launches, which reflects the growth in the satellite-based communications 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

- 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

- Our ability to complete customer specified facility modifications within budgeted costs and time commitments

SPACEHAB Government Services. For nearly 30 years, our Government Services business unit has provided large scale program technical support and specialized engineering analysis, products, and services to NASA and other customers. Our Government Services business unit derives most of its revenue under ARES contract to provide configuration and data management services within NASA s Program Integration & Control (PI&C) contract for the International Space Station. The base contract period extends through September 2008 and can be extended for two additional one year terms at the election of our NASA customer. Under this contract, we facilitate the assurance that the tens of thousands of pieces of hardware and software parts and components meet approved design and configuration requirements for the International Space Station. During the first nine months of fiscal year 2007, our Government Services business unit accounted for 11% of our consolidated revenues.

Earnings from our Government Services business unit 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 PI&C contract with the International Space Station program and exercise of the contract options through 2010

- Our ability to maintain small business qualification for our Government Services business unit under NASA contracting rules

- Our ability to control costs within our budget commitments

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

- Interest expense which has decreased due to the repayment of our mortgage debt during fiscal year 2006 and which will be further reduced if our Exchange Transaction (see Note 28) is successful

- Income taxes, with respect to which we currently only pay alternative minimum tax and minimal state income taxes; income taxes will be impacted by limitations on our net operating loss carry forward upon consummation of our Exchange Transaction, if successful (see Note 28)

New Business Vision

In anticipation of the planned 2010 space shuttle retirement, we began developing new products and services. We are now focusing our business on using our core capabilities for the commercial exploitation of space. These new business initiatives include the following:

- Processing products and services in microgravity;
- Commercializing products manufactured in microgravity;
- Commercializing products developed for use in the space industry;
- Acquiring other U.S. space contractors; and
- Providing end-to-end services for commercial and government satellite operations.

Although we are developing products and services in support of the new business visions, we currently do not have contracts or other arrangements to provide these products and services. We cannot assure you that we will be able to successfully develop these new products and services in the future. We anticipate that we will require substantial additional capital to develop these new products and services, and that this additional financing will likely substantially dilute current holders of our common stock.

New Business Initiatives

Many of our identified new business initiatives are focused on space-based life sciences and end-to-end space mission assurance services, which are natural extensions of our 23 years of space industry experience and our core capabilities in these fields. These new business initiatives will require large investments of capital and technical expertise.

Microgravity. In the early days of the space program, it was determined that the effects of microgravity provide a unique environment that could potentially benefit humans. Since the inception of the Space Shuttle Program and extending through the International Space Station Program, NASA has spent billions of dollars on microgravity infrastructure and research. We have been logistically responsible for several hundred of these experiments on the space shuttle, the Russian Progress vehicle and the International Space Station.

Previous spaceflight research suggests that growing protein crystals in the microgravity environment of space offers the possibility of significantly increasing the x-ray diffraction quality of protein crystals. We believe that because of the high quality of these protein crystal structures, they may be used to better define the protein structures of diseases such as diabetes, cystic fibrosis, sickle cell anemia, Alzheimer s, Parkinson s disease, Lou Gehrig s disease and certain forms of cancer, which in turn may lead to the development of drugs capable of combating these diseases. If we are successful in developing protein crystals in microgravity, we expect to pre-sell these crystals to pharmaceutical companies.

On August 14, 2007, NASA announced that it was seeking private industry proposals for research and manufacturing concepts and opportunities onboard the International Space Station. This announcement indicates NASA s desire to open the International Space Station to commercial projects. Because of our experience with microgravity, we are responding to the solicitation and believe that we are well positioned to transition protein crystal growth, and other identified candidates, from a space research project to a fully commercialized microgravity processing operation.

Advanced Research and Conventional Technology Utilization Spacecraft (ARCTUS). We are assembling a team of industry partners with a common goal of developing a commercial transportation system providing lower cost, lower risk space transportation services than conventional, government-developed transportation systems. ARCTUS is designed to provide cargo transportation services to the International Space Station under the unfunded Space Act Agreement signed with NASA in June 2007.

End-to-End Space Mission Assurance. We believe that Astrotech is a recognized leader in providing commercial spacecraft processing services. Astrotech intends to expand its market by offering end-to-end assurance services to both commercial and government customers. These new end-to-end space mission assurance services would extend

Astrotech s current relationships with customers spacecraft from a condensed few weeks of ground processing at an Astrotech facility to multiple years of space mission assurance services throughout the satellite s lifecycle.

SPACETECH. In 2007, we formed a technology incubator called SPACETECH. The purpose of SPACETECH is to cultivate technology developed for and from space into commercial applications. The following are two examples of new initiatives already underway within SPACETECH:

- Under an unfunded Space Act Agreement with NASA, we began development of a mini-mass spectrometer which we hope to turn into a small, portable, low power unit capable of detecting chemical compounds such as explosives, weapons of mass destruction, and toxic gases. We are negotiating an agreement for the licensing, sale and distribution of the mini mass spectrometer.

- The Federal Aviation Administration and Department of Transportation have enacted new regulations for air transportation of oxygen containers to enhance safety in the event of a fire. Applying decades of experience in the development of specialized containers, we have been working with an industry partner to develop and certify a container to meet these new requirements. If successful, this project will provide us an opportunity to enter a new market.

Our Business Strategy

Our strategic vision is to be a recognized market leader in providing services to support space operations and utilization with consistent growth while increasing shareholder value. Our business strategies to achieve this are:

• Deliver excellence on current work, including providing technical support on space programs and remaining space shuttle missions;

• Leverage decades of experience facilitating bioscience space payloads and developing and operating successful space hardware for expansion into microgravity processing;

• Bring mature space technology and space-based processing to the commercial markets;

• Provide access to space on alternative launch systems for proprietary space processing and for commercial customers;

• Design solutions that encourage private commercial investment in space; and

• Continue to develop space-related hardware.

FINANCIAL CONDITION, CAPITAL RESOURCES, AND LIQUIDITY

Balance Sheet. Our total assets at June 30, 2007 were $72.5 million compared to total assets of $85.5 million at the end of fiscal year 2006. The following table sets forth the significant components of the balance sheet as of June 30, 2007, compared with 2006 (in thousands):

		2007 Restated		2006		Chg.
Assets:						
Current assets	$	19,644	$	20,675	$	(1,031)
Property and equipment (net)		43,884		61,637		(17,753)
Other assets (net)		8,947		3,138		(5,809)
Total	$	72,475	$	85,450		
Liabilities and stockholders equity:						
Current liabilities	$	25,749	$	17,922	$	7,827
Long-term debt-less current portion		52,944		63,250		(10,306)
Other long-term liabilities		6,913		1,469		5,444
Stockholders equity		(13,131)		2,809		(15,940)
Total	$	72,475	$	85,450		

<u>Fiscal Year 2007 Restated Compared to Fiscal Year 2006</u>. Current assets as of June 30, 2007 increased by $5.3 million as compared to June 30, 2006. This increase is primarily due to:

• Decrease in current assets of $1.0 million. These differences are attributed to:

• Increase in cash of $3.4 million partially due to us receiving $3.1 million from our customer before year-end for the in-flight insurance on STS-118. The payment to the insurance carrier was made subsequent to year-end.

- Decrease in accounts receivable of $3.1 million is primarily attributable to the decreased volume of sales in Flight Services due to our contracted missions for our shuttle assets ending their contracted period of performance.

- Decrease in other assets of $1.5 million is primarily a result of us valuing our inventory to market prices. This resulted in a non-cash write-down of the inventory by $1.7 million and the recording of a $1.0 million note receivable.

- Increase in prepaid expenses of $0.3 million.

The decrease in net property and equipment of $17.8 million from June 30, 2007 to June 30, 2006 resulted primarily from the write-down of our flight unit 2 module due to our analysis of the remaining shuttle flights and the potential need for our flight unit 2 module on these flights and depreciation.

The increase in other assets of $5.8 million from June 30, 2007 restated to June 30, 2006 resulted primarily from an increase in restricted cash attributable to a new contract to expand our payload processing facility in our Astrotech subsidiary which generated $6.3 million in restricted cash during fiscal year 2007, and a decrease in net deferred financing costs of approximately $0.5 million as a result of amortization of the deferred financing costs. Additionally, we had a non-cash valuation allowance of $0.1 million for our investment in Applied Astronautical Corporation offset by an increase in other assets of $0.1 million.

Our current liabilities increased by $7.8 million from June 30, 2006 to June 30, 2007. The following summarizes significant items:

- Our accounts payable and accrued expenses decreased from $14.7 million to $11.0 million due a reduction in mission activities in our Flight Services business unit and the timing of payments.

- Our short-term debt decreased by $1.6 million from June 30, 2006 to June 30, 2007 as we paid the remaining payments on our mortgage loan at our Astrotech facility. Additionally, our short-term debt increased from June 30, 2006 to June 30, 2007 by $10.3 million due to our 8% convertible subordinated notes maturing in October 2007.

- Our short-term deposit account increased by $3.1 million during the current fiscal year. This is a result of us receiving $3.1 million from our customer prior to year end for the in-flight insurance on our flight assets for STS-118 that flew in August 2007. The payment to the insurance carrier was made subsequent to year end.

- Our current portion of deferred revenue decreased by $0.2 million for June 30, 2006 to June 30, 2007 due to timing of receiving payments and recognizing revenue for shuttle related and satellite related programs.

Our long-term debt as of June 30, 2007 decreased by $10.3 million due to the maturity of $10.3 million of our 8% convertible subordinated notes in October 2007.

Other long-term liabilities increased by $5.4 million at year end 2007 restated compared to year end 2006 primarily due to recognition of the long-term gain of the $1.6 million that was recorded in the fourth quarter of fiscal year 2005 due to the sale of our Cape Canaveral and Houston Headquarters facilities that will be recognized over the term of the leases offsetting advances on construction contract increased by $5.7 million from June 30, 2006 to June 30, 2007. The increase in advances on the construction contract was primarily due to receiving the initial milestone payments on our contract with a governmental agency to design and build a new processing facility and corresponding payments to subcontractors for work performed during the period.

Liquidity and Capital Resources

As of June 30, 2007 we had cash and restricted cash on hand of $16.0 million and our working capital was approximately ($5.5) million. Restricted cash, which consists of advance payments on a government contract to modify certain spacecraft processing facilities, totaled $6.3 million at June 30, 2007. For fiscal year 2007 restated we generated $6.0 million from operating activities. Our $5.0 million revolving credit facility expired as of February 11, 2007 and we elected not to renew the facility.

Our $10.3 million of outstanding 8.0% convertible notes are due on October 15, 2007 and our $52.9 million of 5.5% senior convertible notes are due in October 2010. A covenant in our 5.5% note indenture restricts us from using the proceeds from the sale or mortgage of our Astrotech Florida assets for purposes other than reducing outstanding balances on our credit facility, repaying our now extinguished mortgage loan, or redeeming outstanding 5.5% senior convertible notes. We do not have sufficient liquidity to repay the principal and interest on our 8.0% convertible notes and the interest on our 5.5% senior convertible notes when due on October 15, 2007 unless our Exchange Offer (see Item 7. Management s Discussion and Analysis of Financial Condition and Results of Operations Liquidity and Capital Resources) is successfully consummated.

Cash Flows From Operating Activities. Cash provided by (used in) operations for the years ended June 30, 2007 restated, 2006, and 2005 was $12.3 million, $4.0 million, and ($7.2) million, respectively. The significant items affecting the differences in cash flows from operating activities in fiscal year 2007 as compared to fiscal year 2006, and fiscal year 2006 compared to fiscal year 2005 are discussed below:

Fiscal Year 2007 Restated Compared to Fiscal Year 2006. For the fiscal year 2007 compared to fiscal year 2006, the significant items affecting cash provided by operating activities were:

- Net loss for fiscal year 2007 was $16.3 million as compared to net loss for fiscal year 2006 of $12.4 million. Included in the net loss for fiscal year 2007 is a $12.5 million non-cash charge for the write-down of our flight unit 2 module and other shuttle related assets. Additionally, the net loss for fiscal year 2007 included a non-cash charge of $0.1 million for the valuation of our investment in Applied Astronautics Corporation. Included in the net loss for fiscal year 2006 is a $6.3 million non-cash charge for the write-down of our flight unit 3 module.

- Fiscal year 2006 included a non-cash charge of $0.6 million related to the acceleration of debt placement costs related to the original issuance costs of our $63.3 million 8% convertible subordinated costs to the exchange of $52.9 million of the notes for $52.9 million of 5.5% senior convertible subordinated notes.

- Fiscal year 2007 Restated cash flows from operations included an increase in restricted cash of $6.3 million due to advances received for the design and construction of a payload processing facility at our Vandenberg Air Force Base location.

- Depreciation and amortization for fiscal year 2007 was $0.3 million more compared to fiscal year 2006, primarily due to increased depreciation expense for our flight assets resulting from the change of the depreciable lives from 2016 to 2010. This change in depreciable lives is based on the most current information available from NASA on the retirement of the space shuttle fleet at the end of 2010.

- Changes in assets for fiscal year 2007 provided cash from operations of $4.3 million. This change is primarily due to:

- Decrease in accounts receivable of $4.6 million which is primarily due to a decrease in shuttle-related project work and the timing of payments.

- Increase in prepaid expenses and other assets of $0.3 million which is mainly due to increased mission activities in our Astrotech business unit for future satellite processing missions.

- Changes in assets for fiscal year 2006 provided cash from operations of $5.6 million. This change is primarily due to:

- Decrease in accounts receivable of $5.5 million which is primarily due to a decrease in shuttle-related project work and the timing of payments.

- Decrease in prepaid expenses and other assets of $0.1 million which is primarily due to a decrease in deferred mission costs for the Japanese Experiment Thermal Incubator Service contract due to the completion of the contract in fiscal year 2006.

- Changes in liabilities for fiscal year 2007 provided cash from operations of $5.3 million. This change is primarily due to:

- Decreases in accounts payable, accrued expenses, and accrued subcontracting costs of $3.3 million which is due to decreased mission activity for shuttle related projects.

- Decrease in deferred revenue of $0.2 million. The decrease in deferred revenue is primarily due to the timing of mission activities and payments in Astrotech business unit.

- Increase in advances on construction contract of $5.7 million. The increase for our advances on the construction contract increased by $5.7 million due to receiving the initial milestone payments on our contract with a governmental agency to design and build a new processing facility and corresponding payments to subcontractors for work performed during the period.

- Increase of $3.1 million in customer deposits. Our short-term deposit account increased by $3.1 million during the current fiscal year. This is a result of us receiving $3.1 million from our customer prior to year end for the in-flight insurance on our flight assets for STS-118 that flew in August 2007. The payment to the insurance carrier was made subsequent to year end.

Changes in liabilities for fiscal year 2006 used cash from operations of $2.2 million. This change was due primarily to the decreases in accounts payable, accrued expenses, and accrued subcontracting costs of $1.8 million and the decrease in deferred revenue of $0.4 million. The decreases in accounts payable, accrued expenses, and accrued subcontracting costs is due to decreased mission activity for shuttle related projects. The decrease in deferred revenue is primarily due to the completion of the Japanese Experiment Thermal Incubator Service contract during fiscal year 2006.

Fiscal Year 2006 Compared to Fiscal Year 2005. For the fiscal year 2006 compared to fiscal year 2005, the significant items affecting cash provided by operating activities were:

- Net loss for fiscal year 2006 was $12.4 million as compared to net income for fiscal year 2005 of $5.2 million. Included in the net loss for fiscal year 2006 is a $6.3 million non-cash charge for the write-down of our flight unit 3 module. Included in net income for fiscal year 2005 is $7.7 million recognized as a net recovery of a previously reported non-recurring loss of our research double module destroyed during the Space Shuttle *Columbia* mission.

- Fiscal year 2006 non-cash charge of $0.6 million related to the acceleration of debt placement costs related to the original issuance costs of our $63.3 million 8% convertible subordinated costs to the exchange of $52.9 million of the notes for $52.9 million of 5.5% senior convertible subordinated notes.

- Depreciation and amortization for fiscal year 2006 was $0.5 million more compared to fiscal year 2005, primarily due to increased depreciation expense for our flight assets resulting from the change of the depreciable lives from 2016 to 2010. This change in depreciable lives is based on the most current information available from NASA on the retirement of the space shuttle fleet at the end of 2010. This increase is partially offset by a portion of assets reaching the end of their useful lives and decreased depreciation expense due to the sale of our facility in Cape Canaveral, Florida during fiscal year 2005.

- Changes in assets for fiscal year 2006 provided cash from operations of $5.6 million. This change is primarily due to a decrease in accounts receivable of $5.5 million and a decrease in prepaid expenses and other assets of $0.1 million. The decrease in accounts receivable is primarily due to a decrease in shuttle-related project work and the timing of payments. The decrease in other assets is primarily due to a decrease in deferred mission costs for the Japanese Experiment Thermal Incubator Service contract due to the completion of the contract in fiscal year 2006. For fiscal year 2005 change in assets used cash from operations of $7.9 million primarily from an increase in accounts receivable of $9.0 million and an increase in prepaid expenses of $0.2 million, which was partially offset by a decrease in other assets of $1.3 million.

- Changes in liabilities for fiscal year 2006 used cash from operations of $2.2 million. This change is due primarily to the decreases in accounts payable, accrued expenses, and accrued subcontracting costs of $1.8 million and the decrease in deferred revenue of $0.4 million. The decreases in accounts payable, accrued expenses, and accrued subcontracting costs is due to decreased mission activity for shuttle related projects. The decrease in deferred revenue is primarily due to the completion of the Japanese Experiment Thermal Incubator Service contract during fiscal year 2006. For fiscal year 2005 changes in liabilities used cash in operations of $1.8 million. This change is due primarily to the decreases in accounts payable and accrued expenses of $1.5 million which includes an increase due to the recording of $0.5 million related to the Lloyd s settlement and the decrease in deferred revenue of $5.4 million.

Cash Flows From Investing Activities. For the years ended June 30, 2007 Restated, 2006, and 2005, cash flows provided by (used in) investing activities were ($1.1) million, ($1.1) million, and $17.7 million, respectively. The significant items affecting the differences in cash flows from investing activities in fiscal year 2007 compared to fiscal year 2006 and fiscal year 2006 compared to fiscal year 2005 are as follows:

Fiscal Year 2007 Compared to Fiscal Year 2006. For the fiscal year 2007 compared to fiscal year 2006, the significant items affecting cash provided by (used in) investing activities were:

- Property and equipment purchases of $0.6 million for fiscal 2007 as compared to $2.1 million for fiscal year 2006. This reduction is a continuation of our efforts to reduce capital expenditures.

- Fiscal year 2007 cash flows from investing activities included a $0.5 million payment to Lloyd s of London as a result of our claim dismissal against NASA for the loss of our RDM.

- Fiscal year 2006 cash flows from investing activities included a decrease in cash securing credit facilities of $0.1 million for fiscal year 2006.

Fiscal Year 2006 Compared to Fiscal Year 2005. For the fiscal year 2006 compared to fiscal year 2005, the significant items affecting cash provided by (used in) investing activities were:

- Property and equipment purchases of $2.1 million for fiscal 2006 as compared to $3.4 million for fiscal year 2005. For fiscal year 2005 cash flows from investing activities included the purchase of the Houston Headquarters facility that was subsequently sold and leased back from the new landlord.

- Fiscal year 2005 cash flows from investing activities were generated from the sale of short-term investments of $6.6 million as compared to no sales of such short-term investments for the fiscal year 2006.

- Fiscal year 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 RDM.

- Fiscal year 2005 cash flows from investing activities included $6.8 million from the sale of our Cape Canaveral and Headquarters facilities.

- Fiscal year 2006 cash flows from investing activities included a decrease of $1.0 million in cash securing credit facilities as compared to an increase in restricted cash of $0.5 million for fiscal year 2005.

Cash Flows From Financing Activities. For the years ended June 30, 2007, 2006, and 2005, cash flows used in financing activities were $1.5 million, $3.9 million, and $3.7 million, respectively. The significant items affecting the differences in cash flows from financing activities in fiscal year 2007 compared to fiscal year 2006 and fiscal year 2006 compared to fiscal year 2005 are as follows:

Fiscal Year 2007 Compared to Fiscal Year 2006. For the fiscal year 2007 compared to fiscal year 2006, the significant items affecting cash used in financing activities were:

- Fiscal year 2007 had a payment of $1.6 million for our mortgage loan as compared to payments of $2.1 million for fiscal year 2006. This decrease is due to the maturity of the term note in January 2007 and complete payment in December 2006.

- Fiscal year 2006 had an increase of $1.9 million from the refinancing of our subordinated convertible notes as compared to fiscal year 2007.

Fiscal Year 2006 Compared to Fiscal Year 2005. For the fiscal year 2006 compared to fiscal year 2005, the significant items affecting cash used in financing activities were:

- Fiscal year 2005 had net repayments of $1.4 million in principal under our revolving credit facility as compared to no borrowings for fiscal year 2006.

- Fiscal year 2006 had a payment of $2.1 million for our mortgage loan as compared to payments of $1.9 million for fiscal year 2005. This increase is due to the term of the mortgage loan approaching its maturity date of January 2007.

- Fiscal year 2006 had an increase of $1.5 million from the refinancing of our subordinated convertible notes as compared to fiscal year 2005.

Liquidity. We continue to focus our efforts on improving 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. 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 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 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 acre parcel for future development or sale. The annual rental for the first year of this lease is approximately $0.3 million and gradually increases through the tenth year of the lease to approximately $0.4 million.

Our cash and restricted cash on hand was approximately $16.0 million as of June 30, 2007. Included in the $16.0 million is $3.1 million for in-flight insurance on STS-118 that was paid in July 2007. Additionally, $6.3 million is restricted cash for a construction contract to expand one of our processing facilities. Our capital requirements for continuing operations consist of our general working capital needs, scheduled principal and interest payments on our debt obligations, certain contractual commitments, and capital expenditures. This includes short-term capital to finance continuing operations at the end of 2007, and long-term capital to finance our growth. Our capital resources which are solely comprised of cash reserves and cash generated from operations may not be sufficient to meet these capital requirements. While we believe that the exchange offer would help address our foreseeable refinancing risk related to the Junior Notes that mature in October 2007, there is no assurance that the exchange offer will be sufficient to alleviate our liquidity issues due to a lack of capital resources. In addition, with the conclusion of STS-118 in August 2007, we expect to have a material decrease in our revenue from our Flight Services business, which has accounted for over 65% of our consolidated revenue during fiscal year 2007. Moreover, our revolving credit line expired on February 11, 2007. As a result, in order to continue to fund our current operations, we will need additional capital. No assurance can be given that we will be able to obtain a new source of capital on terms that are acceptable to us. If we are unable to obtain new capital, we may be forced to subject ourselves to bankruptcy, reorganization, liquidation, dissolution or similar proceeding.

If we are unable to complete the Exchange Offer for any reason, we may restructure through a bankruptcy proceeding. Our ability to restructure in bankruptcy is subject to numerous risks, including the following:

- We may lose customers in bankruptcy because our services are critical to our customers businesses
- The costs of bankruptcy will significantly exceed the costs of an out-of-court transaction
- We may be unable to arrange debtor-in-possession financing or otherwise finance our operations during bankruptcy

Our capital requirements for continuing operations consist of our general working capital needs, scheduled principal and interest payments on our debt obligations, certain contractual commitments, and capital expenditures. This includes short-term capital to finance continuing operations at the end of 2007, and long-term capital to finance our growth. Our capital resources which are solely comprised of cash reserves and cash generated from operations, may not be sufficient to meet these capital requirements. While we believe that the exchange offer would help address our foreseeable refinancing risk related to the Junior Notes that mature in October 2007, there is no assurance that the exchange offer will be sufficient to alleviate our liquidity issues due to a lack of capital resources.

Our contractual obligations as of June 30, 2007 are as follows (in thousands):

Contractual Obligations	At June 30, 2007	Fiscal Year 2008	Fiscal Year 2009	Fiscal Year 2010	Fiscal Year 2011	Fiscal Year 2012	Thereafter
Short-term Debt	$ 10,306	$ 10,306	$		$	$	$
Long-term Debt	52,944				52,944		
ICC/VCC	1,389	1,389					
Operating leases(1)	12,579	2,662	970	982	769	547	6,649
Total Contractual Cash Obligations	$ 77,218	$ 14,357	$ 970	$ 982	$ 53,713	$ 547	$ 6,649

(1) For fiscal years 2008 and 2009 we expect to receive net payments of approximately $0.4 million and $0.1 million, respectively, for subleases. Additionally, we agreed to terminate out ICC and VCC leases (see Note 28) in FY2008.

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. Risk See 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 equitable adjustments on our fixed-price contracts due to launch delays. 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 Provided	Contract Type	Method of Revenue Recognition
Flight Services	Commercial Space Habitat Modules,	Firm Fixed Price	Percentage-of-completion based on costs incurred

	Integration & Operations Support Services		
Astrotech	Payload Processing Facilities	Firm Fixed Price Mission Specific	Ratably, over the occupancy period of a satellite within the facility from arrival through launch
		Firm Fixed Price Guaranteed Number of Missions	For multi-year contract payments recognized ratably over the contract period
Government Services	Configuration Management, Engineering Services	Cost Reimbursable Award/Fixed Fee	Reimbursable costs incurred plus award/fixed fee

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 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.

RESULTS OF OPERATIONS

Results of Operations for the Years Ended June 30, 2007, 2006, and 2005

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, 2007, 2006, and 2005. 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 2007, 2006, and 2005 were 12,919,506, and 12,743,533, and 14,190,281, respectively.

We had net income (loss) of ($16,292,000) or ($1.26) per diluted share on revenues of $52,762,000 for our 2007 fiscal year compared to ($12,397,000) or ($0.97) per diluted share on revenues of $50,746,000 for 2006 and $5,249,000 or $0.37 per diluted share on revenues of $59,401,000 for 2005.

Revenue. Our revenue for the twelve months ended June 30, 2007, 2006, and 2005 was generated primarily from the Lockheed Martin Cargo Mission Contract and contracts with related commercial customers in the Flight Services business unit; the PI&C contract in our Government Services business unit; and our contracts with Lockheed Martin, Boeing, NASA, and other commercial satellite providers in our Astrotech business unit.

During fiscal year 2007, our Flight Services business unit supported NASA s spaceflight activities on both the STS-116 and 118 missions. Our Flight Services business unit prepared a cargo carrier for shuttle mission STS-118, the External Stowage Platform 3 (ESP3) that was deployed and permanently mounted to the International Space Station during the August 2007 mission. For both STS-116 and 118 missions under the Cargo Mission Contract, we provided our pressurized single module and unpressurized integrated cargo carrier for transport of critical cargo and orbital replacement units to and from the International Space Station.

During the three and twelve months ended June 30, 2007, deferred revenue decreased by $0.2 million and $0.2 million, respectively, as we recognized revenue on contracts where milestone payments had been received in prior periods. We expect further reduction of deferred revenue due to customer prepayments 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 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-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 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 and results of operations for our SMI segment.

The following tables provide summary financial data regarding our consolidated and segmented results of operations for our 2007, 2006, and 2005 fiscal years, respectively (in millions):

Fiscal Year Ended June 30, 2007

	Flight Services Business Unit	Astrotech Business Unit	Government Services Business Unit	Other	Total
Income (loss) from operations before charges	$ 4.9	$ 2.0	$ 0.9	$ (8.0)	$ (0.2)
Asset impairment charge	(12.5)			(0.1)	(12.6)
Operating income (loss)	(7.6)	2.0	0.9	(8.1)	(12.8)
Other income/expense, net		0.1		0.6	0.7
Interest expense				(4.3)	(4.3)
Pre-tax income (loss)	(7.6)	2.1	0.9	(11.8)	(16.4)
Income tax benefit				0.1	0.1
Net income (loss)	$ (7.6)	$ 2.1	$ 0.9	$ (11.7)	$ (16.3)

Fiscal Year Ended June 30, 2006

	Flight Services Business Unit	Astrotech Business Unit	Government Services Business Unit	Other	Total
Income (loss) from operations before charges	$ 4.7	$ 2.5	$ 0.5	$ (8.6)	$ (0.9)
Asset impairment charge	(6.3)				(6.3)
Operating income (loss)	(1.6)	2.5	0.5	(8.6)	(7.2)
Other income/expense, net				0.3	0.3
Interest expense				(5.5)	(5.5)
Pre-tax income (loss)	(1.6)	2.5	0.5	(13.8)	(12.4)
Income tax expense					
Net income (loss)	$ (1.6)	$ 2.5	$ 0.5	$ (13.8)	$ (12.4)

Fiscal Year Ended June 30, 2005

	Flight Services Business Unit	Astrotech Business Unit	Government Services Business Unit	Other	Total
Income (loss) from operations before charges	$ 7.6	$ 2.1	$ 0.9	$ (7.8)	$ 2.8

Non recurring item net recovery		7.7								7.7
Operating income (loss)		15.3		2.1		0.9		(7.8)		10.5
Other Income/expense, net				0.1				0.2		0.3
Interest expense								(5.7)		(5.7)
Pre-tax income (loss)		15.3		2.2		0.9		(13.3)		5.1
Income tax benefit								0.1		0.1
Net income (loss)	$	15.3	$	2.2	$	0.9	$	(13.2)	$	5.2

Operating Income (Loss). Operating income (loss) was ($12.8) million in fiscal year 2007, compared to ($7.2) million and $10.5 million for fiscal years 2006 and 2005, respectively. The following summarizes the activity in each of our operating segments:

SPACEHAB Flight Services

Operating income (loss) for our Flight Services business unit was ($7.6) million for fiscal year 2007, compared to ($1.6) million and $15.3 million for fiscal years 2006 and 2005, respectively. Operating loss for 2007 included an asset impairment charge of $12.5 million for the write down of our flight unit 2 module and other flight based assets due to our analysis of the remaining space shuttle flights and NASA s potential need for our module. Operating loss for 2006 included an asset impairment charge of $6.3 million for the write down of our flight unit 3 module due to our analysis of the remaining space shuttle flights and NASA s potential need for our module. Operating income for fiscal year 2005 includes an $8.2 million payment from NASA for the loss of our RDM in the Space Shuttle *Columbia* accident. It also includes $0.5 million expense for our settlement with Lloyd s (see Item 3 Legal Proceedings for more details). Operating income for 2007 included general and administrative expense of $1.2 million and depreciation and amortization expense of $3.6 million as compared to general and administrative expenses of $1.0 million and $0.5 million and depreciation and amortization expense of $3.2 million and $2.8 million for fiscal years 2006 and 2005, respectively. Please see Results of Operations for the Years Ended June 30, 2007, 2006, and 2005 Other for a consolidated discussion of general and administrative expense and depreciation and amortization expense.

Flight Services Business Unit Results of Operations for the Fiscal Year Ended June 30, 2007 as Compared to the Fiscal Year Ended June 30, 2006

The Flight Services business unit s operating income before charges increased by $0.2 million from fiscal year 2006 to fiscal year 2007. The following summarizes significant changes for our fiscal year ended June 30, 2007 as compared to our fiscal year ended June 30, 2006:

Revenue increases of $1.1 million, consisting of the following

- Increase in revenue from STS-116 and STS-118 under the CMC with Lockheed Martin of $9.4 million due to increased mission activities and change orders due to the launch of STS-116 in December 2006 and the launch of STS-118 in August 2007.

- Decrease in revenue from External Stowage Platform 2 (ESP2) of $1.0 million due to the launch of STS-114 in July 2005.

- Decrease in revenue from STS-121 of $5.3 million due to the launch of STS-121 in July 2006.

- Decrease in revenue from the JETIS contract of $1.0 due to the contract being completed during fiscal year 2006.

- Decrease in revenue from the Concept Exploration and Refinement (CE&R) contract of $0.4 million due to the contract being completed during fiscal year 2006.

- Other contract revenue decrease of $0.6 million mainly due to our contract with Astrium to provide a new ICC pallet to replace ESP2 that was permanently affixed to the space station during the STS-114 mission in July 2005.

Cost of Revenue decreases of $0.9 million, consisting of the following:

- Increase in cost of revenue for STS-116 and STS-118 under the CMC with Lockheed Martin, other than depreciation expense, of $5.5 million due to increased mission activities due to the launch of STS-116 in December 2006 and the scheduled launch of STS-118 in August 2007.

- Decrease in cost of revenue of $4.4 million for STS-121 due to the launch of STS-121 in July 2006.

- Decrease in cost of revenue of $0.8 million from External Stowage Platform 2 of $0.3 million due to the launch of STS-114 in July 2005.

- Decrease in cost of revenue for the JETIS contract of $0.5 million due to the contract being completed during fiscal year 2006.

- Decrease in cost of revenue from the Concept Exploration and Refinement (CE&R) contract of $0.2 million due to the contract being completed during fiscal year 2006.

- Other cost of revenue decrease of $0.5 million mainly due to our contract with Astrium to provide a new ICC pallet to replace ESP2 that was permanently affixed to the space station during the STS-114 mission in July 2005.

Included in the revenue decreases is the reduction in workforce for our Flight Services business unit in January 2007. This reduction resulted in a net decrease in personnel and related costs of $1.3 million for the last six months of fiscal year 2007.

Our Flight Services business unit is currently supporting deintegration requirements for shuttle mission STS-118. The Flight Services business unit completed cargo services on the STS-121 mission that launched during the first part of fiscal year 2007. For the space shuttle STS-121 mission, we provided our non-deployable ICC to NASA for transport of several critical International Space Station orbital replacement unit spares. For both shuttle missions STS-116 and 118, we provided our pressurized Logistics Single Module and our unpressurized ICC for transport of critical cargo and orbital replacement units to and from the ISS. As previously described, the Research and Logistics Mission Support contract expired January 31, 2004 and support for shuttle missions STS-116 and 118 was continued under a subcontract agreement to Lockheed Martin effective February 1, 2004.

Flight Services Business Unit Results of Operations for the Fiscal Year Ended June 30, 2006 as Compared to the Fiscal Year Ended June 30, 2005

The Flight Services business unit s operating income before charges decreased by $2.9 million from fiscal year 2005 to fiscal year 2006. The following summarizes significant changes for our fiscal year ended June 30, 2006 as compared to our fiscal year ended June 30, 2005:

Revenue decreases of $8.8 million, consisting of the following:

- Decrease in revenue from the Lockheed Martin Cargo Mission Contract of $1.5 million. This decrease is a result of a(n):

- Decrease in revenue for STS-116 by $2.4 million due to the slip of the launch date from April 2006 to December 2006. During fiscal year 2005 we were performing the contract with a projected launch date of April 2006. During the first quarter of fiscal year 2006, the launch date was slipped to November 2006 and eventually to December 2006. Therefore, for most of fiscal year 2006, we were working under the equitable adjustment clause of the contract.

- Decrease in revenue for STS-121 by $1.3 million due to the slip of the launch date from September 2005 to July 2006. During fiscal year 2005, we were performing the contract with a projected launch date of September 2005. During the first quarter of fiscal year 2006, the launch date was slipped to May 2006 and eventually slipped to July 2006. Therefore, for most of fiscal year 2006 we were working under the equitable adjustment clause of the contract.

- Increase in revenue for STS-118 by $2.2 million due to additional project work being performed on the ESP3 portion of the mission during fiscal year 2006 as compared to fiscal year 2005. Due to the successful return to flight missions STS-114 and STS-121, the Space Shuttle Program has an aggressive schedule to complete the assembly of the International Space Station. Therefore, contracted project work increased on STS-118.

- Decrease in revenue from the Concept Exploration and Refinement (CE&R) contract of $1.2 million that was started first quarter fiscal year 2005 and was completed first quarter fiscal year 2006.

• Decrease in revenue from the External Stowage Platform 2 (ESP2) contract revenue of $5.1 million due to the successful launch in July 2005 aboard STS-114.

• Decrease in revenue from the Japanese Experiment Thermal Incubator Service of $1.6 million due to the completion of the contract in April 2006.

• The various other contract revenue increased $0.6 million mainly due to our contract with Astrium to provide a new ICC pallet to replace the ESP2 that was permanently affixed to the space station during the STS-114 mission in July 2005.

Cost of Revenue decrease of $6.2 million, consisting of the following:

• Decrease in cost of revenue from the Lockheed Martin Cargo Mission Contract of $0.8 million. This decrease is a result of a(n):

• Increase in cost of revenue for STS-116 by $0.3 million due to the slip of the launch date from April 2006 to December 2006. During fiscal year 2005 we were performing the contract with a projected launch date of April 2006. During the first quarter of fiscal year 2006, the launch date was slipped to November 2006 and eventually to December 2006. Therefore, for most of fiscal year 2006 we were working under the equitable adjustment clause of the contract but we were maintaining the workforce for the entire period that is required to perform the contract as though there were no launch slips. Also, due to the change in the depreciable lives of our flight assets, direct depreciation increased by $1.1 million from fiscal year 2005 to fiscal year 2006.

- Decrease in cost of revenue for STS-121 by $1.5 million due to the slip of the launch date from September 2005 to July 2006. During fiscal year 2005 we were performing the contract with a projected launch date of September 2005. During the first quarter of fiscal year 2006, the launch date was slipped to May 2006 and eventually slipped to July 2006. Therefore, for most of fiscal year 2006 we were working under the equitable adjustment clause of the contract. Before the launch slip during the first quarter of fiscal year 2006, the majority of the deliverables for this flight were completed and delivered.

- Increase in cost of revenue for STS-118 by $0.4 million due to more project work being performed on the ESP3 portion of the mission during fiscal year 2006 as compared to fiscal year 2005. Due to the successful return to flight missions STS-114 and STS-121, the Space Shuttle Program has an aggressive schedule to complete the assembly of the International Space Station.

- Decrease in cost of revenue of $4.1 million for ESP2 that launched on STS-114 in July 2005.

- Decrease in CE&R cost of revenue of $0.9 million that was started in the first quarter of fiscal year 2005 and completed in the first quarter of fiscal year 2006.

- Decrease in cost of revenue from the Japanese Experiment Thermal Incubator Service of $0.8 million due to the completion of the contract in April 2006.

- Other cost of revenue increase of $0.4 million mainly due to our contract with Astrium to provide a new ICC pallet to replace ESP2 that was permanently affixed to the space station during the STS-114 mission in July 2005.

- Increase in rent expense of $0.3 million from fiscal year 2005 to fiscal year 2006 due to the sale-leaseback of our payload processing facility in fourth quarter fiscal year 2005. This increase is offset by lower operating costs for the facility during fiscal year 2006 as compared to fiscal year 2005.

Astrotech Space Operations

Operating income for our Astrotech business unit was $2.0 million for fiscal year 2007, compared to $2.5 million and $2.1 million for fiscal years 2006 and 2005, respectively. Operating income for 2007 included selling, general and administrative expense of $0.3 million and depreciation and amortization expense of $2.1 million as compared to selling, general and administrative expense of $0.3 million and $0.3 million and depreciation and amortization expense of $2.1 million and $2.1 million for fiscal years 2006 and 2005, respectively. Please see Results of Operations for the Years Ended June 30, 2007, 2006 and 2005 Other for a consolidated discussion of selling, general and administrative expense and depreciation and amortization expense.

Astrotech Business Unit Operating Results for Fiscal Year ended June 30, 2007 as Compared to the Fiscal Year Ended June 30, 2006

Our Astrotech business unit s operating income before charges decreased by $0.5 million from fiscal year 2006 to fiscal year 2007. The following summarizes significant changes for our fiscal year ended June 30, 2007 as compared to our fiscal year ended June 30, 2006:

Revenue increases of $1.1 million, consisting of the following:

- Increase in revenue of $1.3 million from a new contract to design a satellite processing facility.

- Increase in revenue of $1.6 million due to three different satellites in our Florida facility, one of which was a carry-over from fiscal year 2006, for all of or portions of fiscal year 2007. Whereas, for the same period last fiscal year, there were only two satellites in our Florida facility.

- Increase in other revenue of $0.5 million mainly due to mission unique services requested by the customer.

- Astrotech supported three satellite launches at its Sea Launch facility during fiscal year 2007 as compared to four for fiscal year 2006 which resulted in a decrease in revenue of $0.5 million. On January 30, 2007 Sea Launch experienced a launch failure resulting in the loss of a satellite and damage to the floating launch platform. A full inspection, evaluation, and repair operations of the damage incurred and preliminary reports indicate that Sea Launch will return to operations in October 2007. We are paid under our contract with Sea Launch upon launch of each mission; therefore, anticipated revenues have been delayed until the resumption of normal operations.

- Decrease in revenue of $0.5 million at our Vandenberg facility due to the launch delay of the Calipso/Cloudsat mission during fiscal year 2006 which resulted in increased revenue during fiscal year 2006 as compared to fiscal year 2007.

- Decrease in revenue of $0.3 million due to the reduction of revenue on our Lockheed Martin guaranteed missions contract for two future missions that will be processed for Boeing on Atlas launch vehicles partially offset by one Atlas mission (STP-1) processed at the Titusville facility that was contracted directly with Boeing.

- Decrease in revenue from our Lockheed Martin guaranteed contract of $1.0 million due to the guarantee being reduced this calendar year as compared to the same period last fiscal year.

Cost of revenue from our Astrotech business unit increased for the fiscal year 2007 as compared to fiscal year ended 2006 by $1.6 million. The increase is mainly due to higher professional services of $0.4 million for the new contract to design a satellite processing facility. Additionally, mission specific expenses increased by $1.0 million due to increased mission support services in Florida and Vandenberg. Also, although Astrotech s labor force did not change significantly, they had higher labor and related costs of $0.2 million in fiscal year 2007 as compared to fiscal year 2006 due to cost of living increases.

Astrotech Business Unit Operating Results for Fiscal Year ended June 30, 2006 as Compared to the Fiscal Year Ended June 30, 2005

Our Astrotech business unit s operating income before charges increased by $0.4 million from fiscal year 2005 to fiscal year 2006. The following summarizes significant changes for our fiscal year ended June 30, 2006 as compared to our fiscal year ended June 30, 2005:

Revenue from our ASO business unit increased from fiscal year 2005 to fiscal year 2006 by $0.7 million. This increase is primarily attributable to ASO receiving revenue for one additional guaranteed mission for calendar year 2006 under our Lockheed Martin satellite processing contract in the amount of $0.9 million. This increase is partially offset by a decrease of $0.2 million of revenue due to satellite launch schedules.

Cost of revenue from our Astrotech business unit increased for the fiscal year 2006 as compared to fiscal year ended 2005 by $0.2 million. The increase is mainly due to higher utility costs due to the increase in fuel costs during fiscal year 2006 as compared to fiscal year 2005. Also, although Astrotech s labor force did not change significantly, they had higher labor and related costs in fiscal year 2006 due to cost of living increases. Costs did not increase consistent with revenue due to the $0.9 million guaranteed mission payments for which there was no incremental cost.

***SPACEHAB* Government Services**

Operating income for our Government Services business unit was $0.9 million for fiscal year 2007, compared to $0.5 million and $0.9 million for fiscal years 2006 and 2005, respectively. Operating income for 2007 included selling, general and administrative expense of $0.3 million and depreciation and amortization expense of zero as compared to selling, general and administrative expense of $0.4 and $0.4 and depreciation and amortization expense of zero and $0.1 million for fiscal years 2006 and 2005, respectively. Please see Results of Operations for the Years Ended June 30, 2007, 2006 and 2005 Other for a consolidated discussion of selling, general and administrative expense and depreciation and amortization expense.

Government Services Business Unit Results of Operations for Fiscal year ended June 30, 2007 as Compared to the Fiscal Year Ended June 30, 2006

Our Government Services business unit s operating income before charges increased by $0.4 million from fiscal year 2006 to fiscal year 2007. The following summarizes significant changes for our fiscal year ended June 30, 2007 as compared to our fiscal year ended June 30, 2006:

Revenue increases of $0.4 million, consisting of the following:

- Increase in revenue from a new contract with USA for support of the Constellation Program of $0.7 million.
- Increase in revenue from the sale of our Destiny module to the Seattle Space Museum in the amount of $0.3 million during fiscal year 2007.
- Decrease in revenue from our subcontract with ARES on the PI&C contract of $0.4 million. This decrease is due to a reduction in our statement of work associated with the contract.
- Decrease in other revenue of $0.2 million primarily due to the contract closeout of our contract with Shanghai Scienceland in fiscal year 2006.

Cost of revenue increase of $0.0 million, consisting of the following:

- Increase in cost of revenue of $0.6 million in our Government Services business unit due to the startup of our contract with USA on the Constellation Program.
- Decrease in cost of revenue of $0.3 million for the contract closeout of our contract with Shanghai Scienceland.
- Decrease in cost of revenue from our subcontract with ARES on the PI&C contract of $0.3 million. This decrease is due to a reduction in our statement of work associated with the contract.

Government Services Business Unit Results of Operations for Fiscal year ended June 30, 2006 as Compared to the Fiscal Year Ended June 30, 2005

Our Government Services business unit s operating income before charges decreased by $0.4 million from fiscal year 2005 to fiscal year 2006. The following summarizes significant changes for our fiscal year ended June 30, 2006 as compared to our fiscal year ended June 30, 2005:

Revenue decreased by $0.6 million for our fiscal year ended June 30, 2006 as compared to our fiscal year ended June 30, 2005 primarily as a result of:

The decrease in revenue at the Government Services business segment is primarily due to the delivery of the intravehicular activity (IVA) handrails in the third quarter of fiscal year 2005. The following summarizes the significant items:

- Decrease in revenue of $0.5 million due to the delivery of the IVA handrails in the second quarter of fiscal year 2005.
- Increase in revenue of $0.2 million for the contract closeout of our contract with Shanghai Scienceland.
- Decrease in other revenue of $0.3 million.

The decrease in cost of revenue by $0.2 million is primarily due to the delivery of the IVA handrails in the third quarter of fiscal year 2005, which was partially offset by the costs of revenue associated with the closeout of the Shanghai Scienceland project for the period ending June 30, 2006.

Other

Other operating loss was ($8.1) million for fiscal year 2007, compared to ($8.6) million and ($7.8) million for fiscal years 2006 and 2005, respectively. The $8.1 million operating loss for fiscal year 2007 relates to primarily selling, general and administrative expenses and depreciation and amortization expenses which were incurred at the corporate level and an impairment charge of $0.1 million attributable to our non-cash write-down of our investment in Applied Astronautics Corporation. The operating loss for fiscal 2006 and 2005 relates primarily to selling, general, and administrative expenses and depreciation and amortization expenses which were incurred at the corporate level. Also included in other is the revenues and expenses associated with Space Media, Inc. which included the operations of the Space Store, LLC which was sold during fiscal year 2007.

Consolidated selling, general and administrative expenses, other than the asset impairment charges for our shuttle based assets and our investment in Applied Astronautics Corporation, and research and development were $10.7 million in fiscal year 2007, compared to $11.1 million and $9.5 million in 2006 and 2005, respectively. The $0.4 million decrease for fiscal year 2006 to 2007 is principally due to:

- Increase in our Flight Services business segment labor and related costs of $0.1 million related to less direct contract support as compared to fiscal year 2006.
- Increase of $0.4 million in research and development costs primarily related to our efforts on our micro electro mechanical system program.
- Increase of $0.1 million in travel expenses due to increased efforts in business development activities.
- Increase in audit fees of $0.2 million due to an increase in audit and tax for fiscal year 2007 as compared to fiscal year 2006.
- Decrease in corporate level labor and related costs of $0.1 million. The decrease is primarily due our staff reductions in January 2007 at the corporate level.
- Decrease of $0.5 million in consulting expenses primarily due to expenses related to market studies for space commerce and our on-going cost reduction efforts.
- Decrease of $0.3 million in legal expenses primarily due to us dropping our claims against NASA related to the loss of our RDM (see Item 3 Legal Proceedings).

- Decrease in selling, general, and administrative expenses of $0.2 million for the Space Store, LLC due to the selling of the business in November 2006.

- Decrease in our Government Services business segment labor and associated facilities costs of $0.1 million due to staff reduction during fiscal year 2007.

The $1.6 million increase for fiscal year 2005 to 2006 is principally due to:

- Increase in our Flight Services business segment labor and related costs of $0.6 million related to an increase in business development and bid and proposal activities in fiscal year 2006 and less direct contract support as compared to fiscal year 2005. The bid and proposal costs were related to our response to NASA s request for proposal for the Commercial Orbital Transportation Services contract.

- Increase of $0.3 million in research and development costs related to the efforts of our Apex program.

- Increase in corporate level labor and related costs of $0.2 million. The increase is primarily due to a rise in health care and insurance costs.

- Increase of $0.4 million in consulting expenses primarily due to expenses related to market studies for space commerce.

- Increase of $0.3 million in legal expenses primarily related to our claims against NASA for the loss of our RDM.

- Decrease in corporate depreciation expense of $0.2 million due to assets reaching the end of their useful lives during fiscal year 2006.

Consolidated depreciation and amortization expenses were $5.9 million in fiscal year 2007 compared to $5.6 million and $5.2 million in 2006 and 2005, respectively. The $0.3 million increase in fiscal year 2006 compared to 2007 is primarily due to an increase in depreciation expense of $0.6 million resulting from the change in depreciable lives during the second quarter of fiscal year 2006 of our flight assets based on NASA s direction to retire the space shuttle fleet at the end of 2010. This increase is offset by a decrease in other depreciation expense of $0.3 million primarily due to a portion of fixed assets reaching the end of their useful lives.

The $0.4 million increase in fiscal year 2005 compared to 2006 is primarily due to an increase in depreciation expense of $0.6 million resulting from the change in depreciable lives of our flight assets based on NASA s direction to retire the space shuttle fleet at the end of 2010. This increase is offset by a decrease in other depreciation expense of $0.4 million primarily due to a portion of fixed assets reaching the end of their useful lives and the sale leaseback of our Florida payload facility and corporate headquarters during the fourth quarter of fiscal year 2005.

Interest Expense. Interest expense totaled $4.3 million for fiscal year 2007, compared with $5.5 million and $5.7 million for 2006 and 2005, respectively. The $1.2 million decrease for 2007 as compared to 2006 is related to:

- Decrease in interest expense of $1.1 million due to the exchange of the 8% notes for the 5.5% notes during fiscal year 2006 therefore, for all of fiscal year 2007, we had the reduced interest expense for the $52.9 million of 5.5% convertible notes.

- Decrease of $0.1 million resulting from the mortgage loan on our Astrotech facility reaching maturity in January 2007 with the final payment being made in December 2006.

The $0.2 million decrease for 2006 as compared to 2005 is related to:

- An increase in interest expense due to the write-off of $0.6 million debt placement costs due to the exchange of $52.9 million of our 8% notes for $52.9 million of 5.5% notes.

- Decrease in interest expense of $0.7 million due to the exchange of the 8% notes for the 5.5% notes during fiscal year 2006.

- Decrease of $0.1 million resulting from the refinancing of our Astrotech spacecraft processing facility and the reduced remaining term of the mortgage loan.

Income Tax Provision (Benefit). For fiscal year 2007 we recorded a tax benefit of $0.07 million. We recorded an income tax expense for fiscal year 2006 of $0.03 million, while we recorded an income tax benefit for fiscal year 2005 of $0.1 million. As of June 30, 2007, we had approximately $38.3 million of available net operating loss carryforwards expiring between 2020 and 2025 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, 2007, 2006 and 2005.

Market Risk

Our primary exposure to market risk relates to interest rates. 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 June 30, 2007.

Item 7A. Quantitative and Qualitative Disclosures about Market Risk.

Our primary exposure to market risk relates to interest rates. 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.

Item 8. Financial Statements and Supplementary Data.

Report of Independent Registered Public Accounting Firm

The Board of Directors and Stockholders

SPACEHAB, Incorporated and Subsidiaries:

We have audited the accompanying consolidated balance sheet of SPACEHAB, Incorporated and subsidiaries (the Company) as of June 30, 2007, and the related consolidated statements of operations, stockholders equity (deficit) and comprehensive income (loss) and cash flows for the year then ended. These consolidated financial statements are the responsibility of the Company s management. Our responsibility is to express an opinion on these consolidated financial statements based on our audit.

We conducted our audit in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. The Company is not required to have, nor were we engaged to perform an audit of its internal control over financial reporting. Our audit included consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Company s internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used, and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the consolidated financial position of the Company as of June 30, 2007, and the results of their operations and their cash flows for the year then ended, in conformity with accounting principles generally accepted in the United States of America.

The accompanying consolidated financial statements have been prepared assuming the Company will continue as a going concern. As discussed in Note 1 to the consolidated financial statements, the Company has sustained recurring losses and negative cash flow from operations which raises substantial doubt about its ability to continue as a going concern. Management s plans in regard to these matters are also described in Note 1. The consolidated financial statements do not include any adjustment that might result from the outcome of this uncertainty.

/s/PMB HELIN DONOVAN LLP

Houston, Texas

September 5, 2007

except for Note 24 as to which the date is February 13, 2008

Report of Independent Registered Public Accounting Firm

The Board of Directors and Stockholders

SPACEHAB, Incorporated and Subsidiaries:

We have audited the accompanying consolidated balance sheet of SPACEHAB, Incorporated and subsidiaries (the Company) as of June 30, 2006, and the related consolidated statements of operations, stockholders equity, and comprehensive income (loss) and cash flows for each of the two years in the period ended June 30, 2006. These consolidated financial statements are the responsibility of the Company s management. Our responsibility is to express an opinion on these consolidated financial statements based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. The Company is not required to have, nor were we engaged to perform an audit of its internal control over financial reporting. Our audits included consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Company s internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used, and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the consolidated financial position of the Company as of June 30, 2006, and the results of their operations and their cash flows for each of the two years in the period ended June 30, 2006 in conformity with accounting principles generally accepted in the United States of America.

/s/GRANT THORNTON LLP

Houston, Texas

August 31, 2006

SPACEHAB, INCORPORATED AND SUBSIDIARIES

Consolidated Balance Sheets

(In thousands, except share data)

	June 30, 2007 Restated		June 30, 2006	
Assets				
Current assets				
Cash and cash equivalents	$	9,724	$	6,317
Accounts receivable, net		8,224		11,379
Inventory		695		2,369
Short term note receivable, net		95		
Prepaid expenses and other current assets		906		610
Total current assets		19,644		20,675
Property and equipment				
Flight assets		49,210		49,799
Capital improvements in progress		62		1,612
Payload processing facilities		42,588		42,571
Furniture, fixtures, equipment and leasehold improvements		18,869		18,275
		110,729		112,257
Less accumulated depreciation and amortization		(66,845)		(50,620)
Property and equipment, net		43,884		61,637
Restricted cash		6,282		
Deferred financing costs, net		1,596		2,124
Long term note receivable, net		178		
Other assets, net		891		1,014
Total assets	$	72,475	$	85,450
Liabilities and Stockholders Equity (Deficit)				
Current liabilities				
Convertible subordinated notes payable 8.0%	$	10,306	$	
Mortgage loan payable, current portion				1,636
Accounts payable		1,494		1,598
Accounts payable- Astrium		2,955		3,386
Accrued interest		789		804
Accrued expenses		2,056		2,394
Accrued subcontracting services		3,669		6,562
Deferred gains on sale of buildings		221		221
Customer deposit		3,106		
Deferred revenue, current portion		1,153		1,321
Total current liabilities		25,749		17,922
Advances on construction contract		5,722		
Accrued contract costs and other		39		96
Deferred gains on sale of buildings		1,152		1,373
Convertible subordinated notes payable 8.0%				10,306
Senior convertible subordinated notes payable 5.5%		52,944		52,944
Total liabilities		85,606		82,641
Commitments and contingencies				
Stockholders equity (deficit)				
Preferred stock, no par value, convertible, authorized 2,500,000 shares, issued and outstanding 1,333,334 shares, (liquidation preference of $12,000)		11,892		11,892
		84,122		84,030

Common stock, no par value, 70,000,000 shares authorized 13,143,296 and 12,976,264 shares issued, respectively				
Treasury stock, 116,100 shares at cost		(117)		(117)
Additional paid-in capital		544		284
Accumulated deficit		(109,572)		(93,280)
Total stockholders equity (deficit)		(13,131)		2,809
Total liabilities and stockholders equity	$	72,475	$	85,450

See accompanying notes to consolidated financial statements.

SPACEHAB, INCORPORATED AND SUBSIDIARIES

Audited Consolidated Statements of Operations

(In thousands, except share data)

	Twelve Months Ended June 30, 2007	2006	2005
Revenue	$ 52,762	$ 50,746	$ 59,401
Costs of revenue	40,638	40,572	47,158
Impairment of flight asset	10,391	6,283	
Gross profit	1,733	3,891	12,243
Operating expenses			
Selling, general and administrative	9,883	10,672	9,383
Research and development	801	410	77
Asset impairment charge	3,879		
Nonrecurring items, net recovery related to RDM			(7,744)
Total operating expenses	14,563	11,082	1,716
Income (loss) from operations	(12,830)	(7,191)	10,527
Interest expense	(4,290)	(5,511)	(5,716)
Interest and other income, net	759	337	292
Income (loss) before income taxes	(16,361)	(12,365)	5,103
Income tax (expense) benefit	69	(32)	146
Net income (loss)	$ (16,292)	$ (12,397)	$ 5,249
Income (loss) per share			
Net income (loss) per share basic	$ (1.26)	$ (0.97)	$ 0.42
Shares used in computing net income (loss) per share basic	12,919,506	12,743,533	12,613,491
Net income (loss) per share diluted	$ (1.26)	$ (0.97)	$ 0.37
Shares used in computing net income (loss) per share diluted	12,919,506	12,743,533	14,190,281

See accompanying notes to consolidated financial statements.

SPACEHAB, INCORPORATED AND SUBSIDIARIES

Consolidated Statements of
Stockholders Equity(Deficit) and Comprehensive Income (Loss)

(In thousands, except share data)

	Convertible Preferred Stock Shares	Convertible Preferred Stock Amount	Common Stock Shares	Common Stock Amount	Treasury Stock Amount	Add l. Paid-In-Capital	Accumulated Other Comprehensive Income (Loss)	Accumulated Deficit	Total Stockholders Equity (Deficit)
Balance at June 30, 2004	1,333,334	$ 11,892	12,688,062	$ 83,751	$ (117)	$ 16	$	$ (86,132)	$ 9,410
Common Stock options exercised			27,250	24					24
Common Stock issued under employee stock purchase plan				65,967	114				114
Net income								5,249	5,249
Total comprehensive income									5,249
Balance at June 30, 2005	1,333,334	$ 11,892	12,781,279	$ 83,889	$ (117)	$ 16	$	$ (80,883)	$ 14,797
Common Stock options exercised			17,000	15					15
Stock-based compensation						268			268
Common Stock issued under employee stock purchase plan				177,985	126				126
Net loss								(12,397)	(12,397)
Total comprehensive income									(12,397)
Balance at June 30, 2006	1,333,334	$ 11,892	12,976,264	$ 84,030	$ (117)	$ 284	$	$ (93,280)	$ 2,809
Stock-based compensation						260			260
Common Stock issued under employee stock purchase plan				167,032	92				92
Net loss								(16,292)	(16,292)
Total comprehensive income									(16,292)
Balance at June 30, 2007	1,333,334	$ 11,892	13,143,296	$ 84,122	$ (117)	$ 544	$	$ (109,572)	$ (13,131)

See accompanying notes to consolidated financial statements.

SPACEHAB, INCORPORATED AND SUBSIDIARIES

Consolidated Statements of Cash Flows

(In thousands)

	Twelve Months Ended June 30, 2007 Restated		2006		2005	
Cash flows from operating activities						
Net income (loss)	$	(16,292)	$	(12,397)	$	5,249
Adjustments to reconcile net income (loss) to net cash (used in) provided by operating activities:						
Nonrecurring item, net recovery related to RDM						(8,244)
(Increase) decrease in restricted cash		(6,282)				
Stock-based compensation		260		268		
Impairment of investment in AAC		100				
Depreciation and amortization, including deferred debt issuance		6,362		6,062		5,526
Impairment of inventory		1,674				
Write-off of debt placement fees				591		9
Loss on asset sales and write-offs		12,496		6,304		3
Recognition of deferred gain		(221)		(214)		(33)
Changes in assets and liabilities:						
(Increase) decrease in accounts receivable		2,882		5,527		(9,028)
Decrease in prepaid expenses and other current assets		(296)		(22)		(198)
Increase in other assets		23		108		1,341
Decrease in deferred revenue		(168)		(490)		(5,429)
Decrease in accounts payable and accrued expenses and accounts payable-Astrium		(388)		(638)		(1,504)
(Decrease) increase in accrued subcontracting services and other		(2,893)		(990)		4,876
Increase in advances for construction contract		5,722				
Increase in customer deposits		3,106				
(Decrease) increase in long-term contracts costs and other liabilities		(57)		(125)		279
Net cash (used in) provided by operating activities		6,028		3,984		(7,153)
Cash flows from investing activities						
Purchases of property, equipment and leasehold improvements		(577)		(2,111)		(3,429)
Proceeds received from sale of property and equipment						6,767
Proceeds from sales of investments						6,641
(Increase) decrease in cash securing credit facilities				970		(540)
Proceeds from contract indemnification						8,244
Payment for legal claim settlement		(500)				
Net cash (used in) provided by investing activities		(1,077)		(1,141)		17,683
Cash flows from financing activities						
Proceeds from issuance of Common Stock		92		142		138
Increase in deferred financing				(1,939)		(456)
Net repayments under revolving loan payable						(1,445)
Repayment of mortgage loan		(1,636)		(2,056)		(1,946)
Net cash used in financing activities		(1,544)		(3,853)		(3,709)
Net change in cash and cash equivalents		3,407		(1,010)		6,821
Cash and cash equivalents at beginning of period		6,317		7,327		506
Cash and cash equivalents at end of period	$	9,724	$	6,317	$	7,327

See accompanying notes to consolidated financial statements.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(1) Description of the Company and Operating Environment

SPACEHAB is a developer and operator of space flight hardware assets, a provider of manned and unmanned payload processing services, and an entrepreneurial force in space commerce and developing space utilization applications such as microgravity processing.

A substantial portion of our revenue has been generated under contracts with NASA and our contracts are subject to periodic funding allocations by the agency. NASA s funding is dependent on receiving annual appropriations from the U.S. Government. During the years ended June 30, 2007, 2006, and 2005 approximately 84%, 80%, and 81% of our revenues were generated under U.S. Government contracts, respectively.

Leveraging its heritage of supporting 23 space shuttle missions with the development and provision of flight qualified hardware assets, the Flight Services business unit is continuing to offer a range of engineering, research, logistics, integration, operations, and ground support services. Our experience with the integration of complex science payloads enables our entrance into the field of microgravity processing of high value bioscience products for the benefit of the general public.

Our Astrotech subsidiary provides commercial spacecraft launch processing services and payload processing facilities in the U.S. These services are offered at the Astrotech facilities in Titusville, Florida and VAFB in California, and are provided on a fixed-price basis. Additionally, Astrotech supplies payload processing and facilities maintenance support services to Sea Launch Company, LLC for its Sea Launch program at the Home Port facilities in Long Beach, California.

Our Government Services subsidiary manages projects in need of comprehensive engineering solutions, and provides unique capabilities such as specialty engineering, hardware design and development, and configuration and data management. Government Services also designs and fabricates space flight hardware. We continuously review and seek new business opportunities with NASA, either through current contract expansion or teaming with other aerospace companies on new contract bid initiatives.

We believe that NASA s current major programs, including the Space Shuttle Program (through at least 2010) and the International Space Station Program will continue to be funded and supported by the U.S. Government. While delays have occurred, we believe that it is highly unlikely that any decision to discontinue these programs would be made during the next twelve months. However, we are subject to risks and uncertainties.

The Company has incurred net losses in the years ended June 30, 2007 and 2006. Historically, the Company has financed its capital expenditures, research and development and working capital requirements with progress payments under its various contracts, as well as with proceeds received from both public and private debt and equity offerings and borrowings under credit facilities.

The accompanying consolidated financial statements have been prepared on a going concern basis, which contemplates the realization of assets and satisfaction of liabilities in the normal course of business. The financial statements do not include any adjustments relating to the recoverability of assets and classification of liabilities that might be necessary should the Company be unable to continue as a going concern.

As of June 30, 2007 we had cash and restricted cash on hand of $16.0 million and our working capital was approximately ($5.5) million. Restricted cash, which consists of advance payments on a government contract to modify certain spacecraft processing facilities, totaled $6.3 million at June 30, 2007. For fiscal year 2007 we generated $12.3 million from operating activities. Our $5.0 million revolving credit facility expired as of February 11, 2007 and we elected not to renew the facility.

Our $10.3 million of outstanding 8.0% convertible notes are due on October 15, 2007 and our $52.9 million of 5.5% senior convertible notes are due in October 2010. A covenant in our 5.5% note indenture restricts us from using the proceeds from the sale or mortgage of our Astrotech Florida assets for purposes other than reducing outstanding balances on our bank loan, repaying our now extinguished mortgage loan, or redeeming outstanding 5.5% senior convertible notes. We do not have sufficient liquidity to repay the principle and interest on our 8.0% convertible notes and the interest on our 5.5% senior convertible notes when due on October 15, 2007 unless our Exchange Transaction (see Note 27) is successfully consummated.

On August 31, 2007 we filed a Schedule TO pursuant to Rule 13e-4 promulgated under the Securities Exchange Act of 1934, as amended, in connection with the Company s offer to exchange (the Exchange Offer) 74 shares of common stock and 1.2 shares of Series C Convertible Preferred Stock for each $1,000 principal amount of outstanding 8% Convertible Subordinated Notes due 2007 (the Junior Notes) up to $10,306,000 in aggregate principal amount of the Junior Notes and 667 shares of common stock and 1 share of Series C Convertible Preferred Stock for each $1,000 principal amount of outstanding 5.5% Senior Convertible Notes due 2010 (the Senior Notes) up to $52,944,000 in aggregate principal amount of the Senior Notes, upon the terms and subject to the conditions set forth in the Company s offering memorandum, dated August 31, 2007 (the Offering Memorandum), and the related Exchange Offer materials which are filed as Exhibits (a)(1)(B) to (a)(1)(I) of the Schedule TO (which Offering Memorandum and related Exchange Offer materials, as amended or supplemented from time to time, collectively constitute the Offer Materials).

Additionally, on August 28, 2007, the Company and Astrium, GmbH mutually agreed to terminate the lease agreement dated as of February 28, 2001 in regards to the Company s lease of the Integrated Cargo Carriers (ICC) assets from Astrium, GmbH. Also, we mutually agreed to terminate the lease agreement dated as of July 3, 2001 in regards to the Company s lease of the Vertical Cargo Carrier (VCC) assets from Astrium, GmbH. In order to terminate these two leases, we have mutually agreed that the Company will reimburse Astrium, GmbH $1,389,000 for the period March 1, 2007 through August 31, 2007 for the ICC assets and incur no financial obligations for either the ICC or VCC after August 31, 2007.

We continue to focus our efforts on improving 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. 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.

Our capital resources which are solely comprised of cash reserves and cash generated from operations, may not be sufficient to meet these capital requirements. While we believe that the exchange offer would help address our foreseeable refinancing risk related to the Junior Notes that mature in October 2007, there is no assurance that the exchange offer will be sufficient to alleviate our liquidity issues due to a lack of capital resources. In addition, with the conclusion of STS-118 in August 2007, we expect to have a material decrease in our revenue from our Flight Services business, which has accounted for over 65% of our consolidated revenue during fiscal year 2007. Moreover, our revolving credit line expired on February 11, 2007. As a result, in order to continue to fund our current operations, we will need additional capital. No assurance can be given that we will be able to obtain a new source of capital on terms that are acceptable to us. If we are unable to obtain new capital, we may be forced to subject ourselves to bankruptcy, reorganization, liquidation, dissolution or similar proceeding.

As discussed above, management has implemented significant strategies to address its liquidity requirements and expects that it will be successful in accomplishing the remaining portion of the plan; however, no assurance can be given that the Company will be successful in achieving the remaining goals. If the Company is unable to complete its strategy, cash flow may be insufficient to cover the Company s operating and debt service requirements in fiscal year 2008.

(2) Summary of Significant Accounting Policies

Principles of Consolidation and Basis of Presentation

The consolidated financial statements include the accounts of SPACEHAB, Incorporated and its wholly-owned and majority-owned subsidiaries: Astrotech Space Operations, SPACEHAB Government Services, and Space Media. The Company owns approximately 99% of Space Media, Inc. All significant intercompany transactions have been eliminated in consolidation.

Cash and Cash Equivalents

The Company considers short-term investments with original maturities of three months or less to be cash equivalents. Cash equivalents are primarily made up of money market investments and overnight repurchase agreements recorded at cost, which approximate market value.

Accounts Receivable

The carrying value of the Company s receivable, net of the allowance for doubtful accounts, represents their estimated net realizable value. We estimate the allowance for doubtful accounts based on type of customer, age of outstanding receivable, historical collection trends, and existing economic conditions. Accounts are considered past due after 90 days from invoice date. If events or changes in circumstances indicate that a specific receivable balance may be unrealizable, further consideration is given to the collectibility of those balances and the allowance is adjusted accordingly. Receivable balances deemed uncollectible are written off against the allowance.

Restricted Cash

Restricted cash represents cash that is not readily available for general purpose cash needs. As of June 30, 2007 there was $6.3 million in our restricted cash balance. As of June 30, 2006 there was no restricted cash included in our cash balance.

Inventories

We state inventories at the lower of cost or market as determined by the first-in-first-out (FIFO) method.

Investments

We account for investments in accordance with Statements of Financial Accounting Standards No. 115, Accounting for Certain Investments in Debt and Equity Securities.

Available-for-sale securities are recorded at fair value on the balance sheet, with the change in fair value during the period excluded from earnings and recorded as a component of other comprehensive income. On June 30, 2004 the fair market value of these securities approximated cost. Maturities of the debt securities held by the Company ranged from April 13, 2005 to September 29, 2006. In February 2005 we sold all of our available-for-sale securities.

For the years ended June 30, 2007, 2006, and 2005, interest income was $0.5 million, $0.3 million, and $0.2 million, respectively. Interest income is recorded as a component of other income.

Property and Equipment

Property and equipment are stated at cost. All furniture, fixtures, and equipment are depreciated using the straight-line method over the estimated useful lives of the respective assets, which is generally five years. Our payload processing facilities are depreciated using the straight-line method over their estimated useful lives ranging from sixteen to forty years.

We have estimated the useful lives of our space flight assets, which is a component of property and equipment, through December 31, 2010, based on current available information published by NASA.

Leasehold improvements are amortized over the shorter of the useful life of the building or the term of the lease. Repairs and maintenance are expensed when incurred.

From time to time, we purchase equipment or enhance our facilities to meet specific customer requirements. These enhancements or equipment purchases are compensated through our contract with the customer. The difference between the amount reimbursed and the cost of the enhancements is recognized as revenue.

Deferred Financing Costs

Deferred financing costs represent loan origination fees paid to the lender and related professional fees. These costs are amortized on a straight-line basis over the term of the respective loan agreements. Amortization expense for the years ended June 30, 2007, 2006, and 2005 were $0.5 million, $0.5 million, and $0.4 million, respectively.

Investments in Affiliates

We use the equity method of accounting for our investments in, and earnings of, investees in which we exert significant influence. In accordance with the equity method of accounting, the carrying amount of such an investment is initially recorded at cost and is increased to reflect our share of the investor s income and is reduced to reflect the Company s share of the investor s losses. Investments in which the Company has less than 20% ownership and no significant influence are accounted for under the cost method and are carried at cost.

Impairment of Long- Lived Assets

We account for long-lived assets in accordance with the provisions SFAS No. 144, Accounting for the Impairment or Disposal of Long-Lived Assets. This Statement requires long-lived assets and certain identifiable intangibles 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 assets exceeds the fair value of the assets (see Note 20). Assets to be disposed of are reported at the lower of the carrying amount or fair value less costs to sell.

Share Based Compensation

Effective July 1, 2005 the Company adopted SFAS No. 123R to account for share-based awards to employees. SFAS No. 123R requires measurement of the cost of employee services received in exchange for an award based on the fair value of the award on the grant date. Prior to the adoption of SFAS No. 123R, the Company applied the provisions of Accounting Principles Board (APB) Opinion No. 25, and related interpretations to account for options granted under our various stock option plans. Based on the provisions of this plan, no compensation expense had been recognized for options issued under this plan. The fair value of the stock options is estimated using expected dividend yields of the Company s stock, the expected volatility of the stock, the expected length of time the options remain outstanding and risk-free interest rates. Changes in one or more of these factors may significantly affect the estimated fair value of the stock options. Additionally, SFAS No. 123R requires the Company to estimate the number of instruments for which the required service is expected to be rendered. The Company estimates forfeitures using historical forfeiture rates for previous grants of equity instruments.

Revenue Recognition

SPACEHAB recognizes revenue employing several generally accepted revenue recognition methodologies across its business segments. The methodology used is based on contract type and the manner in which products and services are provided. Revenue generated under existing Flight Services contracts and for all other contract awards for which the capability to successfully complete the contract can be reasonably assured and costs at completion can be reliably estimated at contract inception, is recognized under the percentage-of-completion method based on costs incurred over the period of the contract. Revenue provided by Government Services is primarily derived from cost-plus award fee contracts, whereby revenue is recognized to the extent of reimbursable costs incurred plus award fee. Award fees which provide earnings based on our contract performance, as determined by NASA evaluations, are recorded when the amounts are probable and can be reasonably estimated. Changes in estimated costs to complete and provisions for contract losses and estimated amounts recognized as award fees are recognized in the period they become known. Revenue generated by Astrotech s payload processing services is recognized ratably over the occupancy period of the satellite while in the Astrotech facilities. For the multi-year contract with Lockheed Martin, revenue is billed and recognized on a quarterly basis.

Deferred Revenue

Deferred revenue represents amounts collected from customers for projects, products, or services expected to be provided at a future date. Deferred revenue is shown on the balance sheet as either a short-term or long-term liability, depending on when the service or product is expected to be provided.

Research and Development

Research and development costs are expensed as incurred.

Income Taxes

We recognize income taxes under the asset and liability method. Deferred tax assets and liabilities are recognized for the future tax consequences attributable to differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax bases and operating loss and tax credit carry forward. Deferred tax assets and liabilities are measured using enacted tax rates expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or settled. The effect on deferred tax assets and liabilities of a change in tax rates is recognized in income in the period that includes the enactment date. A valuation allowance is established when it is more likely than not that some portion or all of the deferred tax assets will not be realized.

Net Income (Loss) Per Share

Basic net income (loss) per share is calculated by dividing net income (loss) by the weighted average number of common shares outstanding during the period. Diluted net income (loss) per share includes all Common Stock options and other Common Stock equivalents that potentially may be issued as a result of conversion privileges, including the convertible subordinated notes payable and convertible preferred stock (see Note 12).

Accounting Estimates

The preparation of consolidated financial statements in conformity with accounting principles generally accepted in the U.S. requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the consolidated financial statements and the reported amounts of revenue and expenses during the reporting periods. Actual results could differ from these estimates.

New Accounting Pronouncements