MARTIN MIDSTREAM PARTNERS LP
Form 10-K
March 05, 2007

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

FORM 10-K

Mark One

þ **Annual Report Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934**
For the fiscal year ended December 31, 2006

OR

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 number 000-50056
MARTIN MIDSTREAM PARTNERS L.P.
(Exact name of registrant as specified in its charter)

Delaware	05-0527861
State or other jurisdiction of incorporation or organization	(I.R.S. Employer Identification No.)
4200 Stone Road Kilgore, Texas (Address of principal executive offices)	**75662** (Zip Code)

903-983-6200
(Registrant s telephone number, including area code)

Securities Registered Pursuant to Section 12(b) of the Act:
NONE
Securities Registered Pursuant to Section 12(g) of the Act:

Title of each class	Name of each exchange on which registered
Common Units representing limited partnership interests	NASDAQ

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

Yes o No þ

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 þ

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

Yes þ No o

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of registrant s knowledge, in definitive proxy or information statements

incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K. o

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, or a non-accelerated filer. See definition of accelerated filer and large accelerated filer in Rule 12b-2 of the Exchange Act. (Check one):

Large accelerated filer o Accelerated filer þ Non-accelerated filer o

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

Yes o No þ

As of June 30, 2006, 9,282,652 common units were outstanding. The aggregate market value of the common units held by non-affiliates of the registrant as of such date approximated $245,347,657. There were 10,603,808 of the registrant s common units and 2,552,018 of the registrant s subordinated units outstanding as of March 5, 2007.

DOCUMENTS INCORPORATED BY REFERENCE: None.

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PART I

Item 1. Business

Overview

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

Terminalling and storage services for petroleum products and by-products

Natural gas services

Marine transportation services for petroleum products and by-products

Sulfur gathering, processing and distribution

Fertilizer manufacturing and distribution

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

We were formed in 2002 by Martin Resource Management Corporation (Martin Resource Management), a privately-held company whose initial predecessor was incorporated in 1951 as a supplier of products and services to drilling rig contractors. Since then, Martin Resource Management has expanded its operations through acquisitions and internal expansion initiatives as its management identified and capitalized on the needs of producers and purchasers of hydrocarbon products and by-products and other bulk liquids. Martin Resource Management owns an approximate 38.6% limited partnership interest in us. Furthermore, it owns and controls our general partner, which owns a 2.0% general partner interest and incentive distribution rights in us.

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

Primary Business Segments

Our primary business segments can be generally described as follows:

Terminalling and Storage. We own or operate 17 marine terminal facilities and four inland terminal facilities located in the United States Gulf Coast region that provide storage and handling services for producers and suppliers of petroleum products and by-products, lubricants and other liquids. We also provide land rental to oil and gas companies along with storage and handling services for lubricants and fuel oil.

Natural Gas Services. Through our acquisition of Prism Gas Systems I, L.P. (Prism Gas), we have ownership interests in over 440 miles of natural gas gathering pipelines located in the natural gas producing regions of Central and East Texas, Northwest Louisiana, the Texas Gulf Coast and offshore Texas and federal waters in the Gulf of Mexico as well as a 150 MMcfd capacity natural gas processing plant located in East Texas which is currently being expanded to 250 MMcfd. In addition to our newly acquired natural gas gathering and processing business, we distribute natural gas liquids or, NGLs . We purchase NGLs primarily from natural gas processors. We store NGLs in our supply

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and storage facilities for resale to propane retailers, refineries and industrial NGL users in Texas and the Southeastern United States. We own three NGL supply and storage facilities with an aggregate above ground storage capacity of approximately 132,000 gallons and we lease approximately 72 million gallons of underground storage capacity for NGLs.

Marine Transportation. We own a fleet of 37 inland marine tank barges, 16 inland push boats and four offshore tug barge units that transport petroleum products and by-products primarily in the United States Gulf Coast region. We provide these transportation services on a fee basis primarily under annual contracts. In addition, our marine segment manages our sulfur segment s marine assets.

Sulfur. We gather, process and distribute sulfur predominately produced by oil refineries primarily located in the United States Gulf Coast region. We process molten sulfur into prilled, or pelletized, sulfur under both fee-based volume contracts and buy/sell contracts at our facility in Port of Stockton, California. In December 2005, we completed the construction of an additional sulfur priller at our Neches terminal in Beaumont, Texas. In July 2005, we acquired the remaining interests in CF Martin Sulphur L.P. (CF Martin Sulphur) not previously owned by us. CF Martin Sulphur gathered, transported and stored molten sulfur supplied by oil refineries.

Fertilizer. We own and operate six fertilizer production plants and one emulsified sulfur blending plant that manufacture primarily sulfur-based fertilizer products for wholesale distributors and industrial users. These plants are located in Illinois, Texas and Utah.

2006 Developments and Subsequent Events

Recent Acquisitions

Acquisition of the La Force Marine Vessel. In November 2006, we acquired the *La Force*, an offshore tug, for $6.0 million from a third party. This vessel is a 5,100 horse power offshore tug that was rebuilt in 1999 with new engines installed in 2005. The addition of the *La Force* to our fleet will eliminate the need for chartered offshore horsepower.

Acquisition of Asphalt Terminals. In August 2006 and October 2006, respectively, we acquired the assets of Gulf States Asphalt Company LP and Prime Materials and Supply Corporation (Prime), for $4.9 million. These assets are located in Houston, Texas and Port Neches, Texas. In connection with these acquisitions, we entered into an agreement with Martin Resource Management, whereby Martin Resource Management will operate the acquired facilities through a terminalling service agreement based upon throughput rates and will assume all additional expenses to operate the facilities.

Acquisition of the Corpus Christi Barge Terminal. In July 2006, we acquired a marine terminal located near Corpus Christi, Texas and associated assets from Koch Pipeline Company, L.P. for $6.2 million, which was all allocated to property, plant and equipment. The terminal is located on approximately 25 acres of land and includes three tanks with a combined capacity of approximately 240,000 barrels, pump and piping infrastructure for truck unloading and product delivery to two oil docks.

Acquisition of the Texan, Ponciana and M450. In January 2006, we acquired the *Texan*, an offshore tug, and the *Ponciana*, an offshore NGL barge, for $5.9 million from Martin Resource Management. In February 2006, we acquired the *M450*, an offshore barge, for $1.6 million from a third party.

Other Developments

Increased Quarterly Distribution. We declared a quarterly cash distribution for the fourth quarter of 2006 of $0.62 per common and subordinated unit on January 22, 2007, reflecting an increase of $0.01 per unit over the quarterly distribution paid in respect of the third quarter of 2006.

Issuance of Common Units. In December 2006, we issued 470,484 common units to Martin Product Sales LLC, an affiliate of Martin Resource Management, for approximately $15.3 million, including a capital contribution of approximately $0.3 million made by our general partner in order to maintain its 2% general partner interest in us. These funds were used to pay down our revolving line of credit.

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Conversion of Subordinated Units. On November 14, 2006, 850,672 of our 3,402,690 outstanding subordinated units owned by Martin Resource Management and its subsidiaries converted into common units on a one-for-one basis following our quarterly cash distribution on such date. Additional conversions of our outstanding subordinated units may occur in the future provided that certain distribution thresholds contained in our partnership agreement are met by us.

Public Offering. In January 2006, we completed a follow-on public offering of 3,450,000 common units, resulting in proceeds of $95.4 million, after payment of underwriters discounts, commissions and offering expenses. Our general partner contributed $2.1 million in cash to us in conjunction with the offering in order to maintain its 2% general partner interest in us. Of the net proceeds, $62.0 million was used to pay then current balances under our revolving credit facility and $7.5 million was used to fund a portion of the redemption price for our U.S. Government Guaranteed Ship Financing Bonds. The remainder of the net proceeds has been or will be used to fund future organic growth projects.

Business Strategy

The key components of our business strategy are to:

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

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

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

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

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

Competitive Strengths

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

Asset Base and Integrated Distribution Network. We operate a diversified asset base that, together with the services provided by Martin Resource Management, enables us to offer our customers an

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integrated distribution network consisting of transportation, terminalling and midstream logistical services while minimizing our dependence on the availability and pricing of services provided by third parties. Our integrated distribution network enables us to provide customers a complementary portfolio of transportation, terminalling, distributions and other midstream services for petroleum products and by-products.

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

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

Ability to Grow Our Natural Gas Gathering and Processing Services. We believe that, with our Prism Gas assets, we have opportunities for organic growth in our natural gas gathering and processing operations through increasing fractionation capacity, pipeline expansions, new pipeline construction and bolt-on acquisitions.

Experienced Management Team and Operational Expertise. Members of our executive management team and the heads of our principal business lines have, on average, more than 26 years of experience in the industries in which we operate. Further, these individuals have been employed by Martin Resource Management, on average, for more than 23 years. Our management team has a successful track record of creating internal growth and completing acquisitions. We believe our management team s experience and familiarity with our industry and businesses are important assets that assist us in implementing our business strategies.

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

Financial Flexibility. We believe the borrowings available under our credit facility and our ability to issue additional partnership units provide us with the financial flexibility necessary to enable us to pursue expansion and acquisition opportunities.

Terminalling and Storage Segment

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

In the 1990 s, the petroleum industry entered a period of consolidation. Refiners and marketers developed large-scale, cost-efficient operations resulting in several refinery acquisitions, combinations, alliances and joint ventures. This consolidation resulted in major oil companies integrating the various components of their businesses, including terminalling and storage. However, major integrated oil companies later concentrated their focus and resources on their core competencies of exploration, production, refining and retail marketing and examined ways to

lower their distribution costs. Additionally, the Federal Trade Commission required some divestitures of terminal assets in markets in which merged companies, alliances and joint ventures were regarded as having excessive market power.

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As a result of these factors, oil and gas companies began to increasingly rely on third parties such as us to perform many terminalling and storage services.

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

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

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

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

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

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

Full Service Terminals. We own or operate eight full service terminals. These terminal facilities provide logistical support services, distribute and market lubricants and provide storage and handling services for fuel oil. The significant difference between our full service terminals and our fuel and lubricant terminals is that our full service terminals generate additional revenues by providing shore bases to support our customer s operating activities related

to the offshore exploration and production industry. One typical use for our shore bases is for drilling fluids manufacturers to manufacture and sell drilling fluids to the offshore drilling industry. Offshore drilling companies may also set up service facilities at these terminals to support their offshore operations. Customers are primarily oil and gas

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exploration and production companies, and oilfield service companies such as drilling fluids companies, marine transportation companies, and offshore construction companies.

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

Terminal	Location	Acres	Tanks	Aggregate Capacity
Pelican Island	Galveston, Texas	51.3	14	57,200 Bbls.
Harbor Island(1)	Harbor Island, Texas	25.5	10	37,400 Bbls.
Freeport	Freeport, Texas	17.8	1	8,300 Bbls.
Port O Connor(2)	Port O Connor, Texas	22.8	8	7,000 Bbls.
Sabine Pass(3)	Sabine Pass, Texas	23.1	11	18,100 Bbls.
Cameron East (4)	Cameron, Louisiana	34.3	7	33,000 Bbls.
Cameron West (5)	Cameron, Louisiana	16.9	5	19,000 Bbls.
Venice (6)	Venice, Louisiana	2.8	2	15,000 Bbls.

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

(2) This terminal is located on land owned by a third party and leased under a lease that expires in March 2009 and can be extended by us through March 2014.

(3) A portion of this terminal is located on land owned by a third party and leased under a lease that expires in September 2016 and can be renewed by us through September 2036.

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

(5) This terminal is located on land owned by a third party and leased under a lease that expires in February 2008 and can be extended by us through February 2013.

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

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

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

Terminal	Location	Tanks	Aggregate Capacity
Amelia	Amelia, Louisiana	17	14,900 Bbls.
Berwick(1) Intracoastal	Berwick, Louisiana	4	24,900 Bbls.
City(2)(3)	Intracoastal City, Louisiana	17	34,300 Bbls.
Fourchon(4)	Fourchon, Louisiana	7	30,100 Bbls.

(1) This terminal is located on land owned by third parties and leased under a lease that

expires in September 2007 and can be extended by us through September 2017.

(2) A portion of this terminal is located on land owned by a third party at which we throughput fuel oil pursuant to an agreement that expires in November 2007.

(3) A portion of this terminal is located on land owned by third parties and leased under a lease that expires in April 2009 and can be extended by us through April 2014.

(4) This terminal is located on land owned by a third party at which we throughput lubricants and fuel oil pursuant to an agreement that expires in January 2017.

Specialty Petroleum Terminals. We own or operate five terminal facilities providing storage and handling services for some or all of the following: anhydrous ammonia, asphalt, sulfur, sulfuric acid, fuel oil, crude oil and other petroleum products and by-products. Our specialty terminals have an aggregate storage capacity of approximately 1.75 million barrels. Each of these terminals has storage capacity for petroleum products and by-products and has assets to handle products transported by vessel, barge and truck. Our Tampa terminal is located on approximately 10 acres of land owned by the Tampa Port Authority that was leased to us under a 10-year lease that expired on December 15, 2006. We are currently leasing this facility on a month-to-month basis and have received a proposal for a new lease agreement that extends the term of the lease for 10 years with two five year options. Our Stanolind terminal is located on approximately 11 acres of land owned by Martin Resource Management and us and located on the Neches River in

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Beaumont. Our Neches terminal is a deep water marine terminal located near Beaumont, Texas on approximately 50 acres of land owned by us. Our Ouachita County terminal is located on approximately six acres of land owned by us on the Ouachita River in southern Arkansas. Our Corpus Christi terminal is located on approximately 25 acres of land owned by us and has access to the waterfront via marine docks owned by the Port of Corpus Christi.

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

Terminal	Location	Tanks(3)	Aggregate Capacity	Products	Description
Tampa(1)	Tampa, Florida	7	719,000 Bbls.	Asphalt and fuel oil	Marine terminal, loading/unloading for vessels, barges and trucks
Stanolind(2)	Beaumont, Texas	2	160,000 Bbls.	Asphalt and fuel oil	Marine terminal, loading/unloading for vessels, barges and trucks
Neches	Beaumont, Texas	7	500,400 Bbls.	Ammonia, asphalt, fuel oil, sulfuric acid and fertilizer	Marine terminal, loading/unloading for vessels, barges, railcars and trucks
Ouachita County	Ouachita County, Arkansas	2	77,500 Bbls.	Crude oil	Marine terminal, loading/unloading for vessels, barges and trucks
Corpus Christi	Corpus Christi, Texas	3	249,000Bbls.	Fuel oil and diesel	Marine Terminal, loading/unloading barges and vessels and unloading trucks

(1) This terminal is located on land owned by the Tampa Port Authority that was leased to us under a lease that expired in December 2006. We are currently leasing this

facility on a month-to-month basis and have received a proposal for a new lease agreement that extends the term for 10 years with two additional five year extension options.

(2) A portion of this terminal is located on land owned by Martin Resource Management and on land we own. We use marine terminal, loading and unloading, and other common use facilities owned by Martin Resource Management under a perpetual use, ingress-egress and utility facilities easement.

(3) In addition to the tanks listed in the table we own one tank at our Tampa terminal and three tanks at the Stanolind terminal in connection with our sulfur business. Martin Resource Management owns two tanks

at the Stanolind terminal.

Inland Terminals. We own or operate four inland terminals. At Mont Belvieu, Texas, we own a rail unloading terminal where we unload and measure petroleum by-products and transport these products via a half-mile pipeline to Enterprise Products Texas Operating L.P. s NGL fractionator facility. Our fees for the use of this facility are based on the number of gallons unloaded at the terminal. In Channelview, Texas, we operate an inland terminal used for lubricant storage, packaging and distribution. This terminal is used as our central hub for lubricant distribution where we receive, package, and ship our lubricants to our terminals or directly to customers. In Houston, Texas, we own an asphalt terminal whose use is dedicated to an affiliate of Martin Resource Management through a terminalling

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

The following is a summary description our inland terminals:

Terminal	Location	Aggregate Capacity	Products	Description
Channelview(1)	Houston, Texas	10,000 sq. ft. warehouse	Lubricants	Truck loading/unloading
Mont Belvieu South Houston	Mont Belvieu, Texas	20 rail car spaces	Propane-propylene mix	Rail car unloading
Asphalt	Houston, Texas	71,000 bbls	Asphalt	Asphalt Processing and storage
Port Neches Asphalt	Port Neches, Texas	31,250 bbls	Asphalt	Asphalt Processing and storage

(1) This terminal is located on land owned by a third party and leased to us under a lease that expires in May 2009 and can be extended by us to May 2014.

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

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

We believe we successfully compete for terminal customers because of the strategic location of our terminals along the Gulf Coast, our integrated transportation services, our reputation, the prices we charge for our services and the quality and versatility of our services. Additionally, while some companies have significantly more terminalling and storage capacity than us, not all terminalling and storage facilities located in the markets we serve are equipped to properly handle specialty products such as asphalt, sulfur or sulfuric acid. As a result, our facilities typically command higher terminal fees when compared to fees charged for terminalling and storage of other petroleum products.

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

equipped marine terminals, shore bases and lubricant supply sources.

Natural Gas Services Segment

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

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

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

storage of NGLs purchased in off-peak months;

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

product management expertise to obtain supplies when needed.

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

NGL Facility(1)	Location	Capacity	Description
Retail terminals	Kilgore, Texas	90,000 gallons	Retail propane distribution
	Longview, Texas	30,000 gallons	Retail propane distribution
	Henderson, Texas	12,000 gallons	Retail propane distribution storage
	Arcadia, Louisiana(2)	65 million gallons	Underground storage
	Hattiesburg, Mississippi(3)	4.2 million gallons	Underground storage
	Mt. Belvieu, Texas(3)	2.8 million gallons	Underground storage

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

renews for consecutive one-year periods unless either party terminates the agreement by giving written notice to the other party at least 30 days prior to the expiration of the then-applicable term. This terminal facility has a storage capacity of 330,000 gallons.

(2) We lease our underground storage at Arcadia, Louisiana from Martin Resource Management under a three-year product storage agreement, which is renewable on a yearly basis thereafter subject to a re-determination of the lease rate for each subsequent year.

(3) We lease our underground storage at Hattiesburg, Mississippi and Mont Belvieu, Texas from third parties under one-year lease agreements, which have been

renewed annually for more than 20 years.

Our NGL customers that utilize these assets consist of retail propane distributors, industrial processors and refiners. For the year ended December 31, 2006, we sold approximately 37% of our NGL volume to independent retail propane distributors located in Texas and the southeastern United States and approximately 63% of our NGL volume to refiners and industrial processors.

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

NGL Seasonality. The level of NGL supply and demand is subject to changes in domestic production, weather, inventory levels and other factors. While production is not seasonal, residential and wholesale demand is highly seasonal. This imbalance causes increases in inventories during summer months when consumption is low and decreases in inventories during winter months when consumption is high. If inventories are low at the start of the winter, higher prices are more likely to occur during the winter. Additionally, abnormally cold weather can put extra upward pressure on prices during the winter because there are less readily available sources of additional supply except

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for imports which are less accessible and may take several weeks to arrive. General economic conditions and inventory levels have a greater impact on industrial and refinery use of NGLs than the weather.

Although the NGL industry is subject to seasonality factors, such factors generally do not affect our natural gas services business because we do not consume NGLs. We generally maintain consistent margins in our natural gas services business because we attempt to pass increases and decreases in the cost of NGLs directly to our customers. We generally try to coordinate our sales and purchases of NGLs based on the same daily price index of NGLs in order to decrease the impact of NGL price volatility on our profitability.

Prism Gas Acquisition. On November 10, 2005 we acquired Prism Gas. Following this acquisition, Prism Gas is operated and reported as part of our natural gas services business segment, which has been expanded to include natural gas gathering and processing as well as the NGL services business described herein.

Prism Gas has ownership interests in over 440 miles of natural gas gathering pipelines located in the natural gas producing regions of North Central Texas and East Texas, Northwest Louisiana, the Texas Gulf Coast and offshore Texas and federal waters in the Gulf of Mexico as well as a 150 MMcfd natural gas processing plant located in East Texas which is currently being expanded to 250 MMcfd. The underlying assets are in two operating areas:

North Central Texas and East Texas

The North Central Texas and East Texas area assets consist of the Waskom Processing Plant, the McLeod Gathering System, the Hallsville Gathering System, the Marshall Line, Bosque County Pipeline and the East Texas Gathering System.

Waskom Processing Plant The Waskom Processing Plant, located in Harrison County in East Texas, currently has 150 MMcfd of processing capacity with full fractionation facilities. In January 2007, the Waskom fractionator was expanded to a capacity of 12,500 barrels per day. In addition, an increase in the processing capacity of the plant to 250 MMcfd is expected to be completed by the end of the second quarter of 2007. For the year ended December 31, 2006, inlet throughput and NGL fractionation averaged approximately 183 MMcfd and 7,677 bpd, respectively. Prism Gas owns an unconsolidated 50% operating interest in the Waskom Processing Plant with CenterPoint Energy Gas Processing, Inc. owning the remaining 50% non-operating interest. We reflect the results of operations from this facility using the equity method of accounting.

McLeod Gathering System The McLeod Gathering System, located in East Texas and Northwest Louisiana, is a low pressure gathering system connected to the Waskom Processing Plant, providing processing and blending services for natural gas with high nitrogen and high liquids content gathered by the system. For the year ended December 31, 2006, the McLeod Gathering System gathered approximately 6 MMcfd of natural gas. Prism Gas owns a consolidated 100% interest in this system.

Hallsville Gathering System The Hallsville Gathering System, which Prism Gas constructed in 2006, is located in Harrison County, Texas, provides gathering and centralized compression for producers in the Oak Hill Field of East Texas. The system operates at low pressure and redelivers gas to two interstate and three intrastate markets via the Oakhill Gathering System. Prism Gas owns a consolidated 100% interest in this system.

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

Bosque County Pipeline The Bosque County Pipeline, gathers gas in four North Central Texas counties centered around Bosque County. Prism Gas owns an unconsolidated 20% non-operating

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interest in a partnership that owns the lease rights to the assets of the Bosque County Pipeline, with Panther Pipeline Ltd. owning a 42.5% operating interest and Star of Texas, et al owning the remaining 37.5% interest.

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

The natural gas supply for the Waskom Processing Plant, the McLeod Gathering System, the Hallsville Gathering System, the Marshall Line and the East Texas Gathering System is derived primarily from natural gas wells located in the Cotton Valley formation of East Texas and Northwest Louisiana. The Cotton Valley formation is one of the largest tight gas plays in the U.S. and extends over fourteen counties in East Texas and into Northwest Louisiana. Prism Gas East Texas Operating Area includes assets that provide gathering and processing services to producers in Cass, Gregg, Harrison, Panola, and Rusk Counties, Texas and Caddo Parish, Louisiana. The total number of wells permitted in Prism Gas East Texas Operating Area was 1,878 and 1,512 in calendar years 2006 and 2005, respectively. These annual permit numbers include 22 permits for horizontal wells in 2006 and 10 permits for horizontal wells in 2005. Improved technology, drilling applications and commodity prices have enhanced the economics of drilling in the Cotton Valley formation. This increase in drilling activity has provided us with access to newly developed natural gas supplies.

The natural gas supply for the Bosque County Pipeline is expected to be derived primarily from natural gas wells in the Barnett Shale formation of North Central Texas. The Bosque County Pipeline is located in the southern extension of the Barnett Shale formation.

Our primary suppliers of natural gas to the Waskom Processing Plant include BP America Production Company, Centerpoint Energy Gas Transmission Company and Devon Energy Corporation, which collectively represented approximately 62% of the 160 MMcfd of natural gas supplied in 2005 and approximately 61% of the 183 MMcfd of natural gas supplied for the year ended December 31, 2006. A substantial portion (approximately 35%) of the Waskom Processing Plant s inlet volumes are derived from production at BP s Blocker, East Mountain, Carthage and Woodlawn fields in East Texas. Production from these fields is dedicated to the Waskom Processing Plant under a contract with BP for the life of the Waskom partnership. We receive natural gas at the Waskom Processing Plant from our McLeod Gathering System. We also receive a significant amount of trucked-in NGLs that are fractionated, treated and stabilized at the Waskom Processing Plant. The tightening of pipeline dew point specifications and access to local markets with high NGL demand has resulted in increased trucked-in NGL volumes at the Waskom Processing Plant. In October 2006, we began construction to expand the fractionator to 12,500 bpd. to provide additional capacity for this increase in trucked-in NGL volumes. This expansion was completed in late January 2007.

There are currently three competing processing plants, with another two under construction, that operate or will operate within a 40-mile radius of our Waskom facility. Drilling activity in the Cotton Valley trend is moving north from the Panola-Harrison County line further into Harrison County. Our plant is the preferred gas plant for much of this new production due to its proximity to the increased drilling activity. In addition, the Waskom Processing Plant is the only plant in this area that has full fractionation capability with access to strong local markets for NGLs. Purchasers of NGLs fractionated at Waskom include various chemical companies and other industrial distributors. Prior to the Prism Gas acquisition, we were one of the largest purchasers of NGLs at the Waskom Processing Plant.

The Waskom Processing Plant s processing contracts are predominately percent-of-liquids (POL) contracts, in which we retain a portion of the NGLs recovered as a processing fee. The plant also operates under percent-of-proceeds (POP) contracts in which we retain a portion of both the residue gas and the NGLs as payment for services. There are currently only two minor contracts for processing on a keep-whole basis. We are not contractually required to process these keep-whole volumes and, therefore, only process natural gas related to these contracts under profitable conditions.

The McLeod Gathering System is a low-pressure gathering system that provides an outlet for high nitrogen and high liquids content gas. In June 2003, Prism Gas constructed a pipeline to tie the McLeod Gathering System to the Waskom Processing Plant to provide an outlet for high nitrogen gas. As a result, the majority of gas gathered on

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the McLeod Gathering System is transported to the Waskom Processing Plant for processing and blending. Revenue from the McLeod Gathering System is earned through gathering and compression fees and processing revenue. The processing revenue results from the difference in the processing agreements with the producers and the agreement that we have with the Waskom partnership. The processing contracts in the McLeod Gathering System are predominately percent-of-proceeds (POP) contracts. Natural gas gathered in the region surrounding the McLeod Gathering System has two primary outlets, including the Waskom Processing Plant.

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

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

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

The Bosque County Pipeline is an approximate 67 mile pipeline located in the Barnett Shale extension. The pipeline traverses four counties with the most concentrated drilling occurring in Bosque County. In this area competition is limited due to a lack of existing infrastructure. The lack of infrastructure and the limited development in the area allow it to generally capture new wells drilled in close proximity to its system.

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

Gulf Coast

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

Fishhook Gathering System The Fishhook Gathering System, located in Jefferson County, Texas and offshore federal waters, gathers and transports gas in both offshore and onshore areas. For the year ended December 31, 2006, the Fishhook Pipeline gathered and transported approximately 32 MMcfd of natural gas. Prism Gas owns an unconsolidated 50% non-operating interest in Panther Interstate Pipeline Energy, LLC, the owner of the Fishhook Gathering System, with Panther Pipeline Ltd owning the remaining 50% operating interest. We reflect the results of operations from this system using the equity method of accounting.

Matagorda Offshore Gathering System The Matagorda Offshore Gathering System, located in Matagorda County, Texas and offshore Texas state waters, gathers gas in both the offshore and onshore areas. For the year ended December 31, 2006, the Matagorda Offshore Gathering System gathered approximately 10 MMcfd of natural gas. Prism Gas owns an unconsolidated 50% non-operating interest in the Matagorda Offshore Gathering System, with Panther Pipeline Ltd. owning the remaining 50% operating interest. We reflect the results of operations from this system using the equity method of accounting.

The Fishhook Gathering System and the Matagorda Offshore Gathering System gather and transport natural gas from Texas and federal waters of the Gulf of Mexico to onshore pipelines. The Fishhook Pipeline gathers and transports natural gas principally from the eastern portion of the High Island Area which is further offshore. The offshore natural gas supply for the Matagorda Offshore Gathering System is produced primarily from the Brazos

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Area blocks, which are near shore in the Texas state waters. Additionally, the Matagorda Offshore Gathering System includes onshore gathering in Matagorda, Wharton and Brazoria Counties.

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

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

Marine Transportation Segment

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

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

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

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

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

Class of Equipment	Number in Class	Capacity/Horsepower	Description of Products Carried
Inland tank barges	15	20,000 bbl and under	Asphalt, crude oil, fuel oil, gasoline and sulfur(1)
Inland tank barges	22	20,000 30,000 bbl	Asphalt, crude oil, fuel oil and gasoline(1)
Inland push boats	16	800 1,800 horsepower	N/A

Offshore tank barges	4	40,000 bbl and 95,000 bbl	Asphalt, fuel oil and NGLs
Offshore tugboats	4	3,200 7,200 horsepower	N/A

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(1) One of our 15 inland tank barges with capacity of up to 20,000 bbl, and nine of our 22 inland tank barges with capacity of 20,000 to 30,000 bbl, are specialized and equipped to transport asphalt.

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

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

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

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

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

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

stringent operating standards to adequately address safety and environmental risks;

the elimination of government programs supporting small refineries;

an increase in environmental regulations mandating expensive equipment modification; and

more restrictive and expensive insurance.

There are several barriers to entry into the marine transportation industry that discourage the emergence of new competitors. Examples of these barriers to entry include:

significant start-up capital requirements;

the costs and operational difficulties of complying with stringent safety and environmental regulations;

the cost and difficulty in obtaining insurance; and

the number and expertise of personnel required to support marine fleet operations.

We believe the reduction of the number of tank barges, the consolidation among barging companies and the significant barriers to entry in the industry have resulted in a more stabilized and favorable pricing environment for our marine transportation services.

We believe we compete favorably with many of our competitors. Historically, competition within the marine transportation business was based primarily on price. However, we believe customers are placing an increased emphasis on safety, environmental compliance, quality of service and the availability of a single source of supply of a diversified package of services. In particular, we believe customers are increasingly seeking transportation vendors that

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can offer marine, land, rail and terminal distribution services, as well as provide operational flexibility, safety, environmental and financial responsibility, adequate insurance and quality of service consistent with the customer s own operations and policies. We operate a diversified asset base that, together with the services provided by Martin Resource Management, enables us to offer our customers an integrated distribution network consisting of transportation, terminalling, distribution and midstream logistical services for petroleum products and by-products.

In addition to competitors that provide marine transportation services, we also compete with providers of other modes of transportation, such as rail tank cars, tractor-trailer tank trucks and, to a limited extent, pipelines. We believe we offer a competitive advantage over rail tank cars and tractor-trailer tank trucks because marine transportation is a more efficient, and generally less expensive, mode of transporting petroleum products and by-products. For example, a typical two inland barge unit carries a volume of product equal to approximately 80 rail cars or 250 tanker trucks. Pipelines generally provide a less expensive form of transportation than marine transportation. However, pipelines are not able to transport most of the products we transport and are generally a less flexible form of transportation because they are limited to the fixed point-to-point distribution of commodities in high volumes over extended periods of time.

Seasonality. The demand for our marine transportation business is subject to some seasonality factors. Our asphalt shipments are generally higher during April through November when weather allows for efficient road construction. However, demand for marine transportation of sulfur, fuel oil and gasoline is directly related to production of these products in the oil refining and natural gas processing business, which is fairly stable.

Sulfur Segment

Industry Overview. Sulfur is a natural element and is required to produce a variety of industrial products. In the United States, approximately 11 million tons of sulfur is consumed annually, with the Tampa, Florida area being the largest single market. Currently, all sulfur produced in the United States is recovered sulfur, or sulfur that is a by-product from oil refineries and natural gas processing plants. Sulfur production in the United States is principally located along the Gulf Coast, along major inland waterways and in some areas of the western United States.

Sulfur is an important plant nutrient and is used in the manufacture of phosphate fertilizers. Approximately 53% of worldwide sulfur consumption is currently used for phosphate fertilizers, with the balance used for industrial purposes. The primary application of sulfur in fertilizers occurs in the form of sulfuric acid. Burning sulfur creates sulfur dioxide, which is subsequently oxidized and dissolved in water to create sulfuric acid. The sulfuric acid is then combined with phosphate rock to make phosphoric acid, the base material for most high-grade phosphate fertilizers.

In addition to agricultural applications, sulfur (usually in the form of sulfuric acid) is essential for manufacturing pharmaceuticals, paper, chemicals, paint, steel, petroleum and other products. Sulfuric acid is the most commonly produced chemical in the world.

Our Operations and Products. Our sulfur segment was established in April 2005, as a result of the acquisition of the Bay Sulfur assets and the beginning of construction of a sulfur priller at our Neches facility in Beaumont, Texas. The sulfur prilling assets we acquired from Bay Sulfur are located at the Port of Stockton in California and are used to process molten sulfur into pellets. These dry, bulk pellets are stored and loaded at our facility at the Port of Stockton. The sulfur pellets are sold into certain U.S. and international agricultural markets. Our facility at the Port of Stockton can process approximately 1,000 metric tons of molten sulfur per day. We also have completed the construction of a sulfur priller at our Neches facility in Beaumont, Texas. This facility has the capacity to process approximately 2,000 metric tons of molten sulfur per day. Our sulfur prilling facilities provide refiners with an alternative market for the sale of their residual sulfur.

On July 15, 2005, we acquired the remaining partnership interests in CF Martin Sulphur in which we owned a 49.5% interest since November, 2000 from CF Industries, Inc. and certain affiliates of Martin Resource Management for $18.9 million. Prior to the acquisition, CF Martin Sulphur was managed and operated by its general partner who was equally owned and controlled by certain affiliates of Martin Resource Management and CF Industries. Subsequent to the acquisition, the partnership controlled the management of CF Martin Sulphur and conducted its day to day operations. CF Martin Sulphur, a wholly owned partnership, was included in our consolidated financial statements and included in the financial presentation of our sulfur segment. As of March 30, 2006, CF Martin Sulphur merged into Martin Operating Partnership L.P. and continues to be reported in our sulfur segment and operates doing business as Martin Sulfur.

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Martin Sulfur gathers molten sulfur from refiners, primarily located on the Gulf Coast, and from natural gas processing plants, primarily located in the southwestern United States. We transport sulfur by inland and offshore barges, rail cars and trucks. In 2006, Martin Sulfur handled approximately 1.7 million long tons of sulfur. In the U.S. recovered sulfur is mainly kept in liquid form from production to usage at a temperature of approximately 275 degrees Fahrenheit. Because of the temperature requirement, the sulfur industry uses specialized equipment to store and transport molten sulfur. We have the necessary transportation and storage assets and expertise to handle the unique requirements for transportation and storage of molten sulfur for domestic customers.

The term of our commercial contracts typically range from one to five years in length. The prices in such contracts are usually tied to a published market indicator and fluctuate, typically quarterly, according to the price movement of the indicator. We also provide barge transportation and tank storage to large integrated oil companies that produce sulfur and fertilizer manufacturers that consume sulfur under transportation and storage contracts that range from three to five years in duration.

Our Sulfur Facilities. We lease approximately 180 railcars equipped to transport molten sulfur. We own the following major marine assets and use them to ship molten sulfur from our Beaumont, Texas terminal to our Tampa, Florida terminal:

Asset	Class of Equipment	Capacity/Horsepower	Products Transported
Margaret Sue	Offshore tank barge	10,450 long tons	Molten sulfur
M/V Martin Explorer	Offshore tugboat	7,200 horsepower	N/A
M/V Martin Express	Inland push boat	1,200 horsepower	N/A
MGM 101	Inland tank barge	2,450 long tons	Molten sulfur
MGM 102	Inland tank barge	2,450 long tons	Molten sulfur

We own the following tanks as part of our molten sulfur business:

Terminal	Location	Tanks	Total Aggregate Capacity	Products Stored
Tampa	Tampa, Florida	1	16,000 long tons	Molten sulfur
Stanolind	Beaumont, Texas	3	46,500 long tons	Molten sulfur

We own the following sulfur prilling facilities as part of our sulfur business:

Terminal	Location	Daily Production Capacity	Products Stored
Stockton	Stockton, California	1,000 metric tons per day	Molten and prilled sulfur
Neches	Beaumont, Texas	2,000 metric tons per day	Molten and prilled sulfur

Competition. Seven phosphate fertilizer manufacturers together consume a vast majority of the total United States production of sulfur. These companies buy from resellers as well as directly from producers. We own one of the four vessels currently used to transport molten sulfur between Tampa, Florida and United States ports on the Gulf of Mexico. Our primary competition consists of producers that sell their production directly to a fertilizer manufacturer that has its own transportation assets or foreign suppliers from Mexico or Venezuela that may sell into the Florida market.

Fertilizer Segment

Industry Overview. Fertilizers are manufactured chemicals containing nutrients known to improve the fertility of soils. Nitrogen, phosphorus, potassium and sulfur are the four most important nutrients for crop growth. These nutrients are found naturally in soils. However, soils used for agriculture become depleted of these nutrients and frequently require fertilizers rich in these essential nutrients to restore fertility. The Fertilizer Institute has estimated that the earth s soil contains less than 20% of organic plant nutrients needed to meet worldwide food production needs. As a result, we believe mineral fertilizer production will continue to be an important industrial market.

Industrial sulfur products are used in a wide variety of industries. For example, these products are used in power plants, paper mills, auto and tire manufacturing plants, food processing plants, road construction, cosmetics and pharmaceuticals. The largest consumers of industrial sulfur products are power plants, paper mills and rubber products manufacturers.

Our Operations and Products. We entered the fertilizer manufacturing business in 1990 through an acquisition. We acquired two additional fertilizer manufacturing companies in 1998. Over the next two years we

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expended significant resources to replace and update facilities and other assets at the companies, and to integrate each of the businesses into our business. These acquisitions have subsequently increased the profitability of our fertilizer business. In December 2005, sulfur fertilizer production capacity was added with the purchase of the net operating assets of A & A Fertilizer, Ltd. (A & A Fertilizer). This production capacity is located at our Neches deep-water marine terminal near Beaumont, Texas.

Fertilizer and related sulfur products are a natural extension of our business because of our access to sulfur and our distribution capabilities. This business allows us to leverage the sulfur segment of our business. Our annual fertilizer and industrial sulfur products sales have grown from approximately 62,000 tons in 1997 to approximately 210,000 tons in 2006 as a result of acquisitions and internal growth.

We manufacture and market the following fertilizer and related sulfur products:

Plant nutrient sulfur products. We produce plant nutrient and agricultural ground sulfur products at our two facilities in Odessa, Texas. We also produce plant nutrient sulfur at our facility in Seneca, Illinois. Our plant nutrient sulfur product is a 90% degradable sulfur product marketed under the Disper-Sul® trade name and sold throughout the United States to direct application agricultural markets. Our agricultural ground sulfur products are used primarily in the western United States on grapes and vegetable crops.

Ammonium sulfate products, NPK products and related blended products. We produce various grades of ammonium sulfate including coarse and standard grades, a 40% ammonium sulfate solution and a Kosher-approved food grade material. We also produce nitrogen-phosphorus-potassium products (commonly referred to as NPK products). Our NPK products are an ammoniated phosphate fertilizer containing nitrogen, phosphorus and potash that we manufacture so all particles have a uniform composition. These products primarily serve direct application agricultural markets within a 400-mile radius of our manufacturing plant in Plainview, Texas. We blend our ammonium sulfate to make custom grades of lawn and garden fertilizer at our facility in Salt Lake City, Utah. We package these custom grade products under both proprietary and private labels and sell them to major retail distributors, and other retail customers, of these products.

Industrial sulfur products. We produce industrial sulfur products such as emulsified sulfur, elemental pastille sulfur, and industrial ground sulfur products. We produce emulsified sulfur at our Texarkana, Texas facility. Emulsified sulfur is primarily used to control the sulfur content in the pulp and paper manufacturing processes. We produce elemental pastille sulfur at our two Odessa, Texas facilities and at our Seneca, Illinois facility. Elemental pastille sulfur is used to increase the efficiency of the coal-fired precipitators in the power industry. These industrial ground sulfur products are also used in a variety of dusting and wettable sulfur applications such as rubber manufacturing, fungicides, sugar and animal feeds.

Liquid sulfur products. We produce ammonium thiosulfate at our Neches terminal location in Beaumont, Texas. This agricultural sulfur product is a clear liquid containing 12% nitrogen and 26% sulfur. This product serves as a liquid plant nutrient used directly through spray rigs or irrigation systems. It is also blended with other NPK liquids or suspensions as well. Our market is predominantly the Mid South and Coastal Bend area of Texas.

Our Fertilizer Plants. The following is a summary description of our fertilizer plants:

Facility	Location	Capacity	Description
Two fertilizer plants	Odessa, Texas	70,000 tons/year	Dry sulfur fertilizer production
Fertilizer plant	Seneca, Illinois	36,000 tons/year	Dry sulfur fertilizer production
Fertilizer plant	Plainview Texas	180,000 tons/year	Fertilizer production
Fertilizer plant	Salt Lake City, Utah	25,000 tons/year	Blending and packaging
Industrial sulfur plant	Texarkana, Texas	18,000 tons/year	Emulsified sulfur production
Fertilizer plant	Beaumont, Texas	70,000 tons/year	Liquid sulfur fertilizer Production

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In the United States, fertilizer is generally sold to farmers through local dealers. These dealers are typically owned and supplied by much larger wholesale distributors. We sell primarily to these wholesale distributors, as well as to a small number of independent dealers throughout the United States. Our industrial sulfur products are marketed primarily in the eastern United States, where many paper manufacturers and power plants are located.

Our fertilizer products are sold in accordance with our price lists that vary from state to state. We update our price lists periodically to make seasonal pricing adjustments. If necessary, we adjust our price lists more frequently to maintain competitive pricing. These products are sold at negotiated prices, generally set on an annual basis. We transport our fertilizer and industrial sulfur products to our customers using third party common carriers. We utilize rail shipments for large volume and long distance shipments where available.

Competition. We compete with several other large fertilizer and sulfur products manufacturers. However, we believe our close proximity to our customers is a competitive advantage for us. Because our manufacturing plants are located close to our customer base, we are able to save on freight costs and respond quickly to customer requests, and we also believe we have greater insight about local market conditions. Additionally, we believe the development of our sulfur business affords us a secure and reliable source of sulfur materials.

Seasonality. Sales of our agricultural fertilizer are partly seasonal as a result of increased demand during the growing season. Sales of our industrial sulfur-based products, however, are generally consistent throughout the year. In 2006, approximately 18% of our product sales volumes were to industrial users.

Our Relationship with Martin Resource Management

Martin Resource Management is engaged in the following principal business activities:

providing land transportation of various liquids using a fleet of trucks and road vehicles and road trailers;

distributing fuel oil, asphalt, sulfuric acid, marine fuel and other liquids;

providing marine bunkering and other shore-based marine services in Alabama, Louisiana, Mississippi and Texas;

operating a small crude oil gathering business in Stephens, Arkansas;

operating a lube oil processing facility in Smackover, Arkansas;

operating an underground NGL storage facility in Arcadia, Louisiana;

supplying employees and services for the operation of our business;

operating, for its account and our account, the docks, roads, loading and unloading facilities and other common use facilities or access routes at our Stanolind terminal; and

operating, solely for our account, an NGL truck loading and unloading and pipeline distribution terminal in Mont Belvieu, Texas.

We are and will continue to be closely affiliated with Martin Resource Management as a result of the following relationships.

Ownership

Martin Resource Management owns an approximate 38.6% limited partnership interest and a 2% general partnership interest in us and all of our incentive distribution rights.

Management

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Martin Resource Management directs our business operations through its ownership and control of our general partner. We benefit from our relationship with Martin Resource Management through access to a significant pool of management expertise and established relationships throughout the energy industry. We do not have employees. Martin Resource Management employees are responsible for conducting our business and operating our assets on our behalf.

Related Party Agreements

We are a party to an omnibus agreement with Martin Resource Management. The omnibus agreement requires us to reimburse Martin Resource Management for all direct and indirect expenses it incurs or payments it makes on our behalf or in connection with the operation of our business. We reimbursed Martin Resource Management for $49.1 million of direct costs and expenses for the twelve months ended December 31, 2006 compared to $42.1 million for the twelve months ended December 31, 2005. There is no monetary limitation on the amount we are required to reimburse Martin Resource Management for direct expenses. Under the omnibus agreement, the reimbursement amount with respect to indirect general and administrative and corporate overhead expenses was capped at $2.0 million for the period ending October 31, 2006. Subsequently, this amount may be increased by no more than the percentage increase in the consumer price index. In addition, Martin Resource Management and us can agree, subject to approval of the Conflicts Committee of our general partner, to adjust this amount for expansions of our operations and acquisitions. We reimbursed Martin Resource Management for $1.5 million of indirect expenses for the twelve months ended December 31, 2006 compared to $1.3 million for the twelve months ended December 31, 2005. These indirect expenses cover all of the centralized corporate functions Martin Resource Management provides for us, such as accounting, treasury, clerical billing, information technology, administration of insurance, general office expenses and employee benefit plans and other general corporate overhead functions we share with Martin Resource Management retained businesses. The omnibus agreement also contains significant non-compete provisions and indemnity obligations. Martin Resource Management also licenses certain of its trademarks and trade names to us under the omnibus agreement.

In addition to the omnibus agreement, we and Martin Resource Management have entered into various other agreements that are not the result of arm s-length negotiations and consequently may not be as favorable to us as they might have been if we had negotiated them with unaffiliated third parties. The agreements include, but are not limited to, a motor carrier agreement, a terminal services agreement, a marine transportation agreement, a product storage agreement, a product supply agreement, a throughput agreement, and a Purchaser Use Easement, Ingress-Egress Easement and Utility Facilities Easement. Pursuant to the terms of the omnibus agreement, we are prohibited from entering into certain material agreements with Martin Resource Management without the approval of the conflicts committee of our general partner s board of directors.

For a more comprehensive discussion concerning the omnibus agreement and the other agreements that we have entered into with Martin Resource Management, please see Item 13. Certain Relationships and Related Transactions Agreements.

Commercial

We have been and anticipate that we will continue to be both a significant customer and supplier of products and services offered by Martin Resource Management. Our motor carrier agreement with Martin Resource Management provides us with access to Martin Resource Management s fleet of road vehicles and road trailers to provide land transportation in the areas served by Martin Resource Management. Our ability to utilize Martin Resource Management s land transportation operations is currently a key component of our integrated distribution network.

We also use the underground storage facilities owned by Martin Resource Management in our natural gas services operations. We lease an underground storage facility from Martin Resource Management in Arcadia, Louisiana with a storage capacity of 65 million gallons. Our use of this storage facility gives us greater flexibility in our operations by allowing us to store a sufficient supply of product during times of decreased demand for use when demand increases.

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In the aggregate, our purchases of land transportation services, NGL storage services, sulfuric acid and lube oil product purchases and sulfur and fertilizer payroll reimbursements from Martin Resource Management accounted for approximately 14%, 7% and 6% of our total cost of products sold during the years ended December 31, 2006, 2005 and 2004, respectively. We also purchase marine fuel from Martin Resource Management, which we account for as an operating expense.

Correspondingly, Martin Resource Management is one of our significant customers. It primarily uses our terminalling, marine transportation and NGL distribution services for its operations. We provide terminalling and storage services under a terminal services agreement. We provide marine transportation services to Martin Resource Management under a charter agreement on a spot-contract basis at applicable market rates. Our sales to Martin Resource Management accounted for approximately 4%, 5% and 8% of our total revenues for the years ended December 31, 2006, 2005 and 2004, respectively. In connection with the closing of the Tesoro Marine asset acquisition, we entered into certain agreements with Martin Resource Management pursuant to which we provide terminalling and storage and marine transportation services to Midstream Fuel and Midstream Fuel provides terminal services to us to handle lubricants, greases and drilling fluids.

For a more comprehensive discussion concerning these commercial agreements that we have entered into with Martin Resource Management, please see Item 13. Certain Relationships and Related Transactions Agreements.

Approval and Review of Related Party Transactions

If we contemplate entering into a transaction, other than a routine or in the ordinary course of business transaction, in which a related person will have a direct or indirect material interest, the proposed transaction is submitted for consideration to the board of directors of our general partner or to our management, as appropriate. If the board of directors is involved in the approval process, it determines whether to refer the matter to the Conflicts Committee of our general partner s board of directors, as constituted under our limited partnership agreement. If a matter is referred to the Conflicts Committee, it obtains information regarding the proposed transaction from management and determines whether to engage independent legal counsel or an independent financial advisor to advise the members of the committee regarding the transaction. If the Conflicts Committee retains such counsel or financial advisor, it considers such advice and, in the case of a financial advisor, such advisor s opinion as to whether the transaction is fair and reasonable to us and to our unitholders.

Our Relationship with CF Martin Sulphur, L.P.

On July 15, 2005, we acquired all of the remaining limited partnership interests in CF Martin Sulphur from CF Industries, Inc. and certain affiliates of Martin Resource Management. Prior to this transaction, our unconsolidated non-controlling 49.5% limited partnership interest in CF Martin Sulphur, was accounted for using the equity method of accounting. In addition, on July 15, 2005, we acquired all of the outstanding membership interests in CF Martin Sulphur s general partner. Subsequent to the acquisition, CF Martin Sulphur was a wholly owned partnership which is included in the consolidated financial presentation of our sulfur segment. Effective March 30, 2006, CF Martin Sulphur was merged into us.

Prior to July 15, 2005, we were both an important supplier to and customer of CF Martin Sulphur. We chartered one of our offshore tug/barge tanker units to CF Martin Sulphur for a guaranteed daily rate, subject to certain adjustments. This charter, which had an unlimited term, was terminated on November 18, 2005. CF Martin Sulphur paid to have this tug/barge tanker unit reconfigured to carry molten sulfur. In the event CF Martin Sulphur had terminated this charter agreement, we would have been obligated to reimburse CF Martin Sulphur for a portion of such reconfiguration costs. As a result of the July 15, 2005 acquisition of all the outstanding interests in CF Martin Sulphur, this contingent obligation was terminated.

Insurance

Loss of, or damage to, our vessels and cargo is insured through hull and cargo insurance policies. Vessel operating liabilities such as collision, cargo, environmental and personal injury are insured primarily through our participation in mutual insurance associations and other reinsurance arrangements, pursuant to which we are potentially exposed to assessments in the event claims by us or other members exceed available funds and reinsurance. Protection and indemnity, or P&I, insurance coverage is provided by P&I associations and other insurance underwriters. Our

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vessels are entered in P&I associations that are parties to a pooling agreement, known as the International Group Pooling Agreement, or the Pooling Agreement, through which approximately 95% of the world s commercial shipping tonnage is reinsured through a group reinsurance policy. With regard to collision coverage, the first $1.0 million of coverage is insured by our hull policy and any excess is insured by a P&I association. We insure our owned cargo through a domestic insurance company. We insure cargo owned by third parties through our P&I coverage. As a member of P&I associations that are parties to the Pooling Agreement, we are subject to supplemental calls payable to the associations of which we are a member, based on our claims record and the other members of the other P&I associations that are parties to the Pooling Agreement. Except for our marine operations, we self-insure against liability exposure up to a pre-determined amount, beyond which we are covered by catastrophe insurance coverage.

For marine pollution claims, our insurance covers up to $1.0 billion of liability per accident or occurrence and for non-pollution incidents, our insurance covers up to $2.0 billion of liability per accident or occurrence. We believe our current insurance coverage is adequate to protect us against most accident related risks involved in the conduct of our business and that we maintain appropriate levels of environmental damage and pollution insurance coverage. However, there can be no assurance that all risks are adequately insured against, that any particular claim will be paid by the insurer, or that we will be able to procure adequate insurance coverage at commercially reasonable rates in the future.

Environmental and Regulatory Matters

Our activities are subject to various federal, state and local laws and regulations, as well as orders of regulatory bodies, governing a wide variety of matters, including marketing, production, pricing, community right-to-know, protection of the environment, safety and other matters.

Environmental

We are subject to complex federal, state, and local environmental laws and regulations governing the discharge of materials into the environment or otherwise relating to protection of human health, natural resources and the environment. These laws and regulations can impair our operations that affect the environment in many ways, such as requiring the acquisition of permits to conduct regulated activities; restricting the manner in which we can release materials into the environment; requiring remedial activities or capital expenditures to mitigate pollution from former or current operations; and imposing substantial liabilities on us for pollution resulting from our operations. Many environmental laws and regulations can impose joint and several, strict liability, and any failure to comply with environmental laws and regulations may result in the assessment of administrative, civil, and criminal penalties, the imposition of investigatory and remedial obligations, and, in some circumstances, the issuance of injunctions that can limit or prohibit our operations.

The clear trend in environmental regulation is to place more restrictions and limitations on activities that may affect the environment, and, thus, any changes in environmental laws and regulations that result in more stringent and costly waste handling, storage, transport, disposal, or remediation requirements could have a material adverse effect on our operations and financial position. Moreover, there is inherent risk of incurring significant environmental costs and liabilities in the performance of our operations due to our handling of petroleum hydrocarbons, chemical substances, and wastes as well as the accidental release or spill of such materials into the environment. Consequently, we cannot assure you that we will not incur significant costs and liabilities as result of such handling practices, releases or spills, including those relating to claims for damage to property and persons. In the event of future increases in costs, we may be unable to pass on those increases to our customers. While we believe that we are in substantial compliance with current environmental laws and regulations and that continued compliance with existing requirements would not have a material adverse impact on us, we cannot provide any assurance that our environmental compliance expenditures will not have a material adverse impact on us in the future.

Superfund

The Federal Comprehensive Environmental Response, Compensation and Liability Act, as amended, (CERCLA), also known as the Superfund law, and similar state laws, impose liability without regard to fault or the legality of the original conduct, on certain classes of responsible persons, including the owner or operator of a site where regulated hazardous substances have been released into the environment and companies that disposed or arranged for the disposal of the hazardous substances found at such site. Under CERCLA, these responsible persons may be subject to

joint and several, strict liability for the costs of cleaning up the hazardous substances that have been

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released into the environment, for damages to natural resources, and for the costs of certain health studies, and it is not uncommon for neighboring landowners and other third parties to file claims for personal injury and property damage allegedly caused by the release of hazardous substances into the environment. Although certain hydrocarbons are not subject to CERCLA s reach because petroleum is excluded from CERCLA s definition of a hazardous substance, in the course of our ordinary operations we will generate wastes that may fall within the definition of a hazardous substance. We have not received any notification that we may be potentially responsible for cleanup costs under CERCLA.

Solid Waste

We generate both hazardous and nonhazardous solid wastes which are subject to requirements of the federal Resource Conservation and Recovery Act, as amended (RCRA) and comparable state statutes. From time to time, the U.S. Environmental Protection Agency (EPA) has considered making changes in nonhazardous waste standards that would result in stricter disposal requirements for these wastes. Furthermore, it is possible some wastes generated by us that are currently classified as nonhazardous may in the future be designated as hazardous wastes, resulting in the wastes being subject to more rigorous and costly disposal requirements. Changes in applicable regulations may result in an increase in our capital expenditures or operating expenses.

We currently own or lease, and have in the past owned or leased, properties that have been used for the manufacturing, processing, transportation and storage of petroleum products and by-products. Solid waste disposal practices within oil and gas related industries have improved over the years with the passage and implementation of various environmental laws and regulations. Nevertheless, a possibility exists that hydrocarbons and other solid wastes may have been disposed of on or under various properties owned or leased by us during the operating history of those facilities. In addition, a number of these properties have been operated by third parties over whom we had no control as to such entities handling of hydrocarbons, hydrocarbon by-products or other wastes and the manner in which such substances may have been disposed of or released. State and federal laws and regulations applicable to oil and natural gas wastes and properties have gradually become more strict and, under such laws and regulations, we could be required to remove or remediate previously disposed wastes or property contamination, including groundwater contamination, even under circumstances where such contamination resulted from past operations of third parties.

Clean Air Act

Our operations are subject to the federal Clean Air Act, as amended, and comparable state statutes. Amendments to the Clean Air Act adopted in 1990 contain provisions that may result in the imposition of increasingly stringent pollution control requirements with respect to air emissions from the operations of our terminal facilities, processing and storage facilities and fertilizer and related products manufacturing and processing facilities. Such air pollution control requirements may include specific equipment or technologies to control emissions, permits with emissions and operational limitations, pre-approval of new or modified projects or facilities producing air emissions, and similar measures. For example, the Mont Belvieu terminal we use is located in an EPA-designated ozone non-attainment area, referred to as the Houston-Galveston non-attainment area, which is now subject to a new, EPA-adopted 8-hour standard for complying with the national standard for ozone. Categorized as being in moderate non-attainment for ozone, the Houston-Galveston non-attainment area has until 2010 to achieve compliance with this new standard, which almost certainly will require the adoption of more restrictive regulations in this non- attainment area for the issuance of air permits for new or modified facilities. In addition, existing sources of air emissions in the Houston-Galveston area are already subject to stringent emission reduction requirements. Failure to comply with applicable air statutes or regulations may lead to the assessment of administrative, civil or criminal penalties, and/or result in the limitation or cessation of construction or operation of certain air emission sources. We believe our operations, including our manufacturing, processing and storage facilities and terminals, are in substantial compliance with applicable requirements of the Clean Air Act and analogous state laws.

Clean Water Act

The Federal Water Pollution Control Act, as amended, also known as the Clean Water Act, and analogous state laws impose restrictions and controls on the discharge of pollutants into federal and state waters. Regulations promulgated under these laws require entities that discharge into federal and state waters obtain National Pollutant Discharge Elimination System (NPDES) and/or state permits authorizing these discharges. The Clean Water Act and

analogous state laws assess penalties for releases of unauthorized pollutants into the water and impose substantial liability for the costs of removing spills from such waters. In addition, the Clean Water Act and analogous state laws

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require that individual permits or coverage under general permits be obtained by covered facilities for discharges of storm water runoff and that applicable facilities develop and implement plans for the management of storm water runoff (referred to as storm water pollution prevention plans or SWPPPs) as well as for the prevention and control of oil spills (referred to as spill prevention, control and countermeasure or SPCC plans). As part of the regular overall evaluation of our on-going operations, we are reviewing and, as necessary, updating SWPPPs for certain of our facilities, including facilities recently acquired. In addition, we have reviewed our SPCC plans and, where necessary, amended such plans to comply with applicable regulations adopted by EPA in 2002.. We believe that compliance with the conditions of such permits and plans will not have a material effect on our operations.

On August 7, 2000, a spill of molten sulfur occurred at our Stanolind terminal near Beaumont, Texas, which at the time was owned and operated by Martin Gas Sales LLC, a wholly-owned subsidiary of Martin Resource Management. Martin Gas Sales LLC has since changed its name to Martin Product Sales, LLC. The Texas Department of Health and Texas Natural Resource Conservation Commission (the predecessor agency to the present-day Texas Commission on Environmental Quality) investigated the spill and its clean-up. These agencies found that there was no impact on public health, and that there was no reason to remove the solidified sulfur from the river bottom. However, the United States attorney in Beaumont, Texas, initiated an investigation under the criminal provisions of the Clean Water Act. To avoid protracted litigation and possible criminal claims against employees, Martin Product Sales agreed to plead guilty to a single felony violation of the federal Clean Water Act and was sentenced to pay a $50,000 fine. As part of its plea agreement with the United States, Martin Product Sales also agreed to implement a remedial program at our Stanolind terminal and our sulfur loading facility in Tampa, Florida. Martin Product Sales instituted the remedial program as of March 1, 2002, and we believe that it has been substantially implemented, although it must remain in effect for five years. Martin Product Sales does not have any contracts with the United States government that might be affected by a debarment or listing proceeding, and the United States Attorney s Office has agreed to inform any agency initiating a debarment or listing proceeding of the implementation of the remedial program. A previous criminal conviction, however, may result in increased fines and other sanctions if Martin Product Sales is subsequently convicted or pleads guilty to a similar offense in the future. Martin Resource Management will indemnify us under the omnibus agreement for any losses we suffer within five years from November 6, 2002, the date of our initial public offering that relate to or result from, this event.

Oil Pollution Act

The Oil Pollution Act of 1990, as amended (OPA) imposes a variety of regulations on responsible parties related to the prevention of oil spills and liability for damages resulting from such spills in United States waters. A responsible party includes the owner or operator of a facility or vessel, or the lessee or permittee of the area in which an offshore facility is located. The OPA assigns liability to each responsible party for oil removal costs and a variety of public and private damages including natural resource damages. Under OPA, vessels and shore facilities handling, storing, or transporting oil are required to develop and implement oil spill response plans, and vessels greater than 300 tons in weight must provide to the United States Coast Guard evidence of financial responsibility to cover the costs of cleaning up oil spills from such vessels. The OPA also requires that all newly constructed tank barges engaged in oil transportation in the United States be double hulled and all existing single hull tank barges be retrofitted with double hulls or phased out by 2015. We believe we are in substantial compliance with all of these oil spill-related and financial responsibility requirements.

Safety Regulation

The Company s marine transportation operations are subject to regulation by the United States Coast Guard, federal laws, state laws and certain international treaties. Tank ships, push boats, tugboats and barges are required to meet construction and repair standards established by the American Bureau of Shipping, a private organization, and the United States Coast Guard and to meet operational and safety standards presently established by the United States Coast Guard. We believe our marine operations and our terminals are in substantial compliance with current applicable safety requirements.

Occupational Health Regulations

The workplaces associated with our manufacturing, processing, terminal and storage facilities are subject to the requirements of the federal Occupational Safety and Health Act (OSHA) and comparable state statutes. We believe we

have conducted our operations in substantial compliance with OSHA requirements, including general industry standards, record keeping requirements and monitoring of occupational exposure to regulated substances. In

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May 2001, Martin Resource Management paid a small fine in relation to the settlement of alleged OSHA violations at our facility in Plainview, Texas. Although we believe the amount of this fine and the nature of these violations were not, as an individual event, material to our business or operations, this violation may result in increased fines and other sanctions if we are cited for similar violations in the future. Our marine vessel operations are also subject to safety and operational standards established and monitored by the United States Coast Guard.

In general, we expect to increase our expenditures relating to compliance with likely higher industry and regulatory safety standards such as those described above. These expenditures cannot be accurately estimated at this time, but we do not expect them to have a material adverse effect on our business.

Jones Act

The Jones Act is a federal law that restricts maritime transportation between locations in the United States to vessels built and registered in the United States and owned and manned by United States citizens. Since we engage in maritime transportation between locations in the United States, we are subject to the provisions of the law. As a result, we are responsible for monitoring the ownership of our subsidiaries that engage in maritime transportation and for taking any remedial action necessary to insure that no violation of the Jones Act ownership restrictions occurs. The Jones Act also requires that all United States-flag vessels be manned by United States citizens. Foreign-flag seamen generally receive lower wages and benefits than those received by United States citizen seamen. This requirement significantly increases operating costs of United States-flag vessel operations compared to foreign-flag vessel operations. Certain foreign governments subsidize their nations shipyards. This results in lower shipyard costs both for new vessels and repairs than those paid by United States-flag vessel owners. The United States Coast Guard and American Bureau of Shipping maintain the most stringent regime of vessel inspection in the world, which tends to result in higher regulatory compliance costs for United States-flag operators than for owners of vessels registered under foreign flags of convenience. Following Hurricane Katrina, and again after Hurricane Rita, emergency suspensions of the Jones Act were effectuated by the United States government. The last suspension ended on October 24, 2005. Future suspensions of the Jones Act or other similar actions could adversely affect our cash flow and ability to make distributions to our unitholders.

Merchant Marine Act of 1936

The Merchant Marine Act of 1936 is a federal law that provides that, upon proclamation by the president of the United States of a national emergency or a threat to the national security, the United States secretary of transportation may requisition or purchase any vessel or other watercraft owned by United States citizens (including us, provided that we are considered a United States citizen for this purpose). If one of our push boats, tugboats or tank barges were purchased or requisitioned by the United States government under this law, we would be entitled to be paid the fair market value of the vessel in the case of a purchase or, in the case of a requisition, the fair market value of charter hire. However, if one of our push boats or tugboats is requisitioned or purchased and its associated tank barge is left idle, we would not be entitled to receive any compensation for the lost revenues resulting from the idled barge. We also would not be entitled to be compensated for any consequential damages we suffer as a result of the requisition or purchase of any of our push boats, tugboats or tank barges.

Regulations Affecting Natural Gas Transmission, Processing and Gathering

We own a 50% non-operating interest in Panther Interstate Pipeline Energy, LLC. Panther Interstate Pipeline Energy, LLC s Fishhook Gathering System transports natural gas in interstate commerce and is thus subject to FERC regulations and FERC-approved tariffs as a natural gas company under the National Gas Act of 1938 (the NGA). Under the NGA, FERC has issued orders requiring pipelines to provide open-access transportation on a basis that is equal for all shippers. In addition, FERC has the authority to regulate natural gas companies with respect to: rates, terms and conditions of service; the types of services Panther Interstate Pipeline Energy, LLC may provide to its customers; the construction of new facilities; the acquisition, extension, expansion or abandonment of services or facilities; the maintenance and retention of accounts and records; and relationships of affiliated companies involved in all aspects of the natural gas and energy business.

On August 8, 2005, President Bush signed into law the Domenici-Barton Energy Policy Act of 2005 (the EP Act). The EP Act is a comprehensive compilation of tax incentives, authorized appropriations for grants and guaranteed loans, and significant changes to the statutory policy that affects all segments of the energy industry. With respect to

regulation of natural gas transportation, the EP Act amends the NGA and the Natural Gas Policy Act of 1978

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by increasing the criminal penalties available for violations of each act. The EP Act also adds a new section to the NGA which provides FERC with the power to assess civil penalties of up to $1,000,000 per day per violation of the NGA.

Additional proposals and proceedings that might affect the natural gas industry are pending before Congress, FERC and the courts. However, we do not believe that we will be disproportionately affected as compared to other natural gas producers and marketers by any action taken. We believe that our natural gas gathering operations meet the tests FERC uses to establish a pipeline s status as a gatherer exempt from FERC regulation under the NGA, but FERC regulation still affects these businesses and the markets for products derived from these businesses. FERC s policies and practices across the range of its oil and natural gas regulatory activities, including, for example, its policies on open access transportation, ratemaking, capacity release and market center promotion, indirectly affect intrastate markets. In recent years, FERC has pursued pro-competitive policies in its regulation of interstate oil and natural gas pipelines. However, we cannot assure our unitholders that FERC will continue this approach as it considers matters such as pipeline rates and rules and policies that may affect rights of access to oil and natural gas transportation capacity. In addition, the distinction between FERC-regulated transmission services and federally unregulated gathering services has been the subject of regular litigation, so, in such a circumstance, the classification and regulation of some of our gathering facilities and intrastate transportation pipelines may be subject to change based on future determinations by FERC and the courts.

Other state and local regulations also affect our natural gas processing and gathering business. Our gathering lines are subject to ratable take and common purchaser statutes in Louisiana and Texas. Ratable take statutes generally require gatherers to take, without undue discrimination, oil or natural gas production that may be tendered to the gatherer for handling. Similarly, common purchaser statutes generally require gatherers to purchase without undue discrimination as to source of supply or producer. These statutes restrict our right as an owner of gathering facilities to decide with whom we contract to purchase or transport oil or natural gas. Federal law leaves any economic regulation of natural gas gathering to the states. The states in which we operate have adopted complaint-based regulation of oil and natural gas gathering activities, which allows oil and natural gas producers and shippers to file complaints with state regulators in an effort to resolve grievances relating to oil and natural gas gathering access and rate discrimination. Other state regulations may not directly regulate our business, but may nonetheless affect the availability of natural gas for purchase, processing and sale, including state regulation of production rates and maximum daily production allowable from gas wells. While our gathering lines currently are subject to limited state regulation, there is a risk that state laws will be changed, which may give producers a stronger basis to challenge proprietary status of a line, or the rates, terms and conditions of a gathering line providing transportation service.

Pursuant to the Pipeline Safety Improvement Act of 2002, the United States Department of Transportation (DOT) has adopted regulations requiring pipeline operators to develop integrity management programs for transportation pipelines located where a leak or rupture could do the most harm in high consequence areas. The regulations require operators to:

- perform ongoing assessments of pipeline integrity;
- identify and characterize applicable threats to pipeline segments that could impact a high consequence area;
- improve data collection, integration and analysis;
- repair and remediate the pipeline as necessary; and
- implement preventive and mitigating actions.

Employees

We do not have any employees. Under our omnibus agreement with Martin Resource Management, Martin Resource Management provides us with corporate staff and support services. These services include centralized corporate functions, such as accounting, treasury, engineering, information technology, insurance, administration of employee benefit plans and other corporate services. Martin Resource Management employs approximately 396

individuals who provide direct support to our operations. None of these employees are represented by labor unions.

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Financial Information about Segments

Information regarding our operating revenues and identifiable assets attributable to each of our segments is presented in Note 19 to our consolidated financial statements included in this annual report on Form 10-K.

Access to Public Filings

We provide public access to our annual reports on Form 10-K, quarterly reports on Form 10-Q, current reports on Form 8-K, and amendments to these reports filed with the Securities and Exchange Commission (SEC) under the Securities and Exchange Act of 1934. These documents may be accessed free of charge on our website at the following address: www.martinmidstream.com. These documents are provided as soon as is reasonably practicable after their filing with the SEC. These documents may also be found at the SEC s website at www.sec.gov. This website address is intended to be an inactive, textual reference only, and none of the material on this website is part of this report.

Item 1A. Risk Factors

Limited partner interests are inherently different from the capital stock of a corporation, although many of the business risks to which we are subject are similar to those that would be faced by a corporation engaged in a business similar to ours. If any of the following risks were actually to occur, our business, financial condition or results of operations could be materially adversely affected. In this case, we might not be able to pay distributions on our common units, the trading price of our common units could decline and unitholders could lose all or part of their investment. These risk factors should be read in conjunction with the other detailed information concerning us set forth herein.

Risks Relating to Our Business

Important factors that could cause actual results to differ materially from our expectations include, but are not limited to, the risks set forth below. The risks described below should not be considered to be comprehensive and all-inclusive. Additional risks that we do not yet know of or that we currently think are immaterial may also impair our business operations, financial condition and results of operations. If any events occur that give rise to the following risks, our business, financial condition, or results of operations could be materially and adversely affected, and as a result, the trading price of our common units could be materially and adversely impacted. Many of such factors are beyond our ability to control or predict. Unitholders are cautioned not to put undue reliance on forward-looking statements.

We may not have sufficient cash after the establishment of cash reserves and payment of our general partner s expenses to enable us to pay the minimum quarterly distribution each quarter.

We may not have sufficient available cash each quarter in the future to pay the minimum quarterly distribution on all our units. Under the terms of our partnership agreement, we must pay our general partner s expenses and set aside any cash reserve amounts before making a distribution to our unitholders. The amount of cash we can distribute on our common units principally depends upon the amount of net cash generated from our operations, which will fluctuate from quarter to quarter based on, among other things:

- the costs of acquisitions, if any;
- the prices of petroleum products and by-products;
- fluctuations in our working capital;
- the level of capital expenditures we make;
- restrictions contained in our debt instruments and our debt service requirements;
- our ability to make working capital borrowings under our credit facility; and
- the amount, if any, of cash reserves established by our general partner in its discretion.

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Unitholders should also be aware that the amount of cash we have available for distribution depends primarily on our cash flow, including cash flow from working capital borrowings, and not solely on profitability, which will be affected by non-cash items. In addition, our general partner determines the amount and timing of asset purchases and sales, capital expenditures, borrowings, issuances of additional partnership securities and the establishment of reserves, each of which can affect the amount of cash available for distribution to our unitholders. As a result, we may make cash distributions during periods when we record losses and may not make cash distributions during periods when we record net income.

Adverse weather conditions, including droughts, hurricanes, tropical storms and other severe weather, could reduce our results of operations and ability to make distributions to our unitholders.

Our distribution network and operations are primarily concentrated in the Gulf Coast region and along the Mississippi River inland waterway. Weather in these regions is sometimes severe (including tropical storms and hurricanes) and can be a major factor in our day-to-day operations. Our marine transportation operations can be significantly delayed, impaired or postponed by adverse weather conditions, such as fog in the winter and spring months, and certain river conditions. Additionally, our terminalling and storage and marine transportation operations and our assets in the Gulf of Mexico, including our barges, push boats, tugboats and terminals, can be adversely impacted or damaged by hurricanes, tropical storms, tidal waves or other related events. Demand for our lubricants and the diesel fuel we throughput in our terminalling and storage segment can be affected if offshore drilling operations are disrupted by weather in the Gulf of Mexico.

National weather conditions have a substantial impact on the demand for our products. Unusually warm weather during the winter months can cause a significant decrease in the demand for NGL products, fuel oil and gasoline. Likewise, extreme weather conditions (either wet or dry) can decrease the demand for fertilizer. For example, an unusually wet spring can delay planting of seeds, which can leave insufficient time to apply fertilizer at the planting stage. Conversely, drought conditions can kill or severely stunt the growth of crops, thus eliminating the need to nurture plants with fertilizer. Any of these or similar conditions could result in a decline in our net income and cash flow, which would reduce our ability to make distributions to our unitholders.

If we incur material liabilities that are not fully covered by insurance, such as liabilities resulting from accidents on rivers or at sea, spills, fires or explosions, our results of operations and ability to make distributions to our unitholders could be adversely affected.

Our operations are subject to the operating hazards and risks incidental to terminalling and storage, marine transportation and the distribution of petroleum products and by-products and other industrial products. These hazards and risks, many of which are beyond our control, include:

- accidents on rivers or at sea and other hazards that could result in releases, spills and other environmental damages, personal injuries, loss of life and suspension of operations;
- leakage of NGLs and other petroleum products and by-products;
- fires and explosions;
- damage to transportation, terminalling and storage facilities, and surrounding properties caused by natural disasters; and
- terrorist attacks or sabotage.

Our insurance coverage may not be adequate to protect us from all material expenses related to potential future claims for personal injury and property damage, including various legal proceedings and litigation resulting from these hazards and risks. If we incur material liabilities that are not covered by insurance, our operating results, cash flow and ability to make distributions to our unitholders could be adversely affected.

Changes in the insurance markets attributable to the September 11, 2001 terrorist attacks, and their aftermath, may make some types of insurance more difficult or expensive for us to obtain. In addition, changes in the insurance markets attributable to the effects of Hurricanes Katrina and Rita, and their aftermath, may make some types of insurance more difficult or expensive for us to obtain. As a result, we may be unable to secure the levels and types of

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insurance we would otherwise have secured prior to such events. Moreover, the insurance that may be available to us may be significantly more expensive than our existing insurance coverage.

The price volatility of petroleum products and by-products can reduce our results of operations and ability to make distributions to our unitholders.

We purchase petroleum products and by-products such as molten sulfur, sulfur derivatives and NGLs, and sell these products to wholesale and bulk customers and to other end users. Since the closing of the Tesoro Marine asset acquisition, we and our affiliates also distribute and market lubricants. We also generate revenues through the terminalling and storage of certain products for third parties. The price and market value of petroleum products and by-products can be volatile. Our revenues have been adversely affected by this volatility during periods of decreasing prices because of the reduction in the value and resale price of our inventory. Future price volatility could have an adverse impact on our results of operations, cash flow and ability to make distributions to our unitholders.

Increasing energy prices could adversely affect our results of operations.

Increasing energy prices could adversely affect our results of operations. Diesel fuel, natural gas, chemicals and other supplies are recorded in operating expenses. An increase in price of these products would increase our operating expenses which could adversely affect our results of operations including net income and cash flows. We cannot assure unitholders that we will be able to pass along increased operating expenses to our customers.

Restrictions in our credit facility may prevent us from making distributions to our unitholders.

The payment of principal and interest on our indebtedness reduces the cash available for distribution to our unitholders. In addition, we are prohibited by our credit facility from making cash distributions during an event of default or if the payment of a distribution would cause an event of default thereunder. Our leverage and various limitations in our credit facility may reduce our ability to incur additional debt, engage in certain transactions and capitalize on acquisition or other business opportunities that could increase cash flows and distributions to our unitholders.

If we do not have sufficient capital resources for acquisitions or opportunities for expansion, our growth will be limited.

We intend to explore acquisition opportunities in order to expand our operations and increase our profitability. We may finance acquisitions through public and private financing, or we may use our limited partner interests for all or a portion of the consideration to be paid in acquisitions. Distributions of cash with respect to these equity securities or limited partner interests may reduce the amount of cash available for distribution to the common units. In addition, in the event our limited partner interests do not maintain a sufficient valuation, or potential acquisition candidates are unwilling to accept our limited partner interests as all or part of the consideration, we may be required to use our cash resources, if available, or rely on other financing arrangements to pursue acquisitions. If we use funds from operations, other cash resources or increased borrowings for an acquisition, the acquisition could adversely impact our ability to make our minimum quarterly distributions to our unitholders. Additionally, if we do not have sufficient capital resources or are not able to obtain financing on terms acceptable to us for acquisitions, our ability to implement our growth strategies may be adversely impacted.

Our recent and future acquisitions may not be successful, may substantially increase our indebtedness and contingent liabilities, and may create integration difficulties.

As part of our business strategy, we intend to acquire businesses or assets we believe complement our existing operations. We may not be able to successfully integrate recent or any future acquisitions, including Prism Gas, into our existing operations or achieve the desired profitability from such acquisitions. These acquisitions may require substantial capital expenditures and the incurrence of additional indebtedness. If we make acquisitions, our capitalization and results of operations may change significantly. Further, any acquisition could result in:

post-closing discovery of material undisclosed liabilities of the acquired business or assets;

the unexpected loss of key employees or customers from the acquired businesses;

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difficulties resulting from our integration of the operations, systems and management of the acquired business; and

an unexpected diversion of our management s attention from other operations.

If recent or any future acquisitions are unsuccessful or result in unanticipated events or if we are unable to successfully integrate acquisitions into our existing operations, such acquisitions could adversely affect our results of operations, cash flow and ability to make distributions to our unitholders.

Demand for our terminalling and storage services is substantially dependent on the level of offshore oil and gas exploration, development and production activity.

The level of offshore oil and gas exploration, development and production activity historically has been volatile and is likely to continue to be so in the future. The level of activity is subject to large fluctuations in response to relatively minor changes in a variety of factors that are beyond our control, including:

prevailing oil and natural gas prices and expectations about future prices and price volatility;

the cost of offshore exploration for, and production and transportation of, oil and natural gas;

worldwide demand for oil and natural gas;

consolidation of oil and gas and oil service companies operating offshore;

availability and rate of discovery of new oil and natural gas reserves in offshore areas;

local and international political and economic conditions and policies;

technological advances affecting energy production and consumption;

weather conditions;

environmental regulation; and

the ability of oil and gas companies to generate or otherwise obtain funds for exploration and production.

We expect levels of offshore oil and gas exploration, development and production activity to continue to be volatile and affect demand for our terminalling and storage services.

Our NGL and fertilizer businesses are seasonal and could cause our revenues to vary.

The demand for NGL and natural gas is highest in the winter. Therefore, revenue from our natural gas services business is higher in the winter than in other seasons. Our fertilizer business experiences an increase in demand during the spring, which increases the revenue generated by this business line in this period compared to other periods. The seasonality of the revenue from these business lines may cause our results of operations to vary on a quarter to quarter basis and thus could cause our cash available for quarterly distributions to fluctuate from period to period.

The highly competitive nature of our industry could adversely affect our results of operations and ability to make distributions to our unitholders.

We operate in a highly competitive marketplace in each of our primary business segments. Most of our competitors in each segment are larger companies with greater financial and other resources than we possess. We may lose customers and future business opportunities to our competitors and any such losses could adversely affect our results of operations and ability to make distributions to our unitholders.

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Our business is subject to compliance with environmental laws and regulations that may expose us to significant costs and liabilities and adversely affect our results of operations and ability to make distributions to our unitholders.

Our business is subject to federal, state and local environmental laws and regulations governing the discharge of materials into the environment or otherwise relating to protection of human health, natural resources and the environment. These laws and regulations may impose numerous obligations that are applicable to our operations, such as requiring the acquisition of permits to conduct regulated activities; restricting the manner in which we can release materials into the environment; requiring remedial activities or capital expenditures to mitigate pollution from former of current operations; and imposing substantial liabilities on us for pollution resulting from our operations. Numerous governmental authorities, such as the U.S. Environmental Protection Agency and analogous state agencies, have the power to enforce compliance with these laws and regulations and the permits issued under them, oftentimes requiring difficult and costly actions. Many environmental laws and regulations can impose joint and several strict liability, and any failure to comply with environmental laws, regulations and permits may result in the assessment of administrative, civil, and criminal penalties, the imposition of investigatory and remedial obligations, and, in some circumstances, the issuance of injunctions that can limit or prohibit our operations. The clear trend in environmental regulation is to place more restrictions and limitations on activities that may affect the environment, and, thus, any changes in environmental laws and regulations that result in more stringent and costly waste handling, storage, transport, disposal, or remediation requirements could have a material adverse effect on our operations and financial position.

The loss or insufficient attention of key personnel could negatively impact our results of operations and ability to make distributions to our unitholders. Additionally, if neither Ruben Martin nor Scott Martin is the chief executive officer of our general partner, amounts we owe under our credit facility may become immediately due and payable.

Our success is largely dependent upon the continued services of members of the senior management team of Martin Resource Management. Those senior executive officers have significant experience in our businesses and have developed strong relationships with a broad range of industry participants. The loss of any of these executives could have a material adverse effect on our relationships with these industry participants, our results of operations and our ability to make distributions to our unitholders. Additionally, if neither Ruben Martin nor Scott Martin is the chief executive officer of our general partner, the lender under our credit facility could declare amounts outstanding thereunder immediately due and payable. If such event occurs, our results of operations and our ability to make distribution to our unitholders could be negatively impacted.

We do not have employees. We rely solely on officers and employees of Martin Resource Management to operate and manage our business. Martin Resource Management operates businesses and conducts activities of its own in which we have no economic interest. There could be competition for the time and effort of the officers and employees who provide services to our general partner. If these officers and employees do not or cannot devote sufficient attention to the management and operation of our business, our results of operation and ability to make distributions to our unitholders may be reduced.

Our loss of significant commercial relationships with Martin Resource Management could adversely impact our results of operations and ability to make distributions to our unitholders.

Martin Resource Management provides us with various services and products pursuant to various commercial contracts. The loss of any of these services and products provided by Martin Resource Management could have a material adverse impact on our results of operations, cash flow and ability to make distributions to our unitholders. Additionally, we provide terminalling and storage and marine transportation services to Martin Resource Management to support its businesses under various commercial contracts. The loss of Martin Resource Management as a customer could have a material adverse impact on our results of operations, cash flow and ability to make distributions to our unitholders.

Our business would be adversely affected if operations at our transportation, terminalling and storage and distribution facilities experienced significant interruptions. Our business would also be adversely affected if the operations of our customers and suppliers experienced significant interruptions.

Our operations are dependent upon our terminalling and storage facilities and various means of transportation. We are also dependent upon the uninterrupted operations of certain facilities owned or operated by our suppliers and

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customers. Any significant interruption at these facilities or inability to transport products to or from these facilities or to or from our customers for any reason would adversely affect our results of operations, cash flow and ability to make distributions to our unitholders. Operations at our facilities and at the facilities owned or operated by our suppliers and customers could be partially or completely shut down, temporarily or permanently, as the result of any number of circumstances that are not within our control, such as:

- catastrophic events, including hurricanes;
- environmental remediation;
- labor difficulties; and
- disruptions in the supply of our products to our facilities or means of transportation.

Additionally, terrorist attacks and acts of sabotage could target oil and gas production facilities, refineries, processing plants, terminals and other infrastructure facilities. Any significant interruptions at our facilities, facilities owned or operated by our suppliers or customers, or in the oil and gas industry as a whole caused by such attacks or acts could have a material adverse affect on our results of operations, cash flow and ability to make distributions to our unitholders.

Our marine transportation business would be adversely affected if we do not satisfy the requirements of the Jones Act, or if the Jones Act were modified or eliminated.

The Jones Act is a federal law that restricts domestic marine transportation in the United States to vessels built and registered in the United States. Furthermore, the Jones Act requires that the vessels be manned and owned by United States citizens. If we fail to comply with these requirements, our vessels lose their eligibility to engage in coastwise trade within United States domestic waters.

The requirements that our vessels be United States built and manned by United States citizens, the crewing requirements and material requirements of the Coast Guard and the application of United States labor and tax laws significantly increase the costs of United States flagged vessels when compared with foreign flag vessels. During the past several years, certain interest groups have lobbied Congress to repeal the Jones Act to facilitate foreign flag competition for trades and cargoes reserved for United States flagged vessels under the Jones Act and cargo preference laws. If the Jones Act were to be modified to permit foreign competition that would not be subject to the same United States government imposed costs, we may need to lower the prices we charge for our services in order to compete with foreign competitors, which would adversely affect our cash flow and ability to make distributions to our unitholders. Following Hurricane Katrina and again after Hurricane Rita, emergency suspensions of the Jones Act were effectuated by the United States government. The last suspension ended on October 24, 2005. Future suspensions of the Jones Act or other similar actions could result in similar consequences.

Our marine transportation business would be adversely affected if the United States Government purchases or requisitions any of our vessels under the Merchant Marine Act.

We are subject to the Merchant Marine Act of 1936, which provides that, upon proclamation by the President of the United States of a national emergency or a threat to the national security, the United States Secretary of Transportation may requisition or purchase any vessel or other watercraft owned by United States citizens (including us, provided that we are considered a United States citizen for this purpose). If one of our push boats, tugboats or tank barges were purchased or requisitioned by the United States government under this law, we would be entitled to be paid the fair market value of the vessel in the case of a purchase or, in the case of a requisition, the fair market value of charter hire. However, if one of our push boats or tugboats is requisitioned or purchased and its associated tank barge is left idle, we would not be entitled to receive any compensation for the lost revenues resulting from the idled barge. We also would not be entitled to be compensated for any consequential damages we suffer as a result of the requisition or purchase of any of our push boats, tugboats or tank barges. If any of our vessels are purchased or requisitioned for an extended period of time by the United States government, such transactions could have a material adverse affect on our results of operations, cash flow and ability to make distributions to our unitholders.

Regulations affecting the domestic tank vessel industry may limit our ability to do business, increase our costs and adversely impact our results of operations and ability to make distributions to our unitholders.

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The U.S. Oil Pollution Act of 1990, or OPA 90, provides for the phase out of single-hull vessels and the phase-in of the exclusive operation of double-hull tank vessels in U.S. waters for barges that carry petroleum products that are regulated under OPA 90. Under OPA 90, substantially all tank vessels that do not have double hulls will be phased out by 2015 and will not be permitted to enter U.S. ports or trade in U.S. waters. The phase out dates vary based on the age of the vessel and other factors. All but one of our offshore tank barges are double-hull vessels which have no phase out date. We have 13 single-hull barges that will be phased out of the petroleum product trade by the year 2015. The phase out of these single-hull vessels in accordance with OPA 90 may require us to make substantial capital expenditures, which could adversely affect our operations and market position and reduce our cash available for distribution.

Risks Relating to Our Acquisition of Prism Gas

A decline in the volume of natural gas and NGLs delivered to our facilities could adversely affect our results of operations, cash flows and financial condition.

Our profitability could be materially impacted by a decline in the volume of natural gas and NGLs transported, gathered or processed at our facilities. A material decrease in natural gas production, as a result of depressed commodity prices, a decrease in exploration and development activities or otherwise, could result in a decline in the volume of natural gas and NGLs handled by our facilities.

The natural gas and NGLs available to our facilities will be derived from reserves produced from existing wells. These reserves naturally decline over time. To offset this natural decline, our facilities will need access to additional reserves.

Our profitability is dependent upon prices and market demand for natural gas and NGLs, which are beyond our control and have been volatile.

We are subject to significant risks due to fluctuations in commodity prices. These risks relate primarily to: (1) the purchase of certain volumes of natural gas at a price that is a percentage of a relevant index; and (2) certain processing contracts for Prism Gas whereby we are exposed to natural gas and NGL commodity price risks.

The margins we realize from purchasing and selling a portion of the natural gas that we transport through our pipeline systems decrease in periods of low natural gas prices because our gross margins are based on a percentage of the index price. For the years ended December 31, 2006 and 2005, Prism Gas purchased approximately 40% and 54%, respectively, of our gas at a percentage of relevant index. Accordingly, a decline in the price of natural gas could have an adverse impact on our results of operations.

In the past, the prices of natural gas and NGLs have been extremely volatile and we expect this volatility to continue. For example, in 2005, the spot price of Henry Hub natural gas ranged from a high of $15.39 per MMBtu to a low of $5.50 per MMBtu. From January 1, 2006 through December 31, 2006, the same price ranged from $11.23 per MMBtu to $4.75 per MMBtu. On December 29, 2006 the spot price was $6.30 per MMBtu.

We may not be successful in balancing our purchases and sales. In addition, a producer could fail to deliver contracted volumes or deliver in excess of contracted volumes, or a consumer could purchase less than contracted volumes. Any of these actions could cause our purchases and sales not to be balanced. If our purchases and sales are not balanced, we will face increased exposure to commodity price risks and could have increased volatility in our operating income.

The markets and prices for residue gas and NGLs depend upon factors beyond our control. These factors include demand for oil, natural gas and NGLs, which fluctuate with changes in market and economic conditions and other factors, including:

- the impact of weather on the demand for oil and natural gas;
- the level of domestic oil and natural gas production;