

DIAMOND OFFSHORE DRILLING INC

Form 10-K

February 23, 2010

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**UNITED STATES SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549
FORM 10-K**

**ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES
EXCHANGE ACT OF 1934
For the fiscal year ended December 31, 2009**

OR

**TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES
EXCHANGE ACT OF 1934
For the transition period from _____ to _____**

**Commission file number 1-13926
DIAMOND OFFSHORE DRILLING, INC.
(Exact name of registrant as specified in its charter)**

Delaware **76-0321760**
(State or other jurisdiction of incorporation or (I.R.S. Employer Identification No.)
organization)

**15415 Katy Freeway
Houston, Texas 77094**
(Address and zip code of principal executive offices)
(281) 492-5300
(Registrant's telephone number, including area code)

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

Title of each class	Name of each exchange on which registered
Common Stock, \$0.01 par value per share	New York Stock Exchange

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

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

Yes No

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Act. Yes No

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

Yes No

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes No

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

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

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

reporting company)

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). Yes
o No p

State the aggregate market value of the voting and non-voting common equity held by non-affiliates computed by reference to the price at which the common equity was last sold as of the last business day of the registrant's most recently completed second fiscal quarter.

As of June 30, 2009

\$5,694,071,609

Indicate the number of shares outstanding of each of the registrant's classes of common stock, as of the latest practicable date.

As of February 19, 2010

Common Stock, \$0.01 par value
per share

139,026,178 shares

DOCUMENTS INCORPORATED BY REFERENCE

Portions of the definitive proxy statement relating to the 2010 Annual Meeting of Stockholders of Diamond Offshore Drilling, Inc., which will be filed within 120 days of December 31, 2009, are incorporated by reference in Part III of this report.

DIAMOND OFFSHORE DRILLING, INC.
FORM 10-K for the Year Ended December 31, 2009
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Diamond Offshore Drilling, Inc. is a leading, global offshore oil and gas drilling contractor with a fleet of 47 offshore rigs consisting of 32 semisubmersibles, 14 jack-ups and one drillship. Unless the context otherwise requires, references in this report to Diamond Offshore, we, us or our mean Diamond Offshore Drilling, Inc. and our consolidated subsidiaries. We were incorporated in Delaware in 1989.

The Fleet

Our fleet includes some of the most technologically advanced rigs in the world, enabling us to offer a broad range of services worldwide in various markets, including the deepwater, harsh environment, conventional semisubmersible and jack-up markets.

Semisubmersibles. We own and operate 32 semisubmersibles, consisting of 13 high-specification and 19 intermediate rigs. Semisubmersible rigs consist of an upper working and living deck resting on vertical columns connected to lower hull members. Such rigs operate in a semi-submerged position, remaining afloat, off bottom, in a position in which the lower hull is approximately 55 feet to 90 feet below the water line and the upper deck protrudes well above the surface. Semisubmersibles are typically anchored in position and remain stable for drilling in the semi-submerged floating position due in part to their wave transparency characteristics at the water line. Semisubmersibles can also be held in position through the use of a computer controlled thruster (dynamic-positioning) system to maintain the rig's position over a drillsite. We have five semisubmersible rigs in our fleet with this capability.

Our high-specification semisubmersibles are generally capable of working in water depths of 4,000 feet or greater or in harsh environments and have other advanced features, as compared to intermediate semisubmersibles. As of January 25, 2010, seven of our 13 high-specification semisubmersibles, including the recently acquired *Ocean Courage*, were located in the United States, or U.S., Gulf of Mexico, or GOM. At that date we had two high-specification semisubmersibles rigs operating offshore Brazil, while a third was en route to Brazil from the GOM. Of our remaining high-specification semisubmersibles, one was located offshore each of Malaysia and Angola, while the final rig, the *Ocean Valor*, was completing its commissioning in Singapore. See *Fleet Enhancements and Additions*.

Our intermediate semisubmersibles generally work in maximum water depths up to 4,000 feet. As of January 25, 2010, we had 19 intermediate semisubmersible rigs in various locations around the world. Seven of these semisubmersibles were operating offshore Brazil and an eighth unit was en route to Brazil; three were located in the North Sea; two each were located offshore Australia and offshore Mexico; one was located in the GOM and one offshore Vietnam. One unit was en route to the Falkland Islands, and our final intermediate semisubmersible rig, the *Ocean Bounty*, was in the process of being cold stacked in Malaysia.

Drillship. We have one high-specification drillship, the *Ocean Clipper*, which was located offshore Brazil as of January 25, 2010. Drillships, which are typically self-propelled, are positioned over a drillsite through the use of either an anchoring system or a dynamic-positioning system similar to those used on certain semisubmersible rigs. Deepwater drillships compete in many of the same markets as do high-specification semisubmersible rigs.

Both semisubmersible rigs and drillships are commonly referred to as floaters in the offshore drilling industry.

Jack-ups. We currently have 14 jack-up drilling rigs. Jack-up rigs are mobile, self-elevating drilling platforms equipped with legs that are lowered to the ocean floor until a foundation is established to support the drilling platform. The rig hull includes the drilling rig, jacking system, crew quarters, loading and unloading facilities, storage areas for bulk and liquid materials, heliport and other related equipment. Our jack-ups are used for drilling in water depths from 20 feet to 350 feet. The water depth limit of a particular rig is principally determined by the length of the rig's legs. A jack-up rig is towed to the drillsite with its hull riding in the sea, as a vessel, with its legs retracted. Once over a drillsite, the legs are lowered until they rest on the seabed and jacking continues with the legs penetrating the seabed until resistance is sufficient to elevate the hull above the surface of the water. After

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completion of drilling operations, the hull is lowered until it rests in the water and then the legs are retracted for relocation to another drillsite.

Most of our jack-up rigs are equipped with a cantilever system that enables the rig to cantilever or extend its drilling package over the aft end of the rig. This is particularly important when attempting to drill over existing platforms. Cantilever rigs have historically earned higher dayrates and achieved greater utilization compared to slot rigs, which do not have this capability.

As of January 25, 2010, six of our 14 jack-up rigs were located in the GOM and a seventh rig, the *Ocean Scepter*, was en route from Uruguay for a six-well drilling program in the GOM. Four of those rigs are independent-leg cantilevered units, two are mat-supported cantilevered units, and one is a mat-supported slot unit. We cold-stacked the three mat-supported jack-up rigs located in the GOM during the second quarter of 2009 and are no longer actively marketing these drilling units. Of our seven remaining jack-up rigs, all of which are independent-leg cantilevered units, two each were located offshore Egypt and Mexico, and one was located offshore each of Indonesia, Croatia and the Joint Petroleum Development Area, or JPDA, between Australia and Timor Leste.

Fleet Enhancements and Additions. Our long-term strategy has been to economically upgrade our fleet to meet customer demand for advanced, efficient, high-tech rigs, particularly deepwater semisubmersibles, in order to maximize the utilization of, and dayrates earned by, the rigs in our fleet. During 2009, we acquired two new-build deepwater, semisubmersible, dynamically-positioned drilling rigs, the *Ocean Courage* (June 2009) and the *Ocean Valor* (September 2009). As of January 25, 2010, the *Ocean Courage* was in process of completing its commissioning and preparing for its first contract in the GOM, which we expect to begin in the first quarter of 2010. We expect commissioning of the *Ocean Valor* to be completed in Singapore in the first quarter of 2010.

In addition, excluding our two new deepwater floaters acquired in 2009, we have, since 1995, increased the number of our rigs capable of operating in 3,500 feet or more of water from three rigs to 14 (11 of which are high-specification units), primarily by upgrading our existing fleet. Seven of these upgrades were to our Victory-class semisubmersible rigs, the design of which is well-suited for significant upgrade projects. We have two additional Victory-class intermediate semisubmersibles that could potentially be upgraded at some time in the future.

We will evaluate further rig acquisition and upgrade opportunities as they arise. However, we can provide no assurance whether, or to what extent, we will continue to make rig acquisitions or upgrades to our fleet. See

Management's Discussion and Analysis of Financial Condition and Results of Operations Sources of Liquidity and Capital Resources Liquidity and Capital Requirements in Item 7 of this report.

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More detailed information concerning our fleet of mobile offshore drilling rigs, as of January 25, 2010, is set forth in the table below.

Type and Name High-Specification	Nominal Water Depth Rating (a)	Attributes	Year Built/Latest Enhancement (b)	Current Location (c)	Customer (d)
Floaters					
Semisubmersibles (13):					
Ocean Valor	10,000	DP; 15K; 4M	2009	Singapore	Commissioning Commissioning and contract preparation:
Ocean Courage	10,000	DP; 15K; 4M	2009	GOM	Petrobras Americas
Ocean Confidence	10,000	DP; 15K; 4M	2001/2008	GOM	Murphy Exploration
Ocean Monarch	10,000	VC; 15K; 4M	1974/2008	GOM	Marathon Oil
Ocean Endeavor	10,000	VC; 15K; 4M	1975/2007	GOM	ExxonMobil
Ocean Rover	8,000	VC; 15K; 4M	1973/2008	Malaysia	Shell Malaysia
Ocean Baroness	7,000	VC; 15K; 4M	1973/2002	GOM	Hess
Ocean Victory	5,500	VC; 15K; 3M	1972/2006	GOM	ATP Oil & Gas
Ocean America	5,500	SP; 15K; 3M	1988/1999	GOM	Mariner Energy
Ocean Valiant	5,500	SP; 15K; 3M	1988/1999	Angola	Total
Ocean Star	5,500	VC; 15K; 3M	1974/1999	Brazil	Mobilizing: OGX
Ocean Alliance	5,250	DP; 15K; 3M	1988/1999	Brazil	Petrobras
Ocean Quest	4,000	VC; 15K; 3M	1973/1996	Brazil	OGX
Drillship (1):					
Ocean Clipper	7,875	DP; 15K; 3M	1976/1999	Brazil	Petrobras
Intermediate					
Semisubmersibles (19):					
Ocean Winner	4,000	3M	1977/2004	Brazil	Petrobras
Ocean Worker	4,000	3M	1982/2008	Brazil	Petrobras
Ocean Yatzy	3,300	DP	1989/1998	Brazil	Petrobras
Ocean Voyager	3,200	VC; 3M	1973/1995	Mexico	Actively marketing
Ocean Patriot	3,000	15K; 3M	1982/2003	Australia	Esso Australia
Ocean Epoch	3,000	3M	1977/2000	Australia	BHPB
Ocean General	3,000	3M	1976/2000	Vietnam	PVEP Dai Hung
Ocean Yorktown	2,850	3M	1976/1996	Brazil	Petrobras
Ocean Concord	2,300	3M	1975/1999	Brazil	Petrobras
Ocean Lexington	2,200	3M	1976/1995	Brazil	Mobilizing: OGX
Ocean Saratoga	2,200	3M	1976/1995	GOM	Taylor Energy
Ocean Whittington	1,650	3M	1974/1995	Brazil	Petrobras
Ocean Bounty	1,500	VC; 3M	1977/1992	Malaysia Falkland	Preparing for cold stacking
Ocean Guardian	1,500	15K; 3M	1985	Islands	Mobilizing: AGR/Desire
Ocean New Era	1,500	3M	1974/1990	Mexico North	PEMEX
Ocean Princess	1,500	15K; 3M	1977/1998	Sea/U.K.	Talisman
Ocean Vanguard	1,500	15K; 3M	1982		Statoil

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				North Sea/Norway	
Ocean Nomad	1,200	3M	1975/2001	North Sea/U.K.	Actively Marketing
Ocean Ambassador	1,100	3M	1975/1995	Brazil	OGX
Jack-ups (14):					
Ocean Scepter	350	IC; 15K; 3M	2008	GOM	Mobilizing: Arena Energy Petronas Carigali Timor
Ocean Shield	350	IC; 15K; 3M	2008	JPDA	Leste
Ocean Titan	350	IC; 15K; 3M	1974/2004	GOM	ANKOR Energy Bareboat charter to
Ocean King	300	IC; 3M	1973/1999	Croatia	CROSCO
Ocean Nugget	300	IC	1976/1995	Mexico	PEMEX
Ocean Summit	300	IC	1972/2003	Mexico	PEMEX
Ocean Heritage	300	IC	1981/2002	Egypt	SUCO
Ocean Spartan	300	IC	1980/2003	GOM	Samson Offshore
Ocean Spur	300	IC	1981/2003	Egypt	WEPCO
Ocean Sovereign	300	IC	1981/2003	Indonesia	Kodeco
Ocean Champion	250	MS	1975/2004	GOM	Cold stacked
Ocean Columbia	250	IC	1978/1990	GOM	Shipyard: Survey
Ocean Crusader	200	MC	1982/1992	GOM	Cold stacked
Ocean Drake	200	MC	1983/1986	GOM	Cold stacked

Attributes

DP = Dynamically-Positioned/Self-Propelled

IC = Independent-Leg Cantilevered Rig

MC = Mat-Supported Cantilevered Rig

MS = Mat-Supported Slot Rig

VC = Victory-Class

SP = Self-Propelled

3M = Three Mud Pumps

4M = Four Mud Pumps

15K = 15,000 psi well control
system

See the footnotes to this table on the following page.

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- (a) Nominal water depth (in feet), as described above for semisubmersibles and drillships, reflects the current operating water depth capability for each drilling unit. In many cases, individual rigs are capable of drilling, or have drilled in, greater water depths. In all cases, floating rigs are capable of working successfully at greater depths than their nominal water depth. On a case by case basis, we may achieve a greater depth capacity by providing additional equipment.
- (b) Such enhancements may include water depth upgrades, mud pump additions and increases in deck load capacity
- (c) GOM means U.S. Gulf of Mexico. Four of our drilling rigs were en route between geographic locations. They

have been presented in the preceding table in the geographic location in which they are expected to commence drilling operations in 2010.

- (d) For ease of presentation in this table, customer names have been shortened or abbreviated.

Markets

The principal markets for our offshore contract drilling services are the following:
the Gulf of Mexico, including the U.S. and Mexico;

South America, principally in Brazil;

Europe, principally in the United Kingdom, or U.K., and Norway;

the Mediterranean Basin, including Egypt;

Africa, currently in Angola;

Australia and Asia, including Malaysia, Indonesia and Vietnam; and

the Middle East, including Kuwait, Qatar and Saudi Arabia.

We actively market our rigs worldwide. From time to time our fleet operates in various other markets throughout the world as the market demands. See Note 17 Segments and Geographic Area Analysis to our Consolidated Financial Statements in Item 8 of this report.

We believe our presence in multiple markets is valuable in many respects. For example, we believe that our experience with safety and other regulatory matters in the U.K. has been beneficial in Australia and other international areas in which we operate, while production experience we have gained through our Brazilian and North Sea operations has potential application worldwide. Additionally, we believe our performance for a customer in one market segment or area enables us to better understand that customer's needs and better serve that customer in different market segments or other geographic locations.

Offshore Contract Drilling Services

Our contracts to provide offshore drilling services vary in their terms and provisions. We typically obtain our contracts through competitive bidding, although it is not unusual for us to be awarded drilling contracts without competitive bidding. Our drilling contracts generally provide for a basic drilling rate on a fixed dayrate basis regardless of whether or not such drilling results in a productive well. Drilling contracts may also provide for lower rates during periods when the rig is being moved or when drilling operations are interrupted or restricted by equipment breakdowns, adverse weather conditions or other conditions beyond our control. Under dayrate contracts, we generally pay the operating expenses of the rig, including wages and the cost of incidental supplies. Historically, dayrate contracts have accounted for the majority of our revenues. In addition, from time to time, our dayrate contracts may also provide for the ability to earn an incentive bonus from our customer based upon performance.

A dayrate drilling contract generally extends over a period of time covering either the drilling of a single well or a group of wells, which we refer to as a well-to-well contract, or a fixed term, which we refer to as a term contract, and may be terminated by the customer in the event the drilling unit is destroyed or lost or if drilling operations are suspended for an extended period of time as a result of a breakdown of equipment or, in some cases, due to other events beyond the control of either party to the contract. In addition, certain of our contracts permit the customer to terminate the contract early by giving notice, and in most circumstances may require the payment of an early termination fee by the customer. The contract term in many instances may also be extended by the customer exercising options for the drilling of additional wells or for an additional length of time, generally at competitive market rates and mutually agreeable terms at the time of the extension. See Risk Factors *The terms of our drilling contracts may limit our ability to attain profitability in a declining market or to benefit from increasing dayrates in an improving market*, Risk Factors *Our drilling contracts may be terminated due to events beyond our control*, Risk Factors *Our business involves numerous operating hazards, and we are not fully insured against all of them* and Risk Factors *We*

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have elected to self-insure for physical damage to rigs and equipment caused by named windstorms in the U.S. Gulf of Mexico in Item 1A of this report, which are incorporated herein by reference. For a discussion of our contract backlog, see Management's Discussion and Analysis of Financial Condition and Results of Operations Overview *Contract Drilling Backlog* in Item 7 of this report, which is incorporated herein by reference.

Customers

We provide offshore drilling services to a customer base that includes major and independent oil and gas companies and government-owned oil companies. During 2009, we performed services for 47 different customers and for 49 different customers during each of 2008 and 2007. During 2009, 2008 and 2007, one of our two customers in Brazil, *Petr leo Brasileiro S.A.*, or Petrobras (a Brazilian multinational energy company that is majority-owned by the Brazilian government), accounted for 15%, 13% and 9% of our annual total consolidated revenues, respectively. No other customer accounted for 10% or more of our annual total consolidated revenues during 2009 and 2008, nor did any single customer account for 10% or more of our annual total consolidated revenues during 2007.

Brazil is the most active floater market in the world today. As of the date of this report, the greatest concentration of our operating assets outside the United States is offshore Brazil, where we have 12 rigs in our fleet either currently working or contracted to work during 2010. Our contract backlog attributable to our expected operations offshore Brazil is \$1.1 billion, \$1.1 billion and \$867.0 million for the years 2010, 2011 and 2012, respectively, and \$1.2 billion in the aggregate for the years 2013 to 2016. See Management's Discussion and Analysis of Financial Condition and Results of Operations Overview *Contract Drilling Backlog* included in Item 7 of this report.

We principally market our services in North America through our Houston, Texas office. We market our services in other geographic locations principally from our office in The Hague, The Netherlands with support from our regional offices in Aberdeen, Scotland and Perth, Australia. We provide technical and administrative support functions from our Houston office.

Competition

The offshore contract drilling industry is highly competitive with numerous industry participants, none of which at the present time has a dominant market share. The drilling industry has experienced consolidation in recent years and may experience additional consolidation, which could create additional large competitors. Some of our competitors may have greater financial or other resources than we do. We compete with offshore drilling contractors that together have more than 600 mobile rigs available worldwide.

The offshore contract drilling industry is influenced by a number of factors, including global economies and demand for oil and natural gas, current and anticipated prices of oil and natural gas, expenditures by oil and gas companies for exploration and development of oil and natural gas and the availability of drilling rigs.

Drilling contracts are traditionally awarded on a competitive bid basis. Intense price competition is often the primary factor in determining which qualified contractor is awarded a job. Customers may also consider rig availability and location, a drilling contractor's operational and safety performance record, and condition and suitability of equipment. We believe we compete favorably with respect to these factors.

We compete on a worldwide basis, but competition may vary significantly by region at any particular time. See Markets. Competition for offshore rigs generally takes place on a global basis, as these rigs are highly mobile and may be moved, at a cost that may be substantial, from one region to another. Competing contractors are able to adjust localized supply and demand imbalances by moving rigs from areas of low utilization and dayrates to areas of greater activity and relatively higher dayrates. Significant new rig construction and upgrades of existing drilling units could also intensify price competition. See Risk Factors *Our industry is highly competitive and cyclical, with intense price competition* in Item 1A of this report, which is incorporated herein by reference.

Governmental Regulation

Our operations are subject to numerous international, U.S., state and local laws and regulations that relate directly or indirectly to our operations, including regulations controlling the discharge of materials into the environment, requiring removal and clean-up under some circumstances, or otherwise relating to the protection of

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the environment, and may include laws or regulations pertaining to climate change, carbon emissions or energy use. See Risk Factors *Governmental laws and regulations may add to our costs or limit our drilling activity* and Risk Factors *Compliance with or breach of environmental laws can be costly and could limit our operations* in Item 1A of this report, which are incorporated herein by reference.

Operations Outside the United States

Our operations outside the U.S. accounted for approximately 66%, 59% and 50% of our total consolidated revenues for the years ended December 31, 2009, 2008 and 2007, respectively. See Risk Factors *A significant portion of our operations are conducted outside the United States and involve additional risks not associated with domestic operations*, Risk Factors *Our drilling contracts offshore Mexico expose us to greater risks than we normally assume* and Risk Factors *Fluctuations in exchange rates and nonconvertibility of currencies could result in losses to us* in Item 1A of this report, which are incorporated herein by reference.

Employees

As of December 31, 2009, we had approximately 5,500 workers, including international crew personnel furnished through independent labor contractors. We have experienced satisfactory labor relations and provide comprehensive benefit plans for our employees.

Access to Company Filings

We are subject to the informational requirements of the Securities Exchange Act of 1934, as amended, or the Exchange Act, and accordingly file annual, quarterly and current reports, any amendments to those reports, proxy statements and other information with the United States Securities and Exchange Commission, or SEC. You may read and copy the information we file with the SEC at the public reference facilities maintained by the SEC at 100 F Street, N.E., Washington, DC 20549. Please call the SEC at 1-800-SEC-0330 for further information on the operation of the public reference room. Our SEC filings are also available to the public from the SEC's Internet site at www.sec.gov or from our Internet site at www.diamondoffshore.com. Our website provides a hyperlink to a third-party SEC filings website where these reports may be viewed and printed at no cost as soon as reasonably practicable after we have electronically filed such material with, or furnished it to, the SEC. The information contained on our website, or on other websites linked to our website, is not part of this report.

Item 1A. Risk Factors.

Our business is subject to a variety of risks, including the risks described below. You should carefully consider these risks when evaluating us and our securities. The risks and uncertainties described below are not the only ones facing our company. We are also subject to a variety of risks that affect many other companies generally, as well as additional risks and uncertainties not known to us or that we currently believe are not as significant as the risks described below. If any of the following risks actually occur, our business, financial condition, results of operations and cash flows, and the trading prices of our securities, may be materially and adversely affected.

Our business depends on the level of activity in the oil and gas industry, which is significantly affected by volatile oil and gas prices.

Our business depends on the level of activity in offshore oil and gas exploration, development and production in markets worldwide. Worldwide demand for oil and gas, oil and gas prices, market expectations of potential changes in these prices and a variety of political and economic factors significantly affect this level of activity. However, higher or lower commodity demand and prices do not necessarily translate into increased or decreased drilling activity since our customers' project development time, reserve replacement needs, as well as expectations of future commodity demand and prices all combine to affect demand for our rigs. Oil and gas prices have been, and are expected to continue to be, extremely volatile and are affected by numerous factors beyond our control, including:

worldwide demand for oil and gas;

the level of economic activity in energy-consuming markets;

the worldwide economic environment or economic trends, such as recessions;

the ability of the Organization of Petroleum Exporting Countries, commonly called OPEC, to set and maintain production levels and pricing;

the level of production in non-OPEC countries;

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the worldwide political and military environment, including uncertainty or instability resulting from an escalation or additional outbreak of armed hostilities in the Middle East, other oil-producing regions or other geographic areas or further acts of terrorism in the United States or elsewhere;

the cost of exploring for, producing and delivering oil and gas;

the discovery rate of new oil and gas reserves;

the rate of decline of existing and new oil and gas reserves;

available pipeline and other oil and gas transportation capacity;

the ability of oil and gas companies to raise capital;

weather conditions in the United States and elsewhere;

the policies of various governments regarding exploration and development of their oil and gas reserves;

development and exploitation of alternative fuels;

competition for customers drilling budgets from land-based energy markets around the world;

domestic and foreign tax policy; and

advances in exploration and development technology.

The continuing global financial crisis and worldwide economic downturn has had, and may continue to have, a negative impact on our business and financial condition.

The continuing worldwide financial crisis has reduced the availability of liquidity and in some cases has reduced the availability of and/or increased the cost of credit to fund the continuation and expansion of industrial business operations worldwide, and has led to a worldwide economic recession. This deterioration of the worldwide economy has resulted in reduced demand for crude oil and natural gas, exploration and production activity and offshore drilling services that has had a negative impact on our business and financial condition, including declines in dayrates earned by our drilling rigs and a decrease in new contract activity, which may continue and may worsen.

In addition, the worldwide economic recession has had, and could continue to have, a negative impact on our customers and/or our suppliers including, among other things, causing them to fail to meet their obligations to us. Additionally, if a potential customer is unable to obtain an adequate level of credit, it may preclude us from doing business with that potential customer. Similarly, the restricted credit market could affect lenders participating in our credit facility, making them unable to fulfill their commitments and obligations to us. Any such reductions in drilling activity or failure by our customers, suppliers or lenders to meet their contractual obligations to us, or our inability to secure additional financing, could adversely affect our financial position, results of operations and cash flows.

Our industry is highly competitive and cyclical, with intense price competition.

The offshore contract drilling industry is highly competitive with numerous industry participants, none of which at the present time has a dominant market share. Some of our competitors may have greater financial or other resources than we do. The drilling industry has experienced consolidation in recent years and may experience additional consolidation, which could create additional large competitors. Drilling contracts are traditionally awarded on a competitive bid basis. Intense price competition is often the primary factor in determining which qualified contractor is awarded a job, although rig availability and location, a drilling contractor's safety record and the quality and technical capability of service and equipment may also be considered. Mergers among oil and natural gas exploration and production companies, as well as the contraction of the global economy, have reduced the number of available

customers, increasing competition.

Our industry has historically been cyclical. There have been periods of lower demand, excess rig supply and low dayrates, followed by periods of high demand, short rig supply and high dayrates. We cannot predict the timing or duration of such business cycles. Periods of excess rig supply intensify the competition in the industry and often result in rigs being idle for long periods of time. In response to a contraction in demand for our drilling services, we have cold stacked three of our rigs as of the date of this report and are in the process of cold stacking a fourth unit. We also may be required to idle additional rigs or to enter into lower rate contracts. Prolonged periods of low utilization and dayrates could also result in the recognition of impairment charges on certain of our drilling rigs if future cash flow estimates, based upon information available to management at the time, indicate that the carrying value of these rigs may not be recoverable.

Significant new rig construction and upgrades of existing drilling units could also intensify price competition. As of the date of this report, based on analyst reports, we believe that there are approximately 50 jack-up rigs and 70

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floaters on order and scheduled for delivery between 2010 and 2012. The resulting increases in rig supply could be sufficient to further depress rig utilization and intensify price competition from both existing competitors, as well as new entrants into the offshore drilling market. As of the date of this report, not all of the rigs currently under construction have been contracted for future work, which may further intensify price competition as scheduled delivery dates occur. This potential oversupply of uncontracted rigs is greater in the jack-up market than it is in the floater market. However, the majority of the floaters on order are dynamically-positioned drilling units, which further increases competition with our fleet in certain circumstances, depending on customer requirements.

We can provide no assurance that our current backlog of contract drilling revenue will be ultimately realized.

As of the date of this report, our contract drilling backlog was approximately \$8.5 billion for contracted future work extending, in some cases, until 2016. Generally, contract backlog only includes future earnings under firm commitments; however, from time to time, we may report anticipated commitments for which definitive agreements have not yet been executed. We can provide no assurance that we will be able to perform under these contracts due to events beyond our control or that we will be able to ultimately execute a definitive agreement in cases where one does not currently exist. In addition, we can provide no assurance that our customers will be able to or willing to fulfill their contractual commitments to us. Our inability to perform under our contractual obligations or to execute definitive agreements or our customers' inability to fulfill their contractual commitments to us may have a material adverse effect on our financial position, results of operations and cash flows. See Management's Discussion and Analysis of Financial Condition and Results of Operations Overview *Contract Drilling Backlog* included in Item 7 of this report.

We rely heavily on a relatively small number of customers and the loss of a significant customer and/or a dispute that leads to the loss of a customer could have a material adverse impact on our financial results.

We provide offshore drilling services to a customer base that includes major and independent oil and gas companies and government-owned oil companies. However, the number of potential customers has decreased in recent years as a result of mergers among the major international oil companies and large independent oil companies. In 2009, our five largest customers in the aggregate accounted for 41% of our consolidated revenues. We expect Petrobras, who accounted for approximately 15% of our consolidated revenues in 2009, to continue to be a significant customer in 2010. While it is normal for our customer base to change over time as work programs are completed, the loss of any major customer may have a material adverse effect on our financial position, results of operations and cash flows.

The terms of our drilling contracts may limit our ability to attain profitability in a declining market or to benefit from increasing dayrates in an improving market.

The duration of offshore drilling contracts is generally determined by customer requirements and, to a lesser extent, the respective management strategies of the offshore drilling contractors. In periods of decreasing demand for offshore rigs, drilling contractors generally prefer longer term contracts, but often at flat or slightly lower dayrates, to preserve dayrates at existing levels and ensure utilization, while customers prefer shorter contracts that allow them to more quickly obtain the benefit of lower dayrates. Conversely, in periods of rising demand for offshore rigs, contractors typically prefer shorter contracts that allow them to more quickly profit from increasing dayrates. In contrast, during these periods customers with reasonably definite drilling programs typically prefer longer term contracts to maintain dayrate prices at a consistent level. An inability to obtain longer term contracts in a declining market or to fully benefit from increasing dayrates in an improving market through shorter term contracts may limit our profitability.

Contracts for our drilling units are generally fixed dayrate contracts, and increases in our operating costs could adversely affect our profitability on those contracts.

Our contracts for our drilling units provide for the payment of a fixed dayrate per rig operating day, although some contracts do provide for a limited escalation in dayrate due to increased operating costs incurred by us. Many of our operating costs, such as labor costs, are unpredictable and fluctuate based on events beyond our control. The gross margin that we realize on these fixed dayrate contracts will fluctuate based on variations in our operating costs over the terms of the contracts. In addition, for contracts with dayrate escalation clauses, we may not be able to fully recover increased or unforeseen costs from our customers. Our inability to recover these increased or unforeseen costs from our customers could adversely affect our financial position, results of operations and cash flows.

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Our customers may terminate some of our term drilling contracts if the drilling unit is destroyed or lost or if we have to suspend drilling operations for a specified period of time as a result of a breakdown of major equipment or, in some cases, due to other events beyond the control of either party. In addition, some of our drilling contracts permit the customer to terminate the contract after specified notice periods by tendering contractually specified termination amounts. These termination payments may not fully compensate us for the loss of a contract. In addition, the early termination of a contract may result in a rig being idle for an extended period of time, which could adversely affect our financial position, results of operations and cash flows. During periods of depressed market conditions, we may be subject to an increased risk of our customers seeking to repudiate their contracts. Our customers' ability to perform their obligations under drilling contracts with us may also be adversely affected by restricted credit markets and the economic downturn. If our customers cancel some of their contracts, and we are unable to secure new contracts on a timely basis and on substantially similar terms, or if contracts are suspended for an extended period of time or if a number of our contracts are renegotiated, it could adversely affect our financial position, results of operations or cash flows.

Our business involves numerous operating hazards, and we are not fully insured against all of them.

Our operations are subject to the usual hazards inherent in drilling for oil and gas offshore, such as blowouts, reservoir damage, loss of production, loss of well control, punchthroughs, craterings, fires and natural disasters such as hurricanes. The occurrence of these events could result in the suspension of drilling operations, damage to or destruction of the equipment involved and injury or death to rig personnel, damage to producing or potentially productive oil and gas formations and environmental damage, and could have a material adverse effect on our results of operations and financial condition. Operations also may be suspended because of machinery breakdowns, abnormal drilling conditions, failure of subcontractors to perform or supply goods or services or personnel shortages. In addition, offshore drilling operators are subject to perils peculiar to marine operations, including capsizing, grounding, collision and loss or damage from severe weather, and we do not typically retain loss-of-hire insurance policies to cover our rigs. Damage to the environment could also result from our operations, particularly through oil spillage or extensive uncontrolled fires. Pollution and environmental risks generally are not fully insurable. We may also be subject to damage claims by oil and gas companies or other parties.

Our insurance policies and contractual rights to indemnity may not adequately cover our losses, or may have exclusions of coverage for some losses. We do not have insurance coverage or rights to indemnity for all risks, including, among other things, liability risk for certain amounts of excess coverage and certain physical damage risk. If a significant accident or other event occurs and is not fully covered by insurance or contractual indemnity, it could adversely affect our financial position, results of operations and cash flows. There can be no assurance that we will continue to carry the insurance we currently maintain or that those parties with contractual obligations to indemnify us will necessarily be financially able to indemnify us against all these risks. In addition, no assurance can be made that we will be able to maintain adequate insurance in the future at rates we consider to be reasonable or that we will be able to obtain insurance against some risks.

We have elected to self-insure for physical damage to rigs and equipment caused by named windstorms in the U.S. Gulf of Mexico.

Because the amount of insurance coverage available to us has been limited, and the cost for such coverage has increased substantially, we have elected to self-insure for physical damage to rigs and equipment caused by named windstorms in the U.S. Gulf of Mexico. This results in a higher risk of losses, which could be material, that are not covered by third party insurance contracts. If one or more named windstorms in the U.S. Gulf of Mexico cause significant damage to our rigs or equipment, it could have a material adverse effect on our financial position, results of operations or cash flows.

A significant portion of our operations are conducted outside the United States and involve additional risks not associated with domestic operations.

We operate in various regions throughout the world which may expose us to political and other uncertainties, including risks of:

terrorist acts, war and civil disturbances;

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piracy or assaults on property or personnel;

kidnapping of personnel;

expropriation of property or equipment;

renegotiation or nullification of existing contracts;

changing political conditions;

foreign and domestic monetary policies;

the inability to repatriate income or capital;

difficulties in collecting accounts receivable and longer collection periods;

fluctuations in currency exchange rates;

regulatory or financial requirements to comply with foreign bureaucratic actions;

travel limitations or operational problems caused by public health threats; and

changing taxation policies.

We are subject to the U.S. Treasury Department's Office of Foreign Assets Control and other U.S. laws and regulations governing our international operations. In addition, international contract drilling operations are subject to various laws and regulations in countries in which we operate, including laws and regulations relating to:

the equipping and operation of drilling units;

import-export quotas or other trade barriers;

repatriation of foreign earnings;

oil and gas exploration and development;

taxation of offshore earnings and earnings of expatriate personnel; and

use and compensation of local employees and suppliers by foreign contractors.

Some foreign governments favor or effectively require the awarding of drilling contracts to local contractors, require use of a local agent or require foreign contractors to employ citizens of, or purchase supplies from, a particular jurisdiction. These practices may adversely affect our ability to compete in those regions. It is difficult to predict what governmental regulations may be enacted in the future that could adversely affect the international drilling industry. The actions of foreign governments may adversely affect our ability to compete.

As of the date of this report, the greatest concentration of our operating assets outside the United States was offshore Brazil, where we had 12 rigs in our fleet either currently working or contracted to work during 2010.

Our drilling contracts offshore Mexico expose us to greater risks than we normally assume.

We currently operate, and expect to continue to operate, our drilling rigs offshore Mexico for PEMEX Exploración Y Producción, or PEMEX, the national oil company of Mexico. The terms of these contracts expose us to greater risks than we normally assume, such as exposure to greater environmental liability. In addition, each contract can be terminated by PEMEX on 30 days notice, contractually or by statute, subject to certain conditions. While we

believe that the financial terms of these contracts and our operating safeguards in place mitigate these risks, we can provide no assurance that the increased risk exposure will not have a negative impact on our future operations or financial results.

Fluctuations in exchange rates and nonconvertibility of currencies could result in losses to us.

Due to our international operations, we have experienced currency exchange losses where revenues are received and expenses are paid in nonconvertible currencies or where we do not effectively hedge an exposure to a foreign currency. We may also incur losses as a result of an inability to collect revenues because of a shortage of convertible currency available to the country of operation, controls over currency exchange or controls over the repatriation of income or capital. We can provide no assurance that financial hedging arrangements will effectively hedge any foreign currency fluctuation losses that may arise.

Changes in laws, effective income tax rates or adverse outcomes resulting from examination of our tax returns could adversely affect our financial results.

Tax laws and regulations are highly complex and subject to interpretation and disputes. We conduct our worldwide operations through various subsidiaries and operating structures in a number of different jurisdictions. We are subject to the tax laws, tax regulations and income tax treaties within and between the countries in which we

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operate as well as countries in which we may be resident. We determine our income tax expense based on our interpretation of the applicable tax laws and regulations in effect in each jurisdiction for the period during which we operate and earn income. Our overall effective tax rate could be adversely and suddenly affected by lower than anticipated earnings in countries where we have lower statutory rates and higher than anticipated earnings in countries where we have higher statutory rates, by changes in the valuation of our deferred tax assets and liabilities or by changes in tax law, tax treaties, regulations, accounting principles or interpretations thereof in one or more countries in which we operate.

Our income tax returns are subject to review and examination. We do not recognize the benefit of income tax positions we believe are more likely than not to be disallowed upon challenge by a tax authority. If any tax authority successfully challenges our operational structure, intercompany pricing policies or the taxable presence of our key subsidiaries in certain countries; or if the terms of certain income tax treaties are interpreted in a manner that is adverse to our structure; or if we lose a material tax dispute in any country, our effective tax rate on our worldwide earnings could increase substantially and our earnings and cash flows from operations could be materially adversely affected.

We may be required to accrue additional tax liability on certain of our foreign earnings.

Certain of our international rigs are owned and operated, directly or indirectly, by Diamond Offshore International Limited, or DOIL, our wholly-owned Cayman Islands subsidiary. Since forming this subsidiary it has been our intention to indefinitely reinvest the earnings of this subsidiary to finance foreign operations. During 2007, DOIL made a non-recurring distribution to its U.S. parent company, and we recognized U.S. federal income tax expense on the portion of the distribution that consisted of earnings of the subsidiary that had not previously been subjected to U.S. federal income tax. Notwithstanding the non-recurring distribution made in December 2007, it remains our intention to indefinitely reinvest the future earnings of DOIL to finance foreign activities, except for the earnings of Diamond East Asia Limited, or DEAL, a wholly-owned subsidiary of DOIL formed in December 2008. It is our intention to repatriate the earnings of DEAL, and U.S. income taxes will be provided on such earnings. We do not expect to provide for U.S. taxes on any future earnings generated by DOIL, except to the extent that these earnings are immediately subjected to U.S. federal income tax or as they relate to DEAL. Should a future distribution be made from any unremitted earnings of this subsidiary, we may be required to record additional U.S. income taxes that, if material, could have an adverse effect on our financial position, results of operations and cash flows.

Future acts of terrorism and other political and military events could adversely affect the markets for our drilling services.

Terrorist acts and political events around the world have resulted in military actions in Afghanistan and Iraq, as well as related political and economic unrest in various parts of the world. Future terrorist attacks and the continued threat of terrorism in the U.S. or abroad, the continuation or escalation of existing armed hostilities or the outbreak of additional hostilities could lead to increased political, economic and financial market instability and a downturn in the economies of the U.S. and other countries. A lower level of economic activity could result in a decline in energy consumption or an increase in the volatility of energy prices, either of which could adversely affect the market for our offshore drilling services, our dayrates or utilization and, accordingly, our financial position, results of operations and cash flows. In addition, it has been reported that terrorists might target domestic energy facilities. While we take steps that we believe are appropriate to increase the security of our energy assets, there is no assurance that we can completely secure these assets, completely protect them against a terrorist attack or obtain adequate insurance coverage for terrorist acts at reasonable rates. Moreover, U.S. government regulations may effectively preclude us from actively engaging in business activities in certain countries. These regulations could be amended to cover countries where we currently operate or where we may wish to operate in the future.

Public health threats could have a material adverse effect on our operations and financial results.

Public health threats such as outbreaks of highly communicable diseases, which periodically occur in various parts of the world in which we operate, could adversely impact our operations, the operations of our customers and the global economy, including the worldwide demand for oil and natural gas and the level of demand for our services. Any quarantine of personnel or inability to access our offices or rigs could adversely affect our operations. Travel restrictions or operational problems in any part of the world in which we operate, or any reduction in the demand for

drilling services caused by public health threats in the future, may have a material adverse effect on our financial position, results of operations and cash flows.

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We may be subject to litigation that could have an adverse effect on us.

We are, from time to time, involved in various litigation matters. These matters may include, among other things, contract disputes, personal injury claims, environmental claims or proceedings, asbestos and other toxic tort claims, employment and tax matters and other litigation that arises in the ordinary course of our business. Although we intend to defend these matters vigorously, we cannot predict with certainty the outcome or effect of any claim or other litigation matter, and there can be no assurance as to the ultimate outcome of any litigation. Litigation may have an adverse effect on us because of potential adverse outcomes, defense costs, the diversion of our management's resources and other factors.

Governmental laws and regulations may add to our costs or limit our drilling activity.

Our operations are affected from time to time in varying degrees by governmental laws and regulations. The drilling industry is dependent on demand for services from the oil and gas exploration industry and, accordingly, is affected by