

GULF ISLAND FABRICATION INC
Form DEF 14A
March 19, 2004

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SCHEDULE 14A

Proxy Statement Pursuant to Section 14(a) of the
Securities Exchange Act of 1934 (Amendment No. __)

Filed by the Registrant ☒

Filed by a Party other than the Registrant ☐

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Check the appropriate box:

- ☐ Preliminary Proxy Statement
- ☐ CONFIDENTIAL, FOR USE OF THE COMMISSION ONLY (AS PERMITTED BY RULE 14A-6(E)(2))
- ☒ Definitive Proxy Statement
- ☐ Definitive Additional Materials
- ☐ Soliciting Material Pursuant to § 240.14a-11(c) or § 240.14a-12

GULF ISLAND FABRICATION, INC.

(Name of Registrant as Specified In Its Charter)

(Name of Person(s) Filing Proxy Statement, if other than the Registrant)

Payment of Filing Fee (Check the appropriate box):

- ☒ No fee required.
- ☐ Fee computed on table below per Exchange Act Rules 14a-6(i)(4) and 0-11.

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(3) Filing Party:

(4) Date Filed:

Notes:

Reg. § 240.14a-101.

SEC 1913 (12-03)

GULF ISLAND FABRICATION, INC.

583 THOMPSON ROAD

HOUMA, LOUISIANA 70363

NOTICE OF ANNUAL MEETING OF SHAREHOLDERS

TO BE HELD APRIL 28, 2004

TO THE SHAREHOLDERS OF GULF ISLAND FABRICATION, INC.:

The annual meeting of shareholders of Gulf Island Fabrication, Inc. (the Company) will be held at 10:00 a.m., local time, on Wednesday, April 28, 2004, at the office of the corporation, 583 Thompson Road, Houma, Louisiana, for the following purposes, more fully described in the accompanying proxy statement:

1. To elect three Class I directors.
2. To ratify the appointment of Ernst & Young LLP as the independent auditors to audit the financial statements of the Company and its subsidiaries for the year 2004.
3. To transact such other business as may properly come before the meeting and any adjournments thereof.

The Board of Directors has fixed the close of business on March 12, 2004 as the record date for the determination of shareholders entitled to notice of and to vote at the annual meeting and all adjournments thereof.

Your vote is important regardless of the number of shares you own. Whether or not you plan to attend the annual meeting, **please mark, date and sign the enclosed proxy card and return it promptly in the enclosed stamped envelope**. Furnishing the enclosed proxy will not prevent you from voting in person at the annual meeting should you wish to do so.

By Order of the Board of Directors

ROBIN A. SEIBERT

Secretary

Houma, Louisiana

March 19, 2004

GULF ISLAND FABRICATION, INC.

583 THOMPSON ROAD

HOUMA, LOUISIANA 70363

PROXY STATEMENT

ANNUAL MEETING OF SHAREHOLDERS

TO BE HELD APRIL 28, 2004

This Proxy Statement is furnished to shareholders of Gulf Island Fabrication, Inc. (the "Company") in connection with the solicitation of proxies on behalf of the Company's Board of Directors for use at its annual meeting of shareholders to be held at the date, time and place set forth in the accompanying notice and at any adjournment thereof (the "Meeting"). This Proxy Statement is being mailed to shareholders on or about March 19, 2004.

On March 12, 2004, the record date for determining shareholders entitled to notice of and to vote at the Meeting, the Company had outstanding 11,940,551 shares of common stock ("Common Stock"), each of which is entitled to one vote on all matters to be considered at the Meeting.

Shares represented by all properly executed proxies on the enclosed form received in time for the Meeting will be voted at the Meeting. A proxy may be revoked at any time before it is exercised by filing with the Secretary of the Company an instrument revoking it or a duly executed proxy bearing a later date, or by attending the Meeting and voting in person. Unless revoked, the proxy will be voted as specified and, if no specifications are made, will be voted in favor of the proposed nominees and for the ratification of the appointment of auditors as described herein.

The cost of soliciting proxies will be borne by the Company. Banks, brokerage houses and other institutions, nominees and fiduciaries will be requested to forward solicitation materials to the beneficial owners of the shares of Common Stock of the Company; upon request, the Company will reimburse such persons for reasonable out-of-pocket expenses incurred in connection therewith.

SHAREHOLDER PROPOSALS AND NOMINATIONS FOR 2005 ANNUAL MEETING

Any shareholder who wishes to bring a matter, other than shareholder nominations of directors, before the 2005 annual meeting must notify the Secretary of the Company, in writing at the address shown on the first page of this Proxy Statement, no later than February 2, 2005. However, if the date of the 2005 annual meeting is changed by more than 30 calendar days from the date of the 2004 annual meeting, the notice must be received by the Secretary of the Company at least 45 days prior to the date the Company intends to distribute its proxy materials with respect to the 2005 annual meeting.

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If a shareholder does not provide such notice timely, the chairman of the 2005 annual meeting may exclude the matter and, if the chairman so elects, the matter will not be acted upon at the meeting. If the chairman does not exclude the matter, proxies solicited on behalf of the Board of Directors for the 2005 annual meeting will confer discretionary authority to vote with respect to any such matter, as permitted by the proxy rules of the Securities and Exchange Commission (SEC).

Shareholders intending to nominate a director at the 2005 annual meeting of shareholders may do so if they comply with the Company's Amended and Restated Articles of Incorporation by furnishing timely written notice containing specified information concerning, among other things, information about the nominee and the shareholder making the nomination. See Corporate Governance Consideration of Director Nominees for more information.

Any shareholder who desires to present a proposal for inclusion in the Company's proxy materials for the 2005 annual meeting must forward the proposal in writing to the Secretary of the Company at the address shown on the first page of this Proxy Statement in time to arrive at the Company no later than November 19, 2004, and the proposal must comply with applicable federal proxy rules.

CORPORATE GOVERNANCE

Ethics and Business Conduct Policies

The Company has adopted a Code of Ethics for the Chief Executive Officer and Senior Financial Officers (the "Code of Ethics") and a Code of Business Conduct and Ethics, which applies to all employees and directors, including the Chief Executive Officer and senior financial officers of the Company. The Company will make these codes publicly available by posting the codes on its website at www.gulfisland.com. Any substantive amendments to the Code of Ethics or any waivers granted under the Code of Ethics will be disclosed as required by applicable SEC and Nasdaq rules.

Board Structure and Committee Composition

As of the date of this Proxy Statement, the Company's Board of Directors consists of 8 members. The Board of Directors held five regularly-scheduled meetings during 2003. The Board has established two standing committees: an Audit Committee and a Compensation Committee. Each committee operates under a written charter adopted by the Board, which are available on our website at www.gulfisland.com. The composition of Board committees is reviewed and re-determined each year at the initial meeting of the Board after the annual meeting of shareholders. During 2003, each of the Company's directors attended at least 75% of the aggregate of the total number of meetings of the Board and the total number of meetings held by all committees of the Board on which he served during the periods of his Board membership and committee service.

Audit Committee

The Audit Committee consists of the following four directors: Gregory J. Cotter (Chairman), Thomas E. Fairley, Hugh J. Kelly and Ken C. Tamblyn. Each of these directors is "independent" as such term is defined in the listing standards of the Nasdaq National Market ("Nasdaq"), and also satisfies the additional requirements applicable to an audit committee member under the Nasdaq listing standards. The Board has determined that Mr. Ken C. Tamblyn is an "audit committee financial expert" as such term is defined in the applicable rules of the SEC.

The Audit Committee met five times during 2003. The Audit Committee's primary function is to assist the Board in fulfilling its oversight responsibilities by monitoring (i) the Company's continuing development and performance of its system of financial reporting, auditing, disclosure controls and procedures and internal control over financial reporting, (ii) the operation and integrity of its financial reporting system, (iii) the performance and qualifications of the Company's independent (external) and internal auditors, and (iv) the independence of the Company's independent auditors.

Compensation Committee

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The Compensation Committee consists of the following four directors: Huey J. Wilson (Chairman), Gregory J. Cotter, Alden J. (Doc) Laborde, and John P. (Jack) Laborde. Each of these directors is independent as such term is defined in the listing standards of Nasdaq. The Compensation Committee, which met twice in 2003, (i) periodically reviews, approves and recommends to the Board the Company's goals and objectives relating to the compensation of the Company's officers and the compensation of the President of each of the Company's subsidiaries (including the specific relationship of corporate performance to such officers' compensation), (ii) evaluates the performance of the Company's officers and the performance of the President of each of the

Company's subsidiaries in light of these goals and objectives, (iii) recommends to the Board the compensation of the Company's officers and the compensation of the President of each of the Company's subsidiaries based on such evaluations, (iv) recommends to the Board award grants under the Company's incentive compensation plans and programs, (v) otherwise administers the Company's incentive compensation plans and programs, and (vi) performs such other functions as may be prescribed by the Board.

Board Independence

The Board has determined that seven of the directors are independent as such term is defined in the listing standards of Nasdaq. Mr. Kerry J. Chauvin, the Chairman of the Board, President and Chief Executive Officer of the Company, is the only director who is not independent as defined by Nasdaq.

Consideration of Director Nominees

The Board of Directors has elected not to have a separate nominating committee. The Board made this determination after considering its nomination process and concluding that as many directors as possible should participate in that process. As stated above, the Board has determined that all of its current directors are independent under Nasdaq's listing standards other than Mr. Chauvin, who is not considered independent because he is an officer of the Company. Accordingly, the Board has decided that nominations of directors and related matters will be considered and voted upon by all of the independent directors while meeting in executive session. In this manner, all but one of the directors will be involved in the nominations process.

In evaluating the suitability of nominees for membership on the Board, the independent directors consider many factors, including personal and professional integrity, general understanding of the industry, finance and other elements relevant to the success of a publicly-traded company in today's business environment, educational and professional background, and independence. The independent directors evaluate each individual in the context of the Board as a whole, with the objective of nominating persons for election to the Board who can best perpetuate the success of the Company's business, be an effective director in conjunction with the full Board, and represent shareholder interests through the exercise of sound judgment using their diversity of experience in these various areas.

The independent directors will regularly assesses the appropriate size of the Board, and whether any vacancies on the Board are expected due to retirement or otherwise. In the event that any vacancies are anticipated, or otherwise arise, the independent directors will consider various potential candidates for director who may come to the attention of the Board through current board members, professional search firms, shareholders or other persons. Each candidate brought to the attention of the Board is considered on the basis of the criteria set forth above.

The Board is open to suggestions from our shareholders on candidates for election to the Board. Any shareholder may suggest a nominee by sending the following information to the Board: (i) the proposing shareholder's name, address and telephone number, (ii) the number of shares of Common Stock beneficially owned by the proposing shareholder and the suggested nominee, (iii) the suggested nominee's name, age, business and residential addresses and telephone number, (iii) a statement whether the suggested nominee knows that his or her name is being suggested by the proposing shareholder, and whether he or she has consented to being suggested and is willing to serve, (iv) the suggested nominee's résumé or other description of his or her background and experience, and (v) the proposing shareholder's reasons for suggesting that the individual be considered. The information should be sent to the Board addressed as follows: Secretary of Gulf Island Fabrication, Inc., 583 Thompson Road, Houma, Louisiana 70363, and the Secretary will forward the information to the independent directors.

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The Company's Amended and Restated Articles of Incorporation also permit shareholders to directly nominate directors for consideration at an annual shareholder meeting. In general, to be timely, a shareholder's

notice must be in writing, must include certain specified information about the nominee and the shareholder making the nomination, and must be received by the Secretary of the Company at our principal executive offices no less than 45 days or more than 90 days prior to the shareholder meeting.

Executive Sessions; Communications with the Board; Meeting Attendance

The Board has adopted a policy providing that the independent directors will meet in executive session at each regularly-scheduled Board meeting, or more frequently if necessary. Under this policy, the chair of each executive session meeting will be chosen by the independent directors, by majority vote, immediately prior to the convening of each such meeting.

Any shareholder may communicate with our Board (or with any individual director) by sending a letter by mail addressed to the Chairman of the Board of Gulf Island Fabrication, Inc., 583 Thompson Road, Houma, Louisiana 70363. The Chairman of the Board will forward the shareholder's communication directly to the appropriate director or directors.

The Board has adopted a policy that recommends that all directors personally attend each annual and special meeting of the Company's shareholders. At the last annual meeting of shareholders held on April 30, 2003, all of the directors then in office were in attendance.

Director Compensation

In 2003, each non-employee director received an annual fee of \$16,125 for his services as a director and an attendance fee of \$1,200 for each Board or committee meeting (excluding meetings held via telephone conference call). All directors are reimbursed for reasonable out-of-pocket expenses incurred in attending Board and committee meetings. For 2004, the annual fee will be \$16,500 and the attendance fee will remain \$1,200.

Section 16(a) Beneficial Ownership Reporting Compliance

Section 16(a) of the Securities Exchange Act of 1934 requires the Company's directors, executive officers, controller, and beneficial owners of more than 10% of the Common Stock to file certain beneficial ownership reports with the SEC. Each of Messrs. Chauvin, Meche, Bourke and Gallagher failed to file timely a statement on Form 4 to report the grant of employee stock options on December 11, 2003. These transactions were reported late on Forms 4 dated January 20, 2004, for Messrs. Chauvin, Meche and Gallagher, and January 21, 2004, for Mr. Bourke.

ELECTION OF DIRECTORS

The Company's Amended and Restated Articles of Incorporation provide for a Board of Directors consisting of three classes, with the number of directors to be set forth in the Company's By-laws. The Company's By-laws provide for a Board of Directors of eight persons. The term of office of the Class I directors will expire at the Meeting, and the persons listed as the Class I nominees in the table below will be nominated for election to the Board of Directors for a term expiring in 2007. The term of office of the Class II directors will expire at the 2005 annual meeting. The

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term of office of the Class III directors will expire at the 2006 annual meeting.

The independent directors of the Board of Directors have nominated three candidates for election at the Meeting and recommend that shareholders vote FOR the election of the nominees. Proxies cannot be voted for more than three candidates. In the absence of contrary instructions, the proxy holders will vote for the election of the three nominees listed below. In the unanticipated event that any nominee is unavailable as a candidate for director, the persons named in the accompanying proxy will vote for a substitute candidate nominated by the Board of Directors.

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The following table sets forth as of February 13, 2004, for each nominee, each other director of the Company whose term will continue after the Meeting and each of the executive officers of the Company, the age, positions with the Company, and principal occupations and employment during the past five years of each such person, any family relationships among such persons, and, if a nominee or a director, each person's directorships in other public corporations and the year that he was first elected a director of the Company or its predecessor. All executive officers serve at the pleasure of the Board of Directors of the Company.

Name and Age	Positions with the Company, Principal Occupations, Directorships in Other Public Corporations, and Family Relationships	Director Since
Nominees for Election as Class I Directors (term expires in 2007)		
Thomas E. Fairley, 55	Director of the Company. Director, President and Chief Executive Officer of Trico Marine Services, Inc., a marine vessel operator.	1997
Hugh J. Kelly, 78	Director of the Company. Consultant to the oil and gas industry.	1997
Ken C. Tamblyn, 60	Director of the Company (appointed by the Board of Directors on July 23, 2003). Private Investor. Executive Vice President and Chief Financial Officer of Tidewater, Inc. from March 1986 through August 2000. Member of the Board of Directors of Offshore Logistics.	2003
Continuing Class II Directors (term expires in 2005)		
Gregory J. Cotter, 55	Director of the Company. Director, President and Chief Operating and Financial Officer of Huey Wilson Interests, Inc., a financial and business management company. Chief Financial Officer of Wilson Jewelers, Inc., a jewelry merchandiser, until 2001.	1985
John P. (Jack) Laborde, 54	Director of the Company. President of Overboard Holdings, L.L.C. (Overboard), a management company engaged in oil and gas exploration and development since January 2002. Chief Executive Officer of All Aboard Development Corporation (All Aboard), an independent oil and gas exploration and production company, since 1996. President of All Aboard since 1997. All Aboard is currently being managed by Overboard. Son of Alden J. Laborde.	1997
Continuing Class III Directors (term expires in 2006)		
Kerry J. Chauvin, 56	Chairman of the Board of the Company since April 2001. President and Chief Executive Officer of the Company.	1985
Alden J. (Doc) Laborde, 88	Director of the Company. Chairman of the Board of the Company from 1985 to April 2001. Father of John P. Laborde.	1985
Huey J. Wilson, 76	Director of the Company. Chairman of the Board and Chief Executive Officer of Huey Wilson Interests, Inc. Chairman of the Board and Chief Executive Officer of Wilson Jewelers, Inc. until 2001.	1997
Executive Officers not Serving as Directors		
Kirk J. Meche, 41	Executive Vice President Operations of the Company. President of Gulf Island, L.L.C., a wholly-owned fabrication subsidiary of the Company, since February 2001. President of Southport, Inc., a former wholly-owned subsidiary of the Company, from December 1999 to February 2001. Vice President of Operations for Southport, Inc. from February 1999 to December 1999. From 1996 to December 1999, a project manager for the Company.	N/A
Murphy A. Bourke, 59	Executive Vice President Marketing of the Company. Vice President Marketing of the Company until December 1999.	N/A
Joseph P. Gallagher, III, 53	Vice President Finance, Chief Financial Officer and Treasurer of the Company.	N/A

STOCK OWNERSHIP

The following table sets forth, as of February 20, 2004, certain information regarding beneficial ownership of Common Stock by (i) each director of the Company, (ii) each executive officer of the Company, (iii) all directors and executive officers of the Company as a group, and (iv) each other shareholder known by the Company to be the beneficial owner of more than 5% of the outstanding Common Stock. Unless otherwise indicated, the Company believes that the shareholders listed below have sole investment and voting power with respect to their shares based on information furnished to the Company by such shareholders.

Name of Beneficial Owner	Percent of	
	Number of Shares	Outstanding
	Beneficially Owned(1)	Common Stock(2)
Murphy A. Bourke	60,900	*
Kerry J. Chauvin	225,000	1.9%
Gregory J. Cotter	203,000(3)	1.7%
Thomas E. Fairley	10,000	*
Joseph P. Gallagher, III	59,700	*
Hugh J. Kelly	4,000	*
Alden J. Laborde (4)	1,554,000(5)	13.2%
John P. Laborde	72,600(6)	*
Kirk J. Meche	26,302	*
Ken C. Tamblyn	500	*
Huey J. Wilson (7)	2,032,000(3)	17.2%
All directors and executive officers as a group (11 persons)	4,053,002	33.6%
St. Denis J. Villere & Company, L.L.C. (8)	738,537(9)	6.3%

* Less than one percent.

- (1) Includes shares that could be acquired within sixty days after February 20, 2004 upon the exercise of options granted pursuant to the Company's stock incentive plans, as follows: Mr. Bourke, 38,700 shares; Mr. Chauvin, 158,000 shares; Mr. Gallagher, 58,700 shares; Mr. Meche, 23,300 shares; and all directors and executive officers as a group, 278,700 shares.
- (2) Based on 11,781,430 shares of Common Stock outstanding as of February 20, 2004.
- (3) Includes 200,000 shares held by a charitable foundation of which Messrs. Cotter and Wilson are trustees. Messrs. Cotter and Wilson disclaim beneficial ownership of these shares.
- (4) The address of Mr. Laborde is 400 Poydras Street, Suite 1560, New Orleans, Louisiana 70130.
- (5) Mr. Laborde has sole voting and dispositive power with respect to 9,300 shares and shares voting and dispositive power with respect to 1,544,700 shares, of which 1,524,700 are held by Starboard Enterprises, L.L.C. (Starboard) and 20,000 are held by All Aboard. Mr. Laborde holds a majority equity interest in each of Starboard and All Aboard. The address of each of Starboard and All Aboard is 400 Poydras Street, Suite 1560, New Orleans, LA 70130.
- (6) Includes 45,500 shares owned by Mr. Laborde's two children.
- (7) The address of Mr. Wilson is 3636 South Sherwood Forest Boulevard, Suite 650, Baton Rouge, Louisiana 70816.
- (8) The address of St. Denis J. Villere & Company, L.L.C. is 210 Baronne Street, Suite 808, New Orleans, LA 70112-1727.
- (9) Based on such holder's Schedule 13G/A filed with the SEC on February 10, 2004, St. Denis J. Villere & Company, L.L.C. has sole power to vote and sole power to dispose or direct the disposition of 39,400 shares, and shared power to vote and shared power to dispose or direct the disposition of 699,137 shares.

EXECUTIVE COMPENSATION

The following table summarizes the compensation paid in 2003, 2002, and 2001 by the Company to its Chief Executive Officer and each of its other executive officers (collectively, the Named Executive Officers).

SUMMARY COMPENSATION TABLE

Name and Principal Position	Year	Annual Compensation		Long-Term Compensation Awards	
		Salary	Bonus(1)	Securities Underlying Options (#)	All Other Compensation(2)
Kerry J. Chauvin	2003	\$ 337,580	\$ 251,212	20,000	\$ 11,147
Chairman of the Board,	2002	318,208	165,736	20,000	9,094
President and Chief Executive Officer	2001	301,951	118,051	20,000	7,636
Kirk J. Meche	2003	\$ 159,813	\$ 123,143	10,000	\$ 10,147
Executive Vice President Operations,	2002	149,084	81,243	10,000	8,368
President of Gulf Island, L.L.C. (fabrication subsidiary)	2001	138,846	46,294	10,000	7,325
Murphy A. Bourke	2003	\$ 175,298	\$ 105,903	7,500	\$ 11,147
Executive Vice President	2002	167,005	69,869	7,500	9,093
Marketing	2001	160,335	49,766	10,000	7,635
Joseph P. Gallagher, III	2003	\$ 158,280	\$ 100,978	7,500	\$ 10,879
Vice President Finance, Chief	2002	151,006	66,619	7,500	9,026
Financial Officer and Treasurer	2001	145,296	47,452	10,000	7,568

- (1) For 2003, the Company's executive officers were paid bonuses equal to a specified percentage of the Company's income before taxes and before deduction of the executive bonuses. The percentages for Messrs. Chauvin, Meche, Bourke and Gallagher were 1.02%, .50%, .43% and .41%, respectively.
- (2) Includes (i) matching and profit-sharing contributions of \$10,807, \$10,807, \$10,807, and \$10,539 in 2003, \$8,705, \$7,979, \$8,704 and \$8,637 in 2002, and \$7,247, \$6,936, \$7,246, and \$7,179 in 2001 to the Company's 401(k) plan on behalf of Messrs. Chauvin, Meche, Bourke and Gallagher, respectively, and (ii) premium payments of \$340, \$340, \$340 and \$340 in 2003, \$389, \$389, \$389, and \$389 in 2002, and \$389, \$389, \$389, and \$389 in 2001 for Messrs. Chauvin, Meche, Bourke and Gallagher, respectively, under a long-term disability insurance plan, which premium payments are attributable to benefits in excess of those benefits provided generally for other employees.

Stock Option Grants

The following table sets forth information with respect to all stock options granted in 2003 by the Company to each of the Named Executive Officers.

Option Grants in 2003

Name	Individual Grants				Grant Date Value
	Number of Securities Underlying Options Granted(1)	% of Total Options Granted To Employees in 2003	Exercise or Base Price (\$/Sh)	Expiration Date	Grant Date Present Value (\$)
Kerry J. Chauvin	20,000	19.8%	16.69	12/11/13	160,800(2)
Kirk J. Meche	10,000	9.9%	16.69	12/11/13	80,400(2)
Murphy A. Bourke	7,500	7.4%	16.69	12/11/13	60,300(2)
Joseph P. Gallagher III	7,500	7.4%	16.69	12/11/13	60,300(2)

- (1) Each of the stock options granted in 2003 by the Company to the Named Executive Officers will become exercisable in one-fifth increments over a five-year period. The stock options will become immediately exercisable in their entirety upon (i) a reorganization, merger or consolidation of the Company in which the Company is not the surviving entity, (ii) the sale of all or substantially all of the assets of the Company, (iii) a liquidation or dissolution of the Company, (iv) a person or group of persons, other than Alden J. Laborde or Huey J. Wilson or any employee benefit plan of the Company, becoming the beneficial owner of 30% or more of the Company's voting stock or (v) the replacement of a majority of the Board of Directors in a contested election (each, a "Significant Transaction"). The Compensation Committee has the authority to take several actions regarding outstanding stock options upon the occurrence of a Significant Transaction, including requiring that outstanding stock options remain exercisable only for a limited time, providing for mandatory conversion of outstanding stock options in exchange for either a cash payment or Common Stock, making equitable adjustments to stock options or providing that outstanding stock options will become stock options relating to securities to which a participant would have been entitled in connection with the Significant Transaction if the stock options had been exercised.
- (2) The Black-Scholes option-pricing model was used to determine the grant date present value of the stock options granted in December 2003 by the Company to the Named Executive Officers. Under the Black-Scholes option-pricing model, the grant date present value of each stock option referred to in the table was calculated to be \$8.04. The following facts and assumptions were used in making such calculation: (i) an exercise price of \$16.69 for each such stock option; (ii) a fair market value of \$16.69 for one share of Common Stock on the date of grant; (iii) no dividend payments on Common Stock; (iv) a stock option term of 10 years; (v) a stock volatility of 34.7%, based on an analysis of monthly closing stock prices of shares of Common Stock during a 24-month period; and (vi) an assumed risk-free interest rate of 4.25%, which is equivalent to the yield on a ten-year treasury note on the date of grant. No other discounts or restrictions related to vesting or the likelihood of vesting of stock options were applied. The resulting grant date present value of \$8.04 for each stock option was multiplied by the total number of stock options granted to each of the Named Executive Officers to determine the total grant date present value of such stock options granted to each Named Executive Officer, respectively.

Stock Option Exercises and Outstanding Stock Options

The following table sets forth information with respect to all Company stock option exercises in 2003 by each of the Named Executive Officers and all outstanding Company stock options held by each of the Named Executive Officers as of December 31, 2003.

Aggregated Option Exercises in 2003 and Option Values as of December 31, 2003

	Shares Acquired on Exercise	Value Realized (\$)	Number of Securities Underlying Unexercised Options at 12/31/03		Value of Unexercised In-the-Money Options at 12/31/03 (\$)	
			Exercisable	Unexercisable	Exercisable	Unexercisable
Kerry J. Chauvin	0	0	150,000	71,000	1,082,990	220,315
Kirk J. Meche	0	0	20,500	32,600	64,035	90,758
Murphy A. Bourke	0	0	35,700	29,900	181,376	94,012
Joseph P. Gallagher, III	0	0	55,700	29,900	372,786	94,012

Compensation Committee Interlocks and Insider Participation

During the last fiscal year, none of Messrs. Wilson (Chairman), Cotter, Alden J. Laborde, or John P. Laborde, who comprise the Compensation Committee, were officers or employees of the Company or any of its subsidiaries. Alden J. Laborde was Chief Executive Officer of the Company from 1986 to 1990. No other member of the Compensation Committee is a former officer of the Company.

In connection with the initial public offering of its Common Stock, the Company entered into registration rights agreements (the "Registration Rights Agreements") with Alden J. Laborde and Huey J. Wilson, pursuant to which each of them has one remaining right to require the Company to register shares of Common Stock owned by him under the Securities Act of 1933. If either one of them makes such a demand, the other one is entitled to include his shares in such registration. If the Company proposes to register any Common Stock under the Securities Act in connection with a public offering, each of Messrs. Laborde and Wilson may require the Company to include all or a portion of the shares of Common Stock held by such shareholder. The Company has agreed under the Registration Rights Agreements to pay all the expenses of registration, other than underwriting discounts and commissions.

Compensation Committee Report on Executive Compensation

The Compensation Committee of the Board of Directors of the Company is composed of four directors and operates under a written charter adopted by the Board of Directors. The members of the Compensation Committee are independent as such term is defined under the Nasdaq listing standards. The members of the Compensation Committee are Huey J. Wilson (Chairman), Gregory J. Cotter, Alden J. Laborde and John P. Laborde. The Compensation Committee has the authority, among other things, to review, analyze and recommend compensation programs to the Board of Directors and to administer, and recommend to the Board award grants under, the Company's incentive compensation plans and programs.

The Company's executive compensation is comprised primarily of (i) salaries, (ii) annual cash incentive bonuses and (iii) long-term incentive compensation in the form of stock options granted under the Company's Long-Term Incentive Plan and 2002 Long-Term Incentive Plan of the Company. The salaries of Kerry J. Chauvin, the Chairman of the Board, President and Chief Executive Officer, and the other executive officers of the Company are based on their individual levels of responsibility and the Compensation Committee's subjective assessment of their performances.

The Company has no formal bonus plan, but it has adopted an executive compensation policy that ties a portion of executive compensation to the short-term performance of the Company. This policy is described in footnote 1 to the Summary Compensation Table.

The Company also provides long-term incentives to executive officers in the form of stock options granted under the Company's Long-Term Incentive Plan and 2002 Long-Term Incentive Plan. The stock option awards are intended to reinforce the relationship between compensation and increases in the market price of the Common Stock and to align the executive officers' financial interests with that of the Company's shareholders. The size of awards is based upon the position of each participating officer and the Compensation Committee's subjective assessment of each participant's individual performance. The table entitled "Option Grants in 2003" under the heading "Executive Compensation" sets forth the stock options granted in 2003 to the Named Executive Officers, including Mr. Chauvin, the Chief Executive Officer, based upon position and subjective assessment.

Section 162(m) of the Internal Revenue Code limits the tax deduction to \$1 million for compensation paid to certain highly compensated executive officers. Qualified performance-based compensation is excluded from this deduction limitation if certain requirements are met. The Compensation Committee expects the stock options granted to executive officers, as discussed above, to qualify for the exclusion from the deduction limitation under Section 162(m). The Compensation Committee intends to continue to establish executive officer compensation programs that will maximize the Company's income tax deduction, assuming the Compensation Committee determines that such actions are consistent with its philosophy and in the best interest of the Company and its shareholders.

The Compensation Committee

Huey J. Wilson, Chairman

Gregory J. Cotter

Alden J. Laborde

John P. Laborde

Performance Graph

The following graph compares the cumulative total shareholder return on the Common Stock from December 31, 1998 to December 31, 2003, with the cumulative total return of the Standard & Poor 500 Index and the Standard & Poor 500 Oil & Gas Equipment & Services Index for the same period. The returns are based on an assumed investment of \$100 on December 31, 1998 in the Common Stock and in each of the indexes and on the assumption that dividends were reinvested. In prior years, we measured our performance against the Standard & Poor 500 Oil & Gas (Drilling & Equipment) Index, which no longer exists. During 2002, Standard & Poor divided this index into two indexes, one focusing on equipment and services in the oil and gas industry, and the other on drilling activities. The Company was placed in the Standard & Poor 500 Oil & Gas Equipment & Services Index, which we believe more closely reflects the industry in which we operate and is comprised of companies whose business and operations better match those of the Company.

Comparison of Cumulative Total Return

Gulf Island Fabrication, Inc., S&P 500 Index &

S&P 500 Oil & Gas Equipment & Services Index

Company / Index	Base Period Dec 98	INDEXED RETURNS				
		Years Ending				
		Dec 99	Dec 00	Dec 01	Dec 02	Dec 03
GULF ISLAND FABRICATION, INC.	100	120.97	234.68	161.42	209.68	219.74
S&P 500 INDEX	100	121.04	110.02	2013-C8 ^{(c)(d)}	4.059%	02/15/23
2015-C26 ^{(c)(d)}	4.410%		10/15/25		3,576,000	2,528,608
Morgan Stanley Capital I Trust	2.707%		08/15/26		5,000,000	3,086,735
2016-UB11 ^{(c)(d)}						
Wells Fargo Commercial Mortgage Trust:						
2014-LC18 ^(c)	2.840%		01/15/25		8,635,000	5,639,402
2015-NXS3 ^(c)	3.153%		09/15/57		1,500,000	1,155,681
2015-C31	3.852%		11/15/25		2,886,000	2,300,518
2015-NXS1 ^(d)	4.101%		04/15/25		3,440,000	3,101,561
WFRBS Commercial Mortgage Trust	3.986%		05/15/24		2,650,000	2,126,008
2014-C20 ^(c)						102,726,305

TOTAL COMMERCIAL MORTGAGE BACKED SECURITIES

Cost	122,828,253
(118,480,263)	

	7-Day Yield	Shares	Value (Note 2)
SHORT TERM INVESTMENTS (2.13%)			
State Street Institutional Treasury Plus Money Market Fund	1.813%	2,925,385	2,925,385
TOTAL SHORT TERM INVESTMENTS (Cost \$2,925,385)			2,925,385
TOTAL INVESTMENTS (143.15%) (Cost \$186,255,038)			\$196,657,817
Liabilities in Excess of Other Assets (-43.15%)			(59,280,720)
NET ASSETS (100.00%)			\$137,377,097

(a) *Non-income producing security.*

Securities were purchased pursuant to Regulation S under the Securities Act of 1933, which exempts securities offered and sold outside of the United States from registration. Such securities cannot be sold in the United States

(b) *without either an effective registration statement filed pursuant to the Securities Act of 1933, or pursuant to an exemption from registration. As of July 31, 2018, the aggregate market value of those securities was \$2,558,776, representing 1.86% of net assets.*

Security exempt from registration under Rule 144A of the Securities Act of 1933. Such securities may normally be

(c) *sold to qualified institutional buyers in transactions exempt from registration. The total value of Rule 144A securities amounts \$106,390,293, which represents approximately 77.44% of net assets as of July 31, 2018.*

Variable rate investment. Interest rates reset periodically. Interest rate shown reflects the rate in effect at

(d) *July 31, 2018. Certain variable rate securities are not based on a published reference rate and spread but are determined by the issuer or agent and are based on current market conditions. These securities do not indicate a reference rate and spread in their description above.*

(e) *Interest only security.*

See Notes to Quarterly Statement of Investments.

PRINCIPAL REAL ESTATE INCOME FUND

Notes to Quarterly Statement of Investments

July 31, 2018 (Unaudited)

NOTE 1. ORGANIZATION

Principal Real Estate Income Fund (the “Fund”) is a Delaware statutory trust registered as a non-diversified, closed-end management investment company under the Investment Company Act of 1940, as amended (the “1940 Act”).

The Fund’s investment objective is to seek to provide high current income, with capital appreciation as a secondary investment objective, by investing in commercial real estate related securities.

Investing in the Fund involves risks, including exposure to below-investment grade investments. The Fund’s net asset value will vary and its distribution rate may vary and both may be affected by numerous factors, including changes in the market spread over a specified benchmark, market interest rates and performance of the broader equity markets. Fluctuations in net asset value may be magnified as a result of the Fund’s use of leverage.

NOTE 2. SIGNIFICANT ACCOUNTING POLICIES

Use of Estimates: The preparation of the Statement of Investments in accordance with accounting principles generally accepted in the United States of America (“GAAP”) requires management to make estimates and assumptions that affect the reported amounts and disclosures in the Statement of Investments during the period reported. Management believes the estimates and security valuations are appropriate; however, actual results may differ from those estimates, and the security valuations reflected in the Statement of Investments may differ from the value the Fund’s ultimately realize upon sale of the securities. The Fund is considered an investment company under U.S. GAAP and follows the accounting and reporting guidance applicable to investment companies in the Financial Accounting Standards Board *Accounting Standards Codification* Topic 946 – Investment Companies. The Statement of Investments has been prepared as of the close of the New York Stock Exchange (“NYSE”) on July 31, 2018.

Portfolio Valuation: The net asset value per Common Share of the Fund is determined no less frequently than daily, on each day that the NYSE is open for trading, as of the close of regular trading on the NYSE (normally 4:00 p.m. New York time). The Fund’s net asset value per Common Share is calculated in the manner authorized by the Fund’s Board of Trustees (the “Board”). Net asset value is computed by dividing the value of the Fund’s total assets, less its

liabilities by the number of shares outstanding.

The Board has established the following procedures for valuation of the Fund's assets under normal market conditions. Marketable securities listed on foreign or U.S. securities exchanges generally are valued at closing sale prices or, if there were no sales, at the mean between the closing bid and ask prices on the exchange where such securities are primarily traded.

The Fund values commercial mortgage-backed securities and other debt securities not traded in an organized market on the basis of valuations provided by an independent pricing service, approved by the Board, which uses information with respect to transactions in such securities, interest rate movements, new issue information, cash flows, yields, spreads, credit quality, and other pertinent information as determined by the pricing service, in determining value. If the independent primary or secondary pricing service is unable to provide a price for a security, if the price provided by the independent primary or secondary pricing service is deemed unreliable, or if events occurring after the close of the market for a security but before the time as of which the Fund values its Common Shares would materially affect net asset value, such security will be valued at its fair value as determined in good faith under procedures approved by the Board.

When applicable, fair value of an investment is determined by the Fund's Fair Valuation Committee as a designee of the Board. In fair valuing the Fund's investments, consideration is given to several factors, which may include, among others, the following: the fundamental business data relating to the issuer, borrower, or counterparty; an evaluation of the forces which influence the market in which the investments are purchased and sold; the type, size and cost of the investment; the information as to any transactions in or offers for the investment; the price and extent of public trading in similar securities (or equity securities) of the issuer, or comparable companies; the coupon payments, yield data/cash flow data; the quality, value and salability of collateral, if any, securing the investment; the business prospects of the issuer, borrower, or counterparty, as applicable, including any ability to obtain money or resources from a parent or affiliate and an assessment of the issuer's, borrower's, or counterparty's management; the prospects for the industry of the issuer, borrower, or counterparty, as applicable, and multiples (of earnings and/or cash flow) being paid for similar businesses in that industry; one or more independent broker quotes for the sale price of the portfolio security; and other relevant factors.

Securities Transactions and Investment Income: Investment security transactions are accounted for on a trade date basis. Dividend income is recorded on the ex-dividend date. Certain dividend income from foreign securities will be recorded, in the exercise of reasonable diligence, as soon as the Fund is informed of the dividend if such information is obtained subsequent to the ex-dividend date and may be subject to withholding taxes in these jurisdictions. Interest income, which includes amortization of premium and accretion of discount, is recorded on the accrual basis. Realized gains and losses from securities transactions and unrealized appreciation and depreciation of securities are determined using the first-in/first-out cost basis method for both financial reporting and tax purposes.

Fair Value Measurements: The Fund discloses the classification of its fair value measurements following a three-tier hierarchy based on the inputs used to measure fair value. Inputs refer broadly to the assumptions that market participants would use in pricing the asset or liability, including assumptions about risk. Inputs may be observable or unobservable. Observable inputs reflect the assumptions market participants would use in pricing the asset or liability that are developed based on market data obtained from sources independent of the reporting entity. Unobservable inputs reflect the reporting entity's own assumptions about the assumptions market participants would use in pricing the asset or liability that are developed based on the best information available.

Various inputs are used in determining the value of the Fund's investments as of the end of the reporting period. When inputs used fall into different levels of the fair value hierarchy, the level in the hierarchy within which the fair value measurement falls is determined based on the lowest level input that is significant to the fair value measurement in its entirety. The designated input levels are not necessarily an indication of the risk or liquidity associated with these investments. These inputs are categorized in the following hierarchy under applicable financial accounting standards:

These inputs are categorized in the following hierarchy under applicable financial accounting standards:

Level 1 Unadjusted quoted prices in active markets for identical investments, unrestricted assets or liabilities that a Fund has the ability to access at the measurement date;

Level 2 Quoted prices which are not active, quoted prices for similar assets or liabilities in active markets or inputs other than quoted prices that are observable (either directly or indirectly) for substantially the full term of the asset or liability; and

Level 3 Significant unobservable prices or inputs (including the Fund's own assumptions in determining the fair value of investments) where there is little or no market activity for the asset or liability at the measurement date.

The following is a summary of the inputs used to value the Fund's investments as of July 31, 2018:

Investments in Securities at Value*	Level 1 - Quoted Prices	Level 2 - Other Significant Observable Inputs	Level 3 - Significant Unobservable Inputs	Total
Common Stocks	\$70,904,179	\$—	\$ —	\$70,904,179
Commercial Mortgage Backed Securities	—	122,828,253	—	122,828,253
Short Term Investments	2,925,385	—	—	2,925,385
Total	\$73,829,564	\$122,828,253	\$ —	\$196,657,817

*See Statement of Investments for industry classifications.

The Fund recognizes transfers between levels as of the end of the period. For the nine months ended July 31, 2018, the Fund did not have any significant transfers between Level 1 and Level 2 securities. The Fund did not have any securities that used significant unobservable inputs (Level 3) in determining fair value.

Commercial Mortgage Backed Securities (“CMBS”): As part of its investments in commercial real estate related securities, the Fund will invest in CMBS which are subject to certain risks associated with direct investments in CMBS. A CMBS is a type of mortgage-backed security that is secured by a loan (or loans) on one or more interests in commercial real estate property. Investments in CMBS are subject to the various risks which relate to the pool of underlying assets in which the CMBS represents an interest. CMBS may be backed by obligations (including certificates of participation in obligations) that are principally secured by commercial real estate loans or interests therein having multi-family or commercial use. Securities backed by commercial real estate assets are subject to securities market risks as well as risks similar to those of direct ownership of commercial real estate loans because those securities derive their cash flows and value from the performance of the commercial real estate underlying such investments and/or the owners of such real estate.

Real Estate Investment Trusts (“REITs”): As part of its investments in real estate related securities, the Fund will invest in REITs and is subject to certain risks associated with direct investment in REITs. REITs possess certain risks which differ from an investment in common stocks. REITs are financial vehicles that pool investors’ capital to acquire, develop and/or finance real estate and provide services to their tenants. REITs may concentrate their investments in specific geographic areas or in specific property types, e.g., regional malls, shopping centers, office buildings, apartment buildings and industrial warehouses. REITs may be affected by changes in the value of their underlying properties and by defaults by borrowers or tenants. REITs depend generally on their ability to generate cash flow to make distributions to shareowners, and certain REITs have self-liquidation provisions by which mortgages held may be paid in full and distributions of capital returns may be made at any time.

As REITs generally pay a higher rate of dividends than most other operating companies, to the extent application of the Fund’s investment strategy results in the Fund investing in REIT shares, the percentage of the Fund’s dividend

income received from REIT shares will likely exceed the percentage of the Fund's portfolio that is comprised of REIT shares. Distributions received by the Fund from REITs may consist of dividends, capital gains and/or return of capital.

Dividend income from REITs is recognized on the ex-dividend date. The calendar year-end amounts of ordinary income, capital gains, and return of capital included in distributions received from the Fund's investments in REITs are reported to the Fund after the end of the calendar year; accordingly, the Fund estimates these amounts for accounting purposes until the characterization of REIT distributions is reported to the Fund after the end of the calendar year. Estimates are based on the most recent REIT distribution information available.

The performance of a REIT may be affected by its failure to qualify for tax-free pass-through of income under the Internal Revenue Code of 1986, as amended (the "Code"), or its failure to maintain exemption from registration under the 1940 Act. Due to the Fund's investments in REITs, the Fund may also make distributions in excess of the Fund's earnings and capital gains. Distributions, if any, in excess of the Fund's earnings and profits will first reduce the adjusted tax basis of a holder's Common Shares and, after that basis has been reduced to zero, will constitute capital gains to the Common Shareholder.

Concentration Risk: The Fund invests in companies in the real estate industry, which may include CMBS, REITs, REIT-like structures, and other securities that are secured by, or otherwise have exposure to, real estate. Any fund that concentrates in a particular segment of the market will generally be more volatile than a fund that invests more broadly. Any market price movements, regulatory changes, or economic conditions affecting CMBS, REITs, REIT-like structures, and real estate more generally, will have a significant impact on the Fund's performance.

Foreign Currency Risk: The Fund expects to invest in securities denominated or quoted in currencies other than the U.S. dollar. Changes in foreign currency exchange rates may affect the value of securities owned by the Fund, the unrealized appreciation or depreciation of investments and gains on and income from investments. Currencies of certain countries may be volatile and therefore may affect the value of securities denominated in such currencies, which means that the Fund's net asset value could decline as a result of changes in the exchange rates between foreign currencies and the U.S. dollar. These risks often are heightened for investments in smaller, emerging capital markets.

The accounting records of the Fund are maintained in U.S. dollars. Prices of securities denominated in foreign currencies are translated into U.S. dollars at the closing rates of the exchanges at period end. Amounts related to the purchase and sale of foreign securities and investment income are translated at the rates of exchange prevailing on the respective dates of such transactions.

Reported net realized foreign exchange gains or losses arise from sales of foreign currencies, currency gains or losses realized between the trade and settlement dates on securities transactions, and the difference between the amounts of dividends, interest, and foreign withholding taxes recorded on the Fund's books and the U.S. dollar equivalent of the amounts actually received or paid. Net unrealized foreign exchange gains and losses arise from changes in the fair values of assets and liabilities, other than investments in securities at fiscal period-end, resulting from changes in exchange rates.

A foreign currency contract is a commitment to purchase or sell a foreign currency at a future date, at a negotiated rate. The Fund may enter into foreign currency contracts to settle specific purchases or sales of securities denominated in a foreign currency and for protection from adverse exchange rate fluctuation. Risks to a Fund include the potential inability of the counterparty to meet the terms of the contract.

Item 2 – Controls and Procedures.

The Registrant's Principal Executive Officer and Principal Financial Officer have evaluated the Registrant's disclosure controls and procedures (as defined in Rule 30a-3(c) under the Investment Company Act of 1940) within (a) 90 days of this filing and have concluded that the Registrant's disclosure controls and procedures were effective, as of that date.

There was no change in the Registrant's internal control over financial reporting (as defined in Rule 30a-3(d) under (b) the Investment Company Act of 1940) during Registrant's last fiscal quarter that has materially affected, or is reasonably likely to materially affect, the Registrant's internal control over financial reporting.

Item 3 – Exhibits.

Separate certifications for the Registrant's Principal Executive Officer and Principal Financial Officer, as required by Section 302 of the Sarbanes-Oxley Act of 2002 and Rule 30a-2(a) under the Investment Company Act of 1940, are attached as EX99.CERT.

SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934 and the Investment Company Act of 1940, the registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

PRINCIPAL REAL ESTATE INCOME FUND

By: /s/ Jeremy Held
Jeremy Held
President (Principal Executive Officer)

Date: September 27, 2018

Pursuant to the requirements of the Securities Exchange Act of 1934 and the Investment Company Act of 1940, this report has been signed below by the following persons on behalf of the registrant and in the capacities and on the dates indicated.

By: /s/ Jeremy Held
Jeremy Held
President (Principal Executive Officer)

Date: September 27, 2018

By: /s/ Kathryn Burns
Kathryn Burns
Treasurer (Principal Financial Officer)

Date: September 27, 2018