

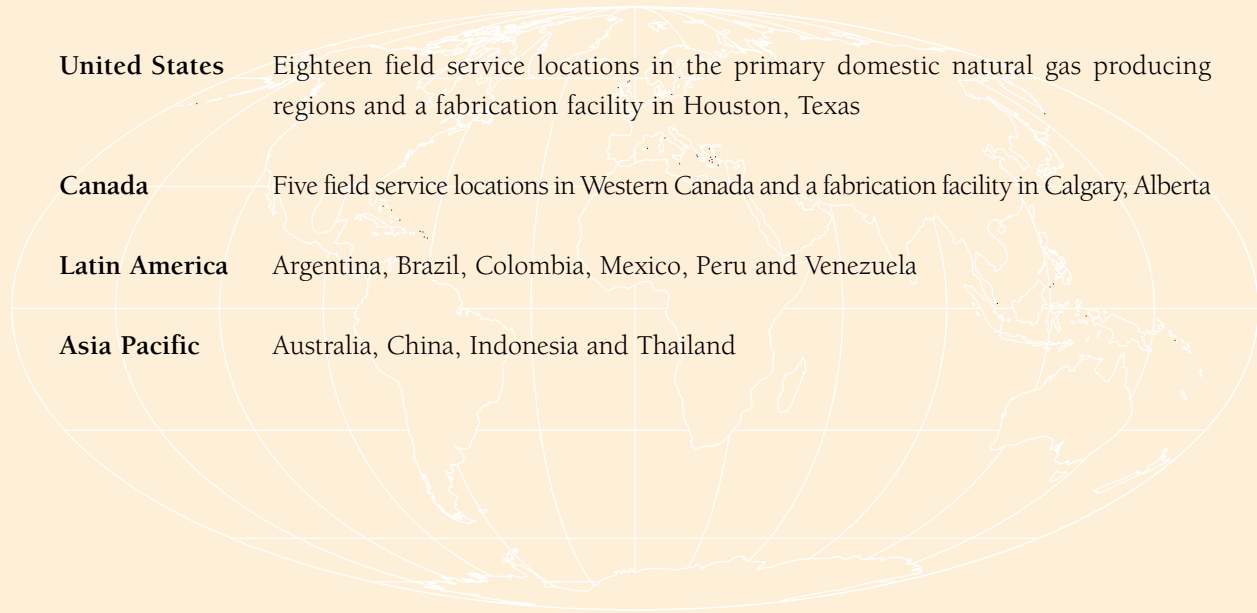
UNIVERSAL COMPRESSION

2004 Annual Report



50 Years of Safety, Service & Integrity

Operations



United States Eighteen field service locations in the primary domestic natural gas producing regions and a fabrication facility in Houston, Texas

Canada Five field service locations in Western Canada and a fabrication facility in Calgary, Alberta

Latin America Argentina, Brazil, Colombia, Mexico, Peru and Venezuela

Asia Pacific Australia, China, Indonesia and Thailand

1954 - Predecessor South Coast Gas Company founded in Houston, Texas

1970 - Name changed to Tidewater Compression Service, Inc. after being acquired by Tidewater Inc.



1980s - A leading national compression company after expansion in western states and Appalachia



1993 - First international gas compression contract in Argentina

1998 - Universal Compression acquired Tidewater's compression business

Company Profile

Universal Compression Holdings, Inc. is a leading provider of natural gas compression services and products to the domestic and international natural gas industry, including contract compression, fabrication and aftermarket services. Our common stock trades on the New York Stock Exchange under the symbol UCO. Based in Houston, Texas, we are celebrating our 50th year of operations during 2004.

Core Values

Safety	We must protect the safety of our employees, customers and suppliers before all else.
Service	Our mission is simply to help our customers improve their performance by supplying the very best gas compression services in the world.
Integrity	We will conduct our business in a manner that will always reflect a high standard of ethics. We are committed to being fair and honest in all dealings.

2000 - Initial public offering and listing on New York Stock Exchange



2001 - Broadened product line and established operations in Canada through several acquisitions, the largest being the compression business of Weatherford International Ltd.



2002 - Established Asia Pacific Division and opened office in Singapore

2004 - Expanded international presence with opening of office in Beijing

Products and Services

Contract Compression	We provide natural gas contract compression services and equipment to our customers.
Fabrication	We design, engineer and assemble compressors for sale to our customers and for use in our contract compression fleet.
Aftermarket Services	We sell parts and components, and maintain and operate equipment owned by others.

Financial Highlights

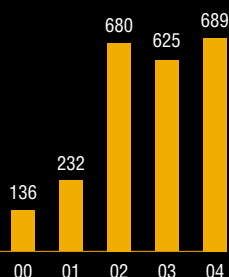
Fiscal Year Ended March 31,

(Dollars in thousands except per share amounts)

	2004	2003
Revenue:		
Domestic contract compression	\$ 280,951	\$ 265,465
International contract compression	82,589	66,505
Fabrication	183,685	162,678
Aftermarket services	141,561	130,570
	688,786	625,218
EBITDA, as adjusted ^(a)	223,848	201,150
Debt extinguishment and facility consolidation costs ^(b)	16,724	-
Net income	30,787	33,518
Net income (before debt extinguishment and facility consolidation costs, net of taxes)	41,323	33,518
Diluted EPS	0.98	1.08
Diluted EPS (before debt extinguishment and facility consolidation costs, net of taxes)	1.32	1.08
Cash	121,189	71,693
Total assets	1,972,451	1,953,887
Total debt ^(c)	884,442	945,155
Stockholders' equity	799,235	744,451
Capital expenditures	86,557	120,751

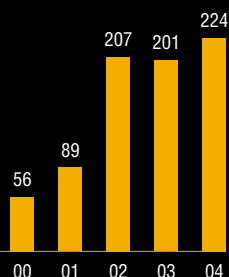
Revenue

\$ Millions



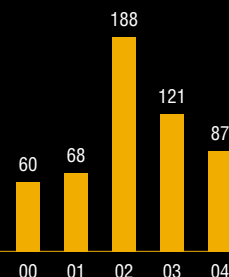
EBITDA, as adjusted

\$ Millions



Capital Expenditures

\$ Millions



(a) EBITDA, as adjusted, is defined as net income plus income taxes, interest expense (including debt extinguishment costs), operating lease expense, management fees, depreciation and amortization, foreign currency gains or losses, excluding non-recurring items (including facility consolidation costs) and extraordinary gains or losses. EBITDA, as adjusted, is reconciled and discussed in our Annual Report on Form 10-K for the fiscal year ended March 31, 2004, page 19, within Item 6, Selected Financial Data.

(b) Debt extinguishment costs of \$14.9 million (\$9.4 million, net of tax) and facility consolidation costs of \$1.8 million (\$1.1 million, net of tax).

(c) Debt includes capital lease obligations.

To Our Stockholders

We are pleased to report to our stockholders on a year of solid performance for Universal. Entering fiscal 2005, we are in the strongest financial and operational position since our initial public offering in 2000.

Improved economic activity and the execution of our focused business strategy resulted in strong financial performance in fiscal 2004 and we were able to strengthen our overall financial position. We have been successful in our efforts to position Universal as a full service compression company and believe this approach is being well accepted in the marketplace.

Financial Highlights

For the year ended March 31, 2004, net income was \$30.8 million, or \$0.98 per diluted share, including charges of \$16.7 million on a pretax basis or \$0.34 per diluted share on an after-tax basis, related to debt extinguishment and facility consolidation costs. These costs were incurred primarily in connection with our debt retirement and refinancing efforts that both lowered our overall debt level and resulted in a reduction of the interest rate on \$175 million of our debt. Excluding the charges, net income was \$41.3 million, or \$1.32 per diluted share. In the prior year, net income was \$33.5 million, or \$1.08 per diluted share.

“We have been successful in our efforts to position Universal as a full service compression company and believe this approach is being well accepted in the marketplace.”

For fiscal 2004, we had revenue of \$688.8 million and EBITDA, as adjusted, of \$223.8 million, both records for us, compared to revenue of \$625.2 million and EBITDA, as adjusted, of \$201.2 million in the previous year. Highlights of fiscal 2004 included improved utilization of our contract compression fleet and increased revenue in our fabrication and aftermarket services segments.

We continue to have a disciplined approach to capital investment. We have reduced capital expenditure levels while seeking to reactivate idle fleet units. Our capital expenditures declined from \$121 million in fiscal 2003 to \$87 million in fiscal 2004. As we target new business opportunities, we work hard to utilize existing assets before considering new builds.

Our financial liquidity continues to improve and our credit availability remains strong. In fiscal 2004, we generated a record \$80 million in free cash flow, which we define as operating cash flow after capital expenditures. We also generated another \$40 million in cash, primarily from the sale of fleet units under purchase options and other property. Our cash position was approximately \$121 million at March 31, 2004. Our \$125 million revolver, which extends into 2006, has no amounts drawn against it and we have an additional \$25 million of capacity on our asset backed debt instrument.

Our balance sheet is strengthening while we improve our financial results. Our overall debt to capitalization ratio, net of cash position, has declined from 54 percent at March 31, 2003 to 49 percent

at March 31, 2004. In early fiscal 2004, we refinanced \$230 million of 9 $\frac{7}{8}$ percent debt with the issuance of \$175 million of 7 $\frac{1}{4}$ percent debt and use of excess cash.

Operations

A primary goal at Universal is to increase the utilization of our contract compression fleet. To help meet this goal, we have invested in the repackaging of existing units to improve their marketability. Our average fleet utilization increased from 83 percent in fiscal 2003 to 86 percent in fiscal 2004, with significant improvements in both domestic and international markets. Our average domestic utilization increased from 83 percent to 85 percent over the course of fiscal 2004 while average international utilization increased from 85 percent to 89 percent.

Our active domestic contract compression markets include coalbed methane and tight sands production in the Rocky Mountains, Texas and Alabama. Our international markets are highlighted by growth in Australia, Argentina, Brazil, Thailand and Indonesia, with new projects slated to start in Mexico, Argentina and Venezuela in early fiscal 2005.

We have consolidated our fabrication activities to increase operating efficiencies and standardize procedures. We consolidated our Tulsa operations into our Houston operations in early fiscal 2004, and

“The continuous improvement of our contract compression fleet enhances our competitive position.”

combined the remaining two large facilities in Calgary and Houston under a common North American organizational structure last fall.

Driven by increased demand in North America, fabrication revenue increased from \$163 million in fiscal 2003 to \$184 million in fiscal 2004. Our fabrication backlog increased from \$56 million on March 31, 2003 to \$88 million on March 31, 2004. The recent opening of a formal office in Beijing is expected to help our penetration of the Chinese market, where we recently received our first onshore order.

We also had increased demand for aftermarket services in fiscal 2004. Revenue increased from \$131 million in fiscal 2003 to \$142 million in fiscal 2004 due to increased activity in all of our principal geographic markets. Business levels increased in Argentina, our largest operation in Latin America, and an acquisition in Australia positioned us for increased coalbed methane activity in the Queensland area.

We will continue efforts to increase maintenance and repair activity on equipment owned by others in field wellhead and gathering applications, as well as in processing plants, pipelines, petrochemical plants and refineries. We plan to further expand aftermarket services in the Asia Pacific and Latin America markets. An acquisition in Venezuela completed in June 2004 improved our competitive position in this important Latin American market and we recently opened a new repair facility in Indonesia.

Strategic Initiatives

The continuous improvement of our contract compression fleet enhances our competitive position. We continue to invest selectively in new equipment at attractive target rates of return. There is a strong demand for larger horsepower multi-stage units. These units, often used in gathering and pipeline applications, are being deployed in both domestic and international markets. During fiscal 2004 we repackaged units in our existing fleet at a cost of approximately \$11 million to increase their operating performance and marketability. This activity includes increasing the number of compression stages and replacing engines and coolers. These modifications are made to improve performance as the market develops more low-pressure applications.

We began the implementation of our compressor remote monitoring system in fiscal 2003 in order to enhance the efficiency of our field operations and improve performance for our customers. We currently have over 1,200 units operating under our remote monitoring system in the United States and expect to further expand this program in fiscal 2005.

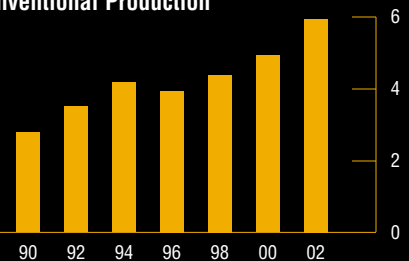
We now offer more integrated products and services to better meet the needs of our customers. These activities include design, engineering, fabrication, construction, installations, operations and maintenance, and may include the combination of compression with other related equipment. For several years we

"The growth of unconventional production from tight sands, coalbed methane and gas shales is boosting compression demand."

Domestic Unconventional Production

Trillion Cubic Feet

Source:
Energy Information
Administration



have offered turnkey installation services for multi-unit contract compression projects in international locations, and recently we began offering turnkey installation services in conjunction with fabrication sales. Current projects include a large pipeline compression installation in the western United States.

Additionally, we will seek to increase activities with existing alliance customers and gain new preferred relationships. The implementation of a new enterprise resource planning system is expected to provide a more enhanced integration of our operating and financial software system. To better prepare our employees, we recently opened a new central training facility on our Houston campus.

Outlook

We have a positive outlook for fiscal 2005 with the continuing implementation of our growth strategies and favorable market conditions. The growing global economy is expected to boost the demand for natural gas and associated compression products and services.

The domestic market drivers are the maturing producing fields, which typically require increasing compression to offset declining natural reservoir pressure, and the growth of compression intensive production from unconventional sources such as tight sands, coalbed methane and gas shales. International market drivers include the increasing world-wide demand for energy, including natural

gas, the growth in the natural gas industry infrastructure, environmental initiatives that encourage the consumption of natural gas and the growth in the global transportation of natural gas.

Our contract compression customers continue to appreciate the benefits of outsourcing, by maximizing production and cash flow levels while reducing capital investment and gaining flexibility to adjust equipment configurations with changing field requirements.

We remain committed to the domestic market and will continue to build on our opportunities in the international arena. We will also seek to enhance our product and service offerings to help our customers meet their objectives.

With our strong financial position, we believe we're well positioned to take advantage of future market opportunities. We are proud of our achievements for fiscal 2004, but remain focused on continuing to increase our financial returns by optimizing current operations, lowering our cost of capital and targeting attractive returns on new investments.

2004 marks a special year for Universal. Our company traces its roots back to a small compressor provider called South Coast Gas Company, which was established almost 50 years ago in Houston. This year we proudly celebrate our 50th anniversary with our loyal team of employees around the world, all of whom share a commitment to our core values of *Safety*, *Service* and *Integrity*.

"With our strong financial position, we believe we're well positioned to take advantage of future market opportunities."



As always, we appreciate the support of our stockholders and pledge our finest effort to achieve our goals. We value the relationships we continue to strengthen with our customers and we salute the dedication and commitment of our employees.

A stylized, handwritten signature in black ink, consisting of several loops and a long horizontal stroke.

STEPHEN A. SNIDER
President and Chief Executive Officer

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

FORM 10-K

FOR ANNUAL AND TRANSITION REPORTS PURSUANT TO SECTIONS 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

(Mark One)

- ☒ **ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**
For the fiscal year ended March 31, 2004
- ☐ **TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**

or
For the transition period from _____ **to** _____
Commission file nos.: 001-15843
333-48279

UNIVERSAL COMPRESSION HOLDINGS, INC.

UNIVERSAL COMPRESSION, INC.

(Exact name of Registrants as Specified in Their Charters)

Delaware	13-3989167
Texas	4-1282680
(States or Other Jurisdictions of Incorporation or Organization)	(I.R.S. Employer Identification Nos.)
4444 Brittmoore Road, Houston, Texas	77041-8004
(Address of Principal Executive Offices)	(Zip Code)

(713) 335-7000

(Registrants' telephone number, including area code)

Securities of Universal Compression Holdings, Inc. Registered Pursuant to Section 12(b) of the Act:

<u>Title of Each Class</u>	<u>Name of Each Exchange on Which Registered</u>
Common Stock, \$.01 par value	New York Stock Exchange, Inc

Securities of Universal Compression Holdings, Inc. Registered Pursuant to Section 12(g) of the Act:

Title of Each Class
None

Securities of Universal Compression, Inc. Registered Pursuant to Section 12(b) of the Act:

<u>Title of Each Class</u>	<u>Name of Each Exchange on Which Registered</u>
None	N/A

Securities of Universal Compression, Inc. Registered Pursuant to Section 12(g) of the Act:

Title of Each Class
None

UNIVERSAL COMPRESSION, INC. MEETS THE CONDITIONS SET FORTH IN GENERAL INSTRUCTION I(1)(a) AND (b) OF FORM 10-K AND IS THEREFORE FILING THIS FORM 10-K WITH THE REDUCED DISCLOSURE FORMAT.

Indicate by check mark whether each of the registrants (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 registrants were required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes ☒ No ☐

Indicate by check mark 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 each of the 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.

Indicate by check mark whether the registrants are accelerated filers (as defined in Rule 12b-2 of the Exchange Act).

Yes ☒ No ☐ (Universal Compression Holdings, Inc.)
Yes ☐ No ☒ (Universal Compression, Inc.)

The aggregate market value of the Common Stock of Universal Compression Holdings, Inc. held by non-affiliates as of the last business day of the registrant's most recently completed second fiscal quarter (September 30, 2003) was approximately \$362 million. For purposes of the above statements only, all directors, executive officers and 10% stockholders are assumed to be affiliates. This calculation does not reflect a determination that such persons are affiliates for any other purpose.

The number of shares of the Common Stock of Universal Compression Holdings, Inc. outstanding as of June 7, 2004: 31,386,796 shares. All 4,910 outstanding shares of common stock of Universal Compression, Inc., par value \$10.00 per share, are owned by Universal Compression Holdings, Inc.

Documents Incorporated by Reference

Portions of Universal Compression Holdings, Inc.'s Proxy Statement for the Annual Meeting of Stockholders to be held on July 23, 2004 are incorporated by reference into Part III, as indicated herein.

The Index to Exhibits is on page 51.

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PART I

The terms “our,” “Company,” “we,” and “us” when used in this report refer to Universal Compression Holdings, Inc. and its subsidiaries, including Universal Compression, Inc., as a combined entity, including its predecessors, except where it is made clear that such term means only the parent company. The term “Universal” refers to Universal Compression, Inc. and its subsidiaries, as a combined entity.

DISCLOSURE REGARDING FORWARD-LOOKING STATEMENTS

This report contains “forward-looking statements” intended to qualify for the safe harbors from liability established by the Private Securities Litigation Reform Act of 1995. All statements other than statements of historical fact contained in this report are forward-looking statements, including, without limitation, statements regarding future financial position, business strategy, proposed acquisitions, budgets, litigation, projected costs and plans and objectives of management for future operations. You can identify many of these statements by looking for words such as “believes,” “expects,” “will,” “intends,” “projects,” “anticipates,” “estimates,” “continues” or similar words or the negative thereof.

Such forward-looking statements in this report include, without limitation:

- our business growth strategy and projected costs;
- our future financial position;
- the sufficiency of available cash flows to fund continuing operations;
- the expected amount of our capital expenditures;
- anticipated cost savings, future revenue, gross profits, EBITDA, as adjusted and other financial measures related to our business and our primary business segments;
- the future value of our equipment; and
- plans and objectives of our management for our future operations.

Such forward-looking statements are subject to various risks and uncertainties that could cause actual results to differ materially from those anticipated as of the date of this report. The risks related to our business described under “Risk Factors” and elsewhere in this report could cause our actual results to differ from those described in, or otherwise projected or implied by, the forward-looking statements. Although we believe that the expectations reflected in these forward-looking statements are based on reasonable assumptions, no assurance can be given that these expectations will prove to be correct. Important factors that could cause our actual results to differ materially from the expectations reflected in these forward-looking statements include, among other things:

- conditions in the oil and gas industry, including a sustained decrease in the level of supply or demand for natural gas and the impact of the price of natural gas;
- competition among the various providers of natural gas compression services;
- changes in political or economic conditions in key operating markets, including international markets;
- changes in safety and environmental regulations pertaining to the production and transportation of natural gas;
- acts of war or terrorism or governmental or military responses thereto;
- introduction of competing technologies by other companies;
- our ability to retain and grow our customer base;

- our level of indebtedness and ability to fund our business;
- our ability to recoup our investment by re-applying our compressors after typically short initial lease terms;
- currency exchange rate fluctuations;
- employment workforce factors, including loss of key employees; and
- liability claims related to the use of our products and services.

All forward-looking statements included in this report are based on information available to us on the date of this report. We undertake no obligation to publicly update or revise any forward-looking statement, whether as a result of new information, future events or otherwise. All subsequent written and oral forward-looking statements attributable to us or persons acting on our behalf are expressly qualified in their entirety by the cautionary statements contained throughout this report.

ITEM 1. *Business*

General

We are the second largest natural gas compression services company in the world in terms of compressor fleet horsepower, with a fleet as of March 31, 2004 of approximately 7,100 compressor units comprising approximately 2.3 million horsepower. We provide a full range of natural gas compression services, sales, operations, maintenance and fabrication services and products to the natural gas industry, both domestically and internationally. These services and products are essential to the natural gas industry as gas must be compressed to be delivered from the wellhead to end-users.

We operate in four primary business segments: domestic contract compression, international contract compression, fabrication and aftermarket services. Our core business, contract compression, involves providing compression equipment and service to customers. By outsourcing their compression needs, we believe our contract compression customers generally are able to increase their revenue by producing a higher volume of natural gas through decreased compressor downtime. In addition, outsourcing allows our customers to reduce their operating and maintenance costs and capital investments and more efficiently meet their changing compression needs.

In addition to contract compression, we provide a broad range of compression services and products to customers who own their compression equipment or use equipment provided by our competitors. Our fabrication business involves the design, engineering and assembly of natural gas and air compressors for sale to third parties in addition to those that we use in our contract compression fleet. Our ability to fabricate compressors ranging in size from under 100 horsepower to over 5,000 horsepower enables us to provide compressors that are used in all facets of natural gas production, transmission and distribution. Our aftermarket services business sells parts and components, and provides maintenance and operations services to customers who own their compression equipment or have agreements with our competitors. Our ability to provide a full range of compression services and products broadens our customer relationships and helps us identify potential new customers and cross-selling opportunities for existing customers. As the compression needs of our customers increase due to the growing demand for natural gas throughout the world, we believe our geographic scope and broad range of compression services and products will enable us to participate in that growth.

Financial information about our business segments is provided in Note 12 in the notes to the Company's financial statements at the end of this report.

We are a Delaware corporation and a holding company that conducts operations through our wholly-owned subsidiary, Universal, a Texas corporation incorporated in 1954. We were formed on December 12, 1997 for the purpose of acquiring Universal's predecessor, Tidewater Compression

Service, Inc. (“TCS”) from Tidewater, Inc. Upon completion of the acquisition on February 20, 1998, TCS became our wholly-owned subsidiary and changed its name to Universal Compression, Inc. Through this subsidiary, our gas compression service operations date back to 1954. We completed an initial public offering of shares of our common stock in June 2000.

Since our initial public offering, we have completed several acquisitions, which have contributed significantly to our growth. Our most significant acquisition was that of Weatherford Global Compression Services, L.P. and certain related entities (“Weatherford Global”), former subsidiaries of Weatherford International Ltd. (“Weatherford”), in February 2001. This added approximately 950,000 horsepower to our fleet, more than doubling our size at that time.

Our principal corporate office is located at 4444 Brittmoore Road, Houston, Texas 77041.

We maintain a website at www.universalcompression.com. Our annual report on Form 10-K, quarterly reports on Form 10-Q, current reports on Form 8-K, and amendments to those reports are available, without charge, on our website, www.universalcompression.com/invest/SECfrX.html, as soon as reasonably practicable after they are filed electronically with the Securities and Exchange Commission. Paper copies are also available, without charge, from Universal Compression Holdings, Inc., 4444 Brittmoore Road, Houston, Texas 77041, Attention: Investor Relations.

Key Operating and Financial Statistics

The following table illustrates our key operating and financial statistics during the last three fiscal years:

	Year Ended March 31,		
	2004	2003	2002
	(Dollars in thousands)		
Domestic horsepower (end of period)	1,903,614	1,957,015	1,890,935
International horsepower (end of period)	417,271	368,437	345,093
Total horsepower (end of period)	2,320,885	2,325,452	2,236,028
Average horsepower utilization rate	85.8%	83.3%	88.8%
Revenue	\$ 688,786	\$ 625,218	\$ 679,989
Percentage of revenue from:			
Domestic contract compression	40.8%	42.5%	39.3%
International contract compression	12.0%	10.6%	8.9%
Fabrication	26.7%	26.0%	31.1%
Aftermarket services	20.5%	20.9%	20.7%
Net income	\$ 30,787	\$ 33,518	\$ 49,408
EBITDA, as adjusted(a)	\$ 223,848	\$ 201,150	\$ 207,315

(a) EBITDA, as adjusted, is defined, reconciled to net income and discussed on page 19 of this report, within Item 6, Selected Financial Data.

Industry

Natural Gas Compression Overview

Natural gas compression is a mechanical process whereby a volume of gas at an existing pressure is compressed to a desired higher pressure. We offer both slow and high speed reciprocating compressors driven either by internal combustion engines or electric motors. We also offer rotary screw and centrifugal compressors for specialized applications. Most natural gas compression applications involve compressing gas for its delivery from one point to another. Low pressure or aging natural gas wells require compression for delivery of produced gas into higher pressured gas gathering or pipeline

systems. Compression at the wellhead is required because, over the life of an oil or gas well, natural reservoir pressure typically declines as reserves are produced. As the natural reservoir pressure of the well declines below the line pressure of the gas gathering or pipeline system used to transport the gas to market, gas no longer naturally flows into the pipeline. It is at this time that compression equipment is applied in both field and gathering systems to boost the well's pressure levels allowing gas to be brought to market. Compression is also used to reinject natural gas down producing oil wells to help lift liquids to the surface, known as gas lift operations. In secondary oil recovery operations, compression is used to inject natural gas into wells to maintain reservoir pressure. Compression is also used in gas storage projects to inject gas into underground reservoirs during off-peak seasons for withdrawal later during periods of high demand. Compressors may also be used in combination with oil and gas production equipment to process and refine oil and gas into more marketable energy sources. In addition, compression services are used for compressing feedstocks in refineries and petrochemical plants, and for refrigeration applications in natural gas processing plants.

Typically, compression is required several times during the natural gas production cycle: at the wellhead, at the gathering lines, into and out of gas processing facilities, into and out of storage facilities and through the pipeline. Natural gas compression that is used to transport gas from the wellhead through the gathering system is considered "field compression." Natural gas compression that is used during the transportation of gas from the gathering systems to storage or the end-user is considered "pipeline compression." During the production phase, compression is used to boost the pressure of natural gas from the wellhead so that natural gas can flow into the gathering system or pipeline for transmission to end-users. Typically, these applications require portable, low to mid-range horsepower compression equipment located at or near the wellhead. The continually dropping pressure levels in natural gas fields require constant modification and variation of on-site compression equipment.

Compression equipment is also used to increase the efficiency of a low capacity gas field by providing a central compression point from which the gas can be produced and injected into a pipeline for transmission to facilities for further processing. In an effort to reduce costs for wellhead operators, operators of gathering systems tend to keep the pressure of the gathering systems low. As a result, more pressure is often needed to force the gas from the low pressure gathering systems into the higher pressure pipelines. Similarly, as gas is transported through a pipeline, compressor units are applied all along the pipeline to allow the natural gas to continue to flow through the pipeline to its destination. These applications generally require larger horsepower compression equipment (600 horsepower and higher).

Gas producers, transporters and processors have historically owned and maintained most of the compression equipment used in their operations. However, over the past several years, there has been a trend toward outsourcing compression equipment. Changing well and pipeline pressures and conditions over the life of a well often require producers to reconfigure their compressor units to optimize the well production or pipeline efficiency.

Outsourcing contract compression equipment offers customers:

- the ability to efficiently meet their changing compression needs over time while limiting their capital investments in compression equipment;
- access to the compression service provider's specialized personnel and technical skills, including engineers, field service and maintenance employees, which generally leads to improved run-times and production rates; and
- overall reduction in their compression costs through the reduction or elimination of capital investment in equipment, spare parts inventory and other expenditures associated with owning and maintaining compressor units.

Customers that elect to outsource compression equipment may vary their level of service for such equipment. Full maintenance calls for the compression service provider to be responsible for certain operational tasks, such as scheduled preventative maintenance, repair and general up-keep of the equipment, while the customer usually remains responsible for the day-to-day inspection of the equipment. Contract compression requires the compression service provider to be responsible for more of the operational tasks. Often, the contract compression service provider will inspect the equipment daily, provide consumables such as oil and antifreeze and, if necessary, be present at the site for several hours each day.

Natural Gas Industry Conditions

A significant factor in the growth of the gas compression services market is the increasing demand and consumption of natural gas, both domestically and internationally. In the United States, natural gas is the second leading fuel in terms of total consumption. In recent years, natural gas has increased its market share of total domestic energy consumption. Domestic consumption of natural gas increased significantly from 1990 to 2000, before declining in the 2001 to 2003 time period due to an economic slowdown. Industry sources forecast increased consumption of natural gas in the United States in the remainder of the decade.

Domestic field compression is estimated to be 17 million horsepower, up from 10 million in 1993. Additionally, the estimated amount of compression outsourced has grown over that same period, from approximately 2 million horsepower in 1993 to in excess of 5 million horsepower in 2002. We believe the domestic gas compression market will continue to grow due to the following factors:

- higher natural gas consumption;
- the aging of producing natural gas fields, which will require more compression to continue producing the same volume of natural gas; and
- increased outsourcing by companies with compression needs in order to reduce operating costs, improve production and efficiency and reallocate capital to their core business activities.

The international gas compression services market currently is substantially smaller than the domestic market. However, we estimate significant growth opportunities in international demand for compression services and products due to the following factors:

- higher natural gas consumption;
- implementation of international environmental and conservation laws preventing the practice of flaring natural gas and recognition of natural gas as a clean air fuel;
- a desire by a number of oil exporting nations to replace oil with natural gas as a fuel source in local markets to allow greater export of oil;
- increasing development of pipeline infrastructure, particularly in Latin America and Asia necessary to transport natural gas to local markets;
- growing demand for electrical power generation, for which the fuel of choice tends to be natural gas; and
- privatization of state-owned energy producers, resulting in increased outsourcing due to the focus on reducing capital expenditures and enhancing cash flow and profitability.

In contrast to the domestic compression market, the international compression market is comprised primarily of large horsepower compressors. A significant portion of this market involves comprehensive installation projects, which include the design, fabrication, delivery, installation, operation and maintenance of compressors and related gas treatment equipment by the contract

compression service provider. In these projects, the customer's only responsibility is to provide fuel gas within specifications. As a result of the full service nature of these projects and that these compressors generally remain on-site for three to seven years, we are able to achieve higher revenue and margins on these projects.

Operations

Contract Compressor Fleet

As of March 31, 2004, our fleet consisted of 7,093 compressors, with an average of 327 horsepower per unit, as reflected in the following table:

Horsepower Range	Total Horsepower As of March 31,		% of Horsepower As of March 31,		Number of Units As of March 31,	
	2004	2003	2004	2003	2004	2003
0-99	177,665	194,160	7.6	8.3	2,385	2,633
100-299	442,946	458,021	19.1	19.7	2,540	2,640
300-599	359,032	359,953	15.5	15.5	939	941
600-999	403,760	404,159	17.4	17.4	552	551
1,000 and over	937,482	909,159	40.4	39.1	677	657
Total	2,320,885	2,325,452	100%	100%	7,093	7,422

For the year ended March 31, 2004, the average horsepower utilization rate for our fleet was approximately 85.8%, which reflects average horsepower utilization based upon our total average fleet horsepower. For the quarter ended March 31, 2004, this average rate was approximately 86.4%. Over the last several years, we have undertaken to standardize our compressor fleet around major components and key suppliers. Our standardized fleet:

- enables us to minimize our fleet operating costs and maintenance capital requirements;
- enables us to minimize inventory costs;
- facilitates low-cost compressor resizing; and
- allows us to develop technical proficiency in our maintenance and overhaul operations, which enables us to achieve high run-time rates while maintaining low operating costs.

Contract Compression

We provide comprehensive contract compression services, which include operation and maintenance services for our domestic and international fleet. When providing full contract compression service, we work closely with a customer's field service personnel so that the compressor can be adjusted to efficiently match changing characteristics of the gas produced. We provide maintenance services on substantially all of our fleet units. Maintenance services include the scheduled preventive maintenance, repair and general up-keep of compressor equipment. As a complement to our maintenance business, we offer supplies and services such as antifreeze and lubricants to the job site. We also may offer installation services, which for our typical mid-range and smaller horsepower units involves significantly less engineering and cost than the comprehensive service concept prevalent in the international markets. We also routinely repackage or reconfigure some of our existing fleet to adapt to our customers' needs.

We generally operate the large horsepower compressors under comprehensive compression services contracts and include the operations fee as part of the contract compression rate. Large horsepower units are more complex and, by operating the equipment ourselves, we reduce maintenance and overhaul expenses. Generally, we train our customers' personnel in fundamental compressor operations

of smaller horsepower units so that they can assume responsibility for the day-to-day inspection of the equipment and certain operational tasks.

Our field compression equipment is maintained in accordance with daily, weekly, monthly and annual maintenance schedules. These maintenance procedures are updated as technology changes and as our operations group develops new techniques and procedures. In addition, because our field technicians provide maintenance on substantially all of our contract compression equipment, they are familiar with the condition of our equipment and can readily identify potential problems. In our experience, these procedures maximize equipment life and unit availability and minimize avoidable downtime. Generally, each of our units undergoes a major overhaul once every six to eight years. A major overhaul involves the rebuilding of the unit in order to materially extend its useful life or to enhance the unit's ability to fulfill broader or different contract compression applications.

We believe that our fabrication and aftermarket services businesses provide us with opportunities to cross-sell our contract compression services.

We have standard contracts for rates and terms on the compressors in our fleet. Through negotiations, these rates and contracts may be modified. Optional items such as oil, antifreeze, freight, insurance and other items may be either itemized or included in the basic monthly contract compression rate. Initial contract compression terms are usually six months, with some projects committed for as long as five years. At the end of the initial term, contract compression services can continue at the option of the customer on a month-to-month basis or the compressor may be returned or replaced with a different compressor.

Domestic Operations. As of March 31, 2004, we operated the second largest domestic fleet of compressors in terms of horsepower with approximately 6,560 units comprising approximately 1.9 million horsepower. We operate sales and service locations in the primary onshore and offshore natural gas producing regions of the United States. For the year ended March 31, 2004, 40.8% of our total revenue was generated from domestic contract compression operations.

We maintain 18 field service locations throughout the United States at which we can service and overhaul our compression equipment.

International Operations. We operate internationally in Argentina, Australia, Brazil, Canada, China, Colombia, Indonesia, Mexico, Peru, Thailand, and Venezuela. As of March 31, 2004, we had approximately 540 units comprising approximately 417,000 horsepower, in the aggregate, in these markets. We intend to continue to expand our presence in these markets and pursue opportunities in other strategic international areas. For the year ended March 31, 2004, 12.0% of our total revenue was generated from international contract compression operations.

International compression service projects usually generate higher gross profit margins than domestic projects. Our international operations are focused on large horsepower compressor markets and frequently involve longer-term and more comprehensive service projects than our domestic projects. International projects generally require us to provide complete engineering and design. International service agreements differ significantly from domestic service agreements as individual contracts are negotiated for each project. We believe our extensive engineering and design capabilities and reputation for high quality fabrication provide us a competitive advantage in these markets.

Risks associated with our foreign operations are described herein under "Risk Factors."

Fabrication

As a complement to our contract compression service operations, we design, engineer, fabricate and sell natural gas compressors and air compressors to engineering and construction firms, exploration and production companies, as well as pipeline and gas transmission companies, both domestically and

internationally. We also fabricate compressor units for our own fleet. Our primary fabrication facilities are located in Houston, Texas and Calgary, Alberta, Canada.

Generally, compressors sold to third parties are assembled according to each customer's specifications. We purchase components for these compressors from third party suppliers, and are original equipment manufacturer representatives for several major engine, compressor, and electric motor manufacturers in the industry. We also sell prepackaged compressor units. For the year-ended March 31, 2004, 26.7% of our total revenue was generated from fabrication operations.

We do not incur material research and development expenditures, as these activities are not a significant aspect of our business. All research and development costs are expensed as incurred.

Aftermarket Services

Our aftermarket services business sells parts and components, and provides maintenance to customers who own their compression equipment or use equipment provided by our competitors.

Our inventory of parts is available either on an over-the-counter basis through our 18 service locations in the United States and 5 in Canada, on a bid basis for larger orders, or as part of our compressor maintenance service. Our maintenance services are available on an individual call basis, on a contract basis (which may cover a particular unit, an entire compression project or all of the customer's compression projects) or as part of our comprehensive operation and maintenance service. We also provide offshore maintenance and service. In addition, we provide overhaul and reconfiguration services for customer-owned compression equipment, either on-site or in our overhaul shops. For the year ended March 31, 2004, 20.5% of our total revenue was generated from aftermarket services operations.

Business Strategy

Our business strategy is to meet the evolving needs of our customers by providing consistent and dependable services and products, and to take advantage of our size and broad geographic scope to expand our customer base. The key elements of our business strategy are described below:

- *Provide a wide range of quality compression services and products.* We plan to continue to leverage our field compression capabilities to provide services and products to customers in all segments of the natural gas compression market, including field and pipeline compression, fabrication and aftermarket services.
- *Seek opportunities for preferred relationships.* We intend to continue to enter into strategic alliances, preferred vendor and similar long-term relationships to provide this full range of services and products to our customers.
- *Seek opportunities in select international markets.* We plan to expand our existing operations in Latin America, Canada and Asia Pacific and offer our services in other key markets. We believe that our experience in international markets and our reputation for providing reliable contract compression services and fabricating high quality, specifically-engineered compressors provides us with a solid foundation from which to further expand our business internationally.
- *Expand and leverage our fabrication and aftermarket services business.* We have significant fabrication and aftermarket services operations and we intend to expand these segments of our business. In addition to providing additional sources of revenue, these segments also provide us with an opportunity to cross-sell our contract compression services and products.
- *Continue to expand beyond field compression.* In addition to our field compression services, we have expanded our large horsepower compression capabilities in gathering, pipeline, processing,

storage and offshore markets. We believe the pipeline compression market has significant growth potential for our services.

- *Maintain financial flexibility.* We intend to maintain ample financial flexibility to be able to take advantage of opportunities as we identify them. Historically, during periods of growth, we have utilized our cash flow from operations as well as borrowings under available debt facilities to fund capital expenditures and acquisitions. This spending has allowed us to significantly grow our business and the amount of cash we generate while maintaining our debt at levels we believe are appropriate for our stable business. During the last fiscal year, we exercised disciplined capital spending and we intend to continue to focus on reducing our operating costs and managing our working capital. We believe our financial flexibility positions us to take advantage of future growth opportunities without incurring debt beyond appropriate levels.

Competitive Strengths

We believe that we have the following key competitive strengths:

- *Comprehensive range of services and products.* We provide a wide range of compression services and products to meet the changing compression needs of our customers in the diverse geographic markets that we serve, whether they outsource or own their compression equipment. For those customers who outsource, we believe our contract compression services and products generally allow our customers to achieve higher run-times than they would achieve with owned equipment, resulting in increased production and revenue for our customers. In addition, outsourcing allows our customers flexibility with regard to their changing compression needs while limiting their capital requirements. We continually expand, upgrade and reconfigure our contract compression fleet and provide our operations and maintenance personnel with extensive training. We are able to fabricate compression units ranging in size from under 100 horsepower to over 5,000 horsepower that meet the varying needs of our customers. Additionally, we sell parts and components and provide maintenance and operations services to customers who own their compression equipment or have agreements with our competitors. This broad range of compression services and products allows us to expand our customer base and gives us the opportunity to cross-sell our services and products.
- *Size and geographic scope.* We operate in the primary onshore and offshore natural gas producing regions of the United States and select international markets. As the second largest provider of natural gas compression services, we have sufficient fleet size, personnel, logistical capabilities, geographic scope, fabrication capabilities and range of compression service and product offerings to meet the full service needs of our customers in the domestic and international markets we serve on a timely and cost-effective basis. Our size, geographic scope and customer base provide us with improved fleet utilization opportunities. By increasing our fleet utilization, we are able to improve our operating leverage and increase returns. As a result, we believe we have relatively lower operating costs and higher margins than most companies with smaller fleets due to economies of scale.
- *Standardization of our compressor fleet.* We have undertaken to standardize our fleet of contract compressors around major components and key suppliers. Standardization enables us to develop extensive expertise in operating and maintaining our compressors, efficiently resizing and reconfiguring our compressors and reducing our operating costs by minimizing inventory costs. Natural gas compressors are long-lived assets with an expected economic life of 25 to 40 years. Our preventive maintenance program is designed to maximize the efficient operation of our fleet and to maintain their economic useful life.
- *Experienced management team.* Our management team has extensive experience in the compression services business. We believe our management team has successfully demonstrated

its ability to maintain our quality standards and commitment to customer service. Our management team has a substantial financial interest in our continued success through direct stock ownership, and participation in our incentive stock option and bonus programs which are linked to our performance.

Oil and Gas Industry Cyclicalities and Volatility

Our financial performance is generally less affected by the short-term market cycles and oil and gas price volatility than the financial performance of companies operating in other sectors of the oilfield services industry because

- compression is necessary in order for gas to be delivered from the wellhead to end-users;
- our operations are tied primarily to natural gas consumption, which is generally less cyclical in nature than exploration activities;
- outsourcing of compression is often economically advantageous for natural gas production, gathering and transportation companies;
- we have a broad customer base; and
- we operate in diverse geographic regions.

Adding to this stability is the fact that, while compressors often must be specifically engineered or reconfigured to meet the unique demands of our customers, the fundamental technology of compression equipment has not experienced significant technological change.

Customers

Our current customer base consists of over 1,000 domestic and international companies engaged in all aspects of the oil and gas industry, including major integrated oil and gas companies, international state-owned oil and gas companies, large and small independent producers, natural gas processors, gatherers and pipelines. We have entered into strategic alliances with some of our customers. These alliances are essentially preferred vendor arrangements and give us preferential consideration for the compression needs of these customers. In exchange, we provide these customers with enhanced product availability, product support and favorable pricing.

In the fiscal year ended March 31, 2004, no single customer accounted for as much as 10% of our total revenue. Our top 20 customers accounted for approximately 34.7% of our contract compression revenue in fiscal year 2004.

Suppliers

Our principal suppliers include Caterpillar and Waukesha for engines, Air Xchangers for coolers, and Ariel and Gemini for compressors. We also purchase Cooper parts and compressors in Canada for sale to customers. Although we rely primarily on these suppliers, we believe alternative sources are generally available. We have not experienced any material supply problems to date, and we believe our relations with our suppliers are good, except as expressed below.

In December 1999, Weatherford Global sold the assets and properties of its Gemini compressor business in Corpus Christi, Texas to GE Packaged Power, L.P., or GEPP. As part of that sale, Weatherford Global entered into an agreement to purchase from GEPP \$38.0 million of compressor components over five years and \$3.0 million of parts over three years, and GEPP agreed to provide compressors to Weatherford Global during that time period at negotiated prices. We assumed this obligation in connection with our acquisition of Weatherford Global in February 2001. As of March 31, 2004, approximately \$25.9 million of components and approximately \$13.5 million of parts have been

purchased from GEPP. As a result of GEPP product performance issues, we have been unable to satisfy and have not satisfied in full our purchase commitment in respect of components under this agreement with GEPP. The unsatisfied portion of the purchase commitment is approximately \$12.1 million. GEPP could assert its right to enforce this obligation, but has not indicated any interest to do so at this time. However, if GEPP should seek to enforce this obligation, we believe we have valid defenses and counter claims and would aggressively defend against such enforcement and pursue such counter claims.

Backlog

As of March 31, 2004, we had a compressor unit fabrication backlog for sale to third parties of approximately \$88.2 million, compared to \$55.7 million as of March 31, 2003. As of June 8, 2004, our backlog was approximately \$88.9 million compared to approximately \$81.1 at June 30, 2003. A majority of the backlog is expected to be completed within a 180-day period.

Insurance

We believe that our insurance coverage is customary for the industry and adequate for our business. As is customary in the natural gas service operations industry, we review our safety equipment and procedures and carry insurance against some, but not all, risks of our business.

Losses and liabilities not covered by insurance would reduce our revenue and increase our costs. The natural gas service operations business can be hazardous, involving unforeseen circumstances such as uncontrollable flows of gas or well fluids, fires and explosions or environmental damage. To address the hazards inherent in our business, we maintain insurance coverage that includes physical damage coverage, third party general liability insurance, employer's liability, environmental and pollution and other coverage, although coverage for environmental and pollution-related losses is subject to significant limitations. In addition, many of our service contracts shift certain risks to our customers, including requirements to have insurance coverage.

Competition

The natural gas contract compression, fabrication and aftermarket services businesses are highly competitive. We face competition from large national and multinational companies with greater financial resources and, on a regional basis, from numerous smaller companies.

Our main competitors in the contract compression business, based on horsepower, are Hanover Compressor Company, Compressor Systems, Inc. and J-W Operating Company. In addition, Weatherford and its subsidiaries may continue to compete with us as they are not contractually restricted from doing so. In our fabrication activities, we currently compete primarily with Hanover Compressor Company, Compressor Systems, Inc., Enerflex Systems, Ltd, Toromont Industries LTD and Collicut Energy Services LTD. Our aftermarket services business faces competition from manufacturers including Cooper Energy Services, Dresser-Rand, Hanover Compressor Company, from distributors of Caterpillar and Waukesha engines, from a number of smaller companies and, in Canada, from Enerflex Systems, Ltd, Toromont Industries LTD and Collicut Energy Services LTD.

We believe that we compete effectively on the basis of customer service, including the availability of our personnel in remote locations, price, technical expertise, parts service system, flexibility in meeting customer needs and quality and reliability of our compressors and related services.

Environmental and Other Regulations

We are subject to stringent and complex foreign, federal, state and local laws and regulations governing the discharge of materials into the environment or otherwise relating to protection of human

health and safety and the environment. Compliance with these laws and regulations may affect the costs of our operations. Moreover, failure to comply with these environmental laws and regulations may result in the assessment of administrative, civil, and criminal penalties, imposition of remedial obligations, and the issuance of injunctions delaying or prohibiting operations. We believe that our operations are in substantial compliance with applicable environmental requirements. As part of the regular evaluation of our operations, we update the environmental condition of our existing and acquired properties as necessary. We further believe that the phasing in of more stringent emission controls and other known regulatory requirements at the rate currently contemplated by environmental laws and regulations will not have a material adverse effect on our business, financial condition or results of operations.

Primary federal environmental laws that our operations are subject to include the Clean Air Act and regulations thereunder, which regulate air emissions, the Clean Water Act, and regulations thereunder, which regulate the discharge of pollutants in industrial wastewater and storm water runoff, and the Resource Conservation and Recovery Act, referred to as “RCRA,” and regulations, thereunder, which regulate the management and disposal of solid and hazardous waste. In addition, we are also subject to regulation under the federal Comprehensive Environmental Response, Compensation, and Liability Act, and regulations thereunder, known more commonly as “Superfund,” which regulates the release of hazardous substances in the environment. Analogous state laws and regulations may also apply.

The Clean Air Act and related regulations establish limits on the levels of various substances which may be emitted to the atmosphere during the operation of our fleet of natural gas compressors. These substances are regulated in permits, which are applied for and obtained through the various regulatory agencies, either state or federal depending on the level of emissions. While our standard contract typically provides that the customer will assume the permitting responsibilities and environmental risks related to compressor operations, we have in some cases obtained air permits as the owner and operator of the compressors. Under most of our contract compression service agreements, our customers must indemnify us for certain losses or liabilities we may suffer as a result of the failure of the compressors to comply with applicable environmental laws, including permit conditions. Increased obligations of operators to reduce air emissions of nitrogen oxides and other pollutants from internal combustion engines in transmission service are anticipated. Any new regulations requiring the installation of more sophisticated emission control equipment on such smaller portable sources potentially could have a material adverse impact on us. However, we believe that in most cases, these obligations would be allocated to our clients under the above-referenced contracts. In any event, we expect that such requirements would not have any more significant effect on our operations or financial condition than on any similarly situated company providing contract compression services.

The Clean Water Act and related regulations prohibit the discharge of industrial wastewater without a permit and establish limits on the levels of pollutants contained in these discharges. In addition, the Clean Water Act, regulates storm water discharges associated with industrial activities depending on a facility’s primary standard industrial classification. Many of our facilities have applied for and obtained industrial wastewater discharge permits as well as sought coverage under local wastewater ordinances. In addition, many of our facilities have filed notices of intent for coverage under statewide storm water general permits and developed and implemented storm water pollution prevention plans, as required.

The RCRA and related regulations, regulate the management and disposal of solid and hazardous waste. These laws and the regulations govern the generation, storage, treatment, transfer and disposal of wastes that we generate. These wastes include, but are not limited to, used oil, antifreeze, filters, sludges, paint, solvents, and sandblast materials. The Environmental Protection Agency and various state agencies have limited the approved methods of disposal for these types of wastes.

Under the Comprehensive Environmental Response, Compensation, and Liability Act, referred to as “CERCLA,” and comparable state laws and regulations, strict and joint and several liability can be imposed without regard to fault or the legality of the original conduct on certain classes of persons that contributed to the release of a hazardous substance into the environment. These persons include the owner and operator of a contaminated site where a hazardous substance release occurred and any company that transported, disposed of, or arranged for the transport or disposal of hazardous substances released at the site. Under CERCLA, such persons may be liable for the costs of remediating the hazardous substances that have been released into the environment and for damages to natural resources. In addition, where contamination may be present it is not uncommon for the neighboring landowners and other third parties to file claims for personal injury, property damage and recovery of response costs.

We currently own or lease, and have in the past owned or leased, a number of properties that have been used, some for many years and some by third parties over whom we have no control, in support of natural gas compression services or other industrial operations. As with any owner or operator of property, we may be subject to remediation costs and liability under CERCLA, RCRA or other environmental laws for hazardous waste, asbestos or any other toxic or hazardous substance that may exist on or under any of our properties, including waste disposed or groundwater contaminated by prior owners or operators. We have performed in the past, are currently performing, and may perform in the future, certain remediation activities governed by environmental laws. The cost of this remediation has not been material to date and we currently do not expect it to be material in the future. We are currently undertaking groundwater monitoring at certain of our facilities, which may further define remedial obligations. Certain of our acquired properties may also warrant groundwater monitoring and other remedial activities. We believe that former owners and operators of many of these properties may be wholly or partly responsible under environmental laws and contractual agreements to pay for or perform remediation, or to indemnify us for our remedial costs. These other entities may fail to fulfill their legal or contractual obligations, which could result in imposing response obligations and material costs to us.

Any new regulations requiring the installation of more sophisticated emission control equipment on such smaller portable sources potentially could have a material adverse impact on us. However, we believe that in most cases, these obligations would be allocated to our clients under the above-referenced contracts. In any event, we expect that such requirements would not have any more significant effect on our operations or financial condition than on any similarly situated company providing contract compression services.

Stricter standards in environmental legislation or regulations that may affect us may be imposed in the future, such as proposals to make hazardous wastes subject to more stringent and costly handling, disposal and remediation requirements. Accordingly, new environmental laws or regulations or amendments to existing environmental laws or regulations (including, but not limited to, regulations concerning ambient air quality standards, waste water and storm water discharges, and global climate changes) could require us to undertake significant capital expenditures and could otherwise have a material adverse effect on our business, results of operations and financial condition.

Our international operations are potentially subject to similar governmental controls and restrictions relating to the environment. We believe that we are in substantial compliance with any such foreign requirements pertaining to the environment.

Since 1992, there have been various proposals to impose taxes with respect to the energy industry, none of which have been enacted and all of which have received significant scrutiny from various industry lobbyists. At the present time, given the uncertainties regarding the proposed taxes, including the uncertainties regarding the terms which the proposed taxes might ultimately contain and the

industries and persons who may ultimately be the subject of such taxes, it is not possible to determine whether any such tax will have a material adverse effect on us.

Employees and Labor Relations

As of March 31, 2004, we had approximately 2,370 employees worldwide. We believe our relationship with our employees is good. Approximately 240 of our employees in Canada, 60 of our employees in Argentina, 40 of our employees in Brazil and 20 of our employees in Mexico are covered by collective bargaining agreements.

ITEM 2. *Properties*

The following table describes our material facilities owned or leased as of March 31, 2004:

<u>Location</u>	<u>Square Feet</u>	<u>Acreage</u>	<u>Status</u>	<u>Uses</u>
Houston, Texas	244,000	30.0	Owned	Corporate headquarters, fabrication, contract compression and aftermarket services
Calgary, Alberta, Canada	105,760	9.2	Owned	Fabrication, contract compression and aftermarket services
Yukon, Oklahoma	72,000	14.7	Owned	Contract compression and aftermarket services
Houma, Louisiana	60,000	91.0	Owned	Aftermarket services
Belle Chase, Louisiana	35,000	4.0	Owned	Contract compression and aftermarket services
Schulenberg, Texas	23,000	13.3	Owned	Fabrication, contract compression and aftermarket services
Broussard, Louisiana	24,700	10.0	Leased	Contract compression and aftermarket services

None of the above referenced facilities are pledged as collateral, except for the Schulenberg, Texas facility, which has been pledged as collateral to secure a \$790,000 loan assumed as part of the acquisition of Gas Compression Services Inc. in 2000.

ITEM 3. *Legal Proceedings*

From time to time, we may be involved in litigation relating to claims arising out of our operations in the normal course of business. We do not believe we are party to any legal proceedings which, if determined adversely to us, individually or in the aggregate, would have a material adverse effect on our results of operations or financial position.

ITEM 4. *Submission of Matters to a Vote of Security Holders*

There were no matters submitted to a vote of security holders during the fourth quarter of fiscal 2004.

PART II

ITEM 5. Market for Registrants' Common Equity, Related Stockholder Matters and Issuer Purchases of Equity Securities

Our common stock is traded on the New York Stock Exchange under the symbol "UCO." The following table sets forth the range of high and low sale prices for our common stock for the periods indicated.

	Price Range	
	High	Low
Quarter Ended:		
June 30, 2002	\$27.00	\$19.50
September 30, 2002	24.85	15.12
December 31, 2002	20.89	14.60
March 31, 2003	19.70	15.36
June 30, 2003	\$22.40	\$16.83
September 30, 2003	24.81	18.53
December 31, 2003	27.00	21.45
March 31, 2004	34.60	25.49
Through June 7, 2004	33.16	28.80

On June 7, 2004, the closing price of our common stock was \$30.00 per share. As of June 7, 2004, there were approximately 569 holders of record of our common stock.

We have never declared or paid any cash dividends to our stockholders and do not plan to pay any cash dividends in the foreseeable future. We currently intend to retain our earnings for use in the operation and expansion of our business.

ITEM 6. Selected Financial Data

SELECTED HISTORICAL FINANCIAL DATA UNIVERSAL COMPRESSION HOLDINGS, INC.

The following selected historical consolidated financial data should be read in conjunction with “Management’s Discussion and Analysis of Financial Condition and Results of Operations” and the consolidated financial statements and related notes included elsewhere in this report. The selected historical financial and operating data for each of the five years in the period ended March 31, 2004 have been derived from the respective audited financial statements. The consolidated financial statements and report thereon, as of March 31, 2004 and 2003 and for the years ended March 31, 2004, 2003 and 2002 are included elsewhere in this report.

	Year Ended March 31,				
	2004	2003	2002	2001	2000
	(In thousands, except per share data)				
Statement of Operations Data:					
Revenue	\$688,786	\$ 625,218	\$ 679,989	\$232,466	\$136,295
Gross profit(1)	289,481	267,968	268,346	109,407	69,000
Selling, general and administrative expenses	67,516	67,944	60,890	21,092	16,797
Depreciation and amortization	85,650	63,706	48,600	33,491	26,006
Interest expense, net(2)	73,475	36,421	23,017	23,220	34,327
Operating lease expense(2)	—	46,071	55,401	14,443	—
Debt extinguishment costs(3)	14,903	—	—	15,204	—
Facility consolidation costs	1,821	—	—	—	—
Income tax expense (benefit)	17,741	20,975	30,931	3,645	(1,994)
Net income (loss)	30,787	33,518	49,408	(4,391)	(5,982)
Earnings (loss) per share					
Basic	1.00	1.09	1.65	(0.30)	(2.44)
Diluted	0.98	1.08	1.63	(0.29)	(2.44)
Weighted average common stock outstanding					
Basic	30,848	30,665	30,008	14,760	2,448
Diluted	31,283	30,928	30,250	15,079	2,448
Other Financial Data:					
EBITDA, as adjusted(4)	\$223,848	\$ 201,150	\$ 207,315	\$ 88,787	\$ 55,561
Capital expenditures:					
Expansion	\$ (47,629)	\$ (67,289)	\$(137,790)	\$(55,384)	\$(45,617)
Overhauls	(27,866)	(29,198)	(27,000)	(9,901)	(9,920)
Other	(11,062)	(24,264)	(23,229)	(2,721)	(4,465)
Cash flows provided by (used in):					
Operating activities	\$166,078	\$ 187,070	\$ 133,078	\$ 89,476	\$ 47,144
Investing activities	(46,850)	(107,704)	(160,256)	(3,318)	(61,103)
Financing activities	(69,732)	(13,849)	21,075	(75,282)	12,435
As of March 31,					
	2004	2003	2002	2001	2000
	(In thousands)				
Balance Sheet Data:					
Cash	\$ 121,189	\$ 71,693	\$ 6,176	\$ 12,279	\$ 1,403
Working capital(5)	174,599	158,405	139,923	97,763	7,209
Total assets	1,972,451	1,953,887	1,277,165	1,176,256	469,942
Total debt(6)(7)	884,442	945,155	226,762	215,107	377,485
Stockholders' equity	799,235	744,451	700,344	652,574	74,677

(1) Gross profit is defined as total revenue less direct costs.

(2) Operating lease expense related to the operating lease facilities has been recognized as interest expense subsequent to consolidation of the operating lease facilities on December 31, 2002.

(3) Debt extinguishment costs in 2001 were previously reported as an extraordinary loss of \$9.5 million, net of \$5.7 million income tax benefit.

(4) EBITDA, as adjusted, is defined, reconciled to net income and discussed on page 19 of this report, within this Item 6, Selected Financial Data.

(5) Working capital is defined as current assets minus current liabilities.

(6) Includes capital lease obligations.

(7) Excludes \$708.5 million and \$527.5 million outstanding under our operating lease facilities as of March 31, 2002 and 2001, respectively. See Note 4 to the consolidated financial statements for a discussion related to the operating lease facilities.

SELECTED HISTORICAL FINANCIAL DATA
UNIVERSAL COMPRESSION, INC.

The following selected historical consolidated financial data should be read in conjunction with “Management’s Discussion and Analysis of Financial Condition and Results of Operations” and the consolidated audited financial statements and related notes included elsewhere in this report. The selected historical financial and operating data for each of the five years in the period ended March 31, 2004 have been derived from the respective audited financial statements. The consolidated audited financial statements and report thereon, as of March 31, 2004 and 2003 and for the years ended March 31, 2004, 2003 and 2002 are included elsewhere in this report.

	Year Ended March 31,				
	2004	2003	2002	2001	2000
	(In thousands)				
Statement of Operations Data:					
Revenue	\$688,786	\$ 625,218	\$ 679,989	\$232,466	\$136,295
Gross profit(1)	289,481	267,968	268,346	109,407	69,000
Selling, general and administrative expenses	67,516	67,944	60,890	21,092	16,797
Depreciation and amortization	85,650	63,706	48,600	33,485	26,000
Interest expense, net(2)	73,475	36,421	23,017	22,622	30,916
Operating lease expense(2)	—	46,071	55,401	14,443	—
Debt extinguishment costs(3)	14,903	—	—	10,611	—
Facility consolidation costs	1,821	—	—	—	—
Income tax expense (benefit)	17,741	20,975	30,931	3,871	(696)
Net income (loss)	30,787	33,518	49,408	(1,142)	(3,863)
Other Financial Data:					
EBITDA, as adjusted(4)	\$223,848	\$ 201,150	\$ 207,315	\$ 88,787	\$ 55,561
Capital expenditures:					
Expansion	\$ (47,629)	\$ (67,289)	\$ (137,790)	\$ (55,384)	\$ (45,617)
Overhauls	(27,866)	(29,198)	(27,000)	(9,901)	(9,920)
Other	(11,062)	(24,264)	(23,229)	(2,721)	(4,465)
Cash flows provided by (used in):					
Operating activities	\$163,259	\$ 186,152	\$ 131,837	\$ 92,881	\$ 47,029
Investing activities	(46,850)	(107,704)	(160,256)	(3,318)	(61,103)
Financing activities	(66,913)	(12,931)	22,316	(78,687)	12,550
	As of March 31,				
	2004	2003	2002	2001	2000
	(In thousands)				
Balance Sheet Data:					
Cash	\$ 121,189	\$ 71,693	\$ 6,176	\$ 12,279	\$ 1,403
Working capital(5)	174,599	158,059	139,544	97,382	5,869
Total assets	1,972,451	1,953,506	1,276,781	1,171,534	466,345
Total debt(6)(7)	884,442	945,155	226,762	215,107	345,832
Stockholder's equity	799,235	739,503	695,396	647,624	101,445

- (1) Gross profit is defined as total revenue less direct costs.
- (2) Operating lease expense related to the operating lease facilities has been recognized as interest expense subsequent to the consolidation of the operating lease facilities on December 31, 2002.
- (3) Debt extinguishment costs in 2001 were previously reported as an extraordinary loss of \$6.6 million, net of \$4.0 million income tax benefit.
- (4) EBITDA, as adjusted, is defined, reconciled to net income and discussed on page 19 of this report, within this Item 6, Selected Financial Data.
- (5) Working capital is defined as current assets minus current liabilities.
- (6) Includes capital lease obligations.
- (7) Excludes \$708.5 million and \$527.5 million outstanding under Universal's operating lease facilities as of March 31, 2002 and 2001, respectively. See Note 4 to the consolidated financial statements for a discussion related to the operating lease facilities.

THE COMPANY'S DEFINITION, RECONCILIATION AND USE OF EBITDA, AS ADJUSTED

EBITDA, as adjusted, is defined as net income plus income taxes, interest expense (including debt extinguishment costs), operating lease expense, management fees, depreciation and amortization, foreign currency gains or losses, excluding non-recurring items (including facility consolidation costs) and extraordinary gains or losses. Beginning with the quarter ended September 30, 2002, the Company changed its definition of EBITDA, as adjusted, to exclude foreign currency gains or losses. All periods prior to September 30, 2002 have been recalculated from amounts previously disclosed by the Company to be consistent with this new definition of EBITDA, as adjusted.

EBITDA, as adjusted, represents a measure upon which management assesses performance and, as such, we believe that the generally accepted accounting principle ("GAAP") measure most directly comparable to it is net income or net loss. The manner in which management uses EBITDA, as adjusted, to evaluate our business follows.

EBITDA, as adjusted, as a supplemental measure to review current period operating performance. Management uses EBITDA, as adjusted, as a supplemental measure to evaluate the current period operating performance of our business. We believe that EBITDA, as adjusted, when viewed with our GAAP results and the accompanying reconciliations and other financial and non-financial measures, provides a more useful additional perspective on, and a more complete understanding of, our performance than our GAAP results alone.

- Management uses EBITDA, as adjusted, to evaluate current operating performance and management decisions made during the reporting period, excluding certain expenses that are driven less by current period operating performance and management decisions than by our capital structure and asset base. These excluded expenses, which are primarily financial costs, include depreciation, interest, taxes and foreign currency exchange costs and more reflect prior period transactions and decisions. The operational factors highlighted in the evaluation using EBITDA, as adjusted, include pricing, marketing, utilization rates, maintenance and repair costs and staffing. EBITDA, as adjusted, presents an assessment of the performance and changes in the profitability driven by these operational factors irrespective of changes in the other factors noted, namely interest, taxes and foreign currency exchange costs. See below for further discussion of each of the items excluded from our calculation of EBITDA, as adjusted.
- EBITDA, as adjusted is not the only measure used by management to evaluate performance, but rather a supplemental one used in conjunction with other measures. Management uses several measures to evaluate performance, including both financial and non-financial measures, as well as GAAP and non-GAAP measures, including utilization rates, maintenance and growth capital expenditures, gross margin and return on invested capital.
- Management uses EBITDA, as adjusted, as well as certain other measures, as an intermediate performance measure, similar to the manner in which management uses gross profit, not as an ultimate performance measure, such as net income. Management does not view or use EBITDA, as adjusted, or any other intermediate measure or item in the Company's financial statements, including revenue, gross profit, gross margin or net cash provided by operating activities, as a measure of the Company's full results of operations or as a substitute for net income. Rather, analyzing an intermediate measure such as EBITDA, as adjusted, allows management to evaluate better the reasons underlying net income results. We urge users of our reports and financial statements to read such reports and financial statements in their entirety and not to use any one measure in isolation to evaluate our results or an investment in the Company.

EBITDA, as adjusted, as a comparability measure. Management uses EBITDA, as adjusted, to compare the Company's performance with that of our competitors. Although our competitors may calculate EBITDA differently, the measure will usually present operating performance on a basis that is

meaningful for comparative purposes. We urge the readers of our reports and financial statements, including our disclosure of EBITDA, as adjusted, to review carefully the reconciliation of the non-GAAP measure to net income or loss set forth in the table below.

- Despite definitional differences, management believes that EBITDA, as adjusted, is a meaningful measure to evaluate and compare the performance of one company against another because of the impact of management estimates on the items that are excluded from EBITDA, as adjusted. For example, depreciation expense is dependent upon, among other things, the estimated depreciable lives of a company's assets, which may vary from company to company depending on management's maintenance practices and operating philosophies, as we have noted through our prior acquisition activity. EBITDA, as adjusted, provides a measure to review operating performance independent of this management estimate.
- Management believes that EBITDA, as adjusted, is a meaningful measure to evaluate performance because the amount of depreciation expense in a company's financial statements may not accurately reflect the costs required to maintain and replenish a company's operational usage of its assets. Rather, depreciation expense reflects the systematic allocation of the historical fixed asset values over the estimated useful lives of those assets. For example, for the year ended March 31, 2004, the Company recorded depreciation and amortization expense of \$85.7 million, substantially all of which was depreciation expense, and had capital expenditures of \$27.9 million for compressor overhauls, our primary maintenance capital expenditure. By excluding depreciation and certain related or consequential costs, including amortization and taxes, EBITDA, as adjusted, provides a measure with which to evaluate the performance independent of, and in a manner that allows one to assess, whether depreciation accurately captures the costs to maintain and replenish the Company's operational usage of its assets.
- We have observed that both equity and debt analysts utilize EBITDA to evaluate the on-going performance of and valuation metrics for a company both over time and relative to its peers. We have observed that several of the analysts who review our company utilize EBITDA as one of the primary valuation metrics. By providing EBITDA, as adjusted, we believe we are providing information and calculations to aid these analysts in more accurately understanding the Company's performance for the benefit of our investors.

EBITDA, as adjusted, as a performance measure for period to period comparisons. Management uses EBITDA, as adjusted, as a measure of the performance of our business over time and as a tool in identifying key trends.

- EBITDA, as adjusted, by excluding items that are infrequent or uncommon in nature, assists management in identifying and understanding changes in performance from period to period that may not be apparent from solely viewing GAAP measures.
- By excluding infrequent or uncommon items, management believes EBITDA, as adjusted, enhances the transparency of the disclosure regarding our performance. As such, the measure allows management to be more accountable to investors' expectations by providing the market with additional information with which to assess our performance and make investment decisions.

EBITDA, as adjusted, as a valuation measure. Just as investors monitor and review a variety of financial and performance indicators, such as the market stock price to earnings ratio and the enterprise value to EBITDA ratio, management monitors these ratios to better understand the value of the Company and how to increase that value for our investors. For example, management has routinely utilized an EBITDA measure as a method to value companies when considering potential acquisition targets. This measure is utilized for the reasons discussed above; it allows for an evaluation of the target independent of its historical capital structure, depreciation estimates, tax position, and incurrence of infrequent or more uncommon items. Moreover, management believes investors that desire to

evaluate the Company as a potential target will also utilize the Company's EBITDA, as adjusted, as part of their evaluation.

The following table reconciles our EBITDA, as adjusted, to net income or (loss):

	Year Ended March 31,				
	2004	2003	2002	2001	2000
	(In thousands)				
EBITDA, as adjusted	\$223,848	\$201,150	\$207,315	\$ 88,787	\$ 55,561
Interest expense, net	(73,475)	(36,421)	(23,017)	(23,220)	(34,327)
Income taxes	(17,741)	(20,975)	(30,931)	(3,645)	1,994
Depreciation and amortization	(85,650)	(63,706)	(48,600)	(33,491)	(26,006)
Operating lease expense	—	(46,071)	(55,401)	(14,443)	—
Foreign currency gain (loss)	529	(459)	42	(177)	(4)
Facility consolidation costs	(1,821)	—	—	—	—
Management fees	—	—	—	—	(3,200)
Debt extinguishment costs	(14,903)	—	—	—	—
Non-recurring charges	—	—	—	(8,699)	—
Debt restructuring charges	—	—	—	(9,503)	—
Net income (loss)	<u>\$ 30,787</u>	<u>\$ 33,518</u>	<u>\$ 49,408</u>	<u>\$ (4,391)</u>	<u>\$ (5,982)</u>

Below are the items excluded from net income in the calculation of EBITDA, as adjusted, and the reasons for the exclusion:

- Interest expense is excluded from the calculation of EBITDA, as adjusted. Although interest expense is a material expense for the Company and it reflects an important component of our overall performance, as it reflects costs incurred to finance our operations, interest expense also reflects the performance of our financial arrangements in ways that are unrelated to the shorter-term performance of our operations. For example, the amount of interest expense incurred in any period reflects, among other things, market availability of funds at separate and historical points in time, the overall historical cost of debt and the results of how management, at a past point in time, decided to capitalize the business through the issuance of debt or equity. EBITDA, as adjusted, removes the effect of the performance of these past historical financial transactions, whether beneficial or detrimental to the Company's GAAP results, both in the current period and from period-to-period, so that the performance of the core operations can be more transparently evaluated. For example, despite how management decided to capitalize the Company either through debt or equity in the past, the measure of EBITDA, as adjusted, would not be impacted and would continue to reflect a consistent measure of the operational performance of the business.
- Income tax expense is excluded from the calculation of EBITDA, as adjusted. Management does not consider tax expense, which is materially impacted by other items excluded from the measure (such as interest expense and depreciation and amortization expense) as well as numerous tax regulations and the Company's tax planning, to be a part of the core operations and are not considered directly within the control of operational management and is therefore excluded from the measure.
- Depreciation and amortization is excluded from the calculation of EBITDA, as adjusted. Although, we are a capital-intensive business and depreciation expense is a material expense for the Company, this expense may not accurately reflect the costs required to maintain and replenish the Company's operational usage of its assets and therefore may not portray the costs from current operational transaction activity. Rather, depreciation expense reflects the systematic allocation of the historical fixed asset values over the estimated useful lives of those assets.

- Operating lease expense is related to the operating lease facilities that, until December 31, 2002, were not included in the Company's consolidated balance sheet and substantively reflected the cost of debt (interest expense) related to these financing arrangements. We excluded the lease expense from EBITDA, as adjusted, as it represents the equivalent of interest expense. It would potentially be misleading to exclude interest expense from EBITDA, as adjusted, but include leasing expense as they both reflect a financial arrangement, not an operational one.
- Foreign currency gains and losses are primarily attributable to foreign currency exchange rate fluctuations relating to our international operations and are impacted by foreign currency risk mitigation strategies the business may or may not undertake. Although these gains or losses have not been significant, they are not viewed by management as part of the core operations and are not considered directly within the control of operational management. Accordingly, these gains or losses are excluded from the measure for these reasons.
- Facility consolidation costs relate to the transfer of the Tulsa, Oklahoma fabrication activity to the Houston fabrication facility. These costs were primarily for severance, personnel and relocation costs. We do not consider these costs to be part of our core operations and the consolidation was disclosed in the footnotes to the financial statements related to the period in which they were incurred. We do not expect to incur similar costs within the two-year period ending September 30, 2005.
- Management fees of approximately \$3 million were incurred in fiscal 2000 pursuant to an agreement with Castle Harlan, Inc. in exchange for management services. In connection with our initial public offering in the quarter ended June 30, 2000, we terminated this agreement. Due to the nature of these expenses and services, the Company does not consider them as part of our core operations and therefore were excluded from EBITDA, as adjusted. These costs were disclosed in the footnotes to the financial statements related to the period in which they were incurred. The Company does not currently have any obligations to pay similar management fees and does not expect to have any similar exclusion to EBITDA, as adjusted, in future periods.
- Debt extinguishment costs relate primarily to the early extinguishment of Universal's outstanding \$229.8 million 9 $\frac{7}{8}$ % senior discount notes due 2008. The net proceeds from the offering of new 7 $\frac{1}{4}$ % senior notes due 2010 and available funds were used to pay for the extinguishment of the 9 $\frac{7}{8}$ % senior discount notes due 2008.
- Non-recurring charges were costs incurred in fiscal year 2001 primarily attributable to an early termination of the management agreement with Castle Harlan, Inc., discussed above, in connection with our initial public offering in the quarter ended June 30, 2000. Due to the nature of these expenses and services, the Company does not consider them as part of our core operations and therefore these costs are excluded from EBITDA, as adjusted. These costs were disclosed in the footnotes to the financial statements related to the period in which they were incurred. The Company does not currently have any obligations to pay similar non-recurring charges and does not expect to have any similar exclusion to EBITDA, as adjusted, in future periods.
- Debt restructuring charges were incurred in fiscal year 2001 in relation to debt restructuring that occurred concurrently with the Company's initial public offering of its common stock and with debt restructuring that occurred concurrently with the Company's acquisition of Weatherford Global Compression Services and related entities. The company does not consider these costs to be a part of our core operations and therefore these costs were excluded from the measure. Further, these costs were disclosed in the footnotes to the financial statements related to the period in which they were incurred. The Company does not currently anticipate incurring similar charges and does not expect to have any similar exclusion to EBITDA, as adjusted, in future periods.

We believe disclosure of this non-GAAP measure provides useful information to investors because, when viewed with our GAAP results and accompanying reconciliations, it provides a more complete understanding of our performance than GAAP results alone. This is the case because this non-GAAP financial measure excludes from earnings financial and other items that have less bearing on operating performance. When using this measure to compare to other companies, which we believe can be a useful tool to evaluate the Company, please note that an EBITDA measure may be calculated differently between companies, as it is a non-GAAP measure. We cannot ensure that EBITDA, as adjusted, is directly comparable to other companies' similarly titled measures. We urge the readers of financial statements to review the reconciliation of the non-GAAP measure to the most comparable GAAP measure to understand any differences that may exist between companies. Nonetheless, we have shown EBITDA, as adjusted, its definition and its calculation in order to disclose how management uses it, to present the exclusions made and the limitations of it as a measure.

EBITDA, as adjusted, has certain material limitations associated with its use as compared to net income. These limitations are primarily due to the exclusion of certain amounts that are material to the Company's consolidated results of operations, as follows:

- EBITDA, as adjusted, does not include interest expense or operating lease expense. Because we have borrowed money in order to finance our operations, interest expense and operating lease expense are necessary elements of our costs and our ability to generate revenue. Therefore any measure that excludes interest expense or operating lease expense has this material limitation.
- EBITDA, as adjusted, does not include income tax expense. Because the payment of taxes is a necessary element of our operations, any measure that excludes income tax expense has this material limitation.
- EBITDA, as adjusted, does not include depreciation and amortization expense. Because we use capital assets, depreciation is a necessary element of our costs and our ability to generate revenue. Therefore any measure that excludes depreciation and amortization expense has this material limitation.
- EBITDA, as adjusted, excludes the impact of foreign currency gains and losses. Because we operate in an international environment, foreign currency gains and losses have a real economic impact on our operations. Therefore any measure that excludes these effects has this material limitation.
- EBITDA, as adjusted, excludes other costs and expenses, such as management fees, non-recurring charges and extraordinary losses, as discussed above. These costs were excluded primarily because the Company does not consider these costs to be part of our core operations. Because the Company will incur costs from time to time that are not part of our core operations, any measure that excludes these costs has this material limitation.

Use of EBITDA, as adjusted, by itself and without consideration of other measures, is not an adequate measure of the Company's performance because this measure excludes certain material items, as noted above. Further, the measure has a limitation in that many users of financial statements believe that EBITDA is a measure of liquidity or of cash flows. We do not use EBITDA, as adjusted, in this way because it excludes interest payments and changes in working capital accounts and therefore we urge the readers of our financial statements to not use the measure in this way either. Management compensates for these limitations by using EBITDA, as adjusted, as a supplemental measure to other GAAP results to provide a more complete understanding of our performance without considering financial and other items that have less bearing on operating performance. The measure has a limitation, as it does not consider the amount of required reinvestment to maintain similar going forward results. Management mitigates this limitation by reviewing and disclosing the Company's capital and maintenance capital expenditures on a regular basis as yet another supplemental tool to evaluate the Company.

EBITDA, as adjusted, is not a measure of financial performance under GAAP and should not be considered an alternative to operating income or net income as an indicator of our operating performance or to net cash provided by operating activities as a measure of our liquidity.

ITEM 7. Management's Discussion and Analysis of Financial Condition and Results of Operations

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

UNIVERSAL COMPRESSION HOLDINGS, INC.

The following discussion and analysis of financial condition and results of operations should be read in conjunction with our financial statements, and the notes thereto, and the other financial information appearing elsewhere in this report. The following discussion includes forward-looking statements that involve certain risks and uncertainties. See "Part I. Disclosure Regarding Forward-Looking Statements" and "Risk Factors."

Overview

We provide a full range of natural gas compression services, including sales, operations, maintenance and fabrication services and products to the natural gas industry, both domestically and internationally. Through our core business, contract compression, and our fleet as of March 31, 2004 of approximately 7,100 compressor units comprising approximately 2.3 million horsepower, we provide natural gas compression to domestic and international customers. Through our equipment fabrication business we design, engineer and assemble natural gas and air compressors for sale to third parties and for use in our contract compression fleet. Through our aftermarket services business, we sell parts and components and provide maintenance and operations services to customers who own their compression equipment or utilize equipment from our competitors. These services and products are essential to the natural gas industry as gas must be compressed to be delivered from the wellhead to end-users. Our customers consist primarily of domestic and international oil and gas companies, international state-owned oil and gas companies, large and small independent producers and natural gas processors, gatherers and pipelines.

Generally, our overall business activity and revenue increase as the demand for compression services increases. In the United States, increases in compression demand are driven by growth in the production of natural gas and by declining reservoir pressure in maturing natural gas producing fields. In international markets, increases in compression demand are driven by growth in natural gas industry infrastructure, environmental initiatives encouraging the production and consumption of natural gas and the growth in the worldwide transportation of natural gas. The demand for compression services is also driven by general increases in the demand for energy fuel stocks, including, natural gas, which is generally driven by economic growth. In addition, the outsourcing of compression needs is driven by the expectation of our customers for improved operating efficiency, increased flexibility to replace compressors as field requirements change and reduced capital requirements.

The compression industry experienced significant merger and acquisition activity in the 1990s and through 2001. The outsourcing of compression services increased as a percentage of total industry activity in the 1990s and early 2000s as leading compression companies increased in overall size. A high level of compression industry capital expenditures and reduced demand due to lackluster economic activity resulted in reduced utilization beginning in late 2001 and continued into 2002. Industry utilization stabilized in the second half of calendar 2002 and increased during calendar 2003 as a result of reduced capital expenditures and increasing demand due to improving economic activity. During calendar 2003 the industry did not materially increase the supply of contract compression units in the United States due to an emphasis on the redeployment of idle units while growth in international markets continued.

Company Performance Trends

During fiscal 2001 and fiscal 2002, we increased our natural gas compression fleet, expanded fabrication capabilities for large horsepower units, added complementary aftermarket services and broadened our international operations. Capital expenditures in fiscal 2003 and fiscal 2004 were significantly lower than fiscal 2002 levels as we emphasized the redeployment of idle fleet units.

In fiscal 2004, we had improved natural gas compression fleet utilization and increased revenues in fabrication and aftermarket services due primarily to improved industry conditions and the implementation of our focused business strategy.

Fiscal 2004 Financial Highlights

Net income for the fiscal year ended March 31, 2004 declined compared to the prior year by \$2.7 million, or 8.1%, primarily as a result of debt extinguishment costs of \$14.9 million (\$9.4 million net of tax) related to our refinancing activity during the three months ended June 30, 2003. Significant items for the fiscal years are discussed as follows:

- *Higher Revenue.* Total revenue was higher by \$63.6 million, or 10.2%, for the fiscal year ended March 31, 2004 due primarily to higher levels of activity across all four of our business segments.
- *Debt Extinguishment Costs.* The debt extinguishment costs of \$14.9 million included in the fiscal year results primarily related to the May 2003 refinancing and consisted of the write-off of deferred financing costs of \$1.9 million, premium costs of \$12.0 million and \$0.5 million in transaction expenses.
- *Lower Combined Operating Lease and Interest Expense.* Compared to the prior fiscal year, on a combined basis, these items were lower by \$9.0 million, or 10.9%, primarily as a result of the Company's refinancing of \$175.0 million of long-term debt in May 2003, which both reduced the amount of the Company's long-term debt outstanding by approximately \$55.0 million and lowered the interest rate on that debt to 7¼% from 9½%.
- *Higher Depreciation and Amortization Expense.* Depreciation and amortization expense increased by \$21.9 million, or 34.4%, due primarily to depreciation of on-going capital expenditures and the inclusion of additional compression equipment on the Company's balance sheet as of December 31, 2002.

Fiscal 2004 Operating Highlights

The higher revenue for the fiscal year ended March 31, 2004, is attributable to increased industry activity and customer demand, which resulted in higher utilization in both the domestic and international contract compression fleets and increased sales in the fabrication and aftermarket services

businesses. The following table summarizes total available horsepower, average contracted horsepower, horsepower utilization percentages and fabrication backlog.

	For the Year Ended March 31,	
	2004	2003
	(Horsepower in thousands)	
Total Available Horsepower (at period end):		
Domestic contract compression	1,904	1,957
International contract compression	417	368
Total	2,321	2,325
Average Contracted Horsepower:		
Domestic contract compression	1,646	1,602
International contract compression	360	311
Total	2,006	1,913
Horsepower Utilization:		
Spot (at period end)	86.1%	83.6%
Average	85.8%	83.3%
	As of March 31,	
	2004	2003
	(In millions)	
Fabrication Backlog	\$88.2	\$55.7

Domestic average contracted horsepower increased by 2.7% for the fiscal year ended March 31, 2004 compared to the fiscal year ended March 31, 2003. International average contracted horsepower increased by 15.8% for the fiscal year ended March 31, 2004 compared to the prior fiscal year. These increases were primarily attributable to higher customer demand.

The decrease in domestic horsepower for the fiscal year ended March 31, 2004 from the prior year was primarily attributable to the sale of units to customers exercising purchase options on compression equipment. The increase in international horsepower was primarily attributable to horsepower that was added in Latin America.

The backlog of fabrication projects at June 8, 2004 was approximately \$88.9 million. A majority of the backlog is expected to be completed within a 180-day period.

Financial Results of Operations

Fiscal Year Ended March 31, 2004 Compared to Fiscal Year Ended March 31, 2003

The following table summarizes revenue, gross profit, gross margin, expenses and the respective percentages for each of our business segments:

	Year Ended March 31,	
	2004	2003
	(Dollars in thousands)	
Revenue:		
Domestic contract compression	\$280,951	\$265,465
% of revenue	40.8%	42.5%
International contract compression	\$ 82,589	\$ 66,505
% of revenue	12.0%	10.6%
Fabrication	\$183,685	\$162,678
% of revenue	26.7%	26.0%
Aftermarket services	\$141,561	\$130,570
% of revenue	20.5%	20.9%
Total revenue	\$688,786	\$625,218
Gross profit:		
Domestic contract compression	\$178,543	\$169,868
International contract compression	64,159	53,769
Fabrication	15,888	16,075
Aftermarket services	30,891	28,256
Total gross profit	\$289,481	\$267,968
Gross margin:		
Domestic contract compression	63.5%	64.0%
International contract compression	77.7%	80.8%
Fabrication	8.6%	9.9%
Aftermarket services	21.8%	21.6%
Total gross margin	42.0%	42.9%
Expenses:		
Depreciation and amortization	(85,650)	(63,706)
Selling, general and administrative	(67,516)	(67,944)
Operating lease expense	—	(46,071)
Interest expense, net	(73,475)	(36,421)
Debt extinguishment costs	(14,903)	—
Foreign currency gain/(loss)	529	(459)
Other income	1,883	1,126
Facility consolidation costs	(1,821)	—
Income taxes	(17,741)	(20,975)
Net income	\$ 30,787	\$ 33,518

Revenue. Total revenue increases were realized across all business segments for the fiscal year ended March 31, 2004 compared to the prior year. Domestic contract compression revenue increased due to higher average contract rates and improved utilization, both of which contributed equally to the increase. International contract compression revenue increased primarily as a result of additional compression business in Brazil and Argentina, which contributed increases of \$10.3 million and \$3.8 million, respectively. Fabrication revenue increased due to additional projects for customers in our United States and Canadian regions resulting in increases of \$24.5 million and \$11.0 million, respectively. These increases were partially offset by declines in the Asia Pacific region of \$7.9 million and the Latin American region of \$6.6 million. Revenue from fabrication fluctuates quarter to quarter due to the timing of receipt of orders placed by customers and due to the timing of recognition of revenue, which occurs at the time of shipment. Aftermarket services revenue was higher due primarily to increased customer demand in the United States (\$3.8 million), Canada (\$3.2 million) and the Asia Pacific region (\$2.8 million).

Gross Profit. The changes to gross profit (defined as total revenues less direct costs) for the fiscal year ended March 31, 2004 compared to the prior year were primarily attributable to revenue increases discussed above for domestic contract compression, international contract compression and aftermarket services. Fabrication gross profit decreased due to higher costs in the first fiscal quarter primarily as a result of cost overruns related to several highly customized fabrication projects for customers in the Asia Pacific region.

EBITDA, as adjusted. EBITDA, as adjusted, for the fiscal year ended March 31, 2004 was \$223.8 million. The increase in EBITDA of 11.3% from the prior year is primarily attributable to the revenue increases discussed above for domestic contract compression, international contract compression and aftermarket services. EBITDA, as adjusted is defined, discussed and reconciled to net income on page 19 of this report, within Item 6, Selected Financial Data.

Depreciation and Amortization. The increase in depreciation and amortization expense for the fiscal year ended March 31, 2004 compared to the prior year resulted from on-going capital additions which increased depreciation by approximately \$14.6 million and the inclusion of additional compression equipment on the balance sheet as of December 31, 2002 due to the consolidation of the operating lease facilities. Depreciation expense related to this equipment began January 1, 2003 and was partially offset by the change in estimated useful lives of the compressor fleet discussed below. The combined impact of the consolidation of the compressor equipment in the operating lease facilities and the extension of the useful lives of the compressor fleet at December 31, 2002 increased depreciation expense by approximately \$7.8 million.

In fiscal 2003, we evaluated the estimated useful lives used for book depreciation purposes for our compressor fleet based upon equipment type, key components and industry experience of the actual useful life in the field. The evaluation was finalized in the fourth quarter of fiscal year 2003. Based upon the findings of the evaluation, the estimated useful lives of the majority of the existing compressor units were extended to 25 years from 15 years. In addition, a portion of the units remained at the previous 15 years or less and a portion of the units were extended to 30 years. The change in useful lives was effective January 1, 2003.

Combined Operating Lease Expense and Interest Expense. Taking into account the effect of the consolidation of the lease facilities on December 31, 2002, the combined operating lease expense and interest expense, for the fiscal year ended March 31, 2004 decreased by \$9.0 million, or 10.9% compared to the prior year. This decrease is primarily attributable to May 2003 refinancing activities, which reduced outstanding long-term debt by approximately \$55.0 million and lowered the interest rate on \$175.0 million of indebtedness to 7¼% from 9½%. Interest expense decreased \$4.8 million as a result of the \$55.0 million reduction in debt and decreased \$4.0 million due to the lower interest rate on the \$175.0 million of indebtedness.

Operating Lease Expense. As a result of the consolidation of the lease facilities, there was no operating lease expense related to the operating lease facilities during the fiscal year ended March 31, 2004. The operating lease expense related to the operating lease facilities has been recognized as interest expense subsequent to the consolidation of the lease facilities on December 31, 2002.

Interest Expense, Net. Interest expense, net, increased for the fiscal year ended March 31, 2004 compared to the prior year primarily due to the consolidation of the operating lease facilities as of December 31, 2002 which resulted in the classification of operating lease expense subsequent to December 31, 2002 as interest expense.

Debt Extinguishment Costs. Debt extinguishment costs incurred during the fiscal year ended March 31, 2004 were primarily due to the early extinguishment of Universal's outstanding \$229.8 million 9½% senior discount notes due 2008 in May 2003. The net proceeds from the offering

by Universal of new 7¼% senior discount notes due 2010 and available funds were used to pay for the extinguishment of the 9⅞% senior discount notes due 2008. As a result of the early extinguishment of debt, a charge of \$14.4 million was recognized resulting from the redemption and tender premiums of \$12.0 million, write-off of unamortized debt issuance costs of \$1.9 million and \$0.5 million of other costs. Additional debt extinguishment costs of \$0.5 million resulted from the buyback of \$5.0 million of our 8⅞% Senior Notes during the three months ended March 31, 2004.

Other Income, Net. Other income, net of other expenses, for both the fiscal year ended March 31, 2004 and the prior year, was primarily comprised of gains from the sale of domestic contract compression equipment, primarily due to customers exercising purchase options.

Facility Consolidation Costs. Facility consolidation costs related to the transfer of the Tulsa, Oklahoma fabrication operations to the Houston fabrication facility were \$1.8 million during the year ended March 31, 2004. These costs were primarily for severance, personnel costs and relocation costs. The Company does not expect to incur additional facility consolidation costs during the two-year period ending September 30, 2005.

Fiscal Year Ended March 31, 2003 Compared to Fiscal Year Ended March 31, 2002

The following table summarizes revenue, gross profit, gross margin, expenses and the respective percentages for each of our business segments:

	<u>Year Ended March 31,</u>	
	<u>2003</u>	<u>2002</u>
	<u>(Dollars in thousands)</u>	
Revenue:		
Domestic contract compression	\$265,465	\$267,550
% of revenue	42.5%	39.3%
International contract compression	\$ 66,505	\$ 60,185
% of revenue	10.6%	8.9%
Fabrication	\$162,678	\$211,265
% of revenue	26.0%	31.1%
Aftermarket services	\$130,570	\$140,989
% of revenue	20.9%	20.7%
Total revenue	\$625,218	\$679,989
Gross profit:		
Domestic contract compression	\$169,868	\$169,892
International contract compression	53,769	43,411
Fabrication	16,075	24,347
Aftermarket services	28,256	30,696
Total gross profit	\$267,968	\$268,346
Gross margin:		
Domestic contract compression	64.0%	63.5%
International contract compression	80.8%	72.1%
Fabrication	9.9%	11.5%
Aftermarket services	21.6%	21.8%
Total gross margin	42.9%	39.5%
Expenses:		
Depreciation and amortization	(63,706)	(48,600)
Selling, general and administrative	(67,944)	(60,890)
Operating lease expense	(46,071)	(55,401)
Interest expense, net	(36,421)	(23,017)
Foreign currency gain/(loss)	(459)	42
Other income/(loss), net	1,126	(141)
Income taxes	(20,975)	(30,931)
Net income	\$ 33,518	\$ 49,408

Revenue. Total revenue for the fiscal year ended March 31, 2003 decreased \$54.8 million, or 8.1%, to \$625.2 million, compared to \$680.0 million for the fiscal year ended March 31, 2002 largely as a result of declines in fabrication and aftermarket services. Domestic contract compression revenue decreased by \$2.1 million, or 1%, to \$265.5 million during the fiscal year ended March 31, 2003 from \$267.6 million during the fiscal year ended March 31, 2002. International contract compression revenue increased by \$6.3 million, or 10.5%, to \$66.5 million during the fiscal year ended March 31, 2003 from \$60.2 million during the fiscal year ended March 31, 2002. The decrease in domestic contract compression revenue was a result of lower horsepower utilization in a period of reduced energy industry activity that resulted in a reduced demand for contract compression services. The increase in international contract compression revenue resulted from new contract settlements negotiated with our Argentina customers in the first quarter of fiscal year 2003 and expansion of our business in the Latin America and Asia Pacific regions.

Domestic average contracted horsepower for the fiscal year ended March 31, 2003 decreased slightly to approximately 1,602,000 horsepower from approximately 1,603,000 horsepower for the fiscal year ended March 31, 2002 primarily due to the general decline in energy industry activity in the United States. International average contracted horsepower for the fiscal year ended March 31, 2003 increased by 2.6% to approximately 311,000 horsepower from approximately 303,000 horsepower for the fiscal year ended March 31, 2002, primarily through expansion of the international contract compression fleet. The combined average horsepower utilization rate for the fiscal year ended March 31, 2003 was approximately 83.3%, down from 88.8% in the fiscal year ended March 31, 2002. As of March 31, 2003, Universal had approximately 2.3 million available horsepower with an average horsepower utilization rate for the quarter then ended of 83.5% and for the same period one year earlier of approximately 86.8%.

Fabrication revenue decreased to \$162.7 million from \$211.3 million, a decrease of 23% due to lower demand for customer-owned compressors in a period of reduced energy industry activity. Backlog of fabrication projects at the fiscal year ended March 31, 2003 was approximately \$55.7 million, compared with a backlog of \$80.0 million at March 31, 2002. From December 31, 2002 to March 31, 2003, backlog decreased \$0.6 million. The backlog as of May 12, 2003 was approximately \$75 million.

Aftermarket services revenue decreased to \$130.6 million during the fiscal year ended March 31, 2003 from \$141.0 million during the fiscal year ended March 31, 2002, a decrease of 7.4%. The decrease resulted from reduced repair and maintenance activity from Universal's North American customer base in a period of reduced energy industry activity.

Gross Profit. Gross profit for the fiscal year ended March 31, 2003 decreased \$0.4 million, or 0.1%, to \$268.0 million from gross profit of \$268.3 million for the fiscal year ended March 31, 2002 reflecting declines in fabrication and aftermarket services that were partially offset by an increase in international contract compression. Fabrication gross profit for the fiscal year ended March 31, 2003 decreased \$8.3 million, or 34.0%, to \$16.1 million compared to a gross profit of \$24.3 million for the fiscal year ended March 31, 2002. Fabrication gross profit decreased primarily due to lower demand during the fiscal year. Aftermarket services gross profit for the fiscal year ended March 31, 2003 decreased \$2.4 million or 7.9%, to \$28.3 million compared to a gross profit of \$30.7 million for the fiscal year ended March 31, 2002. Aftermarket services gross profit decreased primarily due to the overall slowdown in energy industry activity.

Selling, General and Administrative Expenses. Selling, general and administrative expenses increased by \$7.1 million to \$67.9 million for the fiscal year ended March 31, 2003, compared to \$60.9 million for the fiscal year ended March 31, 2002. Selling, general and administrative expenses represented 10.9% of revenue for the fiscal year ended March 31, 2003 compared to 9.0% of revenue for the fiscal year ended March 31, 2002. The increase was primarily due to a greater presence in

international markets, which carries higher administration costs and severance costs related to staff reductions.

EBITDA as adjusted. EBITDA, as adjusted, for the fiscal year ended March 31, 2003 decreased 3.0% to \$201.2 million from \$207.3 million for the fiscal year ended March 31, 2002, primarily due to increases in the selling, general and administrative costs. EBITDA, as adjusted, is defined, discussed and reconciled to net income on page 19 of this report, within Item 6, Selected Financial Data.

Depreciation and Amortization. Depreciation and amortization increased by \$15.1 million to \$63.7 million during the fiscal year ended March 31, 2003, compared to \$48.6 million during the fiscal year ended March 31, 2002. Depreciation expense increased due to a full twelve months of depreciation of fiscal 2002 capital additions and capitalized overhauls. In addition, depreciation expense increased due to the three months of depreciation of gas compressor units that were not previously recorded on Universal's balance sheet until December 31, 2002, when the lessors under the operating lease facilities became fully consolidated entities. Depreciation expense related to these assets began January 1, 2003 and increased depreciation expense for the fiscal year ended March 31, 2003 by approximately \$5.6 million.

In fiscal 2003, Universal evaluated the estimated useful lives used for book depreciation purposes for its compressor fleet based upon equipment type, key components and industry experience of the actual useful life in the field. The evaluation was finalized in the fourth quarter of fiscal year 2003. Based upon the findings of the evaluation, the estimated useful lives of the majority of the existing compressor units were extended to 25 years from 15 years. In addition, a portion of the units remained at the previous 15 years or less and a portion of the units were extended to 30 years. The change in useful lives was effective January 1, 2003. The impact from extending the estimated useful lives of the equipment that was recorded on Universal's balance sheet on December 31, 2002 (excluding the gas compression equipment related to the operating lease facilities) reduced depreciation expense by approximately \$3.0 million for the year ended March 31, 2003.

The combined impact as a result of the consolidation of the compressor equipment in the operating lease facilities and the extension of the estimated useful lives was an increase to depreciation expense of approximately \$2.6 million and a decrease to net income of \$1.6 million for the year ended March 31, 2003.

Operating Lease Expense. Operating lease expense decreased to \$46.1 million during the fiscal year ended March 31, 2003 compared to \$55.4 million during the fiscal year ended March 31, 2002. Operating lease expense related to the operating lease facilities has been recognized as interest expense subsequent to the consolidation of the lease facilities on December 31, 2002. As a result, Universal recognized no operating lease expense for the quarter ended March 31, 2003.

Interest Expense, Net. Interest expense, net, increased \$13.4 million to \$36.4 million for the fiscal year ended March 31, 2003 from \$23.0 million for the fiscal year ended March 31, 2002 primarily due to the consolidation of the operating lease facilities as of December 31, 2002 which resulted in the classification of operating lease expense subsequent to December 31, 2002 as interest expense.

Net Income. Net income decreased \$15.9 million to \$33.5 million for the fiscal year ended March 31, 2003 compared to a net income of \$49.4 million for the fiscal year ended March 31, 2002 for the reasons noted above.

Effects of Inflation

In recent years, inflation has been modest and has not had a material impact upon the results of our operations.

Liquidity and Capital Resources

Our primary uses of cash are operating expenditures, capital expenditures and long-term debt repayments.

Operations. Net cash provided by operating activities exceeded net cash used in investing and financing activities by \$49.5 million and \$65.5 million for the fiscal years ended March 31, 2004 and 2003, respectively. Based on current market conditions, we expect that net cash provided by operating activities will continue to be sufficient to finance our operating expenditures, capital expenditures and debt repayments through the 2005 fiscal year. Working capital, net of cash, was \$53.4 million and \$86.7 million at March 31, 2004 and March 31, 2003, respectively.

Capital expenditures. Capital expenditures for the fiscal year ended March 31, 2004 were \$86.6 million consisting of \$47.6 million for fleet additions, \$27.9 million for compressor overhauls, \$4.9 million for service trucks and \$6.2 million for machinery, equipment, information technology equipment and other items. We expect capital expenditures to be approximately \$90 to \$110 million for the fiscal year ending March 31, 2005, including approximately \$30 million for compression fleet maintenance capital. Historically, we have financed capital expenditures with net cash provided by operations and financing activities.

If we were to make significant additional acquisitions for cash, we might need to obtain additional debt or equity financing.

Long-term debt. As of March 31, 2004, we had approximately \$881.3 million in outstanding debt obligations consisting primarily of \$527.2 million outstanding under the seven-year term senior secured notes operating lease facility, consisting of senior notes due 2008 and term loan due 2008 (together, the "BRL lease facility"), \$175.7 million outstanding of 7¼% senior notes due 2010, and \$175.0 million outstanding under the asset-backed securitization lease facility (the "ABS lease facility"). The maturities of this debt are shown below. We expect to pay these principal payments through cash generated by operations and debt refinancing activity.

	(In thousands)
2005	\$ 12,205
2006	16,214
2007	16,237
2008	543,442
2009	16,138
Thereafter	<u>277,045</u>
Total debt	<u>\$881,281</u>

Availability. As of March 31, 2004, after giving effect to \$9.1 million of outstanding letters of credit under our financing documents, we had an aggregate unused credit availability of approximately \$140.9 million from our revolving credit facility and our ABS lease facility.

Refinancing activity. In May 2003, Universal commenced a tender offer to purchase the outstanding \$229.8 million aggregate principal amount of its 9½% senior discount notes due 2008 at a price equal to 104.938% of the principal amount, plus a premium of 0.412%, for notes tendered prior to the early expiration date for the tender offer. Of these notes, \$169.2 million were tendered on or before the early tender date, and Universal purchased those notes on May 27, 2003. On that date, Universal called for redemption of the remaining \$60.6 million of its 9½% senior discount notes due 2008 at 104.938% of the principal amount in accordance with the terms of the indenture relating to the notes. This redemption price was 0.412% less than the total consideration offered pursuant to the

tender offer for notes tendered on or before the early tender date. During June 2003, the remaining \$60.6 million of this debt was redeemed or repurchased.

Also in May 2003, Universal issued \$175.0 million of its 7¼% senior notes due 2010 in a private placement. The net proceeds from the sale, together with other available funds, were used to purchase the outstanding 9⅞% senior discount notes due 2008 as discussed above. Universal exchanged the private notes for publicly-traded notes during the second quarter of fiscal 2004. During the three months ended March 31, 2004 we repurchased \$5.0 million of our 8⅞% Senior Notes due February 2008. We repurchased an additional \$5.0 million of our 8⅞% Senior Notes in April 2004 and will continue to look at opportunistic repurchases subject to market conditions.

Contractual Obligations. The following table summarizes our cash contractual obligations as of March 31, 2004 (in thousands):

	Payments Due by Period				
	Total	Less Than 1 Year	1-3 Years	4-5 Years	After 5 Years
Total debt	\$881,281	\$12,205	\$32,451	\$559,580	\$277,045
Capital leases	3,381	2,343	764	274	—
Total contractual cash obligations	<u>\$884,662</u>	<u>\$14,548</u>	<u>\$33,215</u>	<u>\$559,854</u>	<u>\$277,045</u>

Critical Accounting Policies and Estimates

Our discussion and analysis of our financial condition and results of operation is based upon our consolidated financial statements. We prepare these financial statements in conformity with GAAP. As such, we are required to make certain estimates, judgments and assumptions that affect the reported amounts of assets and liabilities at the date of the financial statements and the reported amounts of revenue and expenses during the periods presented. We base our estimates on historical experience, available information and various other assumptions we believe to be reasonable under the circumstances. On an on-going basis, we evaluate our estimates; however, actual results may differ from these estimates under different assumptions or conditions. The accounting policies we believe require management's most difficult, subjective or complex judgments and are the most critical to our reporting of results of operations and financial position are as follows:

Allowances and Reserves

Our customers are evaluated for credit worthiness prior to the extension of credit. We maintain an allowance for bad debts based on specific customer collection issues and historical experience. On an on-going basis, we conduct an evaluation of the financial strength of our customers based on payment history and make adjustments to the allowance as necessary. Since most of our customers are in the energy industry, their ability to pay balances due could be affected by dramatic changes in the price and demand for their products.

We record a reserve against our inventory balance for estimated obsolescence. This reserve is based on specific identification and historical experience.

Depreciation

Property, plant and equipment are carried at cost. Depreciation for financial reporting purposes is computed on the straight-line basis using estimated useful lives. For compression equipment, depreciation begins with the first compression service using a 20% salvage value. The estimated useful lives prior to January 1, 2003 for compression equipment was 15 years and for other properties and equipment from 2 to 25 years.

The Company evaluated the estimated useful life used for book depreciation purposes for its compressor fleet based upon equipment type, key components and industry experience of the actual useful life in the field. The evaluation was finalized in the fourth quarter of fiscal year 2003. Based upon the findings of the evaluation, the estimated useful lives of the majority of the existing compressor units were extended to 25 years from 15 years. In addition, a portion of the units remained at 15 years or less and a portion of the units were extended to 30 years.

Business Combinations and Goodwill

Goodwill and intangible assets acquired in connection with business combinations represent the excess of consideration over the fair value of tangible net assets acquired. Certain assumptions and estimates are employed in determining the fair value of assets acquired and liabilities assumed, as well as in determining the allocation of goodwill to the appropriate reporting unit.

In accordance with Statement of Financial Accounting Standard (“SFAS”) No. 142, “Goodwill and Other Intangible Assets,” we no longer amortize goodwill. We perform an impairment test for goodwill assets annually, or earlier if indicators of potential impairment exist. Our goodwill impairment test involves a comparison of the fair value of each of our reporting units with their carrying value. The fair value is determined using discounted cash flows and other market-related valuation models. Certain estimates and judgments are required in the application of the fair value models. During the fourth quarter of fiscal year 2004, we performed an impairment analysis in accordance with SFAS No. 142 and determined that no impairment had occurred; however, if for any reason the fair value of our goodwill or that of any of our reporting units declines below the carrying value in the future, we may incur charges for the impairment.

Long-Lived Assets

Long-lived assets, which include property, plant and equipment, definite-lived intangibles and other assets comprise a significant amount of our total assets. In accordance with SFAS No. 144, Accounting for the Impairment or Disposal of Long-Lived Assets, long-lived assets to be held and used by us are reviewed to determine whether any events or changes in circumstances indicate the carrying amount of the asset may not be recoverable. For long-lived assets to be held and used, we base our evaluation on impairment indicators such as the nature of the assets, the future economic benefit of the assets, any historical or future profitability measurements and other external market conditions or factors that may be present. If such impairment indicators are present or other factors exist that indicate the carrying amount of the asset may not be recoverable, we determine whether an impairment has occurred through the use of undiscounted cash flows analysis of the asset at the lowest level for which identifiable cash flows exist. If an impairment has occurred, we recognize a loss for the difference between the carrying amount and the estimated fair value of the asset. The fair value of the asset is measured using quoted market prices or, in the absence of quoted market prices, is based on an estimate of discounted cash flows.

Self-Insurance

We are self-insured up to certain levels for general liability, vehicle liability, group medical and for workers’ compensation claims for certain of our employees. We record self-insurance accruals based on claims filed and an estimate for significant claims incurred but not reported. We regularly review estimates of reported and unreported claims and provide for losses through insurance reserves. Although we believe adequate reserves have been provided for expected liabilities arising from our self-insured obligations, it is reasonably possible our estimates of these liabilities will change over the near term as circumstances develop.

Income Taxes

We account for income taxes using an asset and liability approach that requires the recognition of deferred tax assets and liabilities for the expected future tax consequences of events that have been recognized in our financial statements or tax returns. In estimating future tax consequences, all expected future events are considered other than enactments of changes in the tax law or rates.

We provide contract compression services to a global market. As such, we are subject to taxation not only in the United States but also in numerous foreign jurisdictions. Having to consider these different jurisdictions complicates the estimate of future taxable income, which in turn determines the realizability of our deferred tax assets. Numerous judgments and assumptions are inherent in the determination of future taxable income, including assumptions on future operating conditions and asset utilization. The judgments and assumptions used to determine future taxable income are consistent with those used for other financial statement purposes.

Additionally, we must consider any prudent and feasible tax planning strategies that would minimize the amount of deferred tax liabilities recognized or the amount of any valuation allowance recognized against deferred tax assets. The principal tax planning strategy available to us relates to the permanent reinvestment of the earnings of foreign subsidiaries. The assumptions related to the permanent reinvestment of the foreign earnings are analyzed and reviewed annually for changes in our international and domestic business outlook.

Recent Accounting Pronouncements

In January 2003, the FASB issued Interpretation No. 46 ("FIN 46"), "Consolidation of Variable Interest Entities." An entity is subject to the consolidation rules of FIN 46 and is referred to as a variable interest entity ("VIE") if the entity's equity investors lack the characteristics of a controlling financial interest or do not have sufficient equity at risk for the entity to finance its operations without additional financial support. In December 2003, the FASB issued modifications to FIN 46 ("FIN 46R"), resulting in multiple effective dates based on the nature as well as the creation date of a VIE. The adoption of the provision of FIN 46 and FIN 46R did not have a material impact on the consolidated statements of operations, cash flows or financial position.

In January 2003, the Emerging Issues Task Force (EITF) issued No. 00-21, "Accounting for Revenue Arrangements with Multiple Deliverables." This EITF establishes the criteria for recognizing revenue in arrangements when several items are bundled into one agreement. EITF 00-21 does not allow revenue recognition unless the fair value of the undelivered element(s) is available and the element has stand-alone value to the customer. EITF 00-21 also provides guidance on allocating the total contract revenue to the individual elements based upon the available fair value of each deliverable. The implementation of this pronouncement for revenue arrangements entered into after June 15, 2003 did not have a material impact on the Company's consolidated statements of operations, cash flows or financial position.

On April 30, 2003, the FASB issued SFAS No. 149, "Amendment of Statement 133 on Derivative Instruments and Hedging Activities." This statement amends and clarifies accounting for derivative instruments, including certain derivative instruments embedded in other contracts, and for hedging activities under SFAS No. 133. This statement is effective for contracts entered into or modified after June 20, 2003, for hedging relationships designated after June 30, 2003, and to certain preexisting contracts. Universal adopted SFAS No. 149 on a prospective basis at its effective date on July 1, 2003. SFAS No. 149 did not have a material impact on the Company's consolidated statements of operations, cash flows or financial position.

In May 2003, the FASB issued SFAS No. 150, "Accounting for Certain Financial Instruments with Characteristics of both Liabilities and Equity." This statement establishes standards for how an issuer

classifies and measures certain financial instruments with characteristics of both liabilities and equity. This statement is effective for financial instruments entered into or modified after May 31, 2003, except for mandatorily redeemable financial instruments. Mandatorily redeemable financial instruments are subject to the provisions of this statement beginning on January 1, 2004. SFAS No. 150 did not have an impact on the Company's consolidated financial statements.

Seasonal Fluctuations

Our results of operations have not historically reflected any material seasonal tendencies.

RISK FACTORS

As described in “Part I. Disclosure Regarding Forward-Looking Statements,” this report contains forward-looking statements regarding us, our business and our industry. The risk factors described below, among others, could cause our actual results to differ materially from the expectations reflected in the forward-looking statements. If any of the following risks actually occur, our business, financial condition and operating results could be materially adversely affected. Additional risks not currently known to us or which we currently consider immaterial may also adversely affect us.

We depend on strong demand for natural gas and a prolonged, substantial reduction in this demand could adversely affect the demand for our services and products.

Gas contract compression operations are significantly dependent upon the demand for natural gas. Demand may be affected by, among other factors, natural gas prices, weather, demand for energy and availability of alternative energy sources. Any prolonged, substantial reduction in the demand for natural gas would, in all likelihood, depress the level of production, exploration and development activity and result in a decline in the demand for our contract compression services and products. Similarly, a decrease in capital spending by our customers could result in reduced demand for our fabrication and aftermarket services businesses. These events could materially adversely affect our business, results of operations and financial condition.

Our international operations subject us to risks that are difficult to predict.

For the year ended March 31, 2004, we derived approximately 28.4% of our revenue from international operations. We intend to continue to expand our business in Latin America, and Asia Pacific and, ultimately, other international markets. This may make it more difficult for us to manage our business. Reasons for this include, but are not limited to, the following:

- political and economic instability in foreign markets;
- foreign governments’ restrictive trade policies;
- inconsistent product regulation or sudden policy changes by foreign agencies or governments;
- the burden of complying with multiple and potentially conflicting laws;
- the imposition of duties, taxes or government royalties;
- foreign exchange rate risks;
- difficulty in collecting international accounts receivable;
- potentially longer payment cycles;
- increased costs in maintaining international manufacturing and marketing efforts;
- the introduction of non-tariff barriers and higher duty rates;
- difficulties in enforcement of contractual obligations;
- restrictions on repatriation of earnings or expropriation of property; and
- the geographic, time zone, language and cultural differences between personnel in different areas of the world.

Any of these factors could materially adversely affect our business, financial condition or results of operations.

We face significant competition that may cause us to lose market share and harm our financial performance.

The contract compression, fabrication, and aftermarket services businesses are highly competitive and there are low barriers to entry for individual projects. In addition, some of our competitors are large national and multinational companies that provide contract compression and fabrication services to third parties; some of these competitors have greater financial and other resources than we do. If our competitors substantially increase the resources they devote to the development and marketing of competitive products and services, we may not be able to compete effectively.

We are dependent on particular suppliers and are vulnerable to product shortages and price increases.

Some of the components used in our products are obtained from a single source or a limited group of suppliers. Our reliance on these suppliers involves several risks, including price increases, inferior component quality and a potential inability to obtain an adequate supply of required components in a timely manner. The partial or complete loss of certain of these sources could have a material adverse effect on our results of operations and could damage our customer relationships. Further, a significant increase in the price of one or more of these components could have a material adverse effect on our results of operations.

Natural gas operations entail inherent risks and we do not insure against all potential losses and could be seriously harmed by unexpected liabilities.

Natural gas service operations are subject to inherent risks such as equipment defects, malfunction and failures, and natural disasters that can result in uncontrollable flows of gas or well fluids, fires and explosions. These risks could expose us to substantial liability for personal injury, death, property damage, pollution and other environmental damages. Although we have obtained insurance against many of these risks, there can be no assurance that our insurance will be adequate to cover our liabilities. Further, insurance covering the risks we face or in the amounts we desire may not be available in the future or, if available, the premiums may not be commercially justifiable. If we were to incur substantial liability and such damages were not covered by insurance or were in excess of policy limits, or if we were to incur liability at a time when we are not able to obtain liability insurance, our business, results of operations and financial condition could be materially adversely affected.

The sale of stock by Weatherford, which currently owns approximately 44% of our common stock, may depress our stock price.

Weatherford has registered with the United States Securities and Exchange Commission, and may sell at any time, up to 7,000,000 of its shares of our common stock. In addition, the other 6,750,000 shares of our common stock owned by Weatherford are subject to registration rights and may be resold at any time. The sale of substantial amounts of our stock owned by Weatherford in the public market, or the belief that these sales may occur, could reduce the market price of our stock, making it more difficult for us to raise funds through future offerings of our common stock and to acquire businesses using our stock as consideration.

Weatherford's voting power may give it the ability to control the outcome of matters submitted to a vote of our stockholders.

Weatherford's 13,750,000 shares, or approximately 44%, of our outstanding common stock may give it the ability to control the outcome of matters submitted to a vote of our stockholders. If Weatherford sells all of the 7,000,000 shares it has registered with the United States Securities and Exchange Commission, it would nonetheless continue to own beneficially approximately 22% of the outstanding shares of our common stock as of such date. In addition to its voting power, Weatherford and its affiliates are entitled to designate three persons to serve on our board of directors for so long as they own at least 20% of our outstanding common stock. If Weatherford's ownership falls below 20%, Weatherford may designate only two directors. If Weatherford's ownership falls below 10%, it will no longer have the right to designate directors to our board.

This significant stock ownership and board representation gives Weatherford the ability to exercise substantial influence over our ownership, policies, management and affairs and significant control over actions requiring approval of our stockholders. Weatherford's interests could conflict with our other stockholders.

We are a holding company and rely on our subsidiaries for operating income.

We are a holding company and, as such, derive all of our operating income from our operating subsidiary, Universal Compression, Inc., and its subsidiaries. We do not have any significant assets other than the stock of our operating subsidiary. Consequently, we are dependent on the earnings and cash flow of our subsidiaries to meet our obligations. Our subsidiaries are separate legal entities that are not legally obligated to make funds available to us, and in some cases may be contractually restricted from doing so. We cannot assure you that our subsidiaries will be able to, or be permitted to, pay to us amounts necessary to meet our obligations.

We are highly leveraged, a significant portion of our cash flow must be used to service our obligations and we are vulnerable to interest rate increases.

We have now and will continue to have a significant amount of debt. As of March 31, 2004, we had approximately \$881.3 million in outstanding debt obligations consisting primarily of \$527.2 million outstanding under the seven-year term senior secured notes operating lease facility, consisting of senior notes due 2008 and term loan due 2008, the BRL lease facility, and \$175.7 million outstanding of 7¼% senior notes due 2010 and \$175.0 million outstanding under the the ABS lease facility. This amount excludes approximately \$9.1 million of letters of credit, as of March 31, 2004, issued under our \$125 million senior secured revolving credit facility.

As of March 31, 2004, approximately \$182.2 million of our outstanding debt bore interest at floating rates. Changes in economic conditions could result in higher interest rates, thereby increasing our interest expense and reducing our funds available to make payments of interest and principal on the notes and for capital investment, operations or other purposes. Our significant leverage increases our vulnerability to general adverse economic and industry conditions.

Our credit facilities and lease facilities impose restrictions on us that may affect our ability to successfully operate our business.

Our credit facilities and lease facilities include certain covenants that, among other things, restrict our ability to:

- borrow money;
- create liens, other than a lien securing the revolving credit facility, the BRL lease facility or the ABS lease facility;
- sell or transfer any of our material property;
- merge into or consolidate with any third party or sell or dispose of all or substantially all of our assets; and
- make capital expenditures.

We and our subsidiaries are also required by our credit facilities to maintain debt coverage ratios, interest coverage ratios and a specified tangible net worth. All of these covenants may restrict our ability to expand or to pursue our business strategies. Our ability to comply with these and other provisions of the indentures and the credit facilities may be affected by changes in our operating and financial performance, changes in business conditions or results of operation, adverse regulatory developments or other events beyond our control. The breach of any of these covenants could result in a default under our debt, which could cause those obligations to become due and payable. If any of our

indebtedness were to be accelerated, there can be no assurance that we would be able to repay or refinance it.

We are exposed to exchange rate fluctuations.

Our reporting currency is the U.S. dollar. Historically, our foreign operations, including assets and liabilities and revenues and expenses, have been denominated in various currencies other than the U.S. dollar, and we expect that our foreign operations will continue to be so denominated. As a result, the U.S. dollar value of our foreign operations has varied, and will continue to vary, with exchange rate fluctuations. In this respect, historically we have been primarily exposed to fluctuations in the exchange rate of the Argentine peso, Brazilian real, Thai baht, Mexican peso, Australian dollar and Canadian dollar against the U.S. dollar.

A decrease in the value of any of these currencies relative to the U.S. dollar could reduce our profits from foreign operations and the value of the net assets of our foreign operations when reported in U.S. dollars in our financial statements. This could have a material adverse effect on our business, financial condition or results of operations as reported in U.S. dollars.

In addition, fluctuations in currencies relative to currencies in which the earnings are generated may make it more difficult to perform period-to-period comparisons of our reported results of operations. For purposes of accounting, the assets and liabilities of our foreign operations, where the local currency is the functional currency, are translated using period-end exchange rates, and the revenues and expenses of our foreign operations are translated using average exchange rates during each period.

Although we attempt to match costs and revenues in local currencies, we anticipate that there may be instances in which costs and revenues will not be matched with respect to currency denomination. As a result, to the extent we continue our expansion on a global basis, we expect that increasing portions of our revenues, costs, assets and liabilities will be subject to fluctuations in foreign currency valuations. We may experience economic loss and a negative impact on earnings or net assets solely as a result of foreign currency exchange rate fluctuations. Further, the markets in which we operate could restrict the removal or conversion of the local or foreign currency, resulting in our inability to hedge against these risks.

We intend to continue to make substantial capital investments to implement our business strategy, which may reduce funds available for other operations.

We anticipate that we will continue to make substantial capital investments to expand and maintain our contract compression fleet. Capital expenditures for the fiscal year ended March 31, 2004 were \$86.6 million consisting of \$47.6 million for fleet additions, \$27.9 million for compressor overhauls, \$4.9 million for service trucks and \$6.2 million for machinery, equipment, information technology equipment and other items. We expect to spend between \$90 and \$110 million on capital expenditures during fiscal year 2005, approximately \$30 million of which would be used for compression fleet maintenance capital. Historically, we have paid for these investments through internally generated funds and external financings. These significant capital investments require cash that we could otherwise apply to other business needs. However, if we do not incur these expenditures while our competitors make substantial fleet investments, our market share may decline and our business may be adversely affected. In addition, if we are unable to generate sufficient cash internally or obtain alternative sources of capital to fund our proposed capital expenditures, it could materially adversely affect our results of operations, financial condition and growth.

Our ability to manage our business effectively will be weakened if we lose key personnel.

We depend on the continuing efforts of our executive officers and senior management. The departure of any of our key personnel could have a material adverse effect on our business, operating

results and financial condition. We do not maintain key man life insurance coverage with respect to our executive officers or key management personnel. We are not aware of the upcoming retirement of any of our executive officers or senior management personnel. In addition, we believe that our success depends on our ability to attract and retain additional qualified employees. If we fail to recruit other skilled personnel, we could be unable to compete effectively.

We are subject to substantial environmental regulation, and changes in these regulations could increase our costs or liabilities.

We are subject to stringent and complex foreign, federal, state and local laws and regulatory standards, including laws and regulations regarding the discharge of materials into the environment, emission controls and other environmental protection and occupational health and safety concerns. Environmental laws and regulations may, in certain circumstances, impose strict liability for environmental contamination, rendering us liable for remediation costs, natural resource damages and other damages as a result of our conduct that was lawful at the time it occurred or the conduct of, or conditions caused by, prior owners or operators or other third parties. In addition, where contamination may be present, it is not uncommon for neighboring land owners and other third parties to file claims for personal injury, property damage and recovery of response costs. Remediation costs and other damages arising as a result of environmental laws and regulations, and costs associated with new information, changes in existing environmental laws and regulations or the adoption of new environmental laws and regulations could be substantial and could have a material adverse effect on our business, financial condition or results of operations. Moreover, failure to comply with these environmental laws and regulations may result in the imposition of administrative, civil and criminal penalties.

We routinely deal with natural gas, oil and other petroleum products. As a result of our fabrication and aftermarket services operations, we generate, manage and dispose of or recycle hazardous wastes and substances such as solvents, thinner, waste paint, waste oil, washdown wastes and sandblast material. Although it is our policy to use generally accepted operating and disposal practices in accordance with applicable environmental laws and regulations, hydrocarbons or other hazardous substances or wastes may have been disposed or released on, under or from properties owned, leased or operated by us or on or under other locations where such substances or wastes have been taken for disposal. These properties may be subject to investigatory, remediation and monitoring requirements under foreign, federal, state and local environmental laws and regulations.

We believe that our operations are in substantial compliance with applicable environmental laws and regulations. Nevertheless, the modification or interpretation of existing environmental laws or regulations, the more vigorous enforcement of existing environmental laws or regulations, or the adoption of new environmental laws or regulations may also negatively impact oil and natural gas exploration and production companies, which in turn could have a material adverse effect on us and other similarly situated service companies.

Future terrorist attacks or responses thereto could adversely affect our company.

The impact that future events arising as a result of the terrorist attacks on the United States on September 11, 2001, or any terrorist attacks that may occur in the future, including military or police activities in the United States, Iraq or other foreign countries, future terrorist activities or threats of such activities, political unrest and instability, riots and protests, could have on the United States economy, the global economy, global financial markets and our business cannot currently be determined with any accuracy.

A third party could be prevented from acquiring control of us because of the anti-takeover provisions in our charter and bylaws.

There are provisions in our restated certificate of incorporation and bylaws that may make it more difficult for a third party to acquire control of us, even if a change in control would result in the purchase of your shares at a premium to the market price or would otherwise be beneficial to you. For example, our restated certificate of incorporation authorizes our board of directors to issue preferred stock without stockholder approval. If our board of directors elects to issue preferred stock, it could be more difficult for a third party to acquire us. In addition, provisions of our restated certificate of incorporation, such as a staggered board of directors and limitations on the removal of directors, no stockholder action by written consent and limitations on stockholder proposals at meetings of stockholders, could make it more difficult for a third party to acquire control of us. Delaware corporation law may also discourage takeover attempts that have not been approved by our board of directors.

**MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION
AND RESULTS OF OPERATIONS**
UNIVERSAL COMPRESSION, INC.

The following discussion and analysis of financial condition and results of operations should be read in conjunction with Universal's financial statements, and the notes thereto, and the other financial information appearing elsewhere in this report. The following discussion includes forward-looking statements that involve certain risks and uncertainties. See "Part I. Disclosure Regarding Forward-Looking Statements" and "Risk Factors."

Financial Results of Operations.

Fiscal Year Ended March 31, 2004 Compared to Fiscal Year Ended March 31, 2003

The following table summarizes revenue, gross profit, gross margin, expenses and the respective percentages for each of Universal's business segments:

	Year Ended March 31,	
	2004	2003
	(Dollars in thousands)	
Revenue:		
Domestic contract compression	\$280,951	\$265,465
% of revenue	40.8%	42.5%
International contract compression	\$ 82,589	\$ 66,505
% of revenue	12.0%	10.6%
Fabrication	\$183,685	\$162,678
% of revenue	26.7%	26.0%
Aftermarket services	\$141,561	\$130,570
% of revenue	20.5%	20.9%
Total revenue	\$688,786	\$625,218
Gross profit:		
Domestic contract compression	\$178,543	\$169,868
International contract compression	64,159	53,769
Fabrication	15,888	16,075
Aftermarket services	30,891	28,256
Total gross profit	\$289,481	\$267,968
Gross margin:		
Domestic contract compression	63.5%	64.0%
International contract compression	77.7%	80.8%
Fabrication	8.6%	9.9%
Aftermarket services	21.8%	21.6%
Total gross margin	42.0%	42.9%
Expenses:		
Depreciation and amortization	(85,650)	(63,706)
Selling, general and administrative	(67,516)	(67,944)
Operating lease expense	—	(46,071)
Interest expense, net	(73,475)	(36,421)
Debt extinguishment costs	(14,903)	—
Foreign currency gain/(loss)	529	(459)
Other income, net	1,883	1,126
Facility consolidation costs	(1,821)	—
Income taxes	(17,741)	(20,975)
Net income	\$ 30,787	\$ 33,518

Revenue. Total revenue increases were realized across all business segments for the fiscal year ended March 31, 2004 compared to the prior year. Domestic contract compression revenue increased due to higher average contract rates and improved utilization, both of which contributed equally to the increase. International contract compression revenue increased primarily as a result of additional

compression business in Brazil and Argentina, which contributed increases of \$10.3 million and \$3.8 million, respectively. Fabrication revenue increased due to additional projects for customers in our United States and Canadian regions resulting in increases of \$24.5 million and \$11.0 million, respectively. These increases were partially offset by declines in the Asia Pacific region of \$7.9 million and the Latin American region of \$6.6 million. Revenue from fabrication fluctuates quarter to quarter due to the timing of receipt of orders placed by customers and due to the timing of recognition of revenue, which occurs at the time of shipment. Aftermarket services revenue was higher due primarily to increased customer demand in the United States (\$3.8 million), Canada (\$3.2 million) and the Asia Pacific region (\$2.8 million).

Gross Profit. The changes to gross profit (defined as total revenues less direct costs) for the fiscal year ended March 31, 2004 compared to the prior year were primarily attributable to revenue increases discussed above for the domestic contract compression, the international contract compression and the aftermarket services business segments. Fabrication gross profit decreased due to higher costs in the first fiscal quarter primarily as a result of cost overruns related to several highly customized fabrication projects for customers in the Asia Pacific region.

EBITDA, as adjusted. EBITDA, as adjusted, for the fiscal year ended March 31, 2004 was \$223.8 million. The increase in EBITDA of 11.3% from the prior year is primarily attributable to the revenue increases discussed above for domestic contract compression, international contract compression and aftermarket services. EBITDA, as adjusted is defined, discussed and reconciled to net income on page 19 of this report, within Item 6, Selected Financial Data.

Depreciation and Amortization. The increase in depreciation and amortization expense for the fiscal year ended March 31, 2004 compared to the prior year resulted from on-going capital additions which increased depreciation by approximately \$14.6 million and the inclusion of additional compression equipment on the balance sheet as of December 31, 2002 due to the consolidation of the operating lease facilities. Depreciation expense related this equipment began January 1, 2003 and was partially offset by the change in estimated useful lives of the compressor fleet discussed below. The combined impact of the consolidation of the compressor equipment in the operating lease facilities and the extension of the useful lives of the compressor fleet at December 31, 2002 increased depreciation expense by approximately \$7.8 million.

In fiscal 2003, Universal evaluated the estimated useful lives used for book depreciation purposes for its compressor fleet based upon equipment type, key components and industry experience of the actual useful life in the field. The evaluation was finalized in the fourth quarter of fiscal year 2003. Based upon the findings of the evaluation, the estimated useful lives of the majority of the existing compressor units were extended to 25 years from 15 years. In addition, a portion of the units remained at the previous 15 years or less and a portion of the units were extended to 30 years. The change in useful lives was effective January 1, 2003.

Combined Operating Lease Expense and Interest Expense. Taking into account the effect of the consolidation of the lease facilities on December 31, 2002, the combined operating lease expense and interest expense, for the fiscal year ended March 31, 2004 decreased by \$9.0 million, or 10.9% compared to the prior year. This decrease is primarily attributable to May 2003 refinancing activities, which reduced outstanding long-term debt by approximately \$55.0 million and lowered the interest rate on \$175.0 million of indebtedness to 7¼% from 9⅞%. Interest expense decreased \$4.8 million as a result of the \$55.0 million reduction in debt and decreased \$4.0 million due to the lower interest rate on the \$175.0 million of indebtedness.

Operating Lease Expense. As a result of the consolidation of the lease facilities, there was no operating lease expense related to the operating lease facilities during the fiscal year ended March 31,

2004. The operating lease expense related to the operating lease facilities has been recognized as interest expense subsequent to the consolidation of the lease facilities on December 31, 2002.

Interest Expense, Net. Interest expense, net, increased for the fiscal year ended March 31, 2004 compared to the prior year primarily due to the consolidation of the operating lease facilities as of December 31, 2002, which resulted in the classification of operating lease expense subsequent to December 31, 2002 as interest expense.

Debt Extinguishment Costs. Debt extinguishment costs incurred during the fiscal year ended March 31, 2004 were primarily due to the early extinguishment of Universal's outstanding \$229.8 million 9 $\frac{7}{8}$ % senior discount notes due 2008 in May 2003. The net proceeds from the offering by Universal of new 7 $\frac{1}{4}$ % senior discount notes due 2010 and available funds were used to pay for the extinguishment of the 9 $\frac{7}{8}$ % senior discount notes due 2008. As a result of the early extinguishment of debt, a charge of \$14.4 million was recognized resulting from the redemption and tender premiums of \$12.0 million, write-off of unamortized debt issuance costs of \$1.9 million and \$0.5 million of other costs. Additional debt extinguishment costs of \$0.5 million resulted from the buyback of \$5.0 million of our 8 $\frac{7}{8}$ % senior notes during the three months ended March 31, 2004.

Other Income, Net. Other income, net of other expenses, for both the fiscal year ended March 31, 2004 and the prior year, was primarily comprised of gains from the sale of domestic contract compression equipment due to customers exercising purchase options.

Facility Consolidation Costs. Facility consolidation costs related to the transfer of the Tulsa, Oklahoma fabrication operations to the Houston fabrication facility were \$1.8 million during the year ended March 31, 2004. These costs were primarily for severance, personnel costs and relocation costs. The Company does not expect to incur additional facility consolidation costs during the two-year period ending September 30, 2005.

Fiscal Year Ended March 31, 2003 Compared to Fiscal Year Ended March 31, 2002

The following table summarizes revenue, gross profit, gross margin, expenses and the respective percentages for each of Universal's business segments:

	Year Ended March 31,	
	2003	2002
	(Dollars in thousands)	
Revenue:		
Domestic contract compression	\$265,465	\$267,550
% of revenue	42.5%	39.3%
International contract compression	\$ 66,505	\$ 60,185
% of revenue	10.6%	8.9%
Fabrication	\$162,678	\$211,265
% of revenue	26.0%	31.1%
Aftermarket services	\$130,570	\$140,989
% of revenue	20.9%	20.7%
Total revenue	\$625,218	\$679,989
Gross profit:		
Domestic contract compression	\$169,868	\$169,892
International contract compression	53,769	43,411
Fabrication	16,075	24,347
Aftermarket services	28,256	30,696
Total gross profit	\$267,968	\$268,346
Gross margin:		
Domestic contract compression	64.0%	63.5%
International contract compression	80.8%	72.1%
Fabrication	9.9%	11.5%
Aftermarket services	21.6%	21.8%
Total gross margin	42.9%	39.5%
Expenses:		
Depreciation and amortization	(63,706)	(48,600)
Selling, general and administrative	(67,944)	(60,890)
Operating lease expense	(46,071)	(55,401)
Interest expense, net	(36,421)	(23,017)
Foreign currency gain/(loss)	(459)	42
Other income/(loss), net	1,126	(141)
Income taxes	(20,975)	(30,931)
Net income	\$ 33,518	\$ 49,408

Revenue. Total revenue for the fiscal year ended March 31, 2003 decreased \$54.8 million, or 8.1%, to \$625.2 million, compared to \$680.0 million for the fiscal year ended March 31, 2002 largely as a result of declines in fabrication and aftermarket services. Domestic contract compression revenue decreased by \$2.1 million, or 1%, to \$265.5 million during the fiscal year ended March 31, 2003 from \$267.6 million during the fiscal year ended March 31, 2002. International contract compression revenue increased by \$6.3 million, or 10.5%, to \$66.5 million during the fiscal year ended March 31, 2003 from \$60.2 million during the fiscal year ended March 31, 2002. The decrease in domestic contract compression revenue was a result of lower horsepower utilization in a period of reduced energy industry activity that resulted in a reduced demand for contract compression services. The increase in international contract compression revenue resulted from new contract settlements negotiated with our Argentina customers in the first quarter of fiscal year 2003 and expansion of our business in the Latin America and Asia Pacific regions.

Domestic average contracted horsepower for the fiscal year ended March 31, 2003 decreased slightly to approximately 1,602,000 horsepower from approximately 1,603,000 horsepower for the fiscal year ended March 31, 2002 primarily due to the general decline in energy industry activity in the United States. International average contracted horsepower for the fiscal year ended March 31, 2003 increased by 2.6% to approximately 311,000 horsepower from approximately 303,000 horsepower for

the fiscal year ended March 31, 2002, primarily through expansion of the international contract compression fleet. The combined average horsepower utilization rate for the fiscal year ended March 31, 2003 was approximately 83.3%, down from 88.8% in the fiscal year ended March 31, 2002. As of March 31, 2003, Universal had approximately 2.3 million available horsepower with an average horsepower utilization rate for the quarter then ended of 83.5% and for the same period one year earlier of approximately 86.8%.

Fabrication revenue decreased to \$162.7 million from \$211.3 million, a decrease of 23% due to lower demand for customer-owned compressors in a period of reduced energy industry activity. Backlog of fabrication projects at the fiscal year ended March 31, 2003 was approximately \$55.7 million, compared with a backlog of \$80.0 million at March 31, 2002. From December 31, 2002 to March 31, 2003, backlog decreased \$0.6 million. The backlog as of May 12, 2003 was approximately \$75 million.

Aftermarket services revenue decreased to \$130.6 million during the fiscal year ended March 31, 2003 from \$141.0 million during the fiscal year ended March 31, 2002, a decrease of 7.4%. The decrease resulted from reduced repair and maintenance activity from Universal's North American customer base in a period of reduced energy industry activity.

Gross Profit. Gross profit for the fiscal year ended March 31, 2003 decreased \$0.4 million, or 0.1%, to \$268.0 million from gross profit of \$268.3 million for the fiscal year ended March 31, 2002 reflecting declines in fabrication and aftermarket services that were partially offset by an increase in international contract compression. Fabrication gross profit for the fiscal year ended March 31, 2003 decreased \$8.3 million, or 34.0%, to \$16.1 million compared to a gross profit of \$24.3 million for the fiscal year ended March 31, 2002. Fabrication gross profit decreased primarily due to lower demand during the fiscal year. Aftermarket services gross profit for the fiscal year ended March 31, 2003 decreased \$2.4 million or 7.9%, to \$28.3 million compared to a gross profit of \$30.7 million for the fiscal year ended March 31, 2002. Aftermarket services gross profit decreased primarily due to the overall slowdown in energy industry activity.

Selling, General and Administrative Expenses. Selling, general and administrative expenses increased by \$7.1 million to \$67.9 million for the fiscal year ended March 31, 2003, compared to \$60.9 million for the fiscal year ended March 31, 2002. Selling, general and administrative expenses represented 10.9% of revenue for the fiscal year ended March 31, 2003 compared to 9.0% of revenue for the fiscal year ended March 31, 2002. The increase was primarily due to a greater presence in international markets, which carries higher administration costs and severance costs related to staff reductions.

EBITDA, as adjusted. EBITDA, as adjusted, for the fiscal year ended March 31, 2003 decreased 3.0% to \$201.2 million from \$207.3 million for the fiscal year ended March 31, 2002, primarily due to increases in the selling, general and administrative costs. EBITDA, as adjusted, is defined, discussed and reconciled to net income on page 19 of this report, within Item 6, Selected Financial Data.

Depreciation and Amortization. Depreciation and amortization increased by \$15.1 million to \$63.7 million during the fiscal year ended March 31, 2003, compared to \$48.6 million during the fiscal year ended March 31, 2002. Depreciation expense increased due to a full twelve months of depreciation of fiscal 2002 capital additions and capitalized overhauls. In addition, depreciation expense increased due to the three months of depreciation of gas compressor units that were not previously recorded on Universal's balance sheet until December 31, 2002, when the lessors under the operating lease facilities became fully consolidated entities. Depreciation expense related to these assets began January 1, 2003 and increased depreciation expense for the fiscal year ended March 31, 2003 by approximately \$5.6 million.

In fiscal 2003, Universal evaluated the estimated useful lives used for book depreciation purposes for its compressor fleet based upon equipment type, key components and industry experience of the

actual useful life in the field. The evaluation was finalized in the fourth quarter of fiscal year 2003. Based upon the findings of the evaluation, the estimated useful lives of the majority of the existing compressor units were extended to 25 years from 15 years. In addition, a portion of the units remained at the previous 15 years or less and a portion of the units were extended to 30 years. The change in useful lives was effective January 1, 2003. The impact from extending the estimated useful lives of the equipment that was recorded on Universal's balance sheet on December 31, 2002 (excluding the gas compression equipment related to the operating lease facilities) reduced depreciation expense by approximately \$3.0 million for the year ended March 31, 2003.

The combined impact as a result of the consolidation of the compressor equipment in the operating lease facilities and the extension of the estimated useful lives was an increase to depreciation expense of approximately \$2.6 million and a decrease to net income of \$1.6 million for the year ended March 31, 2003.

Operating Lease Expense. Operating lease expense decreased to \$46.1 million during the fiscal year ended March 31, 2003 compared to \$55.4 million during the fiscal year ended March 31, 2002. Operating lease expense related to the operating lease facilities has been recognized as interest expense subsequent to the consolidation of the lease facilities on December 31, 2002. As a result, Universal recognized no operating lease expense for the quarter ended March 31, 2003.

Interest Expense, Net. Interest expense, net, increased \$13.4 million to \$36.4 million for the fiscal year ended March 31, 2003 from \$23.0 million for the fiscal year ended March 31, 2002 primarily due to the consolidation of the operating lease facilities as of December 31, 2002 which resulted in the classification of operating lease expense subsequent to December 31, 2002 as interest expense.

Net Income. Net income decreased \$15.9 million to \$33.5 million for the fiscal year ended March 31, 2003 compared to a net income of \$49.4 million for the fiscal year ended March 31, 2002 for the reasons noted above.

ITEM 7A. *Quantitative and Qualitative Disclosures About Market Risk*

We are exposed to some market risk due to the floating or variable interest rates under our financing arrangements. Some of the interest and lease payments under our financing arrangements are based on a floating rate plus an applicable margin. The variable interest rate under our revolving credit facility, which had no amounts outstanding as of March 31, 2004, is based upon either a base rate or LIBOR, at our option, and the applicable margin is a variable amount from 1.5% to 2.5% based on a leverage ratio. The variable interest rate under our \$82.2 million term loan is based upon the one month LIBOR rate and the applicable margin is a fixed 3.25%. The one month LIBOR at June 7, 2004 was 1.1%. The variable interest rate applicable to \$100 million of our 7¼% senior notes due 2010 pursuant to an interest rate swap is based upon the six month LIBOR rate. The six month LIBOR rate at June 7, 2004 was 1.6%. As of March 31, 2004, approximately \$182.2 million of our outstanding indebtedness and other obligations bore interest at floating rates and a 1.0% increase in interest rates would result in an approximate \$1.8 million annual increase in our interest expense.

We hold interest rate swaps related to the ABS lease facility. At March 31, 2004, the fair market value of these interest rate swaps was a liability of approximately \$14.4 million, which was recorded as a noncurrent liability. The interest rate swaps terminate in February 2013. The weighted average fixed rate of these swaps is 5.4%.

To minimize any significant foreign currency credit risk, we generally contractually require that payment by our customers be made in U.S. dollars. If payment is not made in U.S. dollars, we generally utilize the exchange rate into U.S. dollars on the payment date or balance payments in local currency against local expenses.

ITEM 8. Financial Statements and Supplementary Data

The consolidated statements of the Company and Universal included in this Report beginning on page F-1 are incorporated herein by reference.

ITEM 9. Changes in and Disagreements with Accountants on Accounting and Financial Disclosure

None.

ITEM 9A. Controls and Procedures

As required by Rule 13a-15(b) and Rule 15d-15(b) under the Securities Exchange Act of 1934 (the “Exchange Act”), Company management, including the Chief Executive Officer and Chief Financial Officer of the Company and of Universal, evaluated as of the end of the period covered by this report, the effectiveness of the Company’s disclosure controls and procedures as defined in Exchange Act Rule 13a-15(e) and Rule 15d-15(e). Based on that evaluation, the Chief Executive Officer and Chief Financial Officer concluded that the Company’s disclosure controls and procedures, as of the end of the period covered by this report, were effective for the purpose of ensuring that material information required to be in this report is made known to Company management, including the Chief Executive Officer and Chief Financial Officer, by others on a timely basis. As required by Exchange Act Rule 13a-15(d) and Rule 15d-15(d), Company management, including the Chief Executive Officer and Chief Financial Officer of the Company and of Universal, also evaluated whether any change in the Company’s internal control over financial reporting that occurred during the Company’s fourth fiscal quarter ended March 31, 2004 has materially affected, or is reasonably likely to materially affect, the Company’s internal control over financial reporting. Based on that evaluation, there has been no such change during the Company’s fourth fiscal quarter ended March 31, 2004.

PART III**ITEM 10. Directors and Executive Officers of the Company**

The information included or to be included in our definitive proxy statement for our 2004 Annual Meeting of Stockholders under the caption “Proposal 1: Election of Directors” is incorporated by reference herein.

ITEM 11. Executive Compensation

The information included or to be included under the caption “Executive Compensation” in our definitive proxy statement for our 2004 Annual Meeting of Stockholders is incorporated by reference herein.

ITEM 12. Security Ownership of Certain Beneficial Owners and Management and Related Stockholder Matters

The information included or to be included under the captions “Security Ownership of Certain Beneficial Owners and Management” and “Equity Compensation Plan Information” in our definitive proxy statement for our 2004 Annual Meeting of Stockholders is incorporated by reference herein.

ITEM 13. Certain Relationships and Related Transactions

The information included or to be included under the caption “Certain Relationships and Related Transactions” in our definitive proxy statement for our 2004 Annual Meeting of Stockholders is incorporated by reference herein.

ITEM 14. *Principal Accountant Fees and Services*

The information included or to be included under the caption “Proposal 4: Ratification of Appointment of Independent Auditors” in our definitive proxy statement for our 2004 Annual Meeting of Stockholders is incorporated by reference herein.

PART IV

ITEM 15. *Exhibits, Financial Statement Schedules and Reports On Form 8-K*

(a) The following documents are filed as part of this Report:

1. Financial Statements—The financial statements of the Company and Universal listed in the accompanying Index to Consolidated Financial Statements on page F-1 are filed as part of this annual report and such Index to Consolidated Financial Statements is incorporated herein by reference.

2. Financial Statement Schedules—Schedule II Valuation and Qualifying Accounts is included on Page E-1. All other schedules have been omitted as the required information is not present in amounts sufficient to require submission of the schedule or because the information required is included in the consolidated financial statements or notes thereto.

(b) Reports on Form 8-K

On January 27, 2004, the Company filed a Current Report on Form 8-K reporting the issuance of a press release announcing earnings for the quarter ended December 31, 2003.

(c) Exhibits

EXHIBIT INDEX

Exhibit No.	Description
2.1	Agreement and Plan of Merger dated October 23, 2000, by and among Universal Compression Holdings, Inc., Universal Compression, Inc., Weatherford International, Inc., WEUS Holding, Inc. and Enterra Compression Company (incorporated by reference to Exhibit 10.1 of Universal Compression Holdings, Inc.'s Current Report on Form 8-K filed with the SEC on October 26, 2000).
3.1	Restated Certificate of Incorporation of Universal Compression Holdings, Inc. (incorporated by reference to Exhibit 3.1 of Universal Compression Holdings, Inc.'s Quarterly Report on Form 10-Q for the quarter ended June 30, 2000).
3.2	Restated Bylaws of Universal Compression Holdings, Inc. (incorporated by reference to Exhibit 3.2 of Universal Compression Holdings, Inc.'s Quarterly Report on Form 10-Q for the quarter ended June 30, 2000).
	8⁷/₈% Senior Secured Notes due 2008
4.1	Indenture, dated February 9, 2001, among BRL Universal Equipment 2001 A, L.P. and BRL Universal Equipment Corp., as Issuers, and The Bank of New York, as Indenture Trustee, with respect to the 8 ⁷ / ₈ % Senior Secured Notes due 2008 (incorporated by reference to Exhibit 10.4 of Universal Compression Holdings, Inc.'s Quarterly Report on Form 10-Q for the quarter ended December 31, 2000).
4.2	First Supplemental Indenture, dated September 11, 2001, among BRL Universal Equipment 2001 A, L.P. and BRL Universal Equipment Corp., as Issuers, and The Bank of New York, as Indenture Trustee, with respect to the 8 ⁷ / ₈ % Senior Secured Notes due 2008 (incorporated by reference to Exhibit 4.1 of Universal Compression Holdings, Inc.'s Current Report on Form 8-K filed with the SEC on October 24, 2001).

Exhibit No.	Description
	ABS Operating Lease Facility
4.3	Indenture, dated December 31, 2002, between BRL Universal Compression Funding I 2002, L.P., as Issuer, and Wells Fargo Bank Minnesota, National Association, as Indenture Trustee, with respect to the ABS operating lease facility (incorporated by reference to Exhibit 4.1 of Universal Compression Holdings, Inc.'s Quarterly Report on Form 10-Q for the quarter ended December 31, 2002).
4.4	Series 2002-1 Supplement, dated December 31, 2002, to Indenture, dated December 31, 2002, between BRL Universal Compression Funding I 2002, L.P. and Wells Fargo Bank Minnesota, National Association, as Indenture Trustee, with respect to the ABS operating lease facility (incorporated by reference to Exhibit 4.2 of Universal Compression Holdings, Inc.'s Quarterly Report on Form 10-Q for the quarter ended December 31, 2002).
4.5	Amendment Number 1 to Indenture, dated December 18, 2003, between BRL Universal Compression Funding I 2002, L.P., as Issuer, and Wells Fargo Bank Minnesota, National Association, as Indenture Trustee, with respect to the ABS operating lease facility (incorporated by reference to Exhibit 4.1 of Universal Compression Holdings, Inc.'s Quarterly Report on Form 10-Q for the quarter ended December 31, 2003).
4.6*	Amendment Number 2 to Indenture, dated January 14, 2004, between BRL Universal Compression Funding I 2002, L.P., as Issuer, and Wells Fargo Bank, National Association (successor by merger to Wells Fargo Bank Minnesota, National Association), as Indenture Trustee, with respect to the ABS operating lease facility 7¼% Senior Notes due 2010
4.7	Indenture, dated May 27, 2003, by and between Universal Compression, Inc., as Issuer, and The Bank of New York, as Trustee (incorporated by reference to Exhibit 4.11 of Universal Compression Holdings, Inc.'s Annual Report on Form 10-K for the year ended March 31, 2003).
4.8	Specimen of Universal Compression, Inc.'s 7¼% Senior Notes due 2010 (incorporated by reference to Exhibit 4.11 of Universal Compression Holdings, Inc.'s Annual Report on Form 10-K for the year ended March 31, 2003). Senior Secured Notes Operating Lease Facility
10.1	Equipment Lease Agreement, dated February 9, 2001, between BRL Universal Equipment 2001 A, L.P., as Lessor, and Universal Compression, Inc., as Lessee, with respect to the senior secured notes operating lease facility (incorporated by reference to Exhibit 10.2 of Universal Compression Holdings, Inc.'s Registration Statement on Form S-4 filed with the SEC on March 20, 2001 (File No. 333-57302)).
10.2	First Amendment to Equipment Lease Agreement, dated October 15, 2001, between BRL Universal Equipment 2001 A, L.P., as Lessor, and Universal Compression, Inc., as Lessee, with respect to the senior secured notes operating lease facility (incorporated by reference to Exhibit 10.1 of Universal Compression Holdings, Inc.'s Current Report on Form 8-K filed with the SEC on October 24, 2001).
10.3	Second Amendment to Equipment Lease Agreement, dated November 20, 2002, between BRL Universal Equipment 2001 A, L.P., as Lessor, and Universal Compression, Inc., as Lessee, with respect to the senior secured notes operating lease facility (incorporated by reference to Exhibit 10.2 of Universal Compression Holdings, Inc.'s Quarterly Report on Form 10-Q for the quarter ended December 31, 2002).

Exhibit No.	Description
10.4	First Amended and Restated Participation Agreement, dated October 15, 2001, among Universal Compression, Inc., as Lessee; Universal Compression Holdings, Inc., as Guarantor; BRL Universal Compression Equipment 2001 A, L.P., as Lessor; the financial institutions listed on the signature pages as Tranche B Lenders; The Bank of New York, not in its individual capacity but as Indenture Trustee, Paying Agent, Transfer Agent and Registrar for the Tranche A Noteholders; BRL Universal Equipment Management, Inc., as Lessor General Partner; Bankers Trust Company, as Administrative Agent and Collateral Agent for the Tranche B Lenders and Indenture Trustee on behalf of the Tranche A Noteholders; Deutsche Banc Alex. Brown Inc., as Arranger; The Bank of Nova Scotia, as Syndicate Agent for Tranche B Lenders; Bank One, N.A., as Documentation Agent for Tranche B Lenders; and First Union National Bank, as Managing Agent; with respect to the senior secured notes operating lease facility (incorporated by reference to Exhibit 10.2 of Universal Compression Holdings, Inc.'s Current Report on Form 8-K filed with the SEC on October 24, 2001).
10.5	Participation Agreement Supplement No. 1, dated October 23, 2001, among Universal Compression, Inc., as Lessee, Universal Compression Holdings, Inc., as Guarantor, BRL Universal Equipment 2001 A, L.P., as Lessor, and The Bank of New York, not in its individual capacity but as Indenture Trustee for the Tranche A Noteholders, with respect to the senior secured notes operating lease facility (incorporated by reference to Exhibit 10.3 of Universal Compression Holdings, Inc.'s Current Report on Form 8-K filed with the SEC on October 24, 2001).
10.6	First Amendment to First Amended and Restated Participation Agreement, dated November 20, 2002, among Universal Compression, Inc., BRL Universal Equipment 2001 A, L.P. and Deutsche Bank Trust Company Americas, with respect to the senior secured notes operating lease facility (incorporated by reference to Exhibit 10.1 of Universal Compression Holdings, Inc.'s Quarterly Report on Form 10-Q for the quarter ended December 31, 2002).
10.7	Tranche B Loan Agreement, dated February 9, 2001, among BRL Universal Equipment 2001 A, L.P., as Borrower, Bankers Trust Company, as Administrative Agent and Collateral Agent, and the Tranche B Lenders, with respect to the senior secured notes operating lease facility (incorporated by reference to Exhibit 10.4 of Universal Compression Holdings, Inc.'s Registration Statement on Form S-4 filed with the SEC on March 20, 2001 (File No. 333-57302)).
10.8	First Amendment to Tranche B Loan Agreement, dated October 15, 2001, among BRL Universal Equipment 2001 A, L.P. and Bankers Trust Company, as Administrative Agent for Tranche B Lenders and as Collateral Agent, with respect to the senior secured notes operating lease facility (incorporated by reference to Exhibit 10.4 of Universal Compression Holdings, Inc.'s Current Report on Form 8-K filed with the SEC on October 24, 2001).
10.9	Engagement and Indemnity Letter, dated February 9, 2001 among Universal Compression, Inc., Universal Compression Holdings, Inc., Deutsche Banc Alex. Brown Inc., First Union Securities, Inc., Goldman Sachs & Co., Banc One Capital Markets, Inc., Scotia Capital (USA), Inc., BRL Universal Equipment 2001 A, L.P., and BRL Universal Equipment Corp., with respect to the senior secured notes operating lease facility (incorporated by reference to Exhibit 10.12 of Universal Compression Holdings, Inc.'s Quarterly Report on Form 10-Q for the quarter ended December 31, 2000).
	ABS Lease Facility
10.10	Master Equipment Lease Agreement, dated December 31, 2002, between BRL Universal Compression Funding I 2002, L.P., as Head Lessor, and UCO Compression 2002 LLC, as Head Lessee, with respect to the ABS operating lease facility (incorporated by reference to Exhibit 10.3 of Universal Compression Holdings, Inc.'s Quarterly Report on Form 10-Q for the quarter ended December 31, 2002).

Exhibit No.	Description
10.11	Guaranty, dated December 31, 2002, made by Universal Compression Holdings, Inc. for the benefit of UCO Compression 2002 LLC, BRL Universal Compression Funding I 2002, L.P. and Wells Fargo Bank Minnesota, N.A., with respect to the ABS operating lease facility (incorporated by reference to Exhibit 10.4 of Universal Compression Holdings, Inc.'s Quarterly Report on Form 10-Q for the quarter ended December 31, 2002).
10.12	Management Agreement, dated December 31, 2002, among Universal Compression, Inc., UCO Compression 2002 LLC and BRL Universal Compression Funding I 2002, L.P., with respect to the ABS operating lease facility (incorporated by reference to Exhibit 10.5 of Universal Compression Holdings, Inc.'s Quarterly Report on Form 10-Q for the quarter ended December 31, 2002).
10.13	Back-up Management Agreement, dated December 31, 2002, among Caterpillar Inc., UCO Compression 2002 LLC, BRL Universal Compression Funding I 2002, L.P. and Universal Compression, Inc., with respect to the ABS operating lease facility (incorporated by reference to Exhibit 10.6 of Universal Compression Holdings, Inc.'s Quarterly Report on Form 10-Q for the quarter ended December 31, 2002).
10.14	Head Lessee Security Agreement, dated December 31, 2002, between UCO Compression 2002 LLC, as Grantor, and BRL Universal Compression Funding I 2002, L.P., as Secured Party, with respect to the ABS operating lease facility (incorporated by reference to Exhibit 10.7 of Universal Compression Holdings, Inc.'s Quarterly Report on Form 10-Q for the quarter ended December 31, 2002).
10.15	Intercreditor and Collateral Agency Agreement, dated December 31, 2002, among Universal Compression, Inc., UCO Compression 2002 LLC and BRL Universal Compression Funding I 2002, L.P., Wells Fargo Bank Minnesota, National Association, Wachovia Bank, National Association and Bank One, N.A., with respect to the ABS operating lease facility (incorporated by reference to Exhibit 10.8 of Universal Compression Holdings, Inc.'s Quarterly Report on Form 10-Q for the quarter ended December 31, 2002).
10.16	Insurance and Indemnity Agreement, dated December 31, 2002, by and among Ambac Assurance Corporation, BRL Universal Compression Funding I 2002, L.P., Universal Compression, Inc., UCO Compression 2002 LLC and Wells Fargo Bank Minnesota, N.A., with respect to the ABS operating lease facility (incorporated by reference to Exhibit 10.9 of Universal Compression Holdings, Inc.'s Quarterly Report on Form 10-Q for the quarter ended December 31, 2002).
10.17*	Amendment Number 1 to the Head Lessee Security Agreement, dated January 14, 2004, between UCO Compression 2002, as Grantor, and BRL Universal Compression Funding I 2002, L.P., as Secured Party, with respect to the ABS operating lease facility.
	Bank Agreements
10.18	Senior Secured Revolving Credit Agreement, dated February 9, 2001, among Universal Compression, Inc., as Borrower, First Union National Bank, as Administrative Agent, Bank One, N.A., as Syndication Agent, and the lenders signatory thereto (incorporated by reference to Exhibit 10.6 of Universal Compression Holdings, Inc.'s Registration Statement on Form S-4 filed with the SEC on March 20, 2001 (File No. 333-57302)).
10.19	First Amendment and Supplement to Senior Secured Revolving Credit Agreement, dated October 15, 2001, among Universal Compression, Inc., as Borrower, First Union National Bank, as Administrative Agent, Bank One, N.A., as Syndication Agent, and the lenders signatory thereto (incorporated by reference to Exhibit 10.13 of Universal Compression Holdings, Inc.'s Annual Report on Form 10-K for the fiscal year ended March 31, 2002).

Exhibit No.	Description
10.20	Second Amendment and Supplement to Senior Secured Revolving Credit Agreement, dated September 30, 2002, among Universal Compression, Inc., as Borrower, Wachovia Bank, National Association, formerly First Union National Bank, as Administrative Agent, Bank One, N.A., as Syndication Agent, and the lenders signatory thereto (incorporated by reference to Exhibit 10.3 of Universal Compression Holdings, Inc.'s Quarterly Report on Form 10-Q for the quarter ended September 30, 2002).
10.21	Guaranty and Collateral Agreement made by Universal Compression Holdings, Inc. and Universal Compression, Inc. and in favor of First Union National Bank, as Administrative Agent, dated February 9, 2001 (incorporated by reference to Exhibit 10.8 of Universal Compression Holdings, Inc.'s Quarterly Report on Form 10-Q for the quarter ended December 31, 2000).
10.22	Security Agreement (Pledge and Assignment), dated February 9, 2001, between Universal Compression International, Inc. and First Union National Bank, as Administrative Agent (incorporated by reference to Exhibit 10.9 of Universal Compression Holdings, Inc.'s Quarterly Report on Form 10-Q for the quarter ended December 31, 2000).
10.23*	Third Amendment and Supplement to Senior Secured Revolving Credit Agreement, dated February 14, 2004, among Universal Compression, Inc., as Borrower, Wachovia Bank, National Association, formerly First Union National Bank, as Administrative Agent, and the lenders signatory thereto.
	Executive Compensation Plans and Arrangements
10.24†	Universal Compression Holdings, Inc. Incentive Stock Option Plan (incorporated by reference to Exhibit 10 of Universal Compression Holdings, Inc.'s Quarterly Report on Form 10-Q for the period ended September 30, 1998).
10.25†	Amendment Number One to Incentive Stock Option Plan, dated April 20, 2000 (incorporated by reference to Exhibit 10.3 of Amendment No. 2, filed with the SEC on May 22, 2000, to Universal Compression Holdings, Inc.'s Registration Statement on Form S-1 (File No. 333-34090)).
10.26†	Amendment Number Two to Incentive Stock Option Plan, dated May 15, 2000 (incorporated by reference to Exhibit 10.4 of Amendment No. 2, filed with the SEC on May 22, 2000, to Universal Compression Holdings, Inc.'s Registration Statement on Form S-1 (File No. 333-34090)).
10.27†	Amendment Number Three to Incentive Stock Option Plan, dated November 27, 2000 (incorporated by reference to Exhibit 4.7 of Universal Compression Holdings, Inc.'s Registration Statement on Form S-8 filed with the SEC on February 9, 2001 (File No. 333-55260)).
10.28†	Amendment Number Four to Incentive Stock Option Plan, dated August 15, 2002 (incorporated by reference to Exhibit 4.8 of Universal Compression Holdings, Inc.'s Registration Statement on Form S-8 filed with the SEC on September 12, 2002 (File No. 333-99473)).
10.29†	Form of Stock Option Agreement under the Incentive Stock Option Plan for outside directors of Universal Compression Holdings, Inc.'s Board of Directors (incorporated by reference to Exhibit 10.30 of Universal Compression Holdings, Inc.'s Annual Report on Form 10-K for the fiscal year ended March 31, 2002).
10.30*†	Form of Stock Option Agreement under the Incentive Stock Option Plan for employees.
10.31†	Universal Compression Holdings, Inc. Restricted Stock Plan for Executive Officers (incorporated by reference to Exhibit 4.2 of Universal Compression Holdings, Inc.'s Registration Statement on Form S-8 filed with the SEC on August 17, 2001 (File No. 333-67784)).

Exhibit No.	Description
10.32†	Form of Restricted Stock Agreement under the Restricted Stock Plan for Executive Officers (incorporated by reference to Exhibit 10.8 of Universal Compression Holdings, Inc.'s Quarterly Report on Form 10-Q for the quarter ended September 30, 2001).
10.33†	Universal Compression Holdings, Inc. Directors' Stock Plan (incorporated by reference to Exhibit 4.3 of Universal Compression Holdings, Inc.'s Registration Statement on Form S-8 filed with the SEC on August 17, 2001 (File No. 333-67784)).
10.34†	Universal Compression, Inc. Employees' Supplemental Savings Plan (incorporated by reference to Exhibit 10.42 of Universal Compression Holdings, Inc.'s Annual Report on Form 10-K for the year ended March 31, 2001).
10.35†	Amendment Number One to Employees' Supplemental Savings Plan, dated January 1, 2002 (incorporated by reference to Exhibit 10.53 of Universal Compression Holdings, Inc.'s Annual Report on Form 10-K for the year ended March 31, 2002).
10.36†	Amendment Number Two to Employees' Supplemental Savings Plan, dated August 15, 2002 (incorporated by reference to Exhibit 4.13 of Universal Compression Holdings, Inc.'s Registration Statement on Form S-8 filed with the SEC on September 12, 2002 (File No. 333-99473)).
10.37†	Amendment Number Three to Employees' Supplemental Savings Plan, dated September 1, 2002 (incorporated by reference to Exhibit 10.35 of Universal Compression Holdings, Inc.'s Annual Report on Form 10-K for the year ended March 31, 2003).
10.38†	Universal Compression Holdings, Inc. Employee Stock Purchase Plan (incorporated by reference to Exhibit 4.1 of Universal Compression Holdings, Inc.'s Registration Statement on Form S-8 filed with the SEC on August 17, 2001 (File No. 333-67784)).
10.39†	Amendment Number One to Employee Stock Purchase Plan, dated December 20, 2001 (incorporated by reference to Exhibit 10.56 of Universal Compression Holdings, Inc.'s Annual Report on Form 10-K for the year ended March 31, 2002).
10.40†	Form of Indemnification Agreement for executive officers and directors of Universal Compression Holdings, Inc. (incorporated by reference to Exhibit 10.27 of Amendment No. 1, filed with the SEC on May 3, 2000, to Universal Compression Holdings, Inc.'s Registration Statement on Form S-1 (File No. 333-34090)).
10.41†	Form of Change of Control Agreement for executive officers of Universal Compression Holdings, Inc. (incorporated by reference to Exhibit 10.4 of Universal Compression Holdings, Inc.'s Quarterly Report on Form 10-Q for the quarter ended September 30, 2002).
10.42†	Letter dated March 15, 2001, with respect to certain retirement benefits to be provided to Stephen A. Snider (incorporated by reference to Exhibit 10.43 of Universal Compression Holdings, Inc.'s Annual Report on Form 10-K for the year ended March 31, 2001).
10.43†	Involuntary Termination Agreement, dated October 25, 2001, by and between Universal Compression, Inc. and Richard Leong (incorporated by reference to Exhibit 10.41 of Universal Compression Holdings, Inc.'s Annual Report on Form 10-K for the year ended March 31, 2003).
	Registration Rights Agreements
10.44	Registration Rights Agreement, dated February 20, 1998 by and among Universal Compression Holdings, Inc., Castle Harlan Partners III, L.P. and each other party listed as signatory thereto (incorporated by reference to Exhibit 10.14 to Universal Compression Holdings, Inc.'s Registration Statement on Form S-4 dated March 19, 1998 (File No. 333-48283)).
10.45	Form of Instruments of Accession to Registration Rights Agreement for each of Richard W. FitzGerald and Valerie L. Banner (incorporated by reference to Exhibit 4.10 to Universal Compression Holdings, Inc.'s Registration Statement on Form S-1 (File No. 333-34090)).

Exhibit No.	Description
10.46	Instrument of Accession to Registration Rights Agreement, dated April 28, 2000, for Energy Spectrum Partners LP (incorporated by reference to Exhibit 10.19 to Amendment No. 2 dated May 22, 2000, to Universal Compression Holdings, Inc.'s Registration Statement on Form S-1 (File No. 333-34090)).
10.47	Amended and Restated Registration Rights Agreement, dated March 23, 2004, by and between Universal Compression Holdings, Inc. and Weatherford International Ltd. (incorporated by reference to Exhibit 10.1 to Universal Compression Holdings, Inc.'s Registration Statement on Form S-3 (File No. 333-114145)).
21.1*	List of Subsidiaries.
23.1*	Consent of Deloitte & Touche LLP.
24.1*	Powers of attorney (set forth on the signature page hereof).
31.1*	Rule 13a-14(a) Certifications of the CEO.
31.2*	Rule 13a-14(a) Certifications of the CFO.
31.3*	Rule 15d-14(a) Certification of the CEO
31.4*	Rule 15d-14(a) Certification of the CFO
32.1*	Section 1350 Certifications.
32.2*	Section 1350 Certifications.

* Filed herewith.

† Management Contract or Compensatory Plan or Arrangement.

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REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

To the Board of Directors of
Universal Compression Holdings, Inc.

We have audited the accompanying consolidated balance sheets of Universal Compression Holdings, Inc. and subsidiaries (the "Company") as of March 31, 2004 and 2003, and the related consolidated statements of operations, stockholders' equity, and cash flows for each of the three years in the period ended March 31, 2004. Our audits also included the financial statement schedule listed in the Index at E-1, which represents Schedule II to the consolidated financial statements of the Company. These financial statements and financial statement schedule are the responsibility of the Company's management. Our responsibility is to express an opinion on the financial statements and financial statement schedule based on our audits.

We conducted our audits in accordance with standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, such consolidated financial statements present fairly, in all material respects, the financial position of the Company as of March 31, 2004 and 2003, and the results of its operations and its cash flows for each of the three years in the period ended March 31, 2004, in conformity with accounting principles generally accepted in the United States of America. Also, in our opinion, such financial statement schedule, when considered in relation to the basic consolidated financial statements taken as a whole, presents fairly in all material respects the information set forth therein.

/s/ DELOITTE & TOUCHE LLP

Houston, Texas
June 4, 2004

UNIVERSAL COMPRESSION HOLDINGS, INC.
CONSOLIDATED BALANCE SHEETS
(In thousands)

	<u>March 31, 2004</u>	<u>March 31, 2003</u>
ASSETS		
Current assets:		
Cash and cash equivalents	\$ 121,189	\$ 71,693
Accounts receivable, net of allowance for bad debts of \$3,189 and \$8,146 as of		
March 31, 2004 and 2003, respectively	79,587	77,565
Current portion of notes receivable	709	2,722
Inventories, net of reserve for obsolescence of \$12,041 and \$10,468 as of		
March 31, 2004 and 2003, respectively	89,968	91,332
Current deferred tax asset	5,819	10,890
Other	13,938	7,258
Total current assets	311,210	261,460
Contract compression equipment	1,344,218	1,316,214
Other property	117,128	106,496
Accumulated depreciation and amortization	(216,569)	(145,916)
Net property, plant and equipment	1,244,777	1,276,794
Goodwill	390,371	387,711
Notes receivable	444	2,555
Other non-current assets	25,649	25,367
Total assets	<u>\$1,972,451</u>	<u>\$1,953,887</u>
LIABILITIES AND STOCKHOLDERS' EQUITY		
Current liabilities:		
Accounts payable, trade	\$ 44,948	\$ 43,210
Accrued liabilities	40,765	32,317
Unearned revenue	25,596	13,272
Accrued interest	10,933	9,934
Current portion of long-term debt and capital lease obligations	14,369	4,322
Total current liabilities	136,611	103,055
Capital lease obligations	997	3,180
Long-term debt	869,076	937,653
Non-current deferred tax liability	149,554	148,795
Derivative financial instrument used for hedging purposes	14,423	15,404
Other liabilities	2,555	1,349
Total liabilities	1,173,216	1,209,436
Commitments and contingencies (Note 11)		
Stockholders' equity:		
Common stock, \$.01 par value, 200,000 and 200,000 shares authorized, 31,294		
and 30,732 shares issued, 31,293 and 30,731 shares outstanding as of		
March 31, 2004 and 2003, respectively	313	308
Treasury stock, 1 shares at cost outstanding as of March 31, 2004 and 2003	(11)	(17)
Additional paid-in capital	734,124	724,491
Deferred compensation	(1,256)	(2,009)
Other comprehensive loss	(35,344)	(48,944)
Retained earnings	101,409	70,622
Total stockholders' equity	799,235	744,451
Total liabilities and stockholders' equity	<u>\$1,972,451</u>	<u>\$1,953,887</u>

See accompanying notes to consolidated financial statements.

UNIVERSAL COMPRESSION HOLDINGS, INC.
CONSOLIDATED STATEMENTS OF OPERATIONS
(In thousands, except per share amounts)

	For the Year Ended March 31,		
	2004	2003	2002
Revenue:			
Domestic contract compression	\$280,951	\$265,465	\$267,550
International contract compression	82,589	66,505	60,185
Fabrication	183,685	162,678	211,265
Aftermarket services	141,561	130,570	140,989
Total revenue	<u>688,786</u>	<u>625,218</u>	<u>679,989</u>
Costs and expenses:			
Domestic contract compression—direct costs	102,408	95,597	97,658
International contract compression—direct costs	18,430	12,736	16,774
Fabrication—direct costs	167,797	146,603	186,918
Aftermarket services—direct costs	110,670	102,314	110,293
Depreciation and amortization	85,650	63,706	48,600
Selling, general and administrative	67,516	67,944	60,890
Operating lease expense	—	46,071	55,401
Interest expense, net	73,475	36,421	23,017
Debt extinguishment costs	14,903	—	—
Foreign currency (gain)/loss	(529)	459	(42)
Other (income)/expense, net	(1,883)	(1,126)	141
Facility consolidation costs	1,821	—	—
Total costs and expenses	<u>640,258</u>	<u>570,725</u>	<u>599,650</u>
Income before income taxes	48,528	54,493	80,339
Income tax expense	17,741	20,975	30,931
Net income	<u>\$ 30,787</u>	<u>\$ 33,518</u>	<u>\$ 49,408</u>
Weighted average common and common equivalent shares outstanding:			
Basic	30,848	30,665	30,008
Diluted	31,283	30,928	30,250
Earnings per share—Basic	<u>\$ 1.00</u>	<u>\$ 1.09</u>	<u>\$ 1.65</u>
Earnings per share—Diluted	<u>\$ 0.98</u>	<u>\$ 1.08</u>	<u>\$ 1.63</u>

See accompanying notes to consolidated financial statements.

UNIVERSAL COMPRESSION HOLDINGS, INC.
CONSOLIDATED STATEMENTS OF STOCKHOLDERS' EQUITY
For the Years Ended March 31, 2002, 2003 and 2004
(In thousands, except for share data)

	Common Stock Shares	Common Stock Amount	Additional Paid in Capital	Retained Earnings (Deficit)	Treasury Stock	Deferred Compensation	Other Comprehensive Income (Loss)	Total
Balance, March 31, 2001	28,475,136	\$285	\$663,882	\$ (12,304)	\$ (134)	—	\$ 845	\$625,574
Common stock issuance	1,333,333	13	36,118					36,131
Stock issued for acquisition . .	694,927	7	19,993					20,000
Treasury stock redeemed, at \$27 per share	(28,379)				(800)			(800)
Option exercises	109,419	1	1,099					1,100
Shares issued in employee benefit plans	17,606		1,006					1,006
Share issuances costs			(1,122)					(1,122)
Restricted stock transactions . .			2,855			(2,855)		—
Amortization of deferred compensation						409		409
Net income				49,408				49,408
Foreign currency translation adjustment							(58,362)	(58,362)
Comprehensive loss								(8,954)
Balance, March 31, 2002	<u>30,602,042</u>	<u>\$306</u>	<u>\$723,831</u>	<u>\$ 37,104</u>	<u>\$ (934)</u>	<u>\$(2,446)</u>	<u>\$(57,517)</u>	<u>\$700,344</u>
Common stock issuance	10,000		181					181
Treasury stock redeemed, at \$21 per share					(1,000)			(1,000)
Option exercises	22,841	1	(52)		246			195
Shares issued in employee benefit plans	96,495	1	832		1,497			2,330
Restricted stock transactions . .			(301)		174	127		—
Amortization of deferred compensation						310		310
Interest rate swap loss							(566)	(566)
Net income				33,518				33,518
Foreign currency translation adjustment							9,139	9,139
Comprehensive income								42,091
Balance, March 31, 2003	<u>30,731,378</u>	<u>\$308</u>	<u>\$724,491</u>	<u>\$ 70,622</u>	<u>\$ (17)</u>	<u>\$(2,009)</u>	<u>\$(48,944)</u>	<u>\$744,451</u>
Option exercises	350,746	3	7,558		6			7,567
Shares issued in employee benefit plans	116,729	1	2,242					2,243
Restricted stock transactions . .	94,147	1	(167)			167		1
Amortization of deferred compensation						586		586
Interest rate swap loss							(541)	(541)
Net income				30,787				30,787
Foreign currency translation adjustment							14,141	14,141
Comprehensive income								44,387
Balance, March 31, 2004	<u>31,293,000</u>	<u>\$313</u>	<u>\$734,124</u>	<u>\$101,409</u>	<u>\$ (11)</u>	<u>\$(1,256)</u>	<u>\$(35,344)</u>	<u>\$799,235</u>

See accompanying notes to consolidated financial statements.

UNIVERSAL COMPRESSION HOLDINGS, INC.
CONSOLIDATED STATEMENTS OF CASH FLOWS
(In thousands)

	For the Year Ended March 31,		
	2004	2003	2002
Cash flows from operating activities:			
Net income	\$ 30,787	\$ 33,518	\$ 49,408
Adjustments to reconcile net income to cash provided by operating activities, net of effect of acquisitions:			
Depreciation and amortization	85,650	63,706	48,600
Loss on early extinguishment of debt	14,903	—	—
Gain on asset sales	(965)	(741)	(286)
Amortization of debt issuance costs	4,297	3,670	3,006
Amortization of deferred compensation	586	310	409
Accretion of discount notes	—	18,660	20,073
Increase in deferred taxes	7,811	18,058	20,827
(Increase) decrease in other assets	(2,942)	12,913	21,225
(Increase) decrease in receivables	(1,338)	37,105	(10,404)
(Increase) decrease in inventories	4,999	11,871	40,048
Increase (decrease) in accounts payable	1,013	(2,004)	(44,947)
Increase (decrease) in accrued liabilities	7,954	(10,266)	(23,867)
Increase (decrease) in unearned revenue	12,324	(2,778)	9,742
Increase (decrease) in accrued interest	999	3,048	(756)
Net cash provided by operating activities	166,078	187,070	133,078
Cash flows from investing activities:			
Additions to property, plant and equipment	(86,557)	(120,751)	(188,019)
Cash paid for acquisitions	(761)	(1,536)	(160,021)
Proceeds from sale of property, plant and equipment	40,468	14,583	187,784
Net cash used in investing activities	(46,850)	(107,704)	(160,256)
Cash flows from financing activities:			
Principal repayments of long-term debt	(234,750)	(5,818)	(7,401)
Proceeds from issuance of debt	175,000	—	—
Net proceeds (repayment) on sale-leaseback of vehicles	—	(2,800)	(2,878)
Debt extinguishment premium and cost	(12,920)	—	—
Common stock issuance	7,578	1,098	36,285
Purchase of treasury stock	—	—	(800)
Debt issuance costs	(4,640)	(5,009)	(4,131)
Operating lease facilities	—	(1,320)	—
Net cash provided by (used in) financing activities	(69,732)	(13,849)	21,075
Net increase (decrease) in cash and cash equivalents	49,496	65,517	(6,103)
Cash and cash equivalents at beginning of period	71,693	6,176	12,279
Cash and cash equivalents at end of period	121,189	\$ 71,693	\$ 6,176
Supplemental disclosure of cash flow information:			
Cash paid for interest	\$ 77,472	\$ 14,553	\$ 4,073
Cash paid for operating leases	—	\$ 47,171	\$ 54,301
Cash paid for income taxes	\$ 6,480	\$ 2,572	\$ 1,346
Supplemental schedule of non-cash investing and financing activities:			
Changes due to the consolidation of operating lease facilities:			
Additions to property, plant and equipment	—	\$ 614,800	—
Increase in debt	—	\$ 707,200	—
Noncurrent liability assumed	—	\$ 15,200	—
Elimination of deferred gain	—	\$ 107,600	—
Stock issued for acquisition	—	—	\$ 20,000

See accompanying notes to consolidated financial statements.

UNIVERSAL COMPRESSION HOLDINGS, INC.
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

1. Summary of Significant Accounting Policies

Organization

Universal Compression Holdings, Inc. (the “Company”) was formed on December 12, 1997 for the purpose of acquiring Tidewater Compression Service, Inc. (“TCS”) from Tidewater Inc. Upon completion of the acquisition on February 20, 1998, TCS became the Company’s wholly-owned subsidiary and changed its name to Universal Compression, Inc. (“Universal”). Through this subsidiary, the Company’s gas compression service operations date back to 1954. The Company completed an initial public offering of shares of our common stock in June 2000.

Since the initial public offering, the Company has completed several acquisitions, which have contributed significantly to our growth. Our most significant acquisition was that of Weatherford Global Compression Services, L.P. and certain related entities (“Weatherford Global”), former subsidiaries of Weatherford International Ltd. (“Weatherford”), in February 2001. This added approximately 950,000 horsepower, more than doubling our size at that time.

Universal Compression Holdings, Inc. is a holding company, which conducts its operations through its wholly-owned subsidiary, Universal. Accordingly, the Company is dependent upon the distribution of earnings from Universal, whether in the form of dividends, advances or payments on account of intercompany obligations, to service its debt obligations.

Nature of Operations

The Company is the second largest natural gas compression services company in the world in terms of compressor fleet horsepower, with a fleet as of March 31, 2004 of approximately 7,100 compressor units comprising approximately 2.3 million horsepower. The Company provides a full range of contract compression services, sales, operations, maintenance and fabrication services and products to the natural gas industry, both domestically and internationally. These services and products are essential to the natural gas industry, as gas must be compressed to be delivered from the wellhead to end-users.

Principles of Consolidation

The accompanying consolidated financial statements include the Company and its wholly-owned subsidiary, Universal. All significant intercompany accounts and transactions have been eliminated in consolidation.

Reclassifications

Certain reclassifications have been made to the prior year amounts to conform to the current year presentation.

Use of Estimates

In preparing the Company’s financial statements, management makes estimates and assumptions that affect the amounts reported in the financial statements and related disclosures. Actual results may differ from these estimates.

UNIVERSAL COMPRESSION HOLDINGS, INC.
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

1. Summary of Significant Accounting Policies (Continued)

Cash and Cash Equivalents

The Company considers all highly liquid investments purchased with an original maturity of three months or less to be cash equivalents. Cash flows are computed using the indirect method.

Revenue Recognition

Revenue is recognized by the Company's four reportable business segments using the following criteria: (a) persuasive evidence of an exchange arrangement exists, (b) delivery has occurred or services have been rendered, (c) the buyer's price is fixed or determinable and (d) collectibility is reasonably assured.

Revenue from contract compression services is recorded when earned over the period of service and maintenance contracts which generally range from one month to several years. Aftermarket services revenue is recorded as products are delivered or services are performed for the customer. Fabrication revenue is recognized using the completed-contract method which recognizes revenue upon completion of the contract. This method is used because the typical contract is completed within two to three months.

Concentration of Credit Risk

Trade accounts receivable are due from companies of varying size engaged principally in oil and gas activities in the United States and in international locations including Canada, Latin America and Asia Pacific. The Company reviews the financial condition of customers prior to extending credit and periodically updates customer credit information. Payment terms are on a short-term basis and in accordance with industry standards. No single customer accounts for 10% or more of the Company's revenue. For the years ended March 31, 2004, 2003 and 2002, the Company wrote off bad debts, net of recoveries totaling \$5.6 million, \$4.3 million, and \$0.1 million respectively.

Inventories

Inventories are recorded at the lower of average cost or market (net realizable value). Some items of compression equipment are acquired and placed in inventories for subsequent sale or compression services to others. Acquisitions of these assets are considered operating activities in the statement of cash flows.

Properties and Equipment

Property, plant and equipment are carried at cost. Depreciation for financial reporting purposes is computed on the straight-line basis using estimated useful lives. For compression equipment, depreciation begins with the first compression service using a 20% salvage value. During the fiscal year 2002, the Company reevaluated the estimated useful lives used for book depreciation purposes for its compressor fleet based upon equipment type, key components and industry experience of the actual useful life in the field. The evaluation was finalized in the fourth quarter of fiscal year 2003. Based upon the findings of the evaluation, the estimated useful lives of the majority of the existing compressor units were extended to 25 years from 15 years. In addition, a portion of the units remained at 15 years or less and a portion of the units were extended to 30 years. The change in useful lives was effective January 1, 2003. Had the Company depreciated all compression equipment recorded and

UNIVERSAL COMPRESSION HOLDINGS, INC.
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

1. Summary of Significant Accounting Policies (Continued)

consolidated in the Company's balance sheet as of December 31, 2002 using depreciable lives of 15 years instead of the extended estimated depreciable lives, depreciation expense would have been approximately \$5.6 million higher and would have decreased net income by approximately \$3.4 million and decreased earnings per diluted share by approximately \$.11 for the fiscal year ended March 31, 2003. The estimated useful lives as of March 31, 2004 were as follows:

Buildings	20-35 years
Compression equipment	15-30 years
Other properties and equipment	2-25 years

Maintenance and repairs are charged to expenses as incurred. Overhauls and major improvements that increase the value or extend the life of contract compressor units are capitalized and depreciated over the estimated period of 6.5 years. Depreciation expense for the years ended March 31, 2004, 2003 and 2002 was \$84.5 million, \$62.1 million and \$48.3 million, respectively.

Properties and equipment are reviewed for impairment whenever events or circumstances indicate that the carrying amount of an asset may not be recoverable based upon undiscounted cash flows. Any impairment losses are measured based upon the excess of the carrying value over the fair value. The Company has not recognized any significant impairment losses for any of the periods presented.

Goodwill

Goodwill represents the purchase price of an acquired entity in excess of the fair market value assigned to its assets and liabilities. Through March 31, 2001 goodwill was amortized on a straight-line basis over 40 years. Effective April 1, 2001 amortization of goodwill was discontinued with the adoption of Statement of Financial Accounting Standards ("SFAS") No. 142, "Goodwill and Other Intangible Assets." SFAS No. 142 addresses accounting and reporting for intangible assets acquired individually or with a group of other assets (but not those acquired in a business combination) at acquisition. It also addresses financial accounting and reporting for goodwill and other intangible assets subsequent to their acquisition.

Other Non-Current Assets

Included in other non-current assets are debt issuance costs, net of accumulated amortization, totaling approximately \$20.5 million and \$22.3 million at March 31, 2004 and 2003, respectively. Such costs are amortized over the period of the respective debt agreements on a straight-line method which approximates the effective interest method.

Stock-Based Compensation

Under SFAS No. 123, "Accounting for Stock-Based Compensation," the Company elected to measure compensation cost using the intrinsic value-based method as prescribed by Accounting Principles Board Opinion No. 25, "Accounting for Stock Issued to Employees." As such, the Company is required to make pro forma disclosures of net income and earnings per share as if the fair value based method of accounting defined by SFAS No. 123 had been applied.

UNIVERSAL COMPRESSION HOLDINGS, INC.
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

1. Summary of Significant Accounting Policies (Continued)

The following table summarizes results as if we had recorded compensation expense under the provisions of SFAS No. 123 for the 2004, 2003 and 2002 option grants:

	Year Ended March 31,		
	2004	2003	2002
	(In thousands, except per share amounts)		
Net income, as reported	\$30,787	\$33,518	\$49,408
Additional compensation expense, net of tax	\$(3,596)	\$(3,917)	\$(4,969)
Pro forma net income	\$27,191	\$29,601	\$44,439
Basic earnings per share:			
As reported	\$ 1.00	\$ 1.09	\$ 1.65
Pro forma	\$ 0.88	\$ 0.97	\$ 1.48
Diluted earnings per share:			
As reported	\$ 0.98	\$ 1.08	\$ 1.63
Pro forma	\$ 0.87	\$ 0.96	\$ 1.47

Income Taxes

The Company accounts for income taxes using an asset and liability approach that requires the recognition of deferred tax assets and liabilities for the expected future tax consequences of events that have been recognized in the Company's financial statements or tax returns. In estimating future tax consequences, all expected future events are considered other than enactments of changes in the tax law or rates.

The Company provides contract compression services to a global market. As such, the Company is subject to taxation not only in the United States but also in numerous foreign jurisdictions. Having to consider these different jurisdictions complicates the estimate of future taxable income, which in turn determines the realizability of its deferred tax assets. Numerous judgments and assumptions are inherent in the determination of future taxable income, including assumptions on future operating conditions and asset utilization. The judgments and assumptions used to determine future taxable income are consistent with those used for other financial statement purposes.

Additionally, we must consider any prudent and feasible tax planning strategies that would minimize the amount of deferred tax liabilities recognized or the amount of any valuation allowance recognized against deferred tax assets. The principal tax planning strategy available to the Company relates to the permanent reinvestment of the earnings of foreign subsidiaries. The assumptions related to the permanent reinvestment of the foreign earnings are analyzed and reviewed annually for changes in our international and domestic business outlook.

Foreign Currency Translation

The majority of the Company's foreign subsidiaries have designated the local currency as their functional currency and, as such, gains and losses resulting from financial statement translation of foreign operations are included as a separate component of other comprehensive income (loss) within stockholders' equity. Gains and losses from balances that are receivable or payable in currency other than functional currency are included in the consolidated statements of operations.

UNIVERSAL COMPRESSION HOLDINGS, INC.
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

1. Summary of Significant Accounting Policies (Continued)

Currency transaction gains and losses are reflected in the Company's consolidated statements of operations during the period incurred.

For those foreign subsidiaries that have designated the United States dollar as the functional currency, gains and losses resulting from financial statement translation of foreign operations are included in the consolidated statements of operations as incurred.

Fair Value of Financial Instruments

The Company's financial instruments consist of trade receivables and payables (which have carrying values that approximate fair value) and long-term debt. The fair value of the Company's revolving credit facility (see Note 4) is representative of its carrying value based upon variable rate terms. The fair value of the 9 $\frac{7}{8}$ % senior discount notes was approximately \$241.2 million at March 31, 2003. The fair value and the carrying amount of the 7 $\frac{1}{4}$ % senior notes due 2010 was \$175.7 million at March 31, 2004. The fair value of the senior notes due 2008 was approximately \$480.6 million and \$479.3 million at March 31, 2004 and 2003, respectively. The carrying amounts of \$82.2 million for the term loan and \$175.0 million for the notes under the ABS operating lease facility approximate the fair values. The estimated fair value amounts have been determined by the Company using appropriate valuation methodologies and information available to management as of March 31, 2004 based on the quoted market value.

Hedging and Use of Derivative Instruments

The Company utilizes interest rate swaps to minimize interest rate exposure on the \$200 million asset-backed securitization operating lease facility. The swaps are not used for trading or speculative purposes. The fair value of the interest rate swap was a liability of \$14.4 million and \$15.4 million as of March 31, 2004 and March 31, 2003, respectively.

In accordance with SFAS 133, "Accounting for Derivative Instruments and Hedging Activities," we record these interest rate swaps on the balance sheet as either assets or liabilities measured at their fair value. These instruments qualify for hedge accounting as they reduce the interest rate risk of the underlying hedged item and are designated as a cash flow hedge at inception. These swaps result in financial impacts that are inversely correlated to those of the items being hedged. To qualify for hedge accounting treatment, companies must formally document, designate and assess the effectiveness of the transactions. All of the interest rate instruments utilized are placed with a large creditworthy financial institution. If the necessary correlation ceases to exist or if physical delivery of the hedged item becomes improbable, we would discontinue hedge accounting and apply mark-to-market accounting. Amounts paid or received from interest rate swaps are charged or credited to interest expense and matched with the cash flows and interest expense of the debt being hedged, resulting in an adjustment to the effective interest rate.

In March 2004, the Company entered into interest rate swap agreements to hedge \$100 million of our \$175.0 million 7 $\frac{1}{4}$ % senior notes due 2010. The swaps are used to hedge the change in fair value of the debt and, in effect, convert the fixed interest payment to a variable interest payment based on the six-month LIBOR rate.

The swaps were accounted for in accordance with SFAS No. 133 and, as such, were recorded at fair value on the balance sheet. The fair value of the interest rate swap was a gain of \$0.7 million as of

UNIVERSAL COMPRESSION HOLDINGS, INC.
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

1. Summary of Significant Accounting Policies (Continued)

March 31, 2004. The change in the debt's fair value will also be recorded with the offset being recorded to income. The swaps, which Universal has designated as fair value hedging instruments, meet the specific hedge criteria and any changes in their fair values will be recognized in income. Because the terms of the hedged item and the swaps substantially coincide, the hedge is expected to exactly offset changes in fair values due to fluctuations in the variable rate and, therefore, Universal currently does not expect any ineffectiveness.

The counterparties to Universal's interest rate swap agreements are major international financial institutions. Universal continually monitors the credit quality of these financial institutions and does not expect non-performance by them.

Environmental Liabilities

The costs to remediate and monitor environmental matters are accrued when such liabilities are considered probable and a reasonable estimate of such costs is determinable.

Net Income Per Share

Net income per share, basic and diluted, is calculated in accordance with Statement of Financial Accounting Standards ("SFAS") No. 128, "Earnings per share."

The dilutive effect of stock options outstanding for the fiscal years ended March 31, 2004, 2003 and 2002 were 435,000, 263,000 and 242,000 shares, respectively. For the fiscal years ended March 31, 2004, 2003 and 2002 outstanding stock options of 0.8 million, 2.1 million and 1.0 million, respectively, were excluded from the computation of diluted earnings per share as the options' exercise prices were greater than the average market price of the common stock for such periods.

New Accounting Pronouncements

In January 2003, the FASB issued Interpretation No. 46 ("FIN 46"), "Consolidation of Variable Interest Entities." An entity is subject to the consolidation rules of FIN 46 and is referred to as a variable interest entity ("VIE") if the entity's equity investors lack the characteristics of a controlling financial interest or do not have sufficient equity at risk for the entity to finance its operations without additional financial support. In December 2003, the FASB issued modifications to FIN 46 ("FIN 46R"), resulting in multiple effective dates based on the nature as well as the creation date of a VIE. The adoption of the provision of FIN 46 and FIN 46R did not have a material impact on the consolidated statements of operations, cash flows or financial position.

In January 2003, the Emerging Issues Task Force (EITF) issued No. 00-21, "Accounting for Revenue Arrangements with Multiple Deliverables." This EITF establishes the criteria for recognizing revenue in arrangements when several items are bundled into one agreement. EITF 00-21 does not allow revenue recognition unless the fair value of the undelivered element(s) is available and the element has stand-alone value to the customer. EITF 00-21 also provides guidance on allocating the total contract revenue to the individual elements based upon the available fair value of each deliverable. The implementation of this pronouncement for revenue arrangements entered into after June 15, 2003 did not have a material impact on the Company's consolidated statements of operations, cash flows or financial position.

UNIVERSAL COMPRESSION HOLDINGS, INC.
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

1. Summary of Significant Accounting Policies (Continued)

On April 30, 2003, the FASB issued SFAS No. 149, "Amendment of Statement 133 on Derivative Instruments and Hedging Activities." This statement amends and clarifies accounting for derivative instruments, including certain derivative instruments embedded in other contracts, and for hedging activities under SFAS No. 133. This statement is effective for contracts entered into or modified after June 20, 2003, for hedging relationships designated after June 30, 2003, and to certain preexisting contracts. Universal adopted SFAS No. 149 on a prospective basis at its effective date on July 1, 2003. SFAS No. 149 did not have a material impact on the Company's consolidated statements of operations, cash flow, or financial position.

In May 2003, the FASB issued SFAS No. 150, "Accounting for Certain Financial Instruments with Characteristics of both Liabilities and Equity." This statement establishes standards for how an issuer classifies and measures certain financial instruments with characteristics of both liabilities and equity. This statement is effective for financial instruments entered into or modified after May 31, 2003, except for mandatorily redeemable financial instruments. Mandatorily redeemable financial instruments are subject to the provisions of this statement beginning on January 1, 2004. SFAS No. 150 did not have an impact on the Company's consolidated financial statements.

2. Goodwill

The Company's acquisitions were accounted for as purchases and accordingly, the results of operations of the acquired businesses are included in the accompanying financial statements from the dates of acquisition. Goodwill has been recognized for the amount of the excess of the purchase price over the fair value of the net assets acquired and is accounted for in accordance with SFAS 142.

The changes in the carrying amount of goodwill from March 31, 2002 to March 31, 2004, are as follows (in thousands):

	<u>Domestic Contract Compression</u>	<u>International Contract Compression</u>	<u>Aftermarket Services</u>	<u>Fabrication</u>	<u>Total</u>
Balance as of March 31, 2002 . .	\$266,097	\$40,390	\$45,234	\$28,838	\$380,559
Acquisitions	—	—	768	—	768
Purchase adjustments and other .	(4,345)	7,976	321	204	4,156
Impact of foreign currency translation	—	2,228	—	—	2,228
Balance as of March 31, 2003 . .	<u>\$261,752</u>	<u>\$50,594</u>	<u>\$46,323</u>	<u>\$29,042</u>	<u>\$387,711</u>
Acquisitions	—	—	358	—	358
Impact of foreign currency translation	—	2,302	—	—	2,302
Balance as of March 31, 2004 . .	<u>\$261,752</u>	<u>\$52,896</u>	<u>\$46,681</u>	<u>\$29,042</u>	<u>\$390,371</u>

During the fourth quarter of fiscal year 2004, we performed an impairment analysis on our goodwill in accordance with SFAS No. 142 and determined that no impairment had occurred.

UNIVERSAL COMPRESSION HOLDINGS, INC.
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

3. Inventories, Net

Inventories, net consisted of the following (in thousands):

	For the Year Ended March 31,	
	2004	2003
Raw materials	\$ 60,064	\$ 73,827
Work-in-progress	37,510	22,516
Finished goods	4,435	5,457
Total inventories	102,009	101,800
Reserve	(12,041)	(10,468)
Inventories, net	<u>\$ 89,968</u>	<u>\$ 91,332</u>

4. Long-Term Debt

The Company's debt at March 31 consisted of the following (in thousands):

	As of March 31,	
	2004	2003
Senior discount notes, bearing interest of 9 ⁷ / ₈ % per annum, due 2008, net of discount of \$0 at March 31, 2003, unsecured	\$ —	\$229,750
Senior notes, bearing interest of 7 ¹ / ₄ % per annum, due 2010	175,713	—
Senior notes due February 2008, bearing interest at 8 ⁷ / ₈ % per annum, payable semiannually on February 15 and August 15	445,000	450,000
Term loan of \$82.2 million due February 2008, currently bearing interest at a variable rate of LIBOR (1.00% at March 31, 2004), plus 3.25% due quarterly	82,181	82,181
Notes under the ABS operating lease facility are due January 2023, bearing interest at a variable rate of LIBOR, which is effectively fixed through the use of interest rate swaps at a weighted average rate of 5.4%, plus 1.27% due monthly.	175,000	175,000
Other	3,387	3,806
Total debt	881,281	940,737
Less current maturities	12,205	3,084
Total long-term debt	<u>\$869,076</u>	<u>\$937,653</u>

On February 20, 1998, Universal issued \$242.5 million of its 9⁷/₈% senior discount notes due February 15, 2008 in a private placement. The 9⁷/₈% senior discount notes were offered at a substantial discount from their principal amount. Universal subsequently exchanged the notes for publicly tradable notes pursuant to a registered exchange offer under the Securities Act.

In connection with the Weatherford Global acquisition, on February 9, 2001, the Company raised \$427 million under a seven-year term senior secured notes operating lease facility (the "high-yield operating lease facility") funded primarily through an offering of \$350 million of 8⁷/₈% senior secured notes due 2008 by an unaffiliated special operating entity that is the lessor under the operating lease

UNIVERSAL COMPRESSION HOLDINGS, INC.
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

4. Long-Term Debt (Continued)

plus approximately \$64 million in borrowings under a term loan and approximately \$13 million in proceeds from an equity investment in the lessor. On October 23, 2001, the Company increased the high-yield operating lease facility by \$122 million, which was funded through the unaffiliated entity's offering of an additional \$100 million of 8⁷/₈% senior secured notes due 2008, together with an \$18.3 million increase in its borrowings under an existing term loan and an additional \$3.7 million equity investment in the entity that is the lessor under the operating lease. The net proceeds from the sale of equipment under the addition to the high-yield operating lease facility were used to repay all of the outstanding indebtedness under the revolving credit facility, with the remaining proceeds used to repay a portion of the obligations under the asset-backed securitization operating lease facility discussed below and for general corporate purposes.

Also, in February 2001, the Company entered into a \$125 million secured revolving credit facility and a \$200 million asset-backed securitization operating lease facility (the "ABS operating lease facility"). The proceeds received in February 2001 from the high-yield operating lease facility and the ABS operating lease facility were used to restructure previous operating lease obligations and refinance certain existing indebtedness of the Company and Weatherford Global.

The senior secured credit agreement ("Credit Agreement") provides for up to \$125 million under the revolving credit facility, which includes a sub-limit for letters of credit. The revolver bears interest at Universal's option of a base rate or LIBOR plus, in each case, a variable amount depending on its operating results.

The Credit Agreement contains certain financial covenants and limitations on, among other things, acquisitions, sales, indebtedness and liens. The Credit Agreement also limits the payment of cash dividends related to Universal paying up to \$1 million to the Company in any given fiscal year. In addition, Universal has substantial dividend payment restrictions under the indenture related to the senior notes due 2010. Universal was in compliance with all such covenants and limitations at March 31, 2004 and 2003. As defined by the Credit Agreement, any "change of control" would result in an "Event of Default" and all amounts outstanding under the Credit Agreement would become due and payable. All principal amounts and accrued interest would become due without further notice.

On December 31, 2002, the Company purchased all of the equity in the lessor under the high-yield operating lease facility for \$16.7 million, plus accrued and unpaid preferred return on the equity. As a result of this equity investment by the Company in the lessor, the lessor became a fully consolidated entity of the Company as of December 31, 2002.

Also on December 31, 2002, the Company completed the process of having a nationally recognized insurance company provide to the holder of notes associated with the ABS operating lease facility a policy guaranteeing the payment of the principal and interest on the notes and obtaining a credit rating on the notes by Standard & Poor's and Moody's Investors Service. With the policy, the rating agencies rated the underlying notes "AAA" and "Aaa," respectively, resulting in a lower interest rate for the notes. Concurrently with the credit rating process, the equity in the lessor was reduced and the Company no longer considers the remaining outstanding equity of the lessor as comparable to that expected for a substantive business involved in similar leasing transactions with similar risks and rewards. Therefore, the lessor became a fully consolidated entity of the Company as of December 31, 2002. Further, concurrently with the credit rating process, the outstanding debt under the ABS operating lease facility was increased from \$159.5 million to \$175 million at December 31, 2002.

UNIVERSAL COMPRESSION HOLDINGS, INC.
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

4. Long-Term Debt (Continued)

As a result of the changes in the high-yield and ABS operating lease facilities discussed in this Note 4 and consistent with the purchase accounting rules set forth in SFAS No. 141, "Business Combinations," the Company recorded in its consolidated balance sheet approximately \$614.8 million of contract compression equipment, approximately \$707.2 million in long-term debt and a noncurrent liability of approximately \$15.2 million related to interest rate swaps pertaining to the ABS operating lease facility (see Note 8 for discussion of interest rate swaps). Additionally, upon consolidation of the lessors of these operating lease facilities, the deferred gain previously recorded was eliminated.

The Company guaranteed certain of the obligations under the operating lease facilities. The high-yield operating lease facility is collateralized by a first priority security interest in all of the assets owned by the lessor under that facility. The ABS operating lease facility is collateralized by a first priority security interest in all of the assets owned by the lessor and lessee under that facility. The assets owned by the lessee, a wholly owned subsidiary of the Company, were transferred to the lessee from the Company. As discussed above, the assets related to the high-yield and ABS operating lease facilities are included in the consolidated balance sheet.

The results of operations through December 31, 2002 includes operating lease expense since prior to this date, the lessors under the operating leases were unaffiliated entities of the Company.

In May 2003, Universal commenced a tender offer to purchase the remaining outstanding \$229.8 million aggregate principal amount of its 9 $\frac{7}{8}$ % senior discount notes due 2008 at a price equal to 104.938% of the principal amount, plus a premium of 0.412%, for notes tendered prior to the early expiration date for the tender offer. Of these notes, \$169.2 million were tendered on or before the early tender date, and Universal purchased those notes on May 27, 2003. On that date, Universal called for redemption the remaining \$60.6 million of its 9 $\frac{7}{8}$ % senior discount notes due 2008 at 104.938% of the principal amount in accordance with the terms of the indenture relating to the notes. This redemption price was 0.412% less than the total consideration offered pursuant to the tender offer for notes tendered on or before the early tender date. During June 2003, the remaining \$60.6 million of this debt was redeemed or repurchased. Due to this early extinguishment of debt, the Company recognized expenses of \$14.4 million in the first quarter of fiscal year 2004 resulting primarily from the redemption and tender premiums of \$12.0 million, write-off of unamortized debt issuance costs of \$1.9 million and \$0.5 million of other costs.

Also in May 2003, Universal issued \$175.0 million of its 7 $\frac{1}{4}$ % senior notes due 2010 in a private placement. The net proceeds from the sale, together with other available funds, were used to purchase the outstanding 9 $\frac{7}{8}$ % senior discount notes due 2008 as discussed above. Universal exchanged the private notes for publicly-traded notes in the second quarter of fiscal 2004.

The Company has property and compression equipment, with a carrying value of \$4.1 million, that has been pledged as collateral relating to notes payable with a carrying value of \$3.0 million as of March 31, 2004.

UNIVERSAL COMPRESSION HOLDINGS, INC.
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

4. Long-Term Debt (Continued)

Maturities of long-term debt as of March 31, 2004 are as follows (in thousands):

2005	\$ 12,205
2006	16,214
2007	16,237
2008	543,442
2009	16,138
Thereafter	<u>277,045</u>
Total	<u>\$881,281</u>

5. Capital Leases

Properties and equipment at March 31, 2004 and 2003 include the following amounts for capitalized leases (in thousands):

	<u>As of March 31,</u>	
	<u>2004</u>	<u>2003</u>
Compression equipment	\$3,398	\$3,546
Furniture and fixtures	2,556	2,556
Less accumulated depreciation	<u>(968)</u>	<u>(534)</u>
Net assets under capital leases	<u>\$4,986</u>	<u>\$5,568</u>

Compression equipment with a carrying value of \$2.9 million as of March 31, 2004 has been pledged as collateral relating to these capital leases.

Future minimum lease payments under non-cancelable capital leases as of March 31, 2004 are as follows (in thousands):

2005	\$2,343
2006	654
2007	110
2008	274
2009 and thereafter	<u>—</u>
Total minimum lease payments	<u>\$3,381</u>
Less imputed interest costs	<u>(220)</u>
Present value of net minimum lease payments	<u>\$3,161</u>

UNIVERSAL COMPRESSION HOLDINGS, INC.
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

6. Income Taxes

Income tax expense (benefit) for the years ended March 31, 2004, 2003 and 2002 consisted of the following (in thousands):

	<u>2004</u>	<u>2003</u>	<u>2002</u>
Current:			
Foreign	\$ 9,119	\$ 4,142	\$ 6,664
Deferred:			
Federal	6,379	13,624	25,157
State	894	1,551	272
Foreign	1,349	1,658	(1,162)
Total	<u>\$17,741</u>	<u>\$20,975</u>	<u>\$30,931</u>

A reconciliation of the provision (benefit) for income taxes and the amount computed by applying the federal statutory income tax rate to income before taxes and extraordinary item for the years ended March 31, 2004, 2003 and 2002 is as follows (in thousands):

	<u>2004</u>	<u>2003</u>	<u>2002</u>
Income tax expense at statutory rate	\$16,985	\$19,071	\$28,119
State taxes	581	1,008	177
Foreign taxes	600	149	2,491
Non-deductible expenses (benefit) and other	(425)	747	144
Total	<u>\$17,741</u>	<u>\$20,975</u>	<u>\$30,931</u>

Deferred income tax balances are the direct effect of taxable temporary differences between the financial statement carrying amounts and tax basis of assets and liabilities at the enacted tax rates expected to be in effect when the taxes are actually paid or recovered.

The Company has not provided U.S. deferred taxes against the indefinitely (permanently) reinvested cumulative earnings of our non-U.S. affiliate companies. Such amounts relate to ongoing operations and as such, with the availability of U.S. foreign tax credits, it is not practicable to determine the U.S. federal income tax liability that would be payable if such earnings were not indefinitely reinvested.

UNIVERSAL COMPRESSION HOLDINGS, INC.
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

6. Income Taxes (Continued)

The tax effects of temporary differences that give rise to deferred tax assets and deferred tax liabilities at March 31 are (in thousands):

	<u>2004</u>	<u>2003</u>
Deferred tax assets:		
Net operating loss carryforwards	\$ 128,114	\$ 117,341
Accrued reserves	5,820	1,647
Foreign tax credit	1,779	1,779
Other	9,179	3,277
Total	<u>144,892</u>	<u>124,044</u>
Valuation allowance	<u>(1,779)</u>	<u>(1,779)</u>
Total	<u><u>143,113</u></u>	<u><u>122,265</u></u>
Deferred tax liabilities:		
Depreciation differences on properties and equipment	(285,738)	(254,830)
Other	(1,110)	(5,340)
Total	<u>(286,848)</u>	<u>(260,170)</u>
Net deferred tax liability	<u><u>\$(143,735)</u></u>	<u><u>\$(137,905)</u></u>

A valuation allowance was established at March 31, 2000 against the Company's deferred tax assets related to foreign tax credits. The Company believes that it is probable that all other deferred tax assets will be realized on future tax returns, primarily from the generation of future taxable income through both profitable operations and future reversals of existing taxable temporary differences.

At March 31, 2004, the Company had net operating loss ("NOL") carryforwards of approximately \$366.0 million available to offset future taxable income. Annual utilization of the carryforwards could be limited by Section 382 of the Internal Revenue Code of 1986, as amended. If not utilized, the NOL carryforwards will expire as follows (in thousands):

2007	\$ 629
2008	1,849
2009	1,943
2010	953
2012	2
2018	4,872
2019	37,863
2020	62,218
2021	63,971
2022	94,278
2023	51,617
2024	45,846
Total	<u><u>\$366,041</u></u>

UNIVERSAL COMPRESSION HOLDINGS, INC.
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

7. Stockholders' Equity

Stock Options

In order to motivate and retain key employees, the Company established an incentive stock option plan. The incentive stock plan became effective on February 20, 1998, and on that date certain key employees were granted stock options. The options are exercisable over a ten-year period. Upon the closing of the Company's initial public offering in May 2000, all outstanding options were accelerated and became fully vested. All other options generally vest over the following time period:

Year 1	33⅓%
Year 2	33⅓%
Year 3	33⅓%

The Company has elected to follow Accounting Principles Board ("APB") No. 25, "Accounting for Stock Issued to Employees" and related interpretations in accounting for its stock-based compensation and to provide the disclosures required under SFAS No. 123, Accounting for Stock Based Compensation and SFAS No. 148, "Accounting for Stock-Based Compensation-Transition and Disclosure-an amendment of SFAS No. 123."

APB No. 25 requires no recognition of compensation expense for the stock-based compensation arrangements provided by the Company, namely option grants where the exercise price is equal to the market value at the date of grant. However, APB No. 25 requires recognition of compensation expense for variable award plans over the vesting periods of such plans, based upon the then-current market values of the underlying stock. In contrast, SFAS No. 123 requires recognition of compensation expense for grants of stock, stock options, and other equity instruments, over the vesting periods of such grants, based on the estimated grant-date fair values of those grants.

Under the incentive stock option plan, options to purchase common stock may be granted until 2011. Options generally are granted at fair market value at the date of grant, are exercisable in installments beginning one year from the date of grant, and expire 10 years after the date of grant.

UNIVERSAL COMPRESSION HOLDINGS, INC.
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

7. Stockholders' Equity (Continued)

As of March 31, 2004, 2,439,015 stock options were outstanding under the plan. Transactions are summarized as follows:

	<u>Stock Options</u>	<u>Weighted-Average Exercise Price</u>
Options outstanding, March 31, 2001	1,311,544	\$21.63
Granted	1,545,500	25.66
Exercised	(109,419)	10.04
Cancelled	(13,379)	19.00
Options outstanding, March 31, 2002	<u>2,734,246</u>	<u>\$24.52</u>
Granted	659,750	17.12
Exercised	(22,841)	7.03
Cancelled	(460,789)	26.93
Options outstanding, March 31, 2003	<u>2,910,366</u>	<u>\$22.66</u>
Granted	5,000	\$20.97
Exercised	(350,746)	21.75
Cancelled	(125,605)	26.56
Options outstanding, March 31, 2004	<u>2,439,015</u>	<u>\$22.56</u>
Options exercisable at March 31, 2002	570,280	\$17.94
Options exercisable at March 31, 2003	1,310,676	\$22.81
Options exercisable at March 31, 2004	1,700,296	\$23.06

Exercise prices for options outstanding as of March 31, 2004 ranged from \$6.73 to \$37.95. The following table provides certain information with respect to stock options outstanding at March 31, 2004:

<u>Range of Exercise Prices</u>	<u>Stock Options Outstanding</u>	<u>Weighted Average Exercise Price</u>	<u>Weighted Average Remaining Contractual Life</u>
Under \$7.00	191,450	\$ 6.73	3.9
\$7.01-\$19.00	526,277	16.85	8.9
\$19.01-\$22.00	929,191	21.28	7.4
Over \$22.00	792,097	31.70	7.0
	<u>2,439,015</u>	<u>\$22.56</u>	<u>7.3</u>

UNIVERSAL COMPRESSION HOLDINGS, INC.
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

7. Stockholders' Equity (Continued)

The following table provides certain information with respect to stock options exercisable at March 31, 2004:

<u>Range of Exercise Prices</u>	<u>Stock Options Exercisable</u>	<u>Weighted Average Exercise Price</u>
Under \$7.00	191,450	\$ 6.73
\$7.01-\$19.00	197,234	16.83
\$19.01-\$22.00	673,808	21.40
Over \$22.00	637,804	31.64
	<u>1,700,296</u>	<u>\$23.06</u>

In electing to continue to follow APB No. 25 for expense recognition purposes, the Company is obligated to provide the expanded disclosures required under SFAS No. 123 for stock-based compensation granted in 1998 and thereafter, including, if materially different from reported results disclosure of pro forma net income and earnings per share had compensation expense relating to 2002, 2003, and 2004 grants been measured under the fair value recognition provisions of SFAS No. 123.

The weighted-average fair values at date of grant for options granted during 2004, 2003 and 2002 were \$10.16, \$9.78 and \$10.41, respectively, and were estimated using the Black-Scholes option valuation model with the following weighted-average assumptions:

	<u>2004</u>	<u>2003</u>	<u>2002</u>
Expected life in years	7	8	3
Interest rate	3.56%	3.50%	4.95%
Volatility	42.88%	48.85%	54.00%
Dividend yield	0.00%	0.00%	0.00%

The following table summarizes results as if we had recorded compensation expense under the provisions of SFAS No. 123 for the 2004, 2003 and 2002 option grants:

	<u>Year Ended March 31,</u>		
	<u>2004</u>	<u>2003</u>	<u>2002</u>
	<u>(In thousands except per share amounts)</u>		
Net income, as reported	\$30,787	\$33,518	\$49,408
Additional compensation expense, net of tax	\$ 3,596	\$ 3,917	\$ 4,969
Pro forma net income	\$27,191	\$29,601	\$44,439
Basic earnings per share:			
As reported	\$ 1.00	\$ 1.09	\$ 1.65
Pro forma	\$ 0.88	\$ 0.97	\$ 1.48
Diluted earnings per share:			
As reported	\$ 0.98	\$ 1.08	\$ 1.63
Pro forma	\$ 0.87	\$ 0.96	\$ 1.47

UNIVERSAL COMPRESSION HOLDINGS, INC.
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

8. Accounting for Interest Rate Swaps

In accordance with SFAS No. 133, all derivative instruments must be recognized in the balance sheet at fair value, and changes in such fair values are recognized in earnings unless specific hedging criteria are met. Changes in the values of derivatives that meet these hedging criteria will ultimately offset related earnings effects of the hedged item pending recognition in earnings.

As of March 31, 2004, the Company had interest rate swaps to convert variable interest payments related to the \$175 million under the ABS operating lease facility to fixed interest payments. These swaps terminate in February 2013 and have a weighted average fixed rate of 5.4% and total notional amount of \$175 million. As of December 31, 2002, the lessor related to the operating lease facility became a consolidated entity and the swaps were included in the Company's consolidated financial statements. In accordance with SFAS No. 133, the Company has recorded a \$14.4 million noncurrent liability related to the derivative instrument as of March 31, 2004. Consistent with accounting rules discussed in SFAS No. 141, "Business Combinations," the offsetting amount was recorded as an increase to the value of property, plant and equipment.

The swaps, which the Company has designated as cash flow hedging instruments, meet the specific hedge criteria and any changes in their fair values are recognized in other comprehensive income or loss. Because the terms of the hedged item and the swaps substantially coincide, the hedge is expected to exactly offset changes in expected cash flows due to fluctuations in the variable rate and therefore, the Company currently does not expect any ineffectiveness.

In March 2004, the Company entered into interest rate swap agreements to hedge \$100 million of our \$175.0 million 7¼% senior notes due 2010. The swaps are used to hedge the change in fair value of the debt and, in effect, convert the fixed interest payment to a variable interest payment based on the six-month LIBOR rate.

The swaps will be accounted for in accordance with SFAS No. 133 and, as such, will be recorded at fair value on the balance sheet. The change in the debt's fair value will also be recorded with the offset being recorded to income. The swaps, which the Company has designated as fair value hedging instruments, meet the specific hedge criteria and any changes in their fair values will be recognized in income. Because the terms of the hedged item and the swaps substantially coincide, the hedge is expected to exactly offset changes in fair values due to fluctuations in the variable rate and, therefore, the Company currently does not expect any ineffectiveness.

The counterparties to the Company's interest rate swap agreements are major international financial institutions. Universal continually monitors the credit quality of these financial institutions and does not expect non-performance by them.

9. Employee Benefits

The Company has a defined contribution 401(k) plan covering substantially all employees. The Company makes matching contributions under this plan equal to 50% of each participant's contribution of up to 6% of the participant's compensation. In September 2001, the Company amended its 401(k) plan for all domestic employees. The amended plan allows the Company to make matching contributions in the form of Company stock, instead of cash. For the fiscal years ended 2004 and 2003, the Company stock contributions to the plan were approximately \$1.6 million, respectively.

The Employee Stock Purchase Plan ("ESPP") is intended to encourage employees to participate in the Company's growth by providing them the opportunity to acquire a proprietary interest in the

UNIVERSAL COMPRESSION HOLDINGS, INC.
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

9. Employee Benefits (Continued)

Company's long-term performance and success through the purchase of shares of common stock at a price possibly less than fair market value. In 2001, the Company's stockholders approved the ESPP, under which 250,000 shares of the Company's common stock could be purchased by employees. An employee is eligible to participate after completing 90 days of employment. Each quarter, an eligible employee may elect to withhold up to 10% of his or her salary to purchase shares of the Company's common stock at a price equal to 85% to 100% of the fair market value of the stock as of the first day of the quarter or the last day of the quarter, whichever is lower. The ESPP will terminate on the date that all shares of common stock authorized for sale under the ESPP have been purchased, except as otherwise extended by authorizing additional shares under the ESPP. At March 31, 2004, 158,431 shares remained available for purchase under the ESPP. During 2004 and 2003, \$0.8 million was charged to expense relating to the ESPP, respectively.

The Company utilizes grants of restricted stock as long-term compensation for its executive officers. The Company's restricted stock plan provides for the award of up to 350,000 shares of the Company's common stock to certain officers and key employees. Unearned compensation was charged for the market value of the restricted shares as these shares were issued in accordance with the restricted stock plan. The unearned compensation is shown as a reduction on stockholders' equity in the accompanying consolidated balance sheets and is being amortized ratably over the restricted period of five years. During fiscal years ending March 31, 2004 and 2003, \$0.6 million and \$0.3 million, respectively, were charged to expense relating to the restricted stock. The weighted average share price during 2004 and 2003 was \$17.00. Generally, common stock subject to restricted stock grants will vest 0% upon the first anniversary of the grant and 25% on each anniversary thereafter through the fifth anniversary.

The Employees' Supplemental Savings Plan, (the "ESSP") provides executive officers the opportunity to defer up to 25% of their compensation that cannot be deferred under the existing 401(k) plan due to IRS limitations. Participants can also defer up to 100% of their bonuses. The Company matches 50% of the first 6% of compensation, excluding any bonus deferred. The vesting periods are generally the same as the 401(k) plan. Prior to September 1, 2002, the Company's matching contributions were in the form of cash. Since September 1, 2002, the Company's matching contributions related to the Employees' Supplemental Savings Plan have been in the form of common stock. During 2004 and 2003, amounts charged to expense relating to the ESSP were insignificant.

10. Facility Consolidation Costs

On April 28, 2003, the Company announced the transfer of substantially all of its fabrication activities based in Tulsa, Oklahoma to its existing facility in Houston, Texas. Engineering, production and related support functions were consolidated with Houston-based functions. The Company did not incur additional costs related to this consolidation during the last half of the fiscal year ended March 31, 2004 and the Company does not expect to incur additional facility consolidation costs during the two-year period ending September 30, 2005. Total costs related to the facility consolidation were \$1.8 million during the fiscal year ended March 31, 2004 and are shown separately as facility

UNIVERSAL COMPRESSION HOLDINGS, INC.
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

10. Facility Consolidation Costs (Continued)

consolidation costs in the consolidated statements of operations. The costs incurred were related to the fabrication segment. See below for further details of the costs incurred (in thousands):

	<u>Fiscal Year Ended March 31, 2004</u>
Severance and personnel costs	\$1,131
Relocation costs	289
Other costs	<u>401</u>
Total facility consolidation costs	<u>\$1,821</u>

11. Commitments and Contingencies

In the ordinary course of business, the Company is involved in various pending or threatened legal actions. In the opinion of management, the amount of ultimate liability, if any, with respect to these actions will not have a materially adverse effect on the Company's financial position, operating results or cash flows.

In December 1999, Weatherford Global sold the assets and properties of its Gemini compressor business in Corpus Christi, Texas to GE Packaged Power, L.P., or GEPP. As part of that sale, Weatherford Global entered into an agreement to purchase from GEPP \$38.0 million of compressor components over five years and \$3.0 million of parts over three years, and GEPP agreed to provide compressors to Weatherford Global during that time period at negotiated prices. We assumed this obligation in connection with our acquisition of Weatherford Global in February 2001. As of March 31, 2004, approximately \$25.9 million of components and approximately \$13.5 million of parts have been purchased from GEPP. As a result of GEPP product performance issues, we have been unable to satisfy and have not satisfied in full our purchase commitment in respect of components under this agreement with GEPP. The unsatisfied portion of the purchase commitment is approximately \$12.1 million. GEPP could assert its right to enforce this obligation, but has not indicated any interest to do so at this time. However, if GEPP should seek to enforce this obligation, we believe we have valid defenses and counter claims and would aggressively defend against such enforcement and pursue such counter claims.

The Company has no other commitments or contingent liabilities, which, in the judgment of management, would result in losses that would materially affect the Company's consolidated financial position or operating results.

12. Industry Segments and Geographic Information

The Company has four principal business segments: domestic contract compression, international contract compression, fabrication and aftermarket services. The domestic contract compression segment provides natural gas compression to customers in the United States. The international contract compression segment provides natural gas compression to international customers, including Canada. The fabrication segment provides services related to the design, engineering and assembly of natural gas and air compressors for sale to third parties in addition to those that the Company uses in its contract compression fleet. The aftermarket services segment sells parts and components and provides maintenance to customers who own compression equipment and customers who utilize equipment from

UNIVERSAL COMPRESSION HOLDINGS, INC.
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

12. Industry Segments and Geographic Information (Continued)

the Company's competitors. Fabrication and aftermarket services revenue presented in the table below include only sales to third parties.

The Company's reportable segments are strategic business units that offer distinct products and services. They are managed separately since each business segment requires different marketing strategies due to customer specifications. The Company evaluates the performance of its reportable segments based on segment gross profit. Gross profit is defined as total revenue less direct costs. The Company has no material sales between segments and, accordingly, there is no inter-segment revenue to be reported.

The following table presents revenue, gross profit and total assets by business segment for the fiscal years ended March 31, 2004, 2003 and 2002 (in thousands):

	For the Year Ended March 31,		
	2004	2003	2002
Revenue:			
Domestic contract compression	\$ 280,951	\$ 265,465	\$ 267,550
International contract compression	82,589	66,505	60,185
Fabrication	183,685	162,678	211,265
Aftermarket services	141,561	130,570	140,989
Total	<u>\$ 688,786</u>	<u>\$ 625,218</u>	<u>\$ 679,989</u>
Gross Profit:			
Domestic contract compression	\$ 178,543	\$ 169,868	\$ 169,892
International contract compression	64,159	53,769	43,411
Fabrication	15,888	16,075	24,347
Aftermarket services	30,891	28,256	30,696
Total	<u>\$ 289,481</u>	<u>\$ 267,968</u>	<u>\$ 268,346</u>
Depreciation and amortization	85,650	63,706	48,600
Selling, general and administrative	67,516	67,944	60,890
Operating lease expense	—	46,071	55,401
Interest expense, net	73,475	36,421	23,017
Debt extinguishment costs	14,903	—	—
Foreign currency (gain)/loss	(529)	459	(42)
Other (income)/expense, net	(1,883)	(1,126)	141
Facility consolidation costs	1,821	—	—
Income before income taxes	<u>\$ 48,528</u>	<u>\$ 54,493</u>	<u>\$ 80,339</u>
Identifiable Assets:			
Domestic contract compression	\$1,453,716	\$1,497,231	\$ 808,583
International contract compression	258,240	209,141	206,610
Fabrication	107,605	103,468	115,877
Aftermarket services	152,890	144,047	146,095
Total	<u>\$1,972,451</u>	<u>\$1,953,887</u>	<u>\$1,277,165</u>

UNIVERSAL COMPRESSION HOLDINGS, INC.
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

12. Industry Segments and Geographic Information (Continued)

No one customer accounted for more than 10% of net sales for any of the periods presented.

Geographic Area

The following table illustrates revenue, gross profit and total assets by geographic locations for the fiscal years ended March 31, 2004, 2003 and 2002 (in thousands). The basis of attributing revenue and gross profit to specific geographic locations is primarily based upon the geographic location of the sale, service or where the assets are utilized.

	For the Year Ended March 31,		
	2004	2003	2002
Revenue:			
United States	\$ 493,262	\$ 449,480	\$ 524,475
Canada	90,198	74,293	91,615
Latin America	71,320	62,937	55,909
Asia Pacific	34,006	38,508	7,990
Total	<u>\$ 688,786</u>	<u>\$ 625,218</u>	<u>\$ 679,989</u>
Gross Profit:			
United States	\$ 212,602	\$ 198,869	\$ 212,309
Canada	16,238	15,219	17,150
Latin America	50,300	41,770	32,480
Asia Pacific	10,341	12,110	6,407
Total	<u>\$ 289,481</u>	<u>\$ 267,968</u>	<u>\$ 268,346</u>
Depreciation and amortization	85,650	63,706	48,600
Selling, general and administrative	67,516	67,944	60,890
Operating lease expense	—	46,071	55,401
Interest expense, net	73,475	36,421	23,017
Debt extinguishment costs	14,903	—	—
Foreign currency (gain)/loss	(529)	459	(42)
Other (income)/expense, net	(1,883)	(1,126)	141
Facility consolidation costs	1,821	—	—
Income before income taxes	<u>\$ 48,528</u>	<u>\$ 54,493</u>	<u>\$ 80,339</u>
Identifiable Assets:			
United States	\$1,667,163	\$1,703,001	\$1,058,332
Canada	96,116	90,076	85,335
Latin America	158,263	121,872	102,499
Asia Pacific	50,909	38,938	30,999
Total	<u>\$1,972,451</u>	<u>\$1,953,887</u>	<u>\$1,277,165</u>

UNIVERSAL COMPRESSION HOLDINGS, INC.
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

13. Selected Quarterly Financial Data (Unaudited)

Summarized quarterly financial data for the fiscal years ended March 31, 2004 and 2003 is as follows (in thousands, except per share data):

	<u>March 31</u>	<u>December 31</u>	<u>September 30</u>	<u>June 30</u>
2004:				
Revenue	\$190,710	\$170,167	\$175,682	\$152,227
Gross profit	76,788	72,580	71,912	68,199
Net income (loss)	11,725	11,733	9,303	(1,969)
Earnings per common share—basic	\$ 0.38	\$ 0.38	\$ 0.30	\$ (0.06)
Earnings per common share—diluted	\$ 0.37	\$ 0.38	\$ 0.30	\$ (0.06)
2003:				
Revenue	\$154,589	\$164,584	\$154,582	\$151,464
Gross profit	68,682	66,751	64,816	67,718
Net income	6,923	8,583	7,659	10,351
Earnings per common share—basic	\$ 0.23	\$ 0.28	\$ 0.25	\$ 0.34
Earnings per common share—diluted	\$ 0.22	\$ 0.28	\$ 0.25	\$ 0.33

REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

To the Board of Directors of
Universal Compression, Inc.

We have audited the accompanying consolidated balance sheets of Universal Compression, Inc. and subsidiaries (the "Company") as of March 31, 2004 and 2003, and the related consolidated statements of operations, stockholders' equity, and cash flows for each of the three years in the period ended March 31, 2004. Our audits also included the financial statement schedule listed in the Index at E-1, which represents Schedule II to the consolidated financial statements of the Company. These financial statements and financial statement schedule are the responsibility of the Company's management. Our responsibility is to express an opinion on the financial statements and financial statement schedule based on our audits.

We conducted our audits in accordance with standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, such consolidated financial statements present fairly, in all material respects, the financial position of the Company as of March 31, 2004 and 2003, and the results of its operations and its cash flows for each of the three years in the period ended March 31, 2004, in conformity with accounting principles generally accepted in the United States of America. Also, in our opinion, such financial statement schedule, when considered in relation to the basic consolidated financial statements taken as a whole, presents fairly in all material respects the information set forth therein.

/s/ DELOITTE & TOUCHE LLP

Houston, Texas
June 4, 2004

UNIVERSAL COMPRESSION, INC.
CONSOLIDATED BALANCE SHEETS
(In thousands)

	March 31, 2004	March 31, 2003
ASSETS		
Current assets:		
Cash and cash equivalents	\$ 121,189	\$ 71,693
Accounts receivable, net of allowance for bad debts of \$3,189 and \$8,146 as of March 31, 2004 and 2003, respectively	79,587	77,565
Current portion of notes receivable	709	2,722
Inventories, net of reserve for obsolescence of \$12,041 and \$10,468 as of March 31, 2004 and 2003, respectively	89,968	91,332
Current deferred tax asset	5,819	10,890
Other	13,938	7,108
Total current assets	311,210	261,310
Contract compression equipment	1,344,218	1,316,214
Other property	117,128	106,496
Accumulated depreciation and amortization	(216,569)	(145,916)
Net property, plant and equipment	1,244,777	1,276,794
Goodwill	390,371	387,480
Notes receivable	444	2,555
Other non-current assets	25,649	25,367
Total assets	<u>\$1,972,451</u>	<u>\$1,953,506</u>
LIABILITIES AND STOCKHOLDER'S EQUITY		
Current liabilities:		
Accounts payable, trade	\$ 44,948	\$ 43,210
Accrued liabilities	40,765	32,513
Unearned Revenue	25,596	13,272
Accrued interest	10,933	9,934
Current portion of long-term debt and capital lease obligations	14,369	4,322
Total current liabilities	136,611	103,251
Capital lease obligations	997	3,180
Long-term debt	869,076	937,653
Non-current deferred tax liability	149,554	153,166
Derivative financial instrument used for hedging purposes	14,423	15,404
Other liabilities	2,555	1,349
Total liabilities	1,173,216	1,214,003
Commitments and contingencies (Note 10)		
Stockholder's equity:		
Common stock, \$10 par value, 5.0 shares authorized, 4.9 issued and outstanding as of March 31, 2004 and 2003	49	49
Additional paid-in capital	725,694	710,349
Other comprehensive loss	(35,344)	(48,944)
Retained earnings	108,836	78,049
Total stockholder's equity	799,235	739,503
Total liabilities and stockholder's equity	<u>\$1,972,451</u>	<u>\$1,953,506</u>

See accompanying notes to consolidated financial statements.

UNIVERSAL COMPRESSION, INC.
CONSOLIDATED STATEMENTS OF OPERATIONS
(In thousands)

	For the Year Ended March 31,		
	2004	2003	2002
Revenue:			
Domestic contract compression	\$280,951	\$265,465	\$267,550
International contract compression	82,589	66,505	60,185
Fabrication	183,685	162,678	211,265
Aftermarket services	141,561	130,570	140,989
Total revenue	<u>688,786</u>	<u>625,218</u>	<u>679,989</u>
Costs and expenses:			
Domestic contract compression—direct costs	102,408	95,597	97,658
International contract compression—direct costs	18,430	12,736	16,774
Fabrication—direct costs	167,797	146,603	186,918
Aftermarket services—direct costs	110,670	102,314	110,293
Depreciation and amortization	85,650	63,706	48,600
Selling, general and administrative	67,516	67,944	60,890
Operating lease expense	—	46,071	55,401
Interest expense, net	73,475	36,421	23,017
Debt extinguishment costs	14,903	—	—
Foreign currency (gain)/loss	(529)	459	(42)
Other (income)/expense, net	(1,883)	(1,126)	141
Facility consolidation costs	1,821	—	—
Total costs and expenses	<u>640,258</u>	<u>570,725</u>	<u>599,650</u>
Income before income taxes	48,528	54,493	80,339
Income tax expense	17,741	20,975	30,931
Net income	<u>\$ 30,787</u>	<u>\$ 33,518</u>	<u>\$ 49,408</u>

See accompanying notes to consolidated financial statements.

UNIVERSAL COMPRESSION, INC.
CONSOLIDATED STATEMENTS OF STOCKHOLDER'S EQUITY
For the years ended March 31, 2004, 2003 and 2002
(In thousands)

	<u>Common Stock</u>	<u>Additional Paid in Capital</u>	<u>Retained Earnings (Deficit)</u>	<u>Other Comprehensive Income (loss)</u>	<u>Total</u>
Balance, March 31, 2001	<u>\$49</u>	<u>\$651,607</u>	<u>\$ (4,877)</u>	<u>\$ 845</u>	<u>\$647,624</u>
Investment in subsidiary by parent	—	36,726	—	—	36,726
Acquisitions	—	20,000	—	—	20,000
Net income	—	—	49,408	—	49,408
Foreign currency translation adjustment ..	—	—	—	(58,362)	(58,362)
Comprehensive loss	—	—	—	—	(8,954)
Balance, March 31, 2002	<u>\$49</u>	<u>\$708,333</u>	<u>\$ 44,531</u>	<u>\$(57,517)</u>	<u>\$695,396</u>
Investment in subsidiary by parent	—	2,016	—	—	2,016
Net income	—	—	33,518	—	33,518
Foreign currency translation adjustment ..	—	—	—	9,139	9,139
Interest rate swap loss	—	—	—	(566)	(566)
Comprehensive income	—	—	—	—	42,091
Balance, March 31, 2003	<u>\$49</u>	<u>\$710,349</u>	<u>\$ 78,049</u>	<u>\$(48,944)</u>	<u>\$739,503</u>
Investment in subsidiary by parent	—	15,345	—	—	15,345
Net income	—	—	30,787	—	30,787
Foreign currency translation adjustment ..	—	—	—	14,141	14,141
Interest rate swap loss	—	—	—	(541)	(541)
Comprehensive income	—	—	—	—	44,387
Balance, March 31, 2004	<u>\$49</u>	<u>\$725,694</u>	<u>\$108,836</u>	<u>\$(35,344)</u>	<u>\$799,235</u>

See accompanying notes to consolidated financial statements.

UNIVERSAL COMPRESSION, INC.
CONSOLIDATED STATEMENTS OF CASH FLOWS
(In thousands)

	For the Year Ended March 31,		
	2004	2003	2002
Cash flows from operating activities:			
Net income	\$ 30,787	\$ 33,518	\$ 49,408
Adjustments to reconcile net income to cash provided by operating activities, net of effect of acquisitions:			
Depreciation and amortization	85,650	63,706	48,600
Loss on early extinguishment of debt	14,903	—	—
Gain on asset sales	(965)	(741)	(286)
Amortization of debt issuance costs	4,297	3,670	3,006
Accretion of discount notes	—	18,660	20,073
Increase in deferred taxes	7,811	18,058	20,827
(Increase) decrease in other assets	(2,963)	12,913	21,225
(Increase) decrease in receivables	(1,338)	37,105	(10,404)
(Increase) decrease in inventories	4,999	11,871	40,048
Increase (decrease) in accounts payable	1,013	(2,004)	(44,947)
Increase (decrease) in accrued liabilities	5,742	(10,874)	(24,699)
Increase (decrease) in unearned revenue	12,324	(2,778)	9,742
Increase (decrease) in accrued interest	999	3,048	(756)
Net cash provided by operating activities	163,259	186,152	131,837
Cash flows from investing activities:			
Additions to property, plant and equipment	(86,557)	(120,751)	(188,019)
Cash paid for acquisitions	(761)	(1,536)	(160,021)
Proceeds from sale of property, plant and equipment	40,468	14,583	187,784
Net cash used in investing activities	(46,850)	(107,704)	(160,256)
Cash flows from financing activities:			
Principal repayments of long-term debt	(234,750)	(5,818)	(7,401)
Proceeds from issuance of debt	175,000	—	—
Net proceeds (repayment) on sale-leaseback of vehicles	—	(2,800)	(2,878)
Debt extinguishment premium and cost	(12,920)	—	—
Investment in subsidiary by parent	10,397	2,016	36,726
Debt issuance costs	(4,640)	(5,009)	(4,131)
Operating lease facilities	—	(1,320)	—
Net cash provided by (used in) financing activities	(66,913)	(12,931)	22,316
Net increase (decrease) in cash and cash equivalents	49,496	65,517	(6,103)
Cash and cash equivalents at beginning of period	71,693	6,176	12,279
Cash and cash equivalents at end of period	121,189	\$ 71,693	\$ 6,176
Supplemental disclosure of cash flow information:			
Cash paid for interest	\$ 77,472	\$ 14,553	\$ 4,073
Cash paid for operating leases	—	\$ 41,171	\$ 54,301
Cash paid for income taxes	\$ 6,480	\$ 2,572	\$ 1,346
Supplemental schedule of non-cash investing and financing activities:			
Changes due to the consolidation of operating lease facilities:			
Additions to property, plant and equipment	—	\$ 614,800	—
Increase in debt	—	\$ 707,200	—
Noncurrent liability assumed	—	\$ 15,200	—
Elimination of deferred gain	—	\$ 107,600	—

See accompanying notes to consolidated financial statements.

UNIVERSAL COMPRESSION, INC.
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

1. Summary of Significant Accounting Policies

Organization

Universal Compression, Inc. was formed on December 12, 1997 for the purpose of acquiring Tidewater Compression Service, Inc. ("TCS") from Tidewater Inc. Upon completion of the acquisition on February 20, 1998, TCS changed its name to Universal Compression, Inc. ("Universal"). Universal is a wholly owned subsidiary of Universal Compression Holdings, Inc. ("Holdings").

Universal has completed several acquisitions, which have contributed significantly to our growth. Our most significant acquisition was that of Weatherford Global Compression Services, L.P. and certain related entities ("Weatherford Global"), former subsidiaries of Weatherford International Ltd. ("Weatherford"), in February 2001. This added approximately 950,000 horsepower, more than doubling our size at that time.

Nature of Operations

Universal is the second largest natural gas compression services company in the world in terms of compressor fleet horsepower, with a fleet as of March 31, 2004 of approximately 7,100 compressor units comprising approximately 2.3 million horsepower. Universal provides a full range of contract compression services, sales, operations, maintenance and fabrication services and products to the natural gas industry, both domestically and internationally. These services and products are essential to the natural gas industry, as gas must be compressed to be delivered from the wellhead to end-users.

Principles of Consolidation

The accompanying consolidated financial statements include Universal and its wholly-owned subsidiaries. All significant intercompany accounts and transactions have been eliminated in consolidation.

Reclassifications

Certain reclassifications have been made to the prior year amounts to conform to the current year presentation.

Use of Estimates

In preparing Universal's financial statements, management makes estimates and assumptions that affect the amounts reported in the financial statements and related disclosures. Actual results may differ from these estimates.

Cash and Cash Equivalents

Universal considers all highly liquid investments purchased with an original maturity of three months or less to be cash equivalents. Cash flows are computed using the indirect method.

Revenue Recognition

Revenue is recognized by Universal's four reportable business segments using the following criteria: (a) persuasive evidence of an exchange arrangement exists, (b) delivery has occurred or

UNIVERSAL COMPRESSION, INC.
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

1. Summary of Significant Accounting Policies (Continued)

services have been rendered, (c) the buyer's price is fixed or determinable and (d) collectibility is reasonably assured.

Revenue from contract compression services is recorded when earned over the period of service and maintenance contracts which generally range from one month to several years. Aftermarket services revenue is recorded as products are delivered or services are performed for the customer. Fabrication revenue is recognized using the completed-contract method which recognizes revenue upon completion of the contract. This method is used because the typical contract is completed within two to three months.

Concentration of Credit Risk

Trade accounts receivable are due from companies of varying size engaged principally in oil and gas activities in the United States and in international locations including Canada, Latin America and Asia Pacific. Universal reviews the financial condition of customers prior to extending credit and periodically updates customer credit information. Payment terms are on a short-term basis and in accordance with industry standards. No single customer accounts for 10% or more of Universal's revenue. For the years ended March 31, 2004, 2003 and 2002, Universal wrote off bad debts, net of recoveries totaling \$5.6 million, \$4.3 million, and \$0.1 million respectively.

Inventories

Inventories are recorded at the lower of average cost or market (net realizable value). Some items of compression equipment are acquired and placed in inventories for subsequent sale or compression services to others. Acquisitions of these assets are considered operating activities in the statement of cash flows.

Properties and Equipment

Property, plant and equipment are carried at cost. Depreciation for financial reporting purposes is computed on the straight-line basis using estimated useful lives. For compression equipment, depreciation begins with the first compression service using a 20% salvage value. During the fiscal year 2002, Universal evaluated the estimated useful lives used for book depreciation purposes for its compressor fleet based upon equipment type, key components and industry experience of the actual useful life in the field. The evaluation was finalized in the fourth quarter of fiscal year 2003. Based upon the findings of the evaluation, the estimated useful lives of the majority of the existing compressor units were extended to 25 years from 15 years. In addition, a portion of the units remained at 15 years or less and a portion of the units were extended to 30 years. The change in useful lives was effective January 1, 2003. Had Universal depreciated all compression equipment recorded and consolidated in its balance sheet as of December 31, 2002 using depreciable lives of 15 years instead of the extended estimated depreciable lives, depreciation expense would have been approximately \$5.6 million higher and would have decreased net income by approximately \$3.4 million for the fiscal year ended March 31, 2003. The estimated useful lives as of March 31, 2004 were as follows:

Buildings	20-35 years
Compression equipment	15-30 years
Other properties and equipment	2-25 years

UNIVERSAL COMPRESSION, INC.
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

1. Summary of Significant Accounting Policies (Continued)

Maintenance and repairs are charged to expenses as incurred. Overhauls and major improvements that increase the value or extend the life of contract compressor units are capitalized and depreciated over the estimated period of 6.5 years. Depreciation expense for the years ended March 31, 2004, 2003 and 2002 was \$84.5 million, \$62.1 million and \$48.3 million, respectively.

Properties and equipment are reviewed for impairment whenever events or circumstances indicate that the carrying amount of an asset may not be recoverable based upon undiscounted cash flows. Any impairment losses are measured based upon the excess of the carrying value over the fair value. Universal has not recognized any significant impairment losses for any of the periods presented.

Goodwill

Goodwill represents the purchase price of an acquired entity in excess of the fair market value assigned to its assets and liabilities. Through March 31, 2001 goodwill was amortized on a straight-line basis over 40 years. Effective April 1, 2001 Universal discontinued amortization of goodwill with Universal's adoption of Statement of Financial Accounting Standards ("SFAS") No. 142, "Goodwill and Other Intangible Assets." SFAS No. 142 addresses accounting and reporting for intangible assets acquired individually or with a group of other assets (but not those acquired in a business combination) at acquisition. It also addresses financial accounting and reporting for goodwill and other intangible assets subsequent to their acquisition.

Other Non-Current Assets

Included in other non-current assets are debt issuance costs, net of accumulated amortization, totaling approximately \$20.5 million and \$22.3 million at March 31, 2004 and 2003, respectively. Such costs are amortized over the period of the respective debt agreements on a straight-line method which approximates the effective interest method.

Income Taxes

Universal accounts for income taxes using an asset and liability approach that requires the recognition of deferred tax assets and liabilities for the expected future tax consequences of events that have been recognized in Universal's financial statements or tax returns. In estimating future tax consequences, all expected future events are considered other than enactments of changes in the tax law or rates.

Universal provides contract compression services to a global market. As such, Universal is subject to taxation not only in the United States but also in numerous foreign jurisdictions. Having to consider these different jurisdictions complicates the estimate of future taxable income, which in turn determines the realizability of its deferred tax assets. Numerous judgments and assumptions are inherent in the determination of future taxable income, including assumptions on future operating conditions and asset utilization. The judgments and assumptions used to determine future taxable income are consistent with those used for other financial statement purposes.

Additionally, Universal must consider any prudent and feasible tax planning strategies that would minimize the amount of deferred tax liabilities recognized or the amount of any valuation allowance recognized against deferred tax assets. The principal tax planning strategy available to Universal relates to the permanent reinvestment of the earnings of foreign subsidiaries. The assumptions related to the

UNIVERSAL COMPRESSION, INC.
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

1. Summary of Significant Accounting Policies (Continued)

permanent reinvestment of the foreign earnings are analyzed and reviewed annually for changes in Universal's international and domestic business outlook.

Foreign Currency Translation

The majority of Universal's foreign subsidiaries have designated the local currency as their functional currency and, as such, gains and losses resulting from financial statement translation of foreign operations are included as a separate component of accumulated other comprehensive loss within stockholder's equity. Gains and losses from balances that are receivable or payable in currency other than functional currency are included in the consolidated statements of operations.

Currency transaction gains and losses are reflected in Universal's consolidated statements of operations during the period incurred.

For those foreign subsidiaries that have designated the United States dollar as the functional currency, gains and losses resulting from financial statement translation of foreign operations are included in the consolidated statements of operations as incurred.

Fair Value of Financial Instruments

Universal's financial instruments consist of trade receivables and payables (which have carrying values that approximate fair value) and long-term debt. The fair value of Universal's revolving credit facility (see Note 4) is representative of its carrying value based upon variable rate terms. The fair value of the 9 $\frac{7}{8}$ % senior discount notes was approximately \$241.2 million at March 31, 2003. The fair value and the carrying amount of the 7 $\frac{1}{4}$ % senior notes due 2010 was \$175.7 million at March 31, 2004. The fair value of the senior notes was approximately \$480.6 million and \$479.3 at March 31, 2004 and 2003, respectively. The carrying amounts of \$82.2 million for the term loan and \$175 million for the notes under the ABS operating lease facility approximate the fair values. The estimated fair value amounts have been determined by Universal using appropriate valuation methodologies and information available to management as of March 31, 2004 based on the quoted market value.

Hedging and Use of Derivative Instruments

Universal utilizes interest rate swaps to minimize interest rate exposure on the \$200 million asset-backed securitization operating lease facility. The swaps are not used for trading or speculative purposes. The fair value of the interest rate swap was a liability of \$14.4 million and \$15.4 million as of March 31, 2004 and March 31, 2003, respectively.

In accordance with SFAS 133, "Accounting for Derivative Instruments and Hedging Activities," Universal records these interest rate swaps on the balance sheet as either assets or liabilities measured at their fair value. These instruments qualify for hedge accounting as they reduce the interest rate risk of the underlying hedged item and are designated as a cash flow hedge at inception. These swaps result in financial impacts that are inversely correlated to those of the items being hedged. To qualify for hedge accounting treatment, companies must formally document, designate and assess the effectiveness of the transactions. All of the interest rate instruments utilized are placed with a large creditworthy financial institution. If the necessary correlation ceases to exist or if physical delivery of the hedged item becomes improbable, Universal would discontinue hedge accounting and apply mark-to-market accounting. Amounts paid or received from interest rate swaps are charged or credited to interest

UNIVERSAL COMPRESSION, INC.
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

1. Summary of Significant Accounting Policies (Continued)

expense and matched with the cash flows and interest expense of the debt being hedged, resulting in an adjustment to the effective interest rate.

In March 2004, Universal entered into interest rate swap agreements to hedge \$100 million of our \$175.0 million 7¼% senior notes due 2010. The swaps are used to hedge the change in fair value of the debt and, in effect, convert the fixed interest payment to a variable interest payment based on the six-month LIBOR rate.

The swaps were accounted for in accordance with SFAS No. 133 and, as such, were recorded at fair value on the balance sheet. The fair value of the interest rate swap was a gain of \$0.7 million as of March 31, 2004. The change in the debt's fair value will also be recorded with the offset being recorded to income. The swaps, which Universal has designated as fair value hedging instruments, meet the specific hedge criteria and any changes in their fair values will be recognized in income. Because the terms of the hedged item and the swaps substantially coincide, the hedge is expected to exactly offset changes in fair values due to fluctuations in the variable rate and, therefore, Universal currently does not expect any ineffectiveness.

The counterparties to Universal's interest rate swap agreements are major international financial institution. Universal continually monitors the credit quality of these financial institution and does not expect non-performance by them.

Environmental Liabilities

The costs to remediate and monitor environmental matters are accrued when such liabilities are considered probable and a reasonable estimate of such costs is determinable.

New Accounting Pronouncements

In January 2003, the FASB issued Interpretation No. 46 ("FIN 46"), "Consolidation of Variable Interest Entities." An entity is subject to the consolidation rules of FIN 46 and is referred to as a variable interest entity ("VIE") if the entity's equity investors lack the characteristics of a controlling financial interest or do not have sufficient equity at risk for the entity to finance its operations without additional financial support. In December 2003, the FASB issued modifications to FIN 46 ("FIN 46R"), resulting in multiple effective dates based on the nature as well as the creation date of a VIE. The adoption of the provision of FIN 46 and FIN 46R did not have a material impact on the consolidated statements of operations, cash flows or financial position.

In January 2003, the Emerging Issues Task Force (EITF) issued No. 00-21, "Accounting for Revenue Arrangements with Multiple Deliverables." This EITF establishes the criteria for recognizing revenue in arrangements when several items are bundled into one agreement. EITF 00-21 does not allow revenue recognition unless the fair value of the undelivered element(s) is available and the element has stand-alone value to the customer. EITF 00-21 also provides guidance on allocating the total contract revenue to the individual elements based upon the available fair value of each deliverable. The implementation of this pronouncement did not have a material impact on the consolidated statements of operations, cash flows or financial position.

On April 30, 2003, the FASB issued SFAS No. 149, "Amendment of Statement 133 on Derivative Instruments and Hedging Activities." This statement amends and clarifies accounting for derivative instruments, including certain derivative instruments embedded in other contracts, and for hedging

UNIVERSAL COMPRESSION, INC.
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

1. Summary of Significant Accounting Policies (Continued)

activities under SFAS No. 133. This statement is effective for contracts entered into or modified after June 20, 2003, for hedging relationships designated after June 30, 2003, and to certain preexisting contracts. Universal will adopt SFAS No. 149 on a prospective basis at its effective date on July 1, 2003. SFAS No. 149 did not have a material impact on the consolidated statements of operations, cash flow, or financial position.

In May 2003, the FASB issued SFAS No. 150, "Accounting for Certain Financial Instruments with Characteristics of both Liabilities and Equity." This statement establishes standards for how an issuer classifies and measures certain financial instruments with characteristics of both liabilities and equity. This statement is effective for financial instruments entered into or modified after May 31, 2003, except for mandatorily redeemable financial instruments. Mandatorily redeemable financial instruments are subject to the provisions of this statement beginning on January 1, 2004. SFAS No. 150 did not have an impact on the consolidated financial statements.

2. Goodwill

Universal's acquisitions were accounted for as purchases and accordingly, the results of operations of the acquired businesses are included in the accompanying financial statements from the dates of acquisition. Goodwill has been recognized for the amount of the excess of the purchase price over the fair value of the net assets acquired and is accounted for in accordance with SFAS 142.

The changes in the carrying amount of goodwill from March 31, 2002 to March 31, 2004, are as follows (in thousands):

	<u>Domestic Contract Compression</u>	<u>International Contract Compression</u>	<u>Aftermarket Services</u>	<u>Fabrication</u>	<u>Total</u>
Balance as of March 31, 2002 . .	\$265,866	\$40,390	\$45,234	\$28,838	\$380,328
Acquisitions	—	—	768	—	768
Purchase adjustments and other .	(4,345)	7,976	321	204	4,156
Impact of foreign currency translation	—	2,228	—	—	2,228
Balance as of March 31, 2003 . .	<u>\$261,521</u>	<u>\$50,594</u>	<u>\$46,323</u>	<u>\$29,042</u>	<u>\$387,480</u>
Acquisitions	—	—	358	—	358
Purchase adjustments and other .	231	—	—	—	231
Impact of foreign currency translation	—	2,302	—	—	2,302
Balance as of March 31, 2004 . .	<u>\$261,752</u>	<u>\$52,896</u>	<u>\$46,681</u>	<u>\$29,042</u>	<u>\$390,371</u>

During the fourth quarter of fiscal year 2004, Universal performed an impairment analysis on goodwill in accordance with SFAS No. 142 and determined that no impairment had occurred.

UNIVERSAL COMPRESSION, INC.
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

3. Inventories, Net

Inventories, net consisted of the following (in thousands):

	For the Year Ended March 31,	
	2004	2003
Raw materials	\$ 60,064	\$73,827
Work-in-progress	37,510	22,516
Finished goods	4,435	5,457
Total inventories	102,009	101,800
Reserve	(12,041)	(10,468)
Inventories, net	<u>\$ 89,968</u>	<u>\$91,332</u>

4. Long-Term Debt

Universal's debt at March 31 consisted of the following (in thousands):

	As of March 31,	
	2004	2003
Senior discount notes, bearing interest of 9 ⁷ / ₈ % per annum, due 2008, net of discount of \$0 March 31, 2003, unsecured	\$ —	\$229,750
Senior notes, bearing interest of 7 ¹ / ₄ % per annum, due 2010	175,713	—
Senior notes due February 2008, bearing interest at 8 ⁷ / ₈ % per annum, payable semiannually on February 15 and August 15	445,000	450,000
Term loan of \$82.2 million due February 2008, currently bearing interest at a variable rate of LIBOR, (1.00% at March 31, 2004) plus 3.25% due quarterly	82,181	82,181
Notes under the ABS operating lease facility are due January 2023, bearing interest at a variable rate of LIBOR, which is effectively fixed through the use of interest rate swaps at a weighted average rate of 5.4%, plus 1.27% due monthly.	175,000	175,000
Other	3,387	3,806
Total debt	881,281	940,737
Less current maturities	12,205	3,084
Total long-term debt	<u>\$869,076</u>	<u>\$937,653</u>

On February 20, 1998, Universal issued \$242.5 million of its 9⁷/₈% senior discount notes due February 15, 2008 in a private placement. The 9⁷/₈% senior discount notes were offered at a substantial discount from their principal amount. Universal subsequently exchanged the notes for publicly tradable notes pursuant to a registered exchange offer under the Securities Act.

In connection with the Weatherford Global acquisition, on February 9, 2001, Universal raised \$427 million under a seven-year term senior secured notes operating lease facility (the "high-yield operating lease facility") funded primarily through an offering of \$350 million of 8⁷/₈% senior secured notes due 2008 by an unaffiliated special operating entity that is the lessor under the operating lease

UNIVERSAL COMPRESSION, INC.
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

4. Long-Term Debt (Continued)

plus approximately \$64 million in borrowings under a term loan and approximately \$13 million in proceeds from an equity investment in the lessor. On October 23, 2001, Universal increased the high-yield operating lease facility by \$122 million, which was funded through the unaffiliated entity's offering of an additional \$100 million of 8⁷/₈% senior secured notes due 2008, together with an \$18.3 million increase in its borrowings under an existing term loan and an additional \$3.7 million equity investment in the entity that is the lessor under the operating lease. The net proceeds from the sale of equipment under the addition to the high-yield operating lease facility were used to repay all of the outstanding indebtedness under the revolving credit facility, with the remaining proceeds used to repay a portion of the obligations under the asset-backed securitization operating lease facility discussed below and for general corporate purposes.

Also, in February 2001, Universal entered into a \$125 million secured revolving credit facility and a \$200 million asset-backed securitization operating lease facility (the "ABS operating lease facility"). The proceeds received in February 2001 from the high-yield operating lease facility and the ABS operating lease facility were used to restructure previous operating lease obligations and refinance certain existing indebtedness of Universal and Weatherford Global.

Universal's senior secured credit agreement ("Credit Agreement") provides for up to \$125 million under the revolving credit facility, which includes a sub-limit for letters of credit. The revolver bears interest at Universal's option of a base rate or LIBOR plus, in each case, a variable amount depending on its operating results.

The Credit Agreement contains certain financial covenants and limitations on, among other things, acquisitions, sales, indebtedness and liens. The Credit Agreement also limits the payment of cash dividends related to Universal paying up to \$1 million to Holdings in any given fiscal year. In addition, Universal has substantial dividend payment restrictions under the indenture related to the senior notes due 2010. Universal was in compliance with all such covenants and limitations at March 31, 2004 and 2003. As defined by the Credit Agreement, any "change of control" would result in an "Event of Default" and all amounts outstanding under the Credit Agreement would become due and payable. All principal amounts and accrued interest would become due without further notice.

On December 31, 2002, Universal purchased all of the equity in the lessor under the high-yield operating lease facility for \$16.7 million, plus accrued and unpaid preferred return on the equity. As a result of this equity investment by Universal in the lessor, the lessor became a fully consolidated entity of Universal as of December 31, 2002.

Also on December 31, 2002, Universal completed the process of having a nationally recognized insurance company provide to the holder of notes associated with the ABS operating lease facility a policy guaranteeing the payment of the principal and interest on the notes and obtaining a credit rating on the notes by Standard & Poor's and Moody's Investors Service. With the policy, the rating agencies rated the underlying notes "AAA" and "Aaa," respectively, resulting in a lower interest rate for the notes. Concurrently with the credit rating process, the equity in the lessor was reduced and Universal no longer considers the remaining outstanding equity of the lessor as comparable to that expected for a substantive business involved in similar leasing transactions with similar risks and rewards. Therefore, the lessor became a fully consolidated entity of Universal as of December 31, 2002. Further, concurrently with the credit rating process, the outstanding debt under the ABS operating lease facility was increased from \$159.5 million to \$175 million at December 31, 2002.

UNIVERSAL COMPRESSION, INC.
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

4. Long-Term Debt (Continued)

As a result of the changes in the high-yield and ABS operating lease facilities discussed in this Note 4 and consistent with the purchase accounting rules set forth in SFAS No. 141, "Business Combinations," Universal recorded in its consolidated balance sheet approximately \$614.8 million of contract compression equipment, approximately \$707.2 million in long-term debt and a noncurrent liability of approximately \$15.2 million related to interest rate swaps pertaining to the ABS operating lease facility (see Note 7 for discussion of interest rate swaps). Additionally, upon consolidation of the lessors of these operating lease facilities, the deferred gain previously recorded was eliminated.

Universal guaranteed certain of the obligations under the operating lease facilities. The high-yield operating lease facility is collateralized by a first priority security interest in all of the assets owned by the lessor under that facility. The ABS operating lease facility is collateralized by a first priority security interest in all of the assets owned by the lessor and lessee under that facility. The assets owned by the lessee, a wholly owned subsidiary of Universal, were transferred to the lessee from Universal. As discussed above, the assets related to the high-yield and ABS operating lease facilities are included in the consolidated balance sheet.

The results of operations through December 31, 2002 includes operating lease expense since prior to this date, the lessors under the operating leases were unaffiliated entities of Universal.

In May 2003, Universal commenced a tender offer to purchase any and all of the remaining outstanding \$229.8 million aggregate principal amount of its 9 $\frac{7}{8}$ % senior discount notes due 2008 at a price equal to 104.938% of the principal amount, plus a premium of 0.412%, for notes tendered prior to the early expiration date for the tender offer. Of these notes, \$169.2 million were tendered on or before the early tender date, and Universal purchased those notes on May 27, 2003. On that date, Universal called for redemption the remaining \$60.6 million of its 9 $\frac{7}{8}$ % senior discount notes due 2008 at 104.938% of the principal amount in accordance with the terms of the indenture relating to the notes. This redemption price was 0.412% less than the total consideration offered pursuant to the tender offer for notes tendered on or before the early tender date. During June 2003, the remaining \$60.6 million of this debt was redeemed or repurchased. Due to this early extinguishment of debt, the Company recognized expenses of \$14.4 million in the first quarter of fiscal year 2004 resulting primarily from the redemption and tender premiums of \$12.0 million, write-off of unamortized debt issuance costs of \$1.9 million and \$0.5 million of other costs.

Also in May 2003, Universal issued \$175.0 million of its 7 $\frac{1}{4}$ % senior notes due 2010 in a private placement. The net proceeds from the sale, together with other available funds, were used to purchase the outstanding 9 $\frac{7}{8}$ % senior discount notes due 2008 as discussed above. Universal exchanged the private notes for publicly-traded notes in the second quarter of fiscal 2004.

The Company has property and compression equipment, with a carrying value of \$4.1 million, that has been pledged as collateral relating to notes payable with a carrying value of \$3.0 million as of March 31, 2004.

UNIVERSAL COMPRESSION, INC.
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

4. Long-Term Debt (Continued)

Maturities of long-term debt as of March 31, 2004 are as follows (in thousands):

2005	\$ 12,205
2006	16,214
2007	16,237
2008	543,442
2009	16,138
Thereafter	<u>277,045</u>
Total	<u>\$881,281</u>

5. Capital Leases

Properties and equipment at March 31, 2004 and 2003 include the following amounts for capitalized leases (in thousands):

	<u>As of March 31,</u>	
	<u>2004</u>	<u>2003</u>
Compression equipment	\$3,398	\$3,546
Furniture and fixtures	<u>2,556</u>	<u>2,556</u>
Less accumulated depreciation	<u>(968)</u>	<u>(534)</u>
Net assets under capital leases	<u>\$4,986</u>	<u>\$5,568</u>

Compression equipment with a carrying value of \$2.9 million as of March 31, 2004 has been pledged as collateral relating to these capital leases.

Future minimum lease payments under non-cancelable capital leases as of March 31, 2004 are as follows (in thousands):

2005	\$2,343
2006	654
2007	110
2008	274
2009 and thereafter	<u>—</u>
Total minimum lease payments	\$3,381
Less imputed interest costs	<u>(220)</u>
Present value of net minimum lease payments	<u>\$3,161</u>

UNIVERSAL COMPRESSION, INC.
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

6. Income Taxes

Income tax expense (benefit) for the years ended March 31, 2004, 2003 and 2002 consisted of the following (in thousands):

	<u>2004</u>	<u>2003</u>	<u>2002</u>
Current:			
Foreign	\$ 9,119	\$ 4,142	\$ 6,664
Deferred:			
Federal	6,379	13,624	25,157
State	894	1,551	272
Foreign	1,349	1,658	(1,162)
Total	<u>\$17,741</u>	<u>\$20,975</u>	<u>\$30,931</u>

A reconciliation of the provision (benefit) for income taxes and the amount computed by applying the federal statutory income tax rate to income before taxes and extraordinary item for the years ended March 31, 2004, 2003 and 2002 is as follows (in thousands):

	<u>2004</u>	<u>2003</u>	<u>2002</u>
Income tax expense at statutory rate	\$16,985	\$19,071	\$28,119
State taxes	581	1,008	177
Foreign taxes	600	149	2,491
Non-deductible expenses (benefits) and other	(425)	747	144
Total	<u>\$17,741</u>	<u>\$20,975</u>	<u>\$30,931</u>

Deferred income tax balances are the direct effect of taxable temporary differences between the financial statement carrying amounts and tax basis of assets and liabilities at the enacted tax rates expected to be in effect when the taxes are actually paid or recovered.

Universal has not provided U.S. deferred taxes against the indefinitely (permanently) reinvested cumulative earnings of our non-U.S. affiliate companies. Such amounts relate to ongoing operations and as such, with the availability of U.S. foreign tax credits, it is not practicable to determine the U.S. federal income tax liability that would be payable if such earnings were not indefinitely reinvested.

UNIVERSAL COMPRESSION, INC.
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

6. Income Taxes (Continued)

The tax effects of temporary differences that give rise to deferred tax assets and deferred tax liabilities at March 31 are (in thousands):

	<u>2004</u>	<u>2003</u>
Deferred tax assets:		
Net operating loss carryforwards	\$ 128,114	\$ 112,970
Accrued reserves	5,820	1,647
Foreign tax credit	1,779	1,779
Other	9,179	3,277
Total	<u>144,892</u>	<u>119,673</u>
Valuation allowance	<u>(1,779)</u>	<u>(1,779)</u>
Total	<u><u>143,113</u></u>	<u><u>117,894</u></u>
Deferred tax liabilities:		
Depreciation differences on properties and equipment	(285,738)	(254,830)
Other	(1,110)	(5,340)
Total	<u>(286,848)</u>	<u>(260,170)</u>
Net deferred tax liability	<u><u>\$(143,735)</u></u>	<u><u>\$(142,276)</u></u>

A valuation allowance was established at March 31, 2000 against Universal's deferred tax assets related to foreign tax credits. Universal believes that it is probable that all other deferred tax assets will be realized on future tax returns, primarily from the generation of future taxable income through both profitable operations and future reversals of existing taxable temporary differences.

At March 31, 2004, Universal had net operating loss ("NOL") carryforwards of approximately \$366.0 million available to offset future taxable income. Annual utilization of the carryforwards could be limited by Section 382 of the Internal Revenue Code of 1986, as amended. If not utilized, the NOL carryforwards will expire as follows (in thousands):

2007	\$ 629
2008	1,849
2009	1,943
2010	953
2012	2
2018	4,872
2019	37,863
2020	62,218
2021	63,971
2022	94,278
2023	51,617
2024	45,846
Total	<u><u>\$366,041</u></u>

UNIVERSAL COMPRESSION, INC.
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

7. Accounting for Interest Rate Swaps

In accordance with SFAS No. 133, all derivative instruments must be recognized in the balance sheet at fair value, and changes in such fair values are recognized in earnings unless specific hedging criteria are met. Changes in the values of derivatives that meet these hedging criteria will ultimately offset related earnings effects of the hedged item pending recognition in earnings.

As of March 31, 2004 Universal had interest rate swaps to convert variable interest payments related to the \$175 million under the ABS operating lease facility to fixed interest payments. These swaps terminate in February 2013 and have a weighted average fixed rate of 5.4% and total notional amount of \$175 million. As of December 31, 2002, the lessor related to the operating lease facility became a consolidated entity and the swaps were included in Universal's consolidated financial statements. In accordance with SFAS No. 133, Universal has recorded a \$14.4 million noncurrent liability related to the derivative instrument as of March 31, 2004. Consistent with accounting rules discussed in SFAS No. 141, "Business Combinations," the offsetting amount was recorded as an increase to the value of property, plant and equipment.

The swaps, which Universal has designated as cash flow hedging instruments, meet the specific hedge criteria and any changes in their fair values subsequent to March 31, 2004 will be recognized in other comprehensive income or loss. Because the terms of the hedged item and the swaps substantially coincide, the hedge is expected to exactly offset changes in expected cash flows due to fluctuations in the variable rate and therefore, Universal currently does not expect any ineffectiveness.

In March 2004, Universal entered into interest rate swap agreements to hedge \$100 million of our \$175.0 million 7¼% senior notes due 2010. The swaps are used to hedge the change in fair value of the debt and, in effect, convert the fixed interest payment to a variable interest payment based on the six-month LIBOR rate.

The swaps will be accounted for in accordance with SFAS No. 133 and, as such, will be recorded at fair value on the balance sheet. The change in the debt's fair value will also be recorded with the offset being recorded to income. The swaps, which Universal has designated as fair value hedging instruments, meet the specific hedge criteria and any changes in their fair values will be recognized in income. Because the terms of the hedged item and the swaps substantially coincide, the hedge is expected to exactly offset changes in fair values due to fluctuations in the variable rate and, therefore, Universal currently does not expect any ineffectiveness.

The counterparties to Universal's interest rate swap agreements are major international financial institution. Universal continually monitors the credit quality of these financial institution and does not expect non-performance by them.

8. Employee Benefits

Universal has a defined contribution 401(k) plan covering substantially all employees. Universal makes matching contributions under this plan equal to 50% of each participant's contribution of up to 6% of the participant's compensation. In September 2001, Universal amended Universal's 401(k) plan for all domestic employees. The amended plan allows Universal to make matching contributions in the form of Holdings' stock, instead of cash. For the fiscal years ended 2004 and 2003, Holdings' stock contributions to the plan were approximately \$1.6 million, respectively.

The Employee Stock Purchase Plan ("ESPP") is intended to encourage employees to participate in Universal's growth by providing them the opportunity to acquire a proprietary interest in Holdings'

UNIVERSAL COMPRESSION, INC.
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

8. Employee Benefits (Continued)

long-term performance and success through the purchase of shares of common stock at a price possibly less than fair market value. In 2001, Holdings' stockholders approved the ESPP, under which 250,000 shares of the Holdings' common stock could be purchased by employees. An employee is eligible to participate after completing 90 days of employment. Each quarter, an eligible employee may elect to withhold up to 10% of his or her salary to purchase shares of Holdings' stock at a price equal to 85% to 100% of the fair market value of the stock as of the first day of the quarter or the last day of the quarter, whichever is lower. The ESPP will terminate on the date that all shares of common stock authorized for sale under the ESPP have been purchased, except as otherwise extended by authorizing additional shares under the ESPP. At March 31, 2004, 158,431 shares remained available for sale under the ESPP. During 2004 and 2003, \$0.8 million were charged to expense relating to the ESPP, respectively.

Universal utilizes grants of restricted stock as long-term compensation for its executive officers. Universal's restricted stock plan provides for the award of up to 350,000 shares of Holdings' common stock to certain officers and key employees. Unearned compensation was charged for the market value of the restricted shares as these shares were issued in accordance with the restricted stock plan. The unearned compensation is shown as a reduction on stockholders' equity in the accompanying consolidated balance sheets and is being amortized ratably over the restricted period of five years. During fiscal years ending March 31, 2004 and 2003, \$0.6 million and \$0.3, respectively, were charged to expense relating to the restricted stock plan. The weighted average share price during 2004 and 2003 was \$17.00. Generally, common stock subject to restricted stock grants will vest 0% upon the first anniversary of the grant and 25% on each anniversary thereafter through the fifth anniversary.

The Employees' Supplemental Savings Plan, (the "ESSP") provides executive officers the opportunity to defer up to 25% of their compensation that cannot be deferred under the existing 401(k) plan due to IRS limitations. Participants can also defer up to 100% of their bonuses. Holdings' matches 50% of the first 6% of compensation, excluding any bonus deferred. The vesting periods are generally the same as the 401(k) plan. Prior to September 1, 2002, Universal's matching contributions were in the form of cash. Since September 1, 2002, Universal's matching contributions related to the Employees' Supplemental Savings Plan have been in the form of Holdings' common stock. During 2004 and 2003, amounts charged to expense relating to the ESSP were insignificant.

9. Facility Consolidation Costs

On April 28, 2003, Universal announced the transfer of substantially all of its fabrication activities based in Tulsa, Oklahoma to its existing facility in Houston, Texas. Engineering, production and related support functions were consolidated with Houston-based functions. Universal did not incur additional costs related to this consolidation during the final half of the fiscal year and Universal does not expect to incur additional facility consolidation costs during the two-year period ending September 30, 2005. Total costs related to the facility consolidation were \$1.8 million during the fiscal year ended March 31, 2004 and are shown separately as facility consolidation costs in the consolidated statements of

UNIVERSAL COMPRESSION, INC.
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

9. Facility Consolidation Costs (Continued)

operations. The costs incurred were related to the fabrication segment. See below for further details of the costs incurred (in thousands):

	<u>Fiscal Year Ended March 31, 2004</u>
Severance and personnel costs	\$1,131
Relocation costs	289
Other costs	<u>401</u>
Total facility consolidation costs	<u>\$1,821</u>

10. Commitments and Contingencies

In the ordinary course of business, Universal is involved in various pending or threatened legal actions. In the opinion of management, the amount of ultimate liability, if any, with respect to these actions will not have a materially adverse effect on Universal's financial position, operating results or cash flows.

In December 1999, Weatherford Global sold the assets and properties of its Gemini compressor business in Corpus Christi, Texas to GE Packaged Power, L.P., or GEPP. As part of that sale, Weatherford Global entered into an agreement to purchase from GEPP \$38.0 million of compressor components over five years and \$3.0 million of parts over three years, and GEPP agreed to provide compressors to Weatherford Global during that time period at negotiated prices. Universal assumed this obligation in connection with our acquisition of Weatherford Global in February 2001. As of March 31, 2004, approximately \$25.9 million of components and approximately \$13.5 million of parts have been purchased from GEPP. As a result of GEPP product performance issues, we have been unable to satisfy and have not satisfied in full our purchase commitment in respect of components under this agreement with GEPP. The unsatisfied portion of the purchase commitment is approximately \$12.1 million. GEPP could assert its right to enforce this obligation, but has not indicated any interest to do so at this time. However, if GEPP should seek to enforce this obligation, we believe we have valid defenses and counter claims and would aggressively defend against such enforcement and pursue such counter claims.

Universal has no other commitments or contingent liabilities, which, in the judgment of management, would result in losses that would materially affect Universal's consolidated financial position or operating results.

11. Industry Segments and Geographic Information

Universal has four principal business segments: domestic contract compression, international contract compression, fabrication and aftermarket services. The domestic contract compression segment provides natural gas compression to customers in the United States. The international contract compression segment provides natural gas compression to international customers, including Canada. The fabrication segment provides services related to the design, engineering and assembly of natural gas and air compressors for sale to third parties in addition to those that Universal uses in its contract compression fleet. The aftermarket services segment sells parts and components and provides maintenance to customers who own compression equipment and customers who utilize equipment from

UNIVERSAL COMPRESSION, INC.
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

11. Industry Segments and Geographic Information (Continued)

Universal's competitors. Fabrication and aftermarket services revenue presented in the table below include only sales to third parties.

Universal's reportable segments are strategic business units that offer distinct products and services. They are managed separately since each business segment requires different marketing strategies due to customer specifications. Universal evaluates the performance of its reportable segments based on segment gross profit. Gross profit is defined as total revenue less direct costs. Universal has no material sales between segments and, accordingly, there is no inter-segment revenue to be reported.

The following table presents revenue, gross profits and total assets by business segment for the fiscal years ended March 31, 2004, 2003 and 2002 (in thousands):

	For the Year Ended March 31,		
	2004	2003	2002
Revenue:			
Domestic contract compression	\$ 280,951	\$ 265,465	\$ 267,550
International contract compression	82,589	66,505	60,185
Fabrication	183,685	162,678	211,265
Aftermarket services	141,561	130,570	140,989
Total	<u>\$ 688,786</u>	<u>\$ 625,218</u>	<u>\$ 679,989</u>
Gross Profit:			
Domestic contract compression	\$ 178,543	\$ 169,868	\$ 169,892
International contract compression	64,159	53,769	43,411
Fabrication	15,888	16,075	24,347
Aftermarket services	30,891	28,256	30,696
Total	<u>\$ 289,481</u>	<u>\$ 267,968</u>	<u>\$ 268,346</u>
Depreciation and amortization	85,650	63,706	48,600
Selling, general and administrative	67,516	67,944	60,890
Operating lease expense	—	46,071	55,401
Interest expense, net	73,475	36,421	23,017
Debt extinguishment costs	14,903	—	—
Foreign currency (gain)/loss	(529)	459	(42)
Other (income)/expense, net	(1,883)	(1,126)	141
Facility consolidation costs	1,821	—	—
Income before income taxes	<u>\$ 48,528</u>	<u>\$ 54,493</u>	<u>\$ 80,339</u>
Identifiable Assets:			
Domestic contract compression	\$1,453,716	\$1,496,850	\$ 808,200
International contract compression	258,240	209,141	206,610
Fabrication	107,605	103,468	115,877
Aftermarket services	152,890	144,047	146,094
Total	<u>\$1,972,451</u>	<u>\$1,953,506</u>	<u>\$1,276,781</u>

UNIVERSAL COMPRESSION, INC.
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

11. Industry Segments and Geographic Information (Continued)

No one customer accounted for more than 10% of net sales for any of the periods presented.

Geographic Area

The following table illustrates revenue, gross profit and total assets by geographic locations for the fiscal years ended March 31, 2004, 2003, and 2002 (in thousands). The basis of attributing revenue and gross profit to specific geographic locations is primarily based upon the geographic location of the sale, service or where the assets are utilized.

	For the Year Ended March 31,		
	2004	2003	2002
Revenue:			
United States	\$ 493,262	\$ 449,480	\$ 524,475
Canada	90,198	74,293	91,615
Latin America	71,320	62,937	55,909
Asia Pacific	34,006	38,508	7,990
Total	<u>\$ 688,786</u>	<u>\$ 625,218</u>	<u>\$ 679,989</u>
Gross Profit:			
United States	\$ 212,602	\$ 198,869	\$ 212,309
Canada	16,238	15,219	17,150
Latin America	50,300	41,770	32,480
Asia Pacific	10,341	12,110	6,407
Total	<u>\$ 289,481</u>	<u>\$ 267,968</u>	<u>\$ 268,346</u>
Depreciation and amortization	85,650	63,706	48,600
Selling, general and administrative	67,516	67,944	60,890
Operating lease expense	—	46,071	55,401
Interest expense, net	73,475	36,421	23,017
Debt extinguishment costs	14,903	—	—
Foreign currency (gain)/loss	(529)	459	(42)
Other (income)/expense, net	(1,883)	(1,126)	141
Facility consolidation costs	1,821	—	—
Income before income taxes	<u>\$ 48,528</u>	<u>\$ 54,493</u>	<u>\$ 80,339</u>
Identifiable Assets:			
United States	\$1,667,163	\$1,702,620	\$1,057,947
Canada	96,116	90,076	85,336
Latin America	158,263	121,872	102,499
Asia Pacific	50,909	38,938	30,999
Total	<u>\$1,972,451</u>	<u>\$1,953,506</u>	<u>\$1,276,781</u>

UNIVERSAL COMPRESSION, INC.
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

12. Selected Quarterly Financial Data (Unaudited)

Summarized quarterly financial data for the years ended March 31, 2004 and 2003 is as follows (in thousands):

	<u>March 31</u>	<u>December 31</u>	<u>September 30</u>	<u>June 30</u>
2004:				
Revenue	\$190,710	\$170,167	\$175,682	\$152,227
Gross profit	76,788	72,580	71,912	68,199
Net income (loss)	11,725	11,733	9,303	(1,969)
2003:				
Revenue	\$154,589	\$164,584	\$154,582	\$151,464
Gross profit	68,682	66,751	64,816	67,718
Net income	6,923	8,583	7,659	10,351

UNIVERSAL COMPRESSION HOLDINGS, INC.
UNIVERSAL COMPRESSION, INC.
SCHEDULE II—
VALUATION AND QUALIFYING ACCOUNTS

<u>Item</u>	<u>Balance at Beginning of Period</u>	<u>Charged to Costs and Expenses(1)</u>	<u>Collections/ Deductions(2)</u> (In thousands)	<u>Acquired Allowances(3)</u>	<u>Balance at Close of Period</u>
2004 Allowance for doubtful accounts . . .	\$8,146	\$ 653	\$(5,610)	—	\$3,189
2003 Allowance for doubtful accounts . . .	\$7,470	\$4,981	\$(4,305)	—	\$8,146
2002 Allowance for doubtful accounts . . .	\$2,771	\$2,349	\$ (94)	\$2,444	\$7,470

-
- (1) Amounts accrued for uncollectibility
(2) Uncollectible accounts written off, net of recoveries
(3) Amounts recorded on balance sheets of acquired companies

<u>Item</u>	<u>Balance at Beginning of Period</u>	<u>Charged to Costs and Expenses(1)</u>	<u>Inventory Write-offs(2)</u> (In thousands)	<u>Acquired Reserves/ (Deductions)(3)</u>	<u>Balance at Close of Period</u>
2004 Reserve for inventory obsolescence	\$10,468	\$2,313	\$ (740)	—	\$12,041
2003 Reserve for inventory obsolescence	\$10,537	\$3,856	\$(3,925)	—	\$10,468
2002 Reserve for inventory obsolescence	\$17,607	\$ 475	\$(2,522)	\$(5,023)	\$10,537

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- (1) Amounts accrued for inventory obsolescence
(2) Amounts written-off for inventory obsolescence
(3) Amounts recorded related to acquired companies

SIGNATURES

Pursuant to the requirements of Section 13 or 15(d) of the Securities Exchange Act of 1934, the Registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized, on June 10, 2004.

UNIVERSAL COMPRESSION HOLDINGS, INC.

By: /s/ STEPHEN A. SNIDER

Stephen A. Snider
President and Chief Executive Officer

POWER OF ATTORNEY

KNOW ALL MEN BY THESE PRESENTS, that each person whose signature appears below constitutes and appoints Stephen A. Snider, Ernie L. Danner, J. Michael Anderson and D. Bradley Childers, and each of them, his true and lawful attorneys-in-fact and agents, with full power of substitution and resubstitution for him and in his name, place and stead, in any and all capacities, to sign any and all amendments to this Report, and to file the same, with all exhibits thereto, and other documents in connection therewith, with the Securities and Exchange Commission granting unto said attorneys-in-fact and agents full power and authority to do and perform each and every act and thing requisite and necessary to be done as fully to all said attorneys-in-fact and agents, or any of them, may lawfully do or cause to be done by virtue thereof.

Pursuant to the requirements of the Securities Act of 1934, this report has been signed by the following persons in the capacities indicated on June 10, 2004.

<u>Signature</u>	<u>Title</u>
<u>/s/ STEPHEN A. SNIDER</u> Stephen A. Snider	President, Chief Executive Officer and Director (Principal Executive Officer)
<u>/s/ J. MICHAEL ANDERSON</u> J. Michael Anderson	Senior Vice President and Chief Financial Officer (Principal Financial Officer)
<u>/s/ DENNIS S. BALDWIN</u> Dennis S. Baldwin	Controller (Principal Accounting Officer)
<u>/s/ ERNIE L. DANNER</u> Ernie L. Danner	Executive Vice President and Director
<u>/s/ THOMAS C. CASE</u> Thomas C. Case	Director
<u>/s/ JANET F. CLARK</u> Janet F. Clark	Director
<u>/s/ BERNARD J. DUROC-DANNER</u> Bernard J. Duroc-Danner	Director

<u>Signature</u>	<u>Title</u>
/s/ URIEL E. DUTTON Uriel E. Dutton	Director
/s/ LISA W. RODRIGUEZ Lisa W. Rodriguez	Director
/s/ WILLIAM M. PRUELLAGE William M. Pruellage	Director
/s/ SAMUEL URCIS Samuel Urcis	Director

SIGNATURES

Pursuant to the requirements of Section 13 or 15(d) of the Securities Exchange Act of 1934, the Registrant has duly caused this Report to be signed on its behalf by the undersigned, thereunto duly authorized, on June 10, 2004.

UNIVERSAL COMPRESSION, INC.

By: /s/ STEPHEN A. SNIDER

Stephen A. Snider
President and Chief Executive Officer

Pursuant to the requirements of the Securities Exchange act of 1934, this report has been signed by the following persons in the capacities indicated on June 10, 2004.

<u>Signature</u>	<u>Title</u>
<u>/s/ STEPHEN A. SNIDER</u> Stephen A. Snider	President, Chief Executive Officer and Director (Principal Executive Officer)
<u>/s/ J. MICHAEL ANDERSON</u> J. Michael Anderson	Senior Vice President and Chief Financial Officer (Principal Financial Officer)
<u>/s/ DENNIS S. BALDWIN</u> Dennis S. Baldwin	Controller (Principal Accounting Officer)
<u>/s/ ERNIE L. DANNER</u> Ernie L. Danner	Director

CERTIFICATION

I, Stephen A. Snider, certify that:

1. I have reviewed this annual report on Form 10-K of Universal Compression Holdings, Inc. (the “registrant”);
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant’s other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) for the registrant and have:
 - a) designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
 - b) evaluated the effectiveness of the registrant’s disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures as of the end of the period covered by this report based on such evaluation; and
 - c) disclosed in this report any change in the registrant’s internal control over financial reporting that occurred during the registrant’s most recent fiscal quarter (the registrant’s fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant’s internal control over financial reporting; and
5. The registrant’s other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant’s auditors and the audit committee of registrant’s board of directors (or persons performing the equivalent functions):
 - a) all significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant’s ability to record, process, summarize and report financial information; and
 - b) any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant’s internal control over financial reporting.

/s/ STEPHEN A. SNIDER

Name: Stephen A. Snider

Title: Chief Executive Officer

Date: June 10, 2004

CERTIFICATION

I, J. Michael Anderson, certify that:

1. I have reviewed this annual report on Form 10-K of Universal Compression Holdings, Inc. (the “registrant”);
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant’s other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) for the registrant and have:
 - a) designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
 - b) evaluated the effectiveness of the registrant’s disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures as of the end of the period covered by this report based on such evaluation; and
 - c) disclosed in this report any change in the registrant’s internal control over financial reporting that occurred during the registrant’s most recent fiscal quarter (the registrant’s fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant’s internal control over financial reporting; and
5. The registrant’s other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant’s auditors and the audit committee of registrant’s board of directors (or persons performing the equivalent functions):
 - a) all significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant’s ability to record, process, summarize and report financial information; and
 - b) any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant’s internal control over financial reporting.

/s/ J. MICHAEL ANDERSON

Name: J. Michael Anderson

Title: Chief Financial Officer

Date: June 10, 2004

CERTIFICATION

I, Stephen A. Snider, certify that:

1. I have reviewed this annual report on Form 10-K of Universal Compression, Inc. (the “registrant”);

2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;

3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;

4. The registrant’s other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) for the registrant and have:

- a) designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
- b) evaluated the effectiveness of the registrant’s disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures as of the end of the period covered by this report based on such evaluation; and
- c) disclosed in this report any change in the registrant’s internal control over financial reporting that occurred during the registrant’s most recent fiscal quarter (the registrant’s fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant’s internal control over financial reporting; and

5. The registrant’s other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant’s auditors and the audit committee of registrant’s board of directors (or persons performing the equivalent functions):

- a) all significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant’s ability to record, process, summarize and report financial information; and
- b) any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant’s internal control over financial reporting.

/s/ STEPHEN A. SNIDER

Name: Stephen A. Snider

Title: Chief Executive Officer

Date: June 10, 2004

CERTIFICATION

I, J. Michael Anderson, certify that:

1. I have reviewed this annual report on Form 10-K of Universal Compression, Inc. (the “registrant”);

2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;

3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;

4. The registrant’s other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) for the registrant and have:

- a) designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
- b) evaluated the effectiveness of the registrant’s disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures as of the end of the period covered by this report based on such evaluation; and
- c) disclosed in this report any change in the registrant’s internal control over financial reporting that occurred during the registrant’s most recent fiscal quarter (the registrant’s fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant’s internal control over financial reporting; and

5. The registrant’s other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant’s auditors and the audit committee of registrant’s board of directors (or persons performing the equivalent functions):

- a) all significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant’s ability to record, process, summarize and report financial information; and
- b) any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant’s internal control over financial reporting.

/s/ J. MICHAEL ANDERSON

Name: J. Michael Anderson

Title: Chief Financial Officer

Date: June 10, 2004

**UNIVERSAL COMPRESSION HOLDINGS, INC.
CERTIFICATION PURSUANT TO
18 U.S.C. SECTION 1350,
AS ADOPTED PURSUANT TO
SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002**

In connection with the Annual Report of Universal Compression Holdings, Inc. (the "Company") on Form 10-K for the period ending March 31, 2004 (the "Report"), I, Stephen A. Snider, Chief Executive Officer of the Company, certify, pursuant to 18 U.S.C. § 1350, as adopted pursuant to §906 of the Sarbanes-Oxley Act of 2002, that to my knowledge:

- (1) The Report fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934, as amended; and
- (2) The information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

/s/ STEPHEN A. SNIDER

Stephen A. Snider
Chief Executive Officer
June 10, 2004

In connection with the Annual Report of Universal Compression Holdings, Inc. (the "Company") on Form 10-K for the period ending March 31, 2004 (the "Report"), I, J. Michael Anderson, Chief Financial Officer of the Company, certify, pursuant to 18 U.S.C. § 1350, as adopted pursuant to § 906 of the Sarbanes-Oxley Act of 2002, that to my knowledge:

- (1) The Report fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934, as amended; and
- (2) The information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

/s/ J. MICHAEL ANDERSON

J. Michael Anderson
Chief Financial Officer
June 10, 2004

**UNIVERSAL COMPRESSION, INC.
CERTIFICATION PURSUANT TO
18 U.S.C. SECTION 1350,
AS ADOPTED PURSUANT TO
SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002**

In connection with the Annual Report of Universal Compression, Inc. (the "Company") on Form 10-K for the period ending March 31, 2004 (the "Report"), I, Stephen A. Snider, Chief Executive Officer of the Company, certify, pursuant to 18 U.S.C. § 1350, as adopted pursuant to § 906 of the Sarbanes-Oxley Act of 2002, that to my knowledge:

- (1) The Report fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934, as amended; and
- (2) The information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

/s/ STEPHEN A. SNIDER

Stephen A. Snider
Chief Executive Officer
June 10, 2004

In connection with the Annual Report of Universal Compression, Inc. (the "Company") on Form 10-K for the period ending March 31, 2004 (the "Report"), I, J. Michael Anderson, Chief Financial Officer of the Company, certify, pursuant to 18 U.S.C. § 1350, as adopted pursuant to § 906 of the Sarbanes-Oxley Act of 2002, that to my knowledge:

- (1) The Report fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934, as amended; and
- (2) The information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

/s/ J. MICHAEL ANDERSON

J. Michael Anderson
Chief Financial Officer
June 10, 2004

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Corporate Information

Corporate Officers

Stephen A. Snider
President and Chief Executive Officer

Ernie L. Danner
Executive Vice President
President, Latin America Division

J. Michael Anderson
Senior Vice President and
Chief Financial Officer

D. Bradley Childers
Senior Vice President,
General Counsel and Secretary

Kirk E. Townsend
Senior Vice President
President, North America Division

Richard Leong
Vice President
President, Asia Pacific Division

Board of Directors

Thomas C. Case
Consultant

Janet F. Clark
Senior Vice President and
Chief Financial Officer
Marathon Oil Company

Ernie L. Danner
Executive Vice President
President, Latin America Division
Universal Compression Holdings, Inc.

Bernard J. Duroc-Danner
Chairman, President and
Chief Executive Officer
Weatherford International Ltd.

Uriel E. Dutton
Of Counsel
Fulbright & Jaworski L.L.P.

William M. Pruellage
Managing Director
Castle Harlan, Inc.

Lisa W. Rodriguez
Senior Vice President and
Chief Financial Officer
Weatherford International Ltd.

Stephen A. Snider
President and Chief Executive Officer
Universal Compression Holdings, Inc.

Samuel Urcis
Venture Capitalist

Corporate Headquarters

Universal Compression Holdings, Inc.
4444 Brittmoore Road
Houston, Texas 77041
(713) 335-7000
www.universalcompression.com

Registrar and Transfer Agent

EquiServe Trust Company
150 Royall Street
Canton, Massachusetts 02021
(877) 282-1168
www.equiserve.com

Annual Meeting

Friday, July 23, 2004
9:00 a.m., local time
Hilton Houston Westchase & Towers
9999 Westheimer Road
Houston, Texas 77042

Independent Auditors

Deloitte & Touche LLP
Houston, Texas

Stock Exchange Listing

Universal Compression Holdings, Inc.'s common stock is traded on the New York Stock Exchange under the ticker symbol UCO.

Form 10-K

Additional copies of the Company's Annual Report on Form 10-K for the fiscal year ended March 31, 2004 are available at no charge upon request to: Investor Relations
Universal Compression Holdings, Inc.
4444 Brittmoore Road
Houston, Texas 77041
(713) 335-7460
or through our web site at
www.universalcompression.com

This document includes forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995, which statements are subject to risks and uncertainties. Please see our Annual Report on Form 10-K for the fiscal year ended March 31, 2004 included herein for information, as well as our other filings with the Securities and Exchange Commission, concerning our forward-looking statements and important factors that could cause our results to differ materially from those in such statements.

UNIVERSAL COMPRESSION HOLDINGS, INC.

*4444 Brittmoore Road
Houston, Texas 77041
(713) 335-7000*

www.universalcompression.com

