AQUA AMERICA INC
Form S-3ASR
July 28, 2017
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As filed with the Securities and Exchange Commission on July 28, 2017

Registration No. 333-

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM S-3

REGISTRATION STATEMENT

UNDER

THE SECURITIES ACT OF 1933

AQUA AMERICA, INC.

(Exact name of registrant as specified in its charter)

Pennsylvania **(State or other jurisdiction of incorporation or organization)**	**23-1702594** **(I.R.S. Employer Identification No.)**

762 W. Lancaster Avenue

Bryn Mawr, PA 19010-3489

(610) 527-8000

(Address, Including Zip Code, and Telephone Number, Including Area Code, of Registrant s Principal Executive Offices)

Christopher P. Luning

Aqua America, Inc.

Senior Vice President, General Counsel and Corporate Secretary

762 W. Lancaster Avenue

Bryn Mawr, PA 19010-3489

(610) 527-8000

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

Copy of all communications to:

Mary J. Mullany, Esquire

Ballard Spahr LLP

1735 Market Street, 51st Floor

Philadelphia, PA 19103

(215) 864-8500

Approximate date of commencement of proposed sale to the public: From time to time after this registration statement becomes effective.

If the only securities being registered on this form are being offered pursuant to dividend or interest reinvestment plans, please check the following box.

If any of the securities being registered on this form are to be offered on a delayed or continuous basis pursuant to Rule 415 under the Securities Act of 1933, other than securities offered only in connection with dividend or interest reinvestment plans, check the following box.

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

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

If this form is a registration statement filed pursuant to General Instruction I.D. or a post-effective amendment thereto that shall become effective upon filing with the Commission pursuant to Rule 462(e) under the Securities Act, check the following box.

If this form is a post-effective amendment to a registration statement filed pursuant to General Instruction I.D. filed to register additional securities or additional classes of securities pursuant to Rule 413(b) under the Securities Act, check the following box.

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

Large accelerated filer		Accelerated filer
Non-accelerated filer	(Do not check if a smaller reporting company)	Smaller reporting company
		Emerging growth company

If an emerging growth company, indicate by check mark if the registrant has elected not to use the extended transition period for complying with any new or revised financial accounting standards provided pursuant to Section 7(a)(2)(B) of Securities Act.

CALCULATION OF REGISTRATION FEE

Title of Each Class Of Securities to be Registered	**Amount to be Registered(1)**	**Proposed Maximum Offering Price Per Security**	**Proposed Maximum Aggregate Offering Price(2)**	**Amount of Registration Fee(3)**
Common stock, par value $0.50 per share	6,000,000 shares	$33.24	$199,440,000	$23,115.10

(1) Pursuant to Rule 416 under the Securities Act of 1933, the number of shares being registered shall be adjusted to include any additional shares that may become issuable as a result of stock splits, stock dividends, or similar transactions.
(2) Pursuant to Rule 457(c) under the Securities Act of 1933, the offering price is computed on the basis of the average of the high and low prices of the common stock of Aqua America, Inc., as reported on the New York Stock Exchange on July 25, 2017.
(3) Pursuant to Rule 415(a)(6) of the Securities Act of 1933, this registration statement carries over 3,125,000 unsold shares of common stock previously registered on a Registration Statement on Form S-3 (File No. 333-197805) filed with the Securities and Exchange Commission on August 1, 2014 (the 2014 Registration Statement). The filing fee of $13,463.77 being paid herewith relates to the 2,875,000 newly registered shares of common stock. As a result, the offering of unsold securities registered under the 2014 Registration Statement will be deemed terminated as of the date of effectiveness of this registration statement.

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PROSPECTUS

Aqua America, Inc.

Dividend Reinvestment and Direct Stock Purchase Plan

6,000,000

Shares of Common Stock

The Plan gives you a convenient, systematic way to purchase or invest in our common stock.

You can increase your ownership by reinvesting dividends at a discount of between 0% and 5.0%, as designated from time to time in our sole discretion, and by making optional cash investments with brokerage fees and commissions paid by us.

You do not need to be one of our existing shareholders to participate in the Plan.

You can own and transfer shares without holding certificates.

You can purchase shares through an IRA with a portion of the annual maintenance fee paid by us.

IMPORTANT NOTE: Sales of shares through the Plan are subject to fees and commission charges for which you will be responsible. Please see the Costs section of this prospectus for further details regarding these fees and commission charges.

Our common stock is listed on the New York Stock Exchange under the symbol WTR. Our principal executive office is located at 762 W. Lancaster Avenue, Bryn Mawr, Pennsylvania 19010-3489 and our telephone number is 610-527-8000.

Investing in our common stock involves risk. See "Risk Factors" on page 2 for certain risks to consider before participating in the Plan or purchasing shares of our common stock.

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

The date of this prospectus is July 28, 2017.

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As used in this prospectus, the words we, us, our, and Aqua America refer to Aqua America, Inc. and its subsidiaries unless otherwise indicated or the context otherwise requires.

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PLAN OVERVIEW

The Aqua America, Inc. Dividend Reinvestment and Direct Stock Purchase Plan (the Plan) provides you with a convenient and economical way to purchase shares of our common stock and to reinvest your cash dividends in additional shares. The Plan has various features and you can select those features that meet your investment needs.

The Plan is designed for long-term investors who wish to invest and build their share ownership over time. Unlike an individual stock brokerage account, the timing of purchases and sales is subject to the provisions of the Plan.

Please read this prospectus and the documents incorporated by reference herein carefully. If you are a shareholder of record of at least 5 shares of Aqua America common stock and wish to participate in the Plan, please sign and execute a Dividend Reinvestment and Direct Stock Purchase Plan Enrollment Form (the Enrollment Form). If your shares of Aqua America common stock are registered in a nominee name (such as in the name of a bank, broker or other nominee), please see the Participation and Enrollment section below for instructions on how to have such shares participate in the Plan. Investors wishing to make an initial investment of not less than $500 should complete the Dividend Reinvestment and Direct Stock Purchase Plan Initial Enrollment Form (the Initial Enrollment Form). When completed, the form should be mailed to Computershare Trust Company, N.A. (the Administrator). Employees of Aqua America who wish to pay for their investment by having a portion of their compensation withheld and applied to the investment should complete the Employee Enrollment Form provided by the Company.

You can also enroll in the Plan and access your Plan account through the Internet at the Administrator s web site, *www.computershare.com/investor*, at any time. In addition, you can authorize one-time initial and subsequent optional cash investments or establish recurring automatic withdrawals from your U.S. bank account.

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RISK FACTORS

Investing in our common stock involves risks. Please see the risk factors described in our Annual Report on Form 10-K for the fiscal year ended December 31, 2016, filed with the Securities and Exchange Commission (the SEC), which are all incorporated by reference in this prospectus. Before making an investment decision, you should carefully consider these risks as well as other information contained or incorporated by reference in this prospectus.

FORWARD-LOOKING STATEMENTS

Certain statements in this prospectus, or incorporated by reference into this prospectus, are forward-looking statements within the meaning of Section 27A of the Securities Act of 1933 and Section 21E of the Securities Exchange Act of 1934 that are made based upon, among other things, our current assumptions, expectations, plans, and beliefs concerning future events and their potential effect on us. These forward-looking statements involve risks, uncertainties and other factors, many of which are outside our control that may cause our actual results, performance or achievements to be materially different from any future results, performance or achievements expressed or implied by these forward-looking statements. In some cases you can identify forward-looking statements where statements are preceded by, followed by or include the words believes, expects, anticipates, plans, future, potential, probab predictions, intends, will, continue in the event or the negative of such terms or similar expressions. Forward-loo statements in this prospectus, or incorporated by reference into this prospectus, include, but are not limited to, statements regarding:

- recovery of capital expenditures and expenses in rates;
- projected capital expenditures and related funding requirements;
- our capability to pursue timely rate increase requests;
- the availability and cost of capital financing;
- developments, trends and consolidation in the water and wastewater utility and infrastructure industries;
- dividend payment projections;
- opportunities for future acquisitions, the success of pending acquisitions and the impact of future acquisitions;
- the capacity of our water supplies, water facilities and wastewater facilities;

the impact of geographic diversity on our exposure to unusual weather;

the impact of conservation awareness of customers and more efficient plumbing fixtures and appliances on water usage per customer;

our authority to carry on our business without unduly burdensome restrictions;

the continuation of investments in strategic ventures;

our ability to obtain fair market value for condemned assets;

the impact of fines and penalties;

the impact of changes in and compliance with governmental laws, regulations and policies, including those dealing with taxation, the environment, health and water quality, and public utility regulation;

the impact of decisions of governmental and regulatory bodies, including decisions to raise or lower rates;

the development of new services and technologies by us or our competitors;

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- the availability of qualified personnel;
- the condition of our assets;
- the impact of legal proceedings;
- general economic conditions;
- acquisition-related costs and synergies;
- the sale of water and wastewater divisions;
- the impact of federal and/or state tax policies and the regulatory treatment of the effects of those policies; and
- the amount of income tax deductions for qualifying utility asset improvements and the Internal Revenue Service s ultimate acceptance of the deduction methodology.

Because forward-looking statements involve risks and uncertainties, there are important factors that could cause actual results to differ materially from those expressed or implied by these forward-looking statements, including but not limited to:

- changes in general economic, business, credit and financial market conditions;
- changes in governmental laws, regulations and policies, including those dealing with taxation, the environment, health and water quality, and public utility regulation;
- changes to the rules or our assumptions underlying our determination of what qualifies for an income tax deduction for qualifying utility asset improvements;
- the decisions of governmental and regulatory bodies, including decisions on rate increase requests;
- our ability to file rate cases on a timely basis to minimize regulatory lag;
- abnormal weather conditions, including those that result in water use restrictions;

changes in, or unanticipated, capital requirements;

changes in our credit rating or the market price of our common stock;

changes in valuation of strategic ventures;

our ability to integrate businesses, technologies or services which we may acquire;

our ability to manage the expansion of our business;

our ability to treat and supply water or collect and treat wastewater;

the extent to which we are able to develop and market new and improved services;

the effect of the loss of major customers;

our ability to retain the services of key personnel and to hire qualified personnel as we expand;

labor disputes;

increasing difficulties in obtaining insurance and increased cost of insurance;

cost overruns relating to improvements to, or the expansion of, our operations;

increases in the costs of goods and services;

civil disturbance or terroristic threats or acts;

the continuous and reliable operation of our information technology systems, including the impact of cyber security attacks or other cyber-related events;

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- changes in accounting pronouncements;
- litigation and claims; and
- changes in environmental conditions, including the effects of climate change.

Given these risks and uncertainties, you should not place undue reliance on any forward-looking statements. You should read this prospectus and the documents that we incorporate by reference into this prospectus completely and with the understanding that our actual future results, performance and achievements may be materially different from what we expect. These forward-looking statements represent assumptions, expectations, plans, and beliefs only as of the date of this prospectus. Except for our ongoing obligations to disclose certain information under the federal securities laws, we are not obligated, and assume no obligation, to update these forward-looking statements, even though our situation may change in the future. As you read this prospectus and the documents that we incorporate by reference into this prospectus, you should pay particular attention to the Risk Factors included in our most recent Annual Report on Form 10-K and in any filing we make with the SEC after the date of such Annual Report on Form 10-K that is incorporated by reference into this prospectus. We qualify all of our forward-looking statements by these cautionary statements.

A SUMMARY OF IMPORTANT PLAN FEATURES

Participation. You may participate in the Plan if you own at least 5 shares of Aqua America common stock that are registered in your name. You may also participate by making an initial minimum investment of at least $500 through automatic withdrawal from your U.S. bank account, by check or by a one-time online bank debit through the Administrator s web site, *www.computershare.com/investor*. Employees of Aqua America who wish to pay for their investment by having a portion of their compensation withheld and applied to the investment should complete the Employee Enrollment Form provided by the Company. All U.S. citizens are eligible to join the Plan, whether or not they are currently shareholders. Foreign citizens are eligible to participate as long as their participation would not violate any laws in their home countries or other non-U.S. laws. If your shares of Aqua America common stock are registered in a nominee name (such as in the name of a bank, broker or other nominee), please see the Participation and Enrollment section below for instructions on how to have such shares participate in the Plan.

Automatic Dividend Reinvestment. You can reinvest all or a portion of the cash dividends received on your first 100,000 shares toward the purchase of additional shares of our common stock, without paying trading fees or commissions. For purposes of the Plan, the term full dividend reinvestment means the reinvestment of dividends on all shares held by you in your name under the Plan up to a maximum of 100,000 shares.

Electronic Deposit of Cash Dividends. You can authorize the Administrator to deposit your cash dividends directly into your U.S. bank account.

Optional Cash Investments. As a shareholder, you can buy additional shares of our common stock at any time for as little as $50. The maximum optional cash investment you may make in any calendar year is $250,000. You can pay by check or by a one-time online bank debit through the Administrator s web site, *www.computershare.com/investor*, or have your payment automatically withdrawn from your U.S. bank account. Employees of Aqua America who wish to make optional cash investments should complete the Employee Enrollment Form provided by the Company.

IRAs. You may establish a traditional IRA, a Roth IRA or a Coverdell Education Savings Account, which invests in common stock through the Plan. IRA contributions and rollovers do not count against a participant s $250,000 annual investment limitation. There is an annual maintenance fee of forty-five dollars ($45.00) charged by the IRA and Coverdell Education Saving Account Trustee, which we will pay for the first calendar year in which you participate. In all subsequent years, twenty-five dollars ($25.00) of this annual fee will be charged to you, with the balance paid by us.

Full Investment. Full investment of your funds is possible because any initial investment and optional cash investments will be used to buy whole and fractional shares. In addition, the full dividend earned on your shares (up to the first 100,000 shares you own), including fractional shares, will be reinvested or paid out as you designate.

Safekeeping of Certificates. Shares purchased through the Plan for which you request certificates to be issued will be held by the Administrator for safekeeping. You may also deposit any Aqua America, or previously named Philadelphia Suburban Corporation, stock certificates that you hold for safekeeping, at no charge.

Transaction Reporting. You will receive a statement following each transaction showing the details of, and your share balance in, your Plan account.

Internet Account Access. You can also enroll in the Plan and access your Plan account through the Internet at the Administrator s web site, *www.computershare.com/investor*, at any time. In addition, you can authorize one-time initial and subsequent optional cash investments or establish recurring automatic withdrawals from your U.S. bank account.

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ADMINISTRATION

Computershare Trust Company, N.A., administers the Plan and acts as Agent for the participants. Computershare, Inc. acts as service agent to Computershare Trust Company, N.A. in performing certain services for the Plan. These companies purchase and retain shares of our common stock for Plan participants, keep records, send statements and perform other duties required by the Plan.

For information about the Plan, you can contact the Administrator by calling toll-free:

Computershare Trust Company, N.A.	800-205-8314
Outside the United States call collect:	781-575-3100
web site address:	www.computershare.com/investor

All written correspondence and optional cash investments submitted without a proper investment coupon, should be submitted to:

By mail:	Computershare Trust Company, N.A. Attn.: Aqua America, Inc. Dividend Reinvestment and Direct Stock Purchase Plan P.O. Box 505000 Louisville, KY 40233-5000
By courier:	Computershare Trust Company, N.A. Attn.: Aqua America, Inc. Dividend Reinvestment and Direct Stock Purchase Plan 462 South 4th Street, Suite 1600 Louisville, KY 40202

You can contact the Aqua America, Inc. IRA Program Administrator by calling toll free 1-800-597-7736. All written correspondence concerning the IRA Program, should be submitted to:

By mail:	The IRA Program C/O Computershare Trust Company, N.A.

	P.O. Box 2175 Milwaukee, WI 53201-2175
By courier:	The IRA Program C/O Computershare Trust Company, N.A. Attn.: Aqua America, Inc. IRA 235 W. Galena Street Milwaukee, WI 53212-3948

Make checks payable to Computershare-Aqua America in U.S. dollars and drawn on a U.S. bank. The Administrator will not accept cash, traveler s checks, money orders or third party checks for optional cash investments. Please use the cash investment form at the bottom of your statement.

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INTERNET ACCESS

You can also obtain information about your account via the Internet at the Administrator s web site, *www.computershare.com/investor*. At the web site, through Investor Center, you can access your share balance, enroll in the Plan, purchase shares (either as a one-time online bank debit or by recurring automatic monthly withdrawals from your U.S. bank account), sell shares, request a stock certificate, change dividend payment options and obtain online forms. To obtain access, click Create Log In, fill in the required information, accept the Terms & Conditions and select a User ID and password.

PARTICIPATION AND ENROLLMENT

If you already own at least 5 shares of our common stock, you are eligible to participate in the Plan.

If your shares are registered in your name, you can enroll in the Plan through the Internet at the Administrator s web site, *www.computershare.com/investor*, or you can fill out the Enrollment Form and return it to the Administrator.

If your shares are registered in a nominee name but you wish to participate in the Plan you should instruct your bank, broker or other nominee to have some or all of your shares registered in your name. Simply instruct your bank, broker or other nominee to transfer at least 5 of your shares of our common stock electronically through the Direct Registration System from your brokerage account to a new book-entry account at the Administrator. Please contact your bank, broker or other nominee for more information. Once at least 5 of your shares of our common stock are moved from your brokerage account to a new book-entry account registered in your name with the Administrator, you may then participate in the Plan by enrolling in the Plan as set forth above. Alternatively, you may instruct your bank, broker or other nominee to arrange to have a paper stock certificate issued to you for at least 5 of your shares of our common stock. Once at least 5 shares are registered in your name, you may participate in the Plan by enrolling in the Plan as set forth above. If the shares that you hold are in certificated form, you can deposit these certificated shares in your Plan account for safekeeping. In each instance, any fees or charges assessed by your bank or broker are your responsibility and will not be paid by us.

If your shares are held through our retirement plans or any of our other employee benefit plans (each, an employee benefit plan) that participate in the Plan, your participation in the Plan will be through the administrator or trustee of the applicable employee benefit plan and you will be limited to the automatic dividend reinvestment feature of the Plan only. Please contact the administrator or trustee of the employee benefit plan to determine if the plan participates in the Plan. Your participation in the Plan will be subject to the terms and conditions of the applicable employee benefit plan and the administrator or trustee of such plan.

If you do not own any shares of our common stock, or if you wish to establish a separate account, you can go to the Administrator s website, *www.computershare.com/investor*, and follow the instructions provided. You may enroll in the Plan by authorizing a one-time online bank debit from your U.S. bank account for an initial investment of at least $500 or by establishing recurring automatic withdrawals from your U.S. bank account for a minimum of $50 per transaction for at least ten consecutive months. Automatic withdrawal is further described in the Optional Cash Investments section of this prospectus. You can also fill out the Initial Enrollment Form and return it to the

Administrator. Enclose a check, in U.S. dollars, for at least $500 or, if you are an employee of Aqua America and wish to pay for your purchases through the withholding of compensation, fill out the Employee Enrollment Form provided to you by the Company. You can receive an Initial Enrollment Form by contacting the Administrator through the channels outlined in the Administration section of this prospectus. If you wish to make your initial investment through automatic withdrawals, you must agree to continue with the withdrawals until the $500 minimum initial investment is reached. Please note, such automatic withdrawals continue indefinitely beyond the initial investment until you notify the Administrator through the Internet, by telephone or in writing to stop such automatic withdrawals.

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If you open an account for another person by transferring stock from your account, you must transfer a minimum of 5 shares into that account.

DIVIDEND REINVESTMENT

You may choose to reinvest all or a portion of the dividends paid on your first 100,000 shares of our common stock held in your Plan account or participating in the Plan through our employee benefit plans. Your dividends will be used to buy additional shares of our common stock at a discount between 0% and 5.0%, as designated from time to time by us prior to the purchase of the shares with the reinvested dividends, from the prevailing market price. You have the following options for your dividends:

Full Dividend Reinvestment. Your cash dividends received on shares you own up to 100,000 shares will be used to buy additional shares for you.

Partial Dividends Paid in Cash. If you do not want full dividend reinvestment, select a lower number of full shares on which you want your dividends to be paid in cash. The balance of your dividends will be reinvested.

All Dividends Paid in Cash (no dividend reinvestment). Your dividends on all of your shares will be paid in cash.

If you do not indicate which reinvestment option you want on the enrollment form, you will be automatically enrolled in full dividend reinvestment.

You may change your reinvestment option at any time by completing and returning a new Enrollment Form (which can be obtained by contacting the Administrator), by accessing your Plan account through the Internet at the Administrator s web site, *www.computershare.com/investor*, by calling the Administrator at 1-800-205-8314 or by providing written instructions to the Administrator. Dividends will be reinvested or paid on cash in accordance with your most recent instructions received by the Administrator prior to the dividend record date applicable to such dividend.

The 100,000 share reinvestment limitation does not apply to our employee benefit plans.

ELECTRONIC DEPOSIT OF CASH DIVIDENDS

If you are receiving all or a portion of your dividends in cash, you may have them electronically deposited into your U.S. bank account by completing an Authorization for Electronic Direct Deposit Form or by mailing a voided check or deposit slip to the Administrator. Contact the Administrator to receive an Authorization for Electronic Direct Deposit Form. You may also authorize electronic deposit through the Internet at the Administrator s web site, *www.computershare.com/investor*. This feature may be changed or discontinued at any time by notifying the Administrator. If you change your U.S. bank account and fail to notify the Administrator of the change, a check for your dividends will be issued and mailed only after the funds have been returned from the receiving bank.

OPTIONAL CASH INVESTMENTS

Participants in the Plan may buy additional shares of our common stock at any time by investing at least $50. Your total optional cash investment may not exceed $250,000 in a calendar year. Interest will not be paid on amounts held pending investment. Optional cash investments may be made by:

One-time online bank debit. At any time, you may make optional cash investments by going to the Administrator s web site, *www.computershare.com/investor*, and authorizing a one-time online bank debit from your U.S. bank account. Please refer to the online confirmation for your bank account debit date and investment date.

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Check. Mail your check with the cash investment form from the bottom of your account statement to the address on the cash investment form. Do not send cash, traveler s checks, money orders or third party checks. All checks should be in U.S. funds and drawn from a U.S. bank. All payments should be made payable to Computershare-Aqua America .

Recurring automatic withdrawals from a U.S. bank account. You can establish recurring automatic withdrawals through the Internet at the Administrator s web site, *www.computershare.com/investor*, or by filling out a Direct Debit Authorization Form for automatic withdrawals. You can receive a Direct Debit Authorization Form by contacting the Administrator through the channels outlined in the Administration section of this prospectus. All automatic withdrawal enrollment information must be received at least 30 days prior to the first debit date. Funds will be deducted from your bank account on the first business day of each month. These funds may be commingled with other optional cash investments. All funds automatically withdrawn from your bank account will be invested on the next optional cash investment date. Automatic withdrawals will continue at the level you set until you instruct the Administrator otherwise. You can change or stop automatic withdrawals by accessing your Plan account through the Internet at the Administrator s web site, *www.computershare.com/investor*, by calling the Administrator at 1-800-205-8314, by completing and returning a new Direct Debit Authorization Form or by giving written instructions to the Administrator. You must contact the Administrator at least 7 business days prior to the debit date to change or terminate automatic withdrawal.

In the event that a one-time bank debit, check or an automatic withdrawal is not honored for any reason, the Administrator will consider the request for investment of that money null and void and shall immediately remove from the participant s account the shares, if any, purchased upon the prior credit of such money. A fee of $25 will also be assessed against the participant s account. The Administrator will then be entitled to sell those shares to satisfy any uncollected balance. If the net proceeds of the sale of those shares are insufficient to satisfy the balance of such uncollected amounts, the Administrator will be entitled to sell additional shares from the participant s account to satisfy the uncollected balance. Employees of Aqua America who wish to pay for their investment by having a portion of their compensation withheld and applied to the investment should complete the Employee Enrollment Form provided by the Company.

PURCHASE AND SOURCE OF SHARES

Shares of our common stock needed to meet the requirements of the Plan will either be purchased in the open market or issued directly by us. We will pay transaction fees and per share fees (which will include any brokerage commissions the Administrator is required to pay) incurred for the purchase of shares. The Administrator will invest your funds for the optional cash investments as promptly as practicable, at least once each week. However, funds automatically withdrawn from your U.S. bank account will be invested as specified above in Optional Cash Investments By automatic recurring withdrawals from a U.S. bank account. Funds may not be returned once they have been submitted to the Administrator. In the unlikely event that, due to unusual market conditions, the Administrator is unable to purchase shares of our common stock within 30 days (in the case of reinvested dividends) or within 35 days after receipt (in the case of cash investments), the funds will be returned to you by check. No interest will be paid on funds held by the Administrator pending investment. All dividends will be invested independently from optional cash investments. Please note that you will not be able to direct the Administrator to purchase shares at a specific time or at a specific price or through a specific broker or dealer.

PRICE OF SHARES

Open market purchases for initial, optional and IRA investments will be at a price equal to 100% of the weighted average per share price of shares purchased by the Administrator to satisfy Plan requirements. If the

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Administrator purchases shares to meet the dividend reinvestment requirement in the open market, your price per share will be 95% to 100% of the weighted average price of shares purchased, as designated from time to time by us prior to the purchase of the shares with the reinvested dividends. We will pay all transaction fees and per share fees in connection with open market purchases.

For original issue or treasury shares purchased from Aqua America for initial, optional and IRA investments (including investments made by employees through compensation withholding), the price per share will be 100% of the average of the daily high and low trading prices quoted on The New York Stock Exchange on the day of purchase (the investment date).

For original issue or treasury shares purchased from Aqua America to meet the dividend reinvestment requirement under the Plan, the price per share will be 95% to 100% of the average of the daily high and low trading prices quoted on The New York Stock Exchange for the five trading days preceding the dividend payment date, as designated from time to time by us prior to the dividend payment date.

The discount between 0% and 5.0% on the shares purchased or issued to meet the dividend reinvestment requirement will be designated by us in our sole discretion prior to the purchase or issuance of such shares. We reserve the right to change, reduce or discontinue any discount at any time without notice. We will provide the Administrator with notice of the applicable discount and any change in such discount. Please contact the Administrator with any questions about the discount then in effect. We may also provide notice on our website, but have no obligation to do so. As of the date of this prospectus, the discount is 5.0%.

SALE OF SHARES

You can sell some or all of the shares held in your Plan account by contacting the Administrator. You have choices when making a sale, depending on how you submit your sale request, as follows:

Market Order: A market order is a request to sell shares promptly at the current market price. Market order sales are only available at *www.computershare.com/investor* through Investor Centre or by calling the Administrator directly at 1-800-205-8314. Market order sale requests received at *www.computershare.com/investor* through Investor Centre or by telephone will be placed promptly upon receipt during market hours (normally 9:30 a.m. to 4:00 p.m. Eastern time). Any orders received after 4:00 p.m. Eastern time will be placed promptly on the next day the market is open. The price shall be the market price of the sale obtained by the Administrator s broker, less applicable fees. The Administrator will use commercially reasonable efforts to honor requests by participants to cancel market orders placed outside of market hours. Depending on the number of shares being sold and current trading volume in the shares, a market order may only be partially filled or not filled at all on the trading day in which it is placed, in which case the order, or remainder of the order, as applicable, will be cancelled at the end of such day. To determine if your shares were sold, you should check your account online at *www.computershare.com/investor* or call the Administrator directly at 1-800-205-8314. If your market order sale was not filled and you still want the shares to be sold, you will need to re-enter the sale request. For a market order sale, you will be charged a transaction fee of $25, plus $0.12 per share.

Batch Order: A batch order is an accumulation of all sales requests for a security submitted together as a collective request. Batch orders are submitted on each market day, assuming there are sale requests to be processed. Sale instructions for batch orders received by the Administrator will be processed no later than five business days after the date on which the order is received (except where deferral is required under applicable federal or state laws or regulations), assuming the applicable market is open for trading and sufficient market liquidity exists. Batch order sales may only be submitted in writing. All sales requests received in writing will be submitted as batch order sales, including sale requests for IRA Plan accounts and Coverdell Education Savings Accounts, will be submitted as batch order sale.

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The Administrator will cause your shares to be sold on the open market within five business days of receipt of your request. To maximize cost savings for batch order sale requests, the Administrator will seek to sell shares in round lot transactions. For this purpose the Administrator may combine each selling Plan participant s shares with those of other selling Plan participants. In every case of a batch order sale, the price to each selling Plan, participant shall be the weighted average sale price obtained by the Administrator s broker for each aggregate order placed by the Administrator and executed by the broker, less applicable fees. For a batch order sale, you will be charged a transaction fee of $15, plus $0.12 per share.

Day Limit Order: A day limit order is an order to sell shares of our common stock when and if they reach a specific trading price on a specific day. The order is automatically cancelled if the price is not met by the end of that day (or, for orders placed aftermarket hours, the next day the market is open). Depending on the number of shares of our common stock being sold and the current trading volume in the shares, such an order may only be partially filled, in which case the remainder of the order will be cancelled. The order may be cancelled by the applicable stock exchange, by the Administrator at its sole discretion or, if the Administrator s broker has not filled the order, at your request made online at *www.computershare.com/investor* or by calling the Administrator directly at 1-800-205-8314. For a day limit order sale, you will be charged a transaction fee of $25, plus $0.12 per share.

Good-Till-Cancelled (GTC) Limit Order: A GTC limit order is an order to sell shares of our common stock when and if the shares reach a specific trading price at any time while the order remains open (generally up to 30 days). Depending on the number of shares being sold and current trading volume in the shares, sales may be executed in multiple transactions and over more than one day. If shares are traded on more than one day, a separate fee will be charged for each such day. The order (or any unexecuted portion thereof) is automatically cancelled if the trading price is not met by the end of the order period. The order may be cancelled by the applicable stock exchange, by the Administrator at its sole discretion or, if the Administrator s broker has not filled the order, at your request made online at *www.computershare.com/investor* or by calling the Administrator directly at 1-800-205-8314. For a GTC limit order sale, you will be charged a transaction fee of $25, plus $0.12 per share

General: All sales requests processed over the telephone by a customer service representative entail an additional fee of $15.00. All per share fees include any brokerage commissions the Administrator is required to pay. Any fractional share will be rounded up to a whole share for purposes of calculating the per share fee. Fees are deducted from the proceeds derived from the sale. The Administrator may, under certain circumstances, require a transaction request to be submitted in writing. Please contact the Administrator to determine if there are any limitations applicable to your particular sale request. Proceeds are normally paid by check, which are distributed within 24 hours of after your sale transaction has settled.

The Administrator reserves the right to decline to process a sale if it determines, in its sole discretion, that supporting legal documentation is required. In addition, no one will have any authority or power to direct the time or price at which shares for the Plan are sold, and no one, other than the Administrator, will select the broker(s) or dealer(s) through or from whom sales are to be made.

If you elect to sell shares online at *www.computershare.com/investor*, you may utilize the Administrator s international currency exchange service to convert the sale proceeds to your local currency prior to being sent to you. Receiving sales proceeds in a local currency and having your check drawn on a local bank avoids the timely and costly collection process required for cashing U.S. dollar checks. This service is subject to additional terms and conditions and fees, which you must agree to online. We are not responsible for any costs or fees associated with your use of this service.

If your holdings in any account fall below 5 shares, the Administrator may close that account out of the Plan as described in the Minimum Account section of this prospectus.

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INDIVIDUAL RETIREMENT ACCOUNTS (IRA)

You may establish a Traditional IRA, Roth IRA or Coverdell Education Savings Account of our common stock by returning completed Enrollment Forms together with your contribution to the IRA and Coverdell Education Savings Account Trustee. If you are already a shareholder of at least 5 shares, you may open an IRA or Coverdell Education Savings Account with as little as $50. If you are not a shareholder, the minimum contribution to open an account is $500.

You may also open an IRA or Coverdell Education Savings Account to receive a cash rollover or a transfer of Aqua America shares from another IRA or qualified retirement plan. The IRA and Coverdell Savings Account Trustee will invest the cash rollovers into shares of our common stock.

There is an annual maintenance fee of $45.00 charged by the IRA and Coverdell Education Savings Account Trustee, which we will pay for the first calendar year in which you participate. In all subsequent years, twenty- five dollars ($25.00) of this annual fee will be charged to you, with the balance paid by us.

IRA and Coverdell Education Savings Account contributions and rollovers will not count against the $250,000 maximum investment limit under the Plan.

If you are interested in opening a Traditional IRA, Roth IRA or Coverdell Education Savings Account, you may obtain the enrollment and a disclosure statement from Computershare Trust Company, N.A., which will administer the IRA and Coverdell Education Savings Account. For information, call the Computershare IRA Department at its toll-free number, 1-800-597-7736.

SAFEKEEPING OF CERTIFICATES AND BOOK ENTRY

For your convenience, shares purchased under the Plan will be maintained by the Administrator in your name in book-entry form. You may, however, request a stock certificate by accessing your Plan account through the Internet at the Administrator s web site, *www.computershare.com/investor*, by calling the Administrator at 1-800-205-8314 or by providing written instructions to the Administrator. There is a $25 fee for certificate issuance.

If you are holding certificates for Aqua America, Inc., or previously named Philadelphia Suburban Corporation common stock, you may use the Plan s safekeeping service to deposit those stock certificates at no cost. Safekeeping protects your shares against loss, theft or accidental destruction and provides a convenient way for you to keep track of your shares. Only shares held in safekeeping or in book-entry form may be sold through the Plan.

To use the safekeeping service, send your certificates to the Administrator at the address listed on page 6 of this prospectus by registered or certified mail, with a return receipt requested or some other form of traceable mail, and properly insured. **YOU SHOULD NOT ENDORSE THE STOCK CERTIFICATE BEFORE YOU SEND IT IN.**

TRACKING YOUR INVESTMENT

The Administrator will send a statement confirming the details of each transaction you make. For market order transactions, the time of sale will be provided. If you continue to be enrolled in the Plan, but have no transactions, the Administrator will mail you an annual statement reflecting your holdings. For shares acquired in the Plan after January 1, 2011, specific cost basis information will be included in your statement in accordance with applicable law.

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You should notify the Administrator promptly of any change in address since all notices, statements and reports will be mailed to your address of record.

Please retain your statements to establish the cost basis of shares purchased under the Plan for income tax and other purposes. A $20 flat fee per year requested will be charged for all prior year duplicate statement requests.

You may also view

Weighted average Black-Scholes-Merton fair value assumptions

	Nine Months Ended October 31,	
	2006	**2005**
Risk free interest rate	4.7 5.2%	3.0%
Expected life	5.5 6.3yrs	8yrs
Expected volatility	65 - 67%	67 - 68%
Expected dividend yield	0.0%	0.0%

As a result of adopting SFAS 123R, the impact on income before income taxes and net income for the three and nine months ended October 31, 2006 was a reduction of approximately $373,000 and $1.1 million, respectively, from what would have been presented if the Company had continued to account for stock option awards under APB 25. The impact on basic and diluted earnings per share for the three months ended October 31, 2006 was a reduction of $0.04 per share. For the nine months ended October 31, 2006 the impact on basic and diluted earnings per share was $0.12 and $0.11, respectively.

In addition, prior to the adoption of SFAS 123R, the Company presented all tax benefits related to deductions resulting from the exercise of stock options, if any, as operating activities in the consolidated statement of cash flows. SFAS 123R requires that cash flows resulting from tax benefits attributable to tax deductions in excess of the compensation expense recognized for those options (excess tax benefits) be classified as financing in flows and operating out-flows. The Company had excess tax benefits of approximately $497,000 during the nine months ended October 31, 2006. Because the Company had net operating loss (NOL) carry-forwards in the prior year, no excess tax deductions were recorded.

The pro forma table below illustrates the effect on net income and earnings per share as if the Company had applied the fair value recognition provisions of SFAS No. 123, as amended by SFAS No. 148, *Accounting for Stock-Based Compensation Transition and Disclosure* (SFAS 148), to all stock-based employee compensation for the three and nine months ended October 31, 2005.

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		Three Months Ended October 31, 2005		Nine Months Ended October 31, 2005
	(in thousands, except per share amounts)			
Pro forma impact of fair value method				
Reported net income	$	2,850	$	6,231
Less: fair value impact of employee stock compensation		(346)		(830)
Pro forma net income	$	2,504	$	5,401
Income per common share				
Reported net income per share:				
Basic	$	0.31	$	0.69
Diluted	$	0.29	$	0.64
Pro forma net income per share:				
Basic	$	0.27	$	0.60
Diluted	$	0.25	$	0.55

Stock Option Plans

The Company has share-based awards outstanding under five different plans: the 1994 Stock Option Plan (1994 Plan), the 1998 Amended and Restated Stock Awards Plan (1998 Plan), the 2000 Stock Option Plan (2000 Plan), the Mitcham Industries, Inc. Stock Awards Plan (2006 Plan) and the 1994 Non-Employee Director Plan (Director Plan), (collectively, the Plans). Stock options granted and outstanding under each of the plans generally vest evenly over three years (except for the Director Plan, under which options generally vest after one year) and have a 10-year contractual term. The exercise price of a stock option generally is equal to the fair market value of the Company s common stock on the option grant date. All Plans except for the 2006 Plan have been closed for future grants. All shares available but not granted under the 1998 and 2000 Plans as of the date of the approval of the 2006 Plan were transferred to the 2006 Plan. As of October 31, 2006 there were 712,488 shares available for grant under the 2006 Plan. The 2006 Plan provides for awards of nonqualified stock options, incentive stock options, restricted stock awards and restricted stock units.

Stock Based Compensation Activity

The following table presents a summary of the Company s stock option activity for the nine months ended October 31, 2006:

	Number of Shares	Weighted Average Exercise Price	Weighted Average Remaining Contractual Term (in years)	Aggregate Intrinsic Value (in thousands)
Outstanding, beginning of period	1,054,920	$ 5.15		

Granted	332,000	13.47		
Exercised	(177,920)	4.91		
Canceled or expired	(6,520)	4.14		
Outstanding, end of period	1,202,480	$ 7.42	5.97	$ 5,549
Vested and expected to vest in the future at October 31, 2006	1,183,852	$ 7.35	7.01	$ 5,535
Exercisable at October 31, 2006	829,914	$ 5.14	2.34	$ 5,276

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The aggregate intrinsic value in the table above represents the total pre-tax intrinsic value (the difference between the Company s closing stock price on the last trading day of the third quarter of fiscal 2007 and the exercise price, multiplied by the number of in-the-money options) that would have been received by the option holders had all option holders exercised their options on October 31, 2006. This amount changes based upon the fair market value of the Company s common stock. Total intrinsic value of options exercised for the nine months ended October 31, 2006 was $2.7 million. The fair value of options that vested during the nine months ended October 31, 2006 was approximately $300,000. For the nine months ended October 31, 2005 approximately 190,000 options vested.

As of October 31, 2006, there was approximately $2.3 million of total unrecognized compensation expense related to unvested stock options granted under the Company s share-based compensation plans. That expense is expected to be recognized over a weighted average period of 2.3 years.

Cash received from option exercises for the nine months ended October 31, 2006 was an aggregate of approximately $783,000. During the nine months ended October 31, 2006, income taxes payable were reduced by approximately $497,000 as a result of the tax deduction from option exercises.

Restricted stock awards as of October 31, 2006 and changes during the nine months ended October 31, 2006 were as follows:

	Nine Months Ended October 31, 2006	
	Number of Shares	**Weighted Average Grant Date Fair Value**
Unvested, beginning of period	8,500	$ 1.90
Granted	37,000	13.21
Vested	(8,500)	5.15
Canceled	500	16.64
Unvested, end of period	15,500	$ 13.16

As of October 31, 2006, there was approximately $421,000 of unrecognized stock-based compensation expense related to unvested restricted stock awards. That cost is expected to be recognized over a weighted average period of 2.7 years.

9. <u>Income Tax</u>

The Company s provision for income taxes for the three and nine month periods ended October 31, 2006 is less than expected from applying a statutory rate primarily due to the reduction of the valuation allowances provided against deferred tax assets that arose in prior periods. For the three months ended October 31, 2006 the Company recorded current tax expense of approximately $200,000, offset by a deferred tax benefit of approximately $1,500,000. For the nine months ended October 31, 2006 the Company recorded current tax expense of approximately $800,000, offset by a deferred tax benefit of approximately $2,000,000.

10. <u>Discontinued Operations</u>

On August 1, 2003, the Company sold the operating assets of its front-end services segment (DSI) due to the over-capacity in that market segment. The Company accepted a note receivable from the purchaser for a portion of the sales price, which was paid in full during the current fiscal year. The note receivable was the only remaining asset of the discontinued operations.

	October 31, 2006	**January 31, 2006**
	(in thousands)	
Accounts and notes receivable of discontinued operations	$	$ 355
Other current assets of discontinued operations	$	$ 11
Accounts payable and accrued liabilities of discontinued operations	$	$ 10

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11. Segment Reporting

The following information is disclosed as required by SFAS No. 131, *Disclosures about Segments of an Enterprise and Related Information.*

The Mitcham segment offers for lease or sale, new and experienced seismic equipment to the oil and gas industry, seismic contractors, environmental agencies, government agencies and universities. The Mitcham segment is headquartered in Huntsville, Texas, with sales and services offices in Calgary, Canada; Brisbane, Australia; Ufa, Bashkortostan, Russia.

On July 12, 2005, the Company acquired 100% of the outstanding stock of Seamap. For a brief description of the operations of this segment, see Note 2. Manufacturing, support and sales facilities are maintained in the UK and Singapore with a sales office in Huntsville, Texas.

Financial information by business segment is set forth below net of any allocations (in thousands):

	As of October 31, 2006		
	Mitcham	**Seamap**	**Consolidated**
Fixed assets, net	$22,733	$1,232	$23,965
Intangible assets, net	$	$2,241	$ 2,241
Goodwill	$	$3,358	$ 3,358

	For the Three Months Ended October 31, 2006			For the Three Months Ended October 31, 2005		
	Mitcham	**Seamap**	**Consolidated**	**Mitcham**	**Seamap**	**Consolidated**
Revenues	$10,139	$2,602	$12,741	$8,159	$1,656	$9,815
Interest income, net	$ 281	$ 3	$ 284	$ 83	$ 2	$ 85
Income (loss) before taxes	$ 3,261	$ (722)	$ 2,539	$2,859	$ 48	$2,907
Capital expenditures	$ 6,131	$ 290	$ 6,421	$ 926	$ 28	$ 954
Depreciation and amortization expense	$ 2,069	$ 224	$ 2,293	$2,228	$ 26	$2,254

	For the Nine Months Ended October 31, 2006			For the Nine Months Ended October 31, 2005		
	Mitcham	**Seamap**	**Consolidated**	**Mitcham**	**Seamap**	**Consolidated**
Revenues	$29,222	$ 8,593	$37,815	$22,326	$2,129	$24,455
Interest income, net	$ 610	$ 7	$ 617	$ 277	$ 2	$ 279
Income (loss) before taxes	$ 8,768	$(1,402)	$ 7,366	$ 6,149	$ 107	$ 6,256
Capital expenditures	$10,380	$ 1,382	$11,762	$ 3,746	$ 283	$ 4,029
Depreciation and amortization expense	$ 5,856	$ 595	$ 6,451	$ 6,554	$ 31	$ 6,585

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12. New Accounting Pronouncements

In June 2006, the Financial Accounting Standards Board (FASB) issued FASB Interpretation No. 48, *Accounting for Uncertainty in Income Taxes* (FIN 48). FIN 48 clarifies how uncertain tax positions that have been taken or are expected to be taken on a company s tax return should be recognized, measured, presented and disclosed in the financial statements. The cumulative effect of applying this pronouncement to uncertain tax positions at the date of adoption will be recorded during the fiscal year beginning February 1, 2007. The Company is currently evaluating the effect that the adoption of FIN 48 will have on its consolidated financial position and results of operations.

Item 2. Management s Discussion and Analysis of Financial Condition and Results of Operations

Forward-Looking Statements and Risk Factors

Certain information contained in this Quarterly Report on Form 10-Q, as well as other written and oral statements made or incorporated by reference from time to time by us and our representatives in other reports, filings with the SEC, press releases, conferences, or otherwise, may be deemed to be forward-looking statements within the meaning of Section 27A of the Securities Act of 1933, as amended and Section 21E of the Securities Exchange Act of 1934, as amended (the Exchange Act). This information includes, without limitation, statements concerning our future financial position and results of operations; planned capital expenditures; business strategy and other plans for future operations; the future mix of revenues and business; commitments and contingent liabilities; and future demand for our services and predictions concerning in energy industry and seismic service industry conditions. Although we believe that the expectations reflected in such forward-looking statements are reasonable, we can give no assurance that such expectations will prove to have been correct. When used in this report, the words anticipate, believe, estimate, expect, may, and similar expressions, as they relate to the Company and our management, identify forward-looking statements. The actual results of future events described in such forward-looking statements could differ materially from the results described in the forward-looking statements due to the risks and uncertainties set forth in our Annual Report on Form 10-K for the year ended January 31, 2006 and elsewhere within this Quarterly Report on Form 10-Q. Each forward-looking statement speaks only as of its date and we are under no obligation to update those statements.

Business Overview

Mitcham Industries, Inc. (the Company), a Texas corporation, was incorporated in 1987. The Company consists of the operations of Mitcham Industries, Inc. and four wholly owned subsidiaries, MCL, SAP, Seamap, which the Company acquired on July 12, 2005, and MSE, which the Company established in November 2005. The Company is involved in the leasing and sale of equipment to the seismic industry world-wide and, through Seamap, in the design, manufacture and sale of marine seismic equipment. Seamap operates through its three wholly owned subsidiaries, Seamap Inc., Seamap (UK) Ltd., and Seamap Pte, Ltd. Seamap s primary products include the GunLink seismic source acquisition and control systems, which provide operators more precise control of their exploration tools, and the BuoyLink GPS tracking system, which provides precise positioning of seismic sources and streamers. Financial results from Seamap are included from the acquisition date of July 12, 2005.

The following table presents certain operating information by operating segment.

	For the Three Months Ended October 31,		For the Nine Months Ended October 31,	
	2006	2005	2006	2005
	(in thousands)			
Revenues:				
Mitcham	$ 10,139	$ 8,159	$ 29,222	$ 22,326
Seamap	2,602	1,656	8,593	2,129
Total revenues	12,741	9,815	37,815	24,455

Direct costs:				
Mitcham	4,628	3,658	13,858	10,597
Seamap	2,203	738	5,618	948
Total direct costs	6,831	4,396	19,476	11,545

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	For the Three Months Ended October 31,		For the Nine Months Ended October 31,	
	2006	2005	2006	2005
	(in thousands)			
Gross profit	5,910	5,419	18,339	12,910
Operating costs:				
General and administrative	3,330	2,463	10,693	6,649
Depreciation and amortization	337	134	944	286
Total operating costs	3,667	2,597	11,637	6,935
Operating income	$ 2,243	$ 2,822	$ 6,702	$ 5,975
EBITDA [(1)]	$ 4,548	$ 5,076	$ 13,200	$ 12,562
Adjusted EBITDA [(1)]	$ 4,954	$ 5,093	$ 14,398	$ 12,634
Reconciliation of Net Income to EBITDA and Adjusted EBITDA				
Net income	$ 3,863	$ 2,850	$ 8,555	$ 6,231
Interest income, net	(284)	(85)	(617)	(279)
Depreciation and amortization	2,293	2,254	6,451	6,585
Provision for (benefit from) income taxes	(1,324)	57	(1,189)	25
EBITDA [(1)]	4,548	5,076	13,200	12,562
Stock-based compensation	404	17	1,198	72
Adjusted EBITDA [(1)]	$ 4,954	$ 5,093	$ 14,398	$ 12,634

(1) EBITDA is defined as net income (loss) before (i) interest income, net of interest expense, (ii) provision for (or benefit from) income taxes and (iii) depreciation and amortization. Adjusted EBITDA excludes stock-based compensation.

We consider EBITDA and Adjusted EBITDA to be important indicators for the performance of our business, but not measures of performance calculated in accordance with accounting principles generally accepted in the United States of America (GAAP). We have included these non-GAAP financial measures because they provide management with important information for assessing our performance and as indicators of our ability to make capital expenditures and finance working capital requirements. EBITDA and Adjusted EBITDA are not measures of financial performance under GAAP and should not be considered in isolation or as alternatives to cash flow from operating activities or as alternatives to net income as indicators of operating performance or any other measures of performance derived in accordance with GAAP. Other companies in our industry may calculate EBITDA or Adjusted EBITDA differently than we do and EBITDA and Adjusted EBITDA may not be comparable with similarly titled measures reported by other companies.

Our revenues are directly related to the level of worldwide oil and gas exploration activities, which in turn are affected by expectations regarding the supply and demand for oil and natural gas, energy prices and finding and development costs. We believe that we are the largest independent lessor of seismic equipment. Due to our position, we have access to information about future projects from many data acquisition contractors. Based on our analysis of various indicators, including recent bid activity, equipment movement and public announcements of companies adding crew capacity, we believe the seismic exploration market is continuing to experience increased activity. We believe that this increase is being driven by the high level of world oil and North American natural gas prices, combined with the maturation of the world s hydrocarbon producing basins. The future direction and magnitude of changes in seismic data acquisition activity levels will continue to depend, in large part, upon oil and natural gas prices.

We lease and sell seismic data acquisition equipment primarily to seismic data acquisition companies conducting land, transition zone and marine seismic surveys worldwide. We provide short-term leasing of seismic equipment to meet a customer s requirements and offer technical support during the lease term. Our leases generally have a term of three to nine months. Seismic equipment held for lease is carried at cost, net of accumulated depreciation. In addition to leasing of seismic equipment, SAP sells equipment, consumables, systems integration, engineering hardware and software maintenance support services to the seismic, hydrographic, oceanographic, environmental and defense industries throughout Southeast Asia and Australia. Through Seamap we also design, manufacture and sell marine seismic equipment.

Seismic equipment leasing is susceptible to weather patterns in certain geographic regions. Our lease revenue is seasonal, especially in Canada and Russia, where a significant percentage of seismic survey activity occurs in the winter months, from December through March or April. During the months in which the weather is warmer, certain areas are not accessible to trucks, large earth vibrators and other equipment because of the unstable terrain. This seasonal leasing activity has generally resulted in higher lease revenues in our first and fourth fiscal quarters as compared to the second and third quarters. An anticipated increase in our leasing activity in Russia is expected to

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contribute to this seasonality. Additionally, periods of heavy rain in certain areas of the Pacific Rim can disrupt activity, most often in our second fiscal quarter.

In late September 2006, we were notified by a customer of certain mechanical failures relating to a specific version of our GunLink 4000 system that had recently been placed in service by that customer. The GunLink product line is utilized on seismic vessels to coordinate and control the energy sources utilized in marine seismic surveys. This version of the GunLink 4000 product is designed to operate with an energy source, an airgun in this case, recently introduced by another manufacturer. In cooperation with our customer we immediately began to investigate the cause of the failures. In addition, out of caution, we suspended further deliveries of this version of the GunLink 4000 product pending the results of our investigation. The investigation revealed an isolated design flaw in this particular version of the GunLink 4000 product. The design flaw noted did not affect the functionality of the conventional airgun version of the GunLink 4000 product, which is operating without exceptions for the customers who have received it. We have implemented design changes to correct the problems noted and expect these changes to be completed by January 2007. Shortly after that, we expect to resume shipments of the specific version of GunLink 4000 product. As of October 31, 2006, we have a backlog of firm orders for the GunLink 4000 product of approximately $7.0 million. We have had extensive discussions with each of our customers for this product regarding the issues described above. We do not expect these issues to impact existing orders or future orders for either version of the GunLink 4000 product.

As a result of the suspension of deliveries of the specific version of the GunLink 4000, we have not shipped two systems that we expected to deliver in the quarter ended October 31, 2006. Accordingly, our revenues from other equipment sales were approximately $2.0 million less than we had expected. In addition, in the quarter ended October 31, 2006 we incurred approximately $215,000 in non-recurring costs related to the investigation and resolution of the issues discussed above.

The following table presents items in our consolidated statements of operations as a percentage of total revenue for the three and nine months ended October 31, 2006 and 2005. These operating results are not necessarily indicative of results for any future period.

	For the Three Months Ended October 31,		**For the Nine Months Ended October 31,**	
	2006	**2005**	**2006**	**2005**
Revenues:				
Equipment leasing	48%	68%	48%	72%
Lease pool equipment sales	7	8	11	10
Other equipment sales	45	24	41	18
Total revenues	100	100	100	100
Direct costs:				
Equipment leasing	4	10	5	9
Lease pool depreciation	15	22	15	25
Cost of lease pool equipment sales	2		5	
Cost of other equipment sales	33	13	26	13
Total direct costs	54	45	51	47
Gross profit	46	55	49	53
Operating expenses:				
General and administrative	26	25	29	27
Depreciation and amortization	2	1	2	1

Total operating expenses	28	26	31	28
Operating income	18	29	18	25
Interest and other income, net	2	1	2	1
Income before income taxes	20	30	20	26
(Provision for) benefit from income taxes	(10)	1	(3)	
Net income	30%	29%	23%	26%

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Results of Operations

Three Months Ended October 31, 2006 Compared to Three Months Ended October 31, 2005

Revenues

During the quarter ended October 31, 2006, our consolidated revenues increased approximately $2.9 million as compared to the same quarter a year ago, reflecting an approximately $0.9 million increase in equipment sales in our Seamap segment, which we acquired in July 2005, and a $2.5 million increase in equipment sales, offset by a decrease in equipment leasing in Mitcham Industries segment.

Mitcham Industries

For the quarter ended October 31, 2006, the Mitcham segment s revenues increased by approximately $2.0 million to a total of $10.1 million, as compared to $8.2 million for the corresponding quarter in 2005. Sales of new equipment increased by $2.3 million primarily due to higher sales of seismic equipment and were offset by a decrease in equipment leasing. Leasing revenues in the third quarter of fiscal year 2006 were higher than normally expected due to a large project in South America during that period. As discussed above, due to seasonal factors, our second and third fiscal quarters generally produce lower leasing revenues than our first and fourth fiscal quarters. Due to these seasonal factors and recent and planned increases to our inventory of lease pool equipment, we expect subsequent periods to produce higher levels of leasing revenues.

Seamap

For the three months ended October 31, 2006, revenues from the Seamap segment totaled $2.6 million. During the quarter ended October 31, 2005, we recorded $1.7 million in revenues from Seamap. Sales of the GunLink systems during the second fiscal quarter of 2007 account for a substantial portion of the increase. We expect revenues from the sale of Seamap s products to increase in future periods. As of October 31, 2006, Seamap had a backlog of firm orders amounting to approximately $7.0 million, which we expect to deliver through the second quarter of fiscal 2008. We had expected revenues from the Seamap segment to be higher in the current quarter; however, we suspended shipments of the GunLink 4000 product during the quarter. See the Business Overview section above for additional discussion of the GunLink 4000 product.

Direct Costs

Mitcham Industries

Direct costs of seismic leasing are comprised of fixed costs (depreciation) and variable expenses that fluctuate with our equipment leasing revenues. In addition, we have costs associated with our equipment sales. The primary components of the variable expenses are freight, sublease expenses, repairs and maintenance, to the extent that repairs performed are normal wear and tear and not billable to the lease customer.

For the quarter ended October 31, 2006, lease pool depreciation expense was $2.0 million, which was $0.2 million lower than the lease pool depreciation expense for the comparable quarter in 2005. The decrease in depreciation expense from the quarter ended October 31, 2005 to the comparable quarter in 2006 was primarily due to certain equipment reaching the end of its depreciable life during each of those years, coupled with the sales of assets with remaining depreciable life during the intervening period. During the quarter ended October 31, 2006 we had an increase in the cost of previously leased equipment sold, as well as a $1.4 million increase in the cost of other equipment sold.

Variable expenses related to equipment leasing for the quarter ended October 31, 2006 decreased by approximately $0.5 million when compared to the same quarter in 2005, principally due to an increase in reimbursements of repair costs and to reduced costs for third-party rentals.

Our fixed and variable costs are important factors affecting our results of operations. Lease pool depreciation expense will vary between periods based on acquisitions of new equipment and sales of equipment with remaining depreciable life. We are experiencing increased demand for our equipment, including fully depreciated equipment, and increased demand for our equipment results in higher revenues with little impact on depreciation. During periods of high demand, such as the one we are currently experiencing, our ability to lease older equipment, including fully depreciated equipment, is enhanced; whereas in periods of low demand, the opposite is true. As a result, revenues and lease pool depreciation expense will not necessarily correlate directly. Over the long-term, lease

pool depreciation expense is impacted by increases in equipment purchases to meet growing demand for our leased equipment.

Seamap

Seamap s cost of sales for the three months ended October 31, 2006 were $2.2 million or $1.5 million more than the same quarter in 2005. Included in those costs are approximately $0.2 million non-recurring expenses related to the resolution of the problems associated with the GunLink 4000 discussed previously in the Business Overview. Material and labor, including fixed production costs, to manufacture the GunLink and BuoyLink systems are the major components of Seamap s cost of sales. We have increased many of these fixed costs in response to expected increased production requirements. These costs were not fully absorbed in the production process during the third quarter of fiscal 2007 due to the lower than expected sales of the GunLink products,. In addition, the initial production of the updated GunLink units resulted in higher than expected labor and material costs. We expect these costs to decrease in relation to sales as the production process is refined.

Operating Costs

Operating costs for the quarter ended October 31, 2006 totaled approximately $3.7 million or $1.1 million more than the $2.6 million for the corresponding period ending October 31, 2005. Operating costs includes general and administrative expenses and depreciation and amortization expense for non-lease pool equipment. The increase was primarily due to a non-cash charge of $0.4 million for stock-based compensation costs, increased depreciation and amortization cost of $0.3 million for additional equipment, primarily computers and software, $0.3 million of increased wages and benefits expense, primarily in the Seamap segment, costs related to the implementation of procedures related to the Sarbanes-Oxley Act of 2002, and the addition of our Russian operations.

Interest and Other Income, net

Interest income for the three months ended October 31, 2006 was approximately $0.3 million, compared to approximately $0.1 million for the same period a year ago. The increase was due an increase in interest rates, as well as an increase in the balance of invested funds. Other income was not significant for either period.

Provision for Income Taxes

For the quarter ended October 31, 2006, we recorded a benefit from income taxes of $1.3 million, consisting of a current tax provision of $0.2 million and a deferred benefit of $1.5 million. This compares with a current tax provision of $0.1 million for the quarter ended October 31, 2005. The deferred tax benefit in the quarter ended October 31, 2006 resulted from the reduction of the valuation allowance related to our deferred tax assets. Because of our continued profitability in certain taxation jurisdictions, specifically the United States, Canada and Australia, we can reasonably expect to realize increased amounts of our deferred tax assets. During the quarter ended October 31, 2006, current income taxes payable were reduced by approximately $0.2 million as a result of excess tax deductions relating to the exercise of non-qualified stock options. This reduction in income taxes payable was offset with a credit to additional paid-in capital and therefore did not reduce our provision for income taxes.

Nine Months Ended October 31, 2006 Compared to Nine Months Ended October 31, 2005

Revenues

During the nine months ended October 31, 2006, our consolidated revenues increased approximately $13.4 million as compared to the same period a year ago, reflecting an increase in leasing revenues of approximately $0.5 million, and an increase in equipment sales of $12.9 million, of which $6.5 million came from Seamap revenues, which we acquired in July 2005.

Mitcham Industries

For the nine months ended October 31, 2006, the Mitcham segment s revenues increased by $6.9 million to a total of $29.2 million, as compared to $22.3 million for the corresponding nine-month period in 2005. The increase was comprised of approximately a $0.5 million increase in leasing revenues, in addition to a $1.6 million increase in sales of lease pool equipment and $4.8 million increase in other equipment sales.

Seamap

For the nine months ended October 31, 2006, revenues from the Seamap segment totaled $8.6 million, compared to

$2.1 million for the same period last year. The revenues were generated primarily from the sales of Seamap s proprietary GunLink and BuoyLink products. The prior year period included the results of Seamap from July 12, 2005, the date of the Seamap acquisition. See the Business Overview section above for additional discussion of the GunLink 4000 product.

Direct Costs

Mitcham Industries

Our variable costs associated with equipment leasing decreased $0.4 million during the nine months ended October 31, 2006 when compared to the nine months ended October 31, 2005 due primarily to increased repair reimbursements. For the nine months ended October 31, 2006, lease pool depreciation expense, which makes up our fixed costs, was $5.5 million, which was $0.8 million lower than the lease pool depreciation expense for the comparable period in 2005. The decrease in depreciation expense from the nine months ended October 31, 2005 to the same period for 2006 was primarily due to certain equipment reaching the end of its depreciable life during each of those periods, coupled with the sales of assets with remaining depreciable life. During the nine months ended October 31, 2006, we had an increase in the cost of previously leased equipment sold of $1.4 million and a $3.0 million increase in the cost of other equipment sold.

Our fixed and variable costs are important factors affecting our results of operations. Lease pool depreciation expense will vary between periods based on acquisitions of new equipment and sales of equipment with remaining depreciable life. We are experiencing increased demand for our equipment, including fully depreciated equipment, and increased demand for our equipment results in higher revenues with little impact on depreciation. During periods of high demand, such as the one we are currently experiencing, our ability to lease older equipment, including fully depreciated equipment, is enhanced; whereas in periods of low demand, the opposite is true. As a result, revenues and lease pool depreciation expense will not necessarily correlate directly. Over the long-term, lease pool depreciation expense is impacted by increases in equipment purchases to meet growing demand for our leased equipment.

Seamap

Seamap s cost of sales for the nine-month period ended October 31, 2006 was $5.6 million. We reported $0. 9 million in direct costs for Seamap for the period beginning with the acquisition date of July 12, 2005 and ending October 31, 2005. Included in the cost of sales for Seamap were one-time expenditures related to the resolution of problems encountered with a specific version of the GunLink 4000 that totaled approximately $0.2 million and the effect of increased production costs, as discussed in connection with the three months ended October 31, 2006.. See the discussion under Business Overview for additional information on the GunLink 4000.

Operating Costs

Operating costs include general and administrative expenses and depreciation and amortization expense for non-lease pool equipment. For the nine months ended October 31, 2006, operating costs totaled approximately $11.6 million or $4.7 million more than operating costs of $6.9 million for the same period in fiscal 2006. The increase was primarily due to a full nine months of general and administrative costs related to Seamap and a non-cash charge of $1.1 million of stock-based compensation cost as required by SFAS 123R. Seamap general and administrative charges increased from $1.1 million for the nine month period ended October 31, 2005 to $4.4 million for the comparable period in fiscal 2007. Wages and research and development costs contributed the majority of Seamap s general and administrative expense.

Interest and Other Income, net

Interest income for the nine months ended October 31, 2006 was approximately $0.6 million, compared to approximately $0.3 million for the same period a year ago. The increase was due to rising interest rates and an increase in the balance of our invested funds.

Provision for Income Taxes

For the nine months ended October 31, 2006, we recorded a benefit from income taxes of $1.2 million, consisting of a current tax provision of $0.8 million and a deferred tax benefit of $2.0 million. This compares to a current tax provision of $25,000 for the nine months ended October 31, 2005. Because of our continued profitability in certain taxation jurisdictions, specifically the United States, Canada and Australia, we can reasonably expect to realize increased amounts of our deferred tax assets. The deferred tax benefit in the nine months ended October 31, 2006 results from the reduction of the valuation allowance related to our deferred tax assets. As of October 31, 2006, current income taxes payable had been reduced by approximately $0.5 million as a result of excess tax deductions relating to the exercise of non-qualified stock options. This reduction in income taxes payable was offset with a credit to additional paid-in capital and therefore did not reduce our provision for income taxes.

Liquidity and Capital Resources

As of October 31, 2006, we had net working capital of approximately $27.0 million as compared to net working capital of $22.6 million at January 31, 2006. Historically, our principal liquidity requirements and uses of cash have been for capital expenditures and working capital. Our principal source of cash has been from operations. Net cash provided by operating activities for the nine months ended October 31, 2006 was approximately $6.5 million, as compared $6.1 million for the nine months ended October 31, 2005. The increase in cash provided by operations resulted primarily from increased net income and non-cash charges for stock-based compensation, offset by the effect of the deferred tax benefit recognized in the nine months ended October 31, 2006. In the nine months ended October 31, 2006 net cash provided by operations was reduced by increases in accounts receivable, notes receivable and inventories during the period. The increase in accounts receivable resulted from generally higher levels of business and the timing of certain transactions. The increase in inventories relates primarily to increased raw materials and work in progress in our Seamap segment, specifically related to increased production activities surrounding the GunLink products. Also during the nine months ended October 31, 2006 cash provided by operating activities was increased by increases in accounts payable and accrued liabilities. This increase resulted from significant purchases of lease pool assets during the quarter for which payment is not due until after October 31, 2006.

We occasionally offer extended payment terms on equipment sales transactions. These terms are generally one to two years in duration. Generally, the sales revenue and cost of goods sold are recognized at the inception of the transaction. During the nine months ended October 31, 2006 we entered into four such transactions which resulted in approximately $3.5 million of deferred payments. As of October 31, 2006, we had approximately $3.3 million of notes receivable, net of allowances for doubtful accounts related to such transactions, while at January 31, 2006 we had approximately $3.1 million of such notes.

Net cash used in investing activities was $6.2 million for the nine months ended October 31, 2006, compared to net cash used in investing activities of $5.0 million for the nine months ended October 31, 2005. Increased purchases of seismic equipment and other equipment were offset to some extent with an increase in sales of used lease pool equipment.

Capital expenditures for the nine months ended October 31, 2006 totaled approximately $11.8 million (with $10.2 million being for purchase of lease pool equipment), as compared to capital expenditures of $4.0 million (of which $3.7 million was for purchases of lease pool equipment), for the comparable period in 2005. Our capital expenditures for the seismic equipment lease pool are generally made to fulfill specific lease contracts. The Company has been able to purchase new equipment for our lease pool at lower prices in recent years through volume purchasing discounts, which has allowed the Company to maintain a constant level of equipment at a lower unit cost. We have increased our purchases of lease pool equipment in the nine months ended October 31, 2006 as compared to the same period last year because of increased demand from our leasing customers. At October 31, 2006 we had purchase orders outstanding for the purchase of approximately $14.4 million of additional lease pool equipment. We expect the majority of this equipment to be delivered during the fourth quarter of our fiscal 2007. In addition we expect to add five GunLink 2000 systems, which are manufactured by Seamap, to the Mitcham segment lease pool. The units have an aggregate value of approximately $700,000.

In September 2006, we amended and extended our Exclusive Equipment Lease Agreement with Sercel, Inc. Pursuant to this agreement, and in return for certain exclusivity rights and discounts on purchases of equipment, we have agreed to certain levels of equipment purchases. Under these purchase commitments we are required to purchase approximately $20.0 million of equipment before December 31, 2008. We do not believe that these commitments exceed amounts that we would acquire in the normal course of our business. A portion of the capital expenditures made through October 31, 2006 and the majority of the outstanding purchase orders as of that date will be applied against our purchase commitment with Sercel.

The Seamap stock purchase agreement allowed for up to two additional payments to the former shareholders of Seamap if Seamap achieved certain annual revenue goals within a five-year time period. Seamap has met one of the two earn-out goals by generating a minimum of $8.0 million of revenues during the period of May 1, 2005 to April 30, 2006. As a result, the Company made a $1.0 million payment to the former shareholders of Seamap during the third quarter of fiscal 2007.

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Net cash provided by financing activities for the nine months ended October 31, 2006 was approximately $1.3 million, compared to net cash used in financing activities for the comparable period in 2005 of $36,000. Payments on borrowings accounted for the use of cash in 2005. Employee exercises of stock options and the excess tax benefits associated with the exercises accounted for the cash provided by financing in 2006.

We have a revolving credit facility with First Victoria National Bank (the Bank) which allows us to borrow up to $12.5 million through July 2007. We have not borrowed any amounts under this facility. Amounts available under the facility are determined by a borrowing base computed based upon our accounts receivable, existing inventory of lease equipment and the value of equipment to be purchased with proceeds of the facility. We believe that the full amount of the facility is available to us based on these criteria. Any amounts outstanding under the facility are due July 27, 2007, bear interest at prime and are secured by essentially all of our assets. The agreement contains certain covenants that require, among other things, that we maintain a debt to shareholders equity ratio of not more than 1.3 to 1.0, maintain a ratio of current assets to current liabilities of not less than 1.25 to 1.0, and not incur or maintain indebtedness, as defined in the agreement, of more than $1.0 million in the aggregate, without the prior written consent of the Bank. Prior to the maturity of this facility we expect to negotiate an extension of the facility or to negotiate a replacement facility.

On July 12, 2005, we acquired 100% of Seamap s outstanding common stock for $6.5 million, consisting of $3.5 million paid in cash at closing and $3.0 million issued in promissory notes payable to Seamap s former shareholders. The cash was provided from cash flow from operations. See Note 5 of the Notes to the Condensed Consolidated Financial Statements for a description of the notes.

At the present time, we believe that cash on hand and cash provided by future operations will be sufficient to fund our anticipated capital and liquidity needs over the next twelve months. However, should demand warrant, we may pursue additional sources of capital to fund capital expenditures or acquisitions.

Russian Operations

In November 2005, Mitcham established a wholly owned subsidiary, MSE, in Ufa, Bashkortostan, Russia. This subsidiary performs equipment rental and technical assistance services primarily for the Russian, Commonwealth of Independent States and the Eurasian theatre of operations. MSE has begun leasing equipment and we expect that the funds generated will be sufficient to meet the needs for operating the facility.

Critical Accounting Policies and Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires us to make estimates and assumptions in determining the reported amounts of assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the period. Significant estimates made by us in the accompanying condensed consolidated financial statements relate to reserves for uncollectible accounts receivable and useful lives of our lease pool assets, useful lives of amortizable intangible assets and our impairment assessment of the lease pool and various intangible assets.

Critical accounting policies are those that are most important to the portrayal of a company s financial position and results of operations and require management s subjective judgment. Below is a brief discussion of our critical accounting policies and estimates. A more comprehensive discussion of our critical accounting policies is included in our Annual Report on Form 10-K for the year ended January 31, 2006.

Revenue Recognition

Leases

We recognize lease revenue ratably over the term of the lease unless there is a question as to whether it is collectible. Commission income is recognized once it has been paid to us. We do not enter into leases with embedded maintenance obligations. Under our standard lease contract, the lessee is responsible for maintenance and repairs to the equipment, excluding normal wear and tear. We provide technical advice to our customers as part of our customer service practices.

Equipment Sales

We recognize revenue and cost of goods sold from the equipment sales upon agreement of terms and when delivery has occurred unless there is a question as to its collectibility. We occasionally offer extended payment terms on equipment sales transactions. These terms are generally one to two years in duration.

Allowance for Doubtful Accounts

We make provisions to the allowance for doubtful accounts periodically, as conditions warrant, based on the collectibility of receivables. In certain instances when customers have been unable to repay their open accounts receivable balances, we have agreed to a structured repayment program using an interest-bearing promissory note. In these cases, we provide a reserve for doubtful accounts against the balance and do not recognize interest earned until the entire principal balance has been collected.

Long-Lived Assets

We carry property and equipment at cost, net of accumulated depreciation, and compute depreciation on the straight-line method over the estimated useful lives of the property and equipment, which range from two to ten years. Cables are depreciated over two years, geophones over three years, channel boxes over a five year period and earth vibrators and other heavy equipment are depreciated over a ten year period. Buildings are depreciated over 40 years, property improvements are amortized over ten years and leasehold improvements are amortized over the shorter of useful life or the life of the leases. Intangible assets are amortized from three to 15 years. Seismic equipment held for lease consists primarily of recording channels and peripheral equipment and is carried at cost, net of accumulated depreciation. As this equipment is subject to technological obsolescence and wear and tear, no salvage value is assigned to it.

The estimated useful lives for rental equipment are based on the Company s experience as to the economic useful life of its products. We review and consider industry trends in determining the appropriate useful life for our lease pool equipment, including technological obsolescence, market demand and actual historical useful service life of our lease pool equipment. Additionally, to the extent information is publicly available, the Company also compares its depreciation policies to other companies with similar rental products for reasonableness. When we purchase new equipment for our lease pool, we begin to depreciate it upon its first use and depreciation continues each month until the equipment is fully depreciated, whether or not the equipment is actually in use during that entire time period. Fully depreciated assets are removed from our books only if they are not expected to have any future revenue generating capacity, otherwise they remain on our books.

In accordance with SFAS 144, the Company performs a review of its lease pool assets for potential impairment when events or changes in circumstances indicate that the carrying amount may not be fully recoverable. We typically review all major categories of assets (not each individual asset) in our consolidated lease pool with remaining net book value to ascertain whether or not we believe that a particular asset group will generate sufficient cash flow over their remaining life to recover the remaining carrying value of those assets. Assets that we believe will not generate cash flow sufficient to cover the remaining net book value are subject to impairment. We make our assessments based on customer demand, current market trends and market value of our equipment to determine if it will be able to recover its remaining net book value from future leasing or sales. During fiscal 2006, we recorded an impairment charge of $0.6 million related to the valuation of our seismic equipment lease pool.

Income Taxes

Deferred tax assets and liabilities are determined based on temporary differences between income and expenses reported for financial reporting and tax reporting. We have assessed, using all available positive and negative evidence, the likelihood that the deferred tax assets will be recovered from future taxable income.

Under SFAS No. 109, *Accounting for Income Taxes*, an enterprise must use judgment in considering the relative impact of negative and positive

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evidence. The weight given to the potential effect of negative and positive evidence should be commensurate with the extent to which it can be objectively verified. The more negative evidence that exists, (a) the more positive evidence is necessary and (b) the more difficult it is to support a conclusion that a valuation allowance is not needed for some portion or all of the deferred tax asset. Among the more significant types of evidence that we consider are:

- taxable income projections in future years;
- whether the carry forward period is so brief that it would limit realization of tax benefits;
- future sales and operating cost projections that will produce more than enough taxable income to realize the deferred tax asset based on existing sales prices and cost structures; and
- our earnings history exclusive of the loss that created the future deductible amount coupled with evidence indicating that the loss is an aberration rather than a continuing condition.

We intend to maintain the recorded valuation allowances until sufficient positive evidence exists to support a reversal of the tax valuation allowances. In determining the valuation allowance as of October 31, 2006, we considered the following positive indicators:

- the current level of worldwide oil and gas exploration activities resulting from historically high prices for oil and natural gas;
- increasing world demand for oil;
- our anticipated positive income in certain jurisdictions; and
- our existing customer relationships.

We also considered the following negative indicators:

- the risk of the world oil supply increasing, thereby depressing the price of oil and natural gas;
- the risk of decreased global demand for oil; and
- the potential for increased competition in the seismic equipment leasing and sales business.

Based on our evaluation of the evidence, we believed that it was appropriate to reduce our valuation allowance on the deferred tax asset by $3.0 million during fiscal year 2006. In the nine months ended October 31, 2006 our deferred tax assets increased by approximately $2.5 million. We provided an additional $500,000 of valuation allowance against this amount, resulting in a net benefit of approximately $2.0 million.

Stock Options

On February 1, 2006, we adopted the provisions of SFAS 123R, *Share-Based Payments*, using the modified prospective method. Under this method, prior periods are not restated. We use the Black-Scholes-Merton option model, which requires extensive use of accounting judgment and financial estimates, including estimates of how long an associate will hold their vested stock option before exercise, the estimated volatility of the Company s common stock over the expected term, and the number of options that will be forfeited prior to the completion of vesting requirements. Application of other assumptions could result in significantly different estimates of fair value of stock-based compensation and consequently, the related expense recognized in our financial statements. The provisions of SFAS 123R apply to new stock option grants and stock options outstanding, but not yet vested, as of February 1, 2006.

Prior to the adoption of SFAS 123R, we accounted for our stock-based compensation in accordance with SFAS No. 123 and the disclosure requirements of SFAS 148 under the intrinsic value method described in the provisions of APB 25 and related accounting interpretations. Since stock options were granted at prices that equaled or exceeded their estimated fair market value at the date of the grant, under APB 25 no compensation expense was recognized at the date of the grant.

As a result of the adoption of SFAS 123R, we recognized approximately $1.1 million in non-cash compensation expense related to our stock option plans for the nine months ended October 31, 2006. Accordingly, net income was reduced by approximately $1.1 million, and basic and diluted net income per common share was reduced by approximately $0.11 and $0.12 per share, respectively, for the same nine-month period.

As of October 31, 2006, there was approximately $2.3 million of total unrecognized compensation expense related to unvested stock options granted under the Company s share-based compensation plans. That expense is expected

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to be recognized over a weighted average period of 2.3 years. As of October 31, 2006, there was approximately $421,000 of unrecognized stock-based compensation expense related to unvested restricted stock awards. That cost is expected to be recognized over a weighted average period of 2.7 years.

New Accounting Pronouncements

In June 2006, FASB issued FASB Interpretation No. 48, *Accounting for Uncertainty in Income Taxes* (FIN 48). FIN 48 clarifies how uncertain tax positions that have been taken or are expected to be taken on a company s tax return should be recognized, measured, presented and disclosed in the financial statements. The cumulative effect of applying this pronouncement to uncertain tax positions at the date of adoption will be recorded during the fiscal year beginning February 1, 2007. The Company is currently evaluating the effect that the adoption of FIN 48 will have on its consolidated financial position and results of operations.

Item 3. *Quantitative and Qualitative Disclosures About Market Risk*

Market Risk

We are exposed to market risk, which is the potential loss arising from adverse changes in market prices and rates. We have not entered, or intend to enter, into derivative financial instruments for hedging or speculative purposes.

Foreign Currency Risk

We operate in a number of foreign locations which gives rise to risk from changes in foreign exchange rates. To the extent possible, we attempt to denominate our transactions in foreign locations in U.S. dollars. For those cases in which transactions are not denominated in U.S. dollars, we are exposed to risk from changes in exchange rates to the extent that non-U.S. dollar revenues exceed non-U.S. dollar expenses related to those operations. Our non-U.S. dollar transactions are denominated primarily in British pounds sterling, Canadian dollars, Australian dollars and Singapore dollars. As a result of these transactions, we generally hold cash balances that are denominated in these foreign currencies. At October 31, 2006, our consolidated cash and cash equivalents included foreign currency denominated amounts equivalent to approximately $5.5 million in U.S. dollars. A ten percent increase in the U.S. dollar versus each of these currencies would result in a loss of approximately $550,000 in the U.S. dollar value of these deposits. We do not currently hold or issue foreign exchange contracts or other derivative instruments to hedge these exposures.

Certain of our foreign operations are conducted through wholly owned foreign subsidiaries that have functional currencies other than the U.S. dollar. We currently have subsidiaries whose functional currencies are the Canadian dollar, British pound sterling, Australian dollar and the Singapore dollar. Assets and liabilities from these subsidiaries are translated into U.S. dollars at the exchange rate in effect at each balance sheet date. The resulting translation gains or losses are reflected as Accumulated Other Comprehensive Income in the Shareholders Equity section of our Consolidated Balance Sheets. Approximately 51% of our net assets are impacted by changes in foreign currencies in relation to the U.S. dollar. We recorded an increase of approximately $718,000 in our equity in the nine months ended October 31, 2006 related to weakening of the U.S. dollar against the foreign currencies mentioned above.

Item 4. *Controls and Procedures*

Evaluation of Disclosure Controls and Procedures

As required by Exchange Act Rule 13a-15(b), we have evaluated, under the supervision and with the participation of our management, including our principal executive officer and principal financial officer, the effectiveness of the design and operation of our disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e) under the Exchange Act) as of the end of the period covered by this report. Our disclosure controls and procedures are designed to provide reasonable assurance that the information required to be disclosed by the Company in reports that it files under the Exchange Act is accumulated and communicated to the Company s management, including our principal executive officer and principal financial officer, as appropriate, to allow timely decisions regarding required disclosure and is recorded, processed, summarized and reported within the time periods specified in the rules and forms of the SEC. Based on this evaluation, our principal executive officer and principal financial officer

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have concluded that our disclosure controls and procedures were effective as of October 31, 2006 at the reasonable assurance level.

Changes in Internal Controls over Financial Reporting

There was no change in our system of internal control over financial reporting during the three months ended October 31, 2006, that has materially affected, or is reasonably likely to materially affect, our internal control over financial reporting.

PART II. OTHER INFORMATION

Item 1. *Legal Proceedings*

From time to time, we are a party to legal proceedings arising in the ordinary course of business. We are not currently a party to any litigation that we believe could have a material adverse effect on our results of operations or financial condition.

Item 1A. *Risk Factors*

The Risk Factors included in our Annual Report on Form 10-K for the year ended January 31, 2006 have not materially changed.

Item 2. *Unregistered Sales of Equity Securities and Use of Proceeds*

Not applicable.

Item 3. *Defaults Upon Senior Securities*

Not applicable.

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

Not applicable

Item 5. *Other Information*

Not applicable.

Item 6. *Exhibits*

The following documents are filed as exhibits to this Report:

3.1	Amended and Restated Articles of Incorporation of Mitcham Industries, Inc. (1)
3.2	Second Amended and Restated Bylaws of Mitcham Industries, Inc. (2)
10.1	Exclusive Equipment Lease Agreement, dated September 12, 2006, between Sercel, Inc. and Mitcham Industries, Inc.(3)
31.1	Certification of Billy F. Mitcham, Jr., Chief Executive Officer, pursuant to Rule 13a-14(a) of the Securities Exchange Act of 1934, as amended.
31.2	Certification of Robert P. Capps, Executive Vice President-Finance and Chief Financial Officer, pursuant to Rule 13a-14(a) of the Securities Exchange Act of 1934, as amended.
32.1	Certification of Billy F. Mitcham, Jr., Chief Executive Officer, pursuant to 18 U.S.C. § 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
32.2	Certification of Robert P. Capps, Executive Vice President-Finance and Chief Financial Officer, pursuant to 18 U.S.C. § 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.

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(1) Incorporated by reference to Exhibit 3.1 of the Company s Registration Statement on Form S-8 (File No. 333-67208), filed with the SEC on August 9, 2001.

(2) Incorporated by reference to Exhibit 3.2 of the Company s Annual Report on Form 10-K for the fiscal year ended January 31, 2004, filed with the SEC on May 28, 2004.

(3) Incorporated by reference to Exhibit 10.1 of the Company s Current Report on form 8-K, filed with the SEC on September 12, 2006.

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SIGNATURES

Pursuant to the requirements 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.

	MITCHAM INDUSTRIES, INC.
	/s/ Robert P. Capps
Date: December 12, 2006	
	Robert P. Capps Executive Vice President-Finance and Chief Financial Officer (Duly Authorized Officer and Chief Accounting Officer)

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