SMART ONLINE INC
Form DEF 14A
April 30, 2009

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

SCHEDULE 14A
Proxy Statement Pursuant to Section 14(a) of
the Securities Exchange Act of 1934

Filed by the Registrant x

Filed by a Party other than the Registrant ¨

Check the appropriate box:

¨ Preliminary Proxy Statement

¨ Confidential, for Use of the Commission Only (as permitted by Rule 14a-6(e)(2))

x Definitive Proxy Statement

¨ Definitive Additional Materials

¨ Soliciting Material Pursuant to Rule 14a-12

SMART ONLINE, INC.
(Name of Registrant as Specified In Its Charter)

Not Applicable
(Name of Person(s) Filing Proxy Statement if other than the Registrant)

Payment of Filing Fee (Check the appropriate box):

x No fee required.

¨ Fee computed on table below per Exchange Act Rules 14a-6(i)(1) and 0-11.

(1) Title of each class of securities to which transaction applies:

(2) Aggregate number of securities to which transaction applies:

(3) Per unit price or other underlying value of transaction computed pursuant to Exchange Act Rule 0-11 (set forth the amount on which the filing fee is calculated and state how it was determined):

(4) Proposed maximum aggregate value of transaction:

(5) Total fee paid:

¨ Fee paid previously with preliminary materials.

¨ Check box if any part of the fee is offset as provided by Exchange Act Rule 0-11(a)(2) and identify the filing for which the offsetting fee was paid previously. Identify the previous filing by registration statement number, or the Form or Schedule and the date of its filing.

(1) Amount Previously Paid:
(2) Form, Schedule or Registration Statement No.:
(3) Filing Party:
(4) Date Filed:

SMART ONLINE, INC.
4505 Emperor Boulevard
Suite 320
Durham, North Carolina 27703

NOTICE OF ANNUAL MEETING OF STOCKHOLDERS

TO BE HELD JUNE 16, 2009

You are cordially invited to attend the Annual Meeting of Stockholders of Smart Online, Inc., which will be held on Tuesday, June 16, 2009, at 9:00 a.m. local time, in the Board Room at the offices of the corporation at 4505 Emperor Boulevard, Suite 320, Durham, North Carolina 27703, to consider and vote upon the election of five directors and to transact such other business as may be properly brought before the meeting.

Stockholders of record at the close of business on April 20, 2009 are entitled to notice of and to vote at the annual meeting and any and all adjournments or postponements thereof.

By Order of the Board of Directors

/s/ Timothy L. Krist

Timothy L. Krist
Secretary

Durham, North Carolina
April 30, 2009

IMPORTANT: Whether or not you plan to attend the meeting in person, please submit voting instructions for your shares promptly using the directions on your proxy card to vote by one of the following methods: (1) over the Internet, by accessing the website address printed on your proxy card; or (2) by marking, dating, and signing your proxy card and returning it in the accompanying postage-paid envelope.

SMART ONLINE, INC.

PROXY STATEMENT

MEETING INFORMATION

The Board of Directors of Smart Online, Inc. (the "Company") is asking for your proxy for use at the 2009 Annual Meeting of Stockholders and any adjournments of the meeting. The meeting will be held in the Board Room at the Company's offices at 4505 Emperor Boulevard, Suite 320, Durham, North Carolina 27703 on Tuesday, June 16, 2009, at 9:00 a.m. local time, to elect five directors and to conduct such other business as may be properly brought before the meeting.

The Board of Directors recommends that you vote FOR the election of the director nominees listed in this proxy statement.

The Company intends to mail its Annual Report on Form 10-K for the fiscal year ended December 31, 2008 (the "Annual Report"), this proxy statement, and the accompanying proxy card to stockholders beginning on or about May 4, 2009. The Annual Report is not part of the Company's proxy soliciting materials.

Important Notice Regarding the Availability of Proxy Materials
For the Stockholder Meeting to be held on June 16, 2009

The Annual Report and proxy statement are also available on the Internet at
https://materials.proxyvote.com/83171V

VOTING PROCEDURES

Who Can Vote

Only stockholders of record at the close of business on April 20, 2009 are entitled to vote at the meeting and any adjournments of the meeting. At that time, there were 18,333,122 shares of the Company's common stock outstanding, each of which is entitled to one vote on each matter submitted to a vote at the meeting. The common stock is the only class of securities of the Company that has the right to vote at the meeting.

How You Can Vote

You may vote shares by proxy or in person using one of the following methods:

- Voting by Internet. You can vote over the Internet using the directions on your proxy card by accessing the website address printed on the card. The deadline for voting over the Internet is Monday, June 15, 2009 at 7:00 p.m. Eastern Daylight Time. If you vote over the Internet, you need not return your proxy card.

- Voting by Proxy Card. You can vote by completing and returning your signed proxy card. To vote using your proxy card, please mark, date, and sign the card and return it by mail in the accompanying postage-paid envelope. You should mail your signed proxy card sufficiently in advance for it to be received by Monday, June 15, 2009.

- Voting in Person. You can vote in person at the meeting if you are the record owner of the shares to be voted. You also can vote in person at the meeting if you present a properly signed proxy that authorizes you to vote shares on behalf of the record owner. If a broker, bank, custodian, or other nominee holds your shares, to vote in person at the meeting you must present a letter or other proxy appointment, signed on behalf of the broker or nominee, granting you authority to vote the shares.

How You Can Revoke Your Proxy and Change Your Vote

You can revoke your proxy and change your vote by (1) attending the meeting and voting in person, (2) delivering written notice of revocation of your proxy to the Secretary of the Company at any time before voting is closed, (3) timely submitting another signed proxy card bearing a later date, or (4) timely submitting new voting instructions over the Internet as described above.

How Your Proxy Will Be Voted

If you timely submit your proxy over the Internet or by proxy card as described above and have not revoked it, your shares will be voted or withheld from voting in accordance with the voting instructions you gave. If you timely submit your proxy without giving contrary voting instructions, your shares will be voted “FOR” election of the director nominees listed in this proxy statement.

How You Can Vote Shares Held by a Broker or Other Nominee

If your shares are held by a broker, bank, custodian, or other nominee, you may have received a voting instruction form with this proxy statement instead of a proxy card. The voting instruction form is provided on behalf of the broker or other nominee to permit you to give directions to the broker or nominee on how to vote your shares. Please refer to the voting instruction form or contact the broker or nominee to determine the voting methods available to you.

Quorum Required

A quorum must be present at the meeting before business can be conducted. A quorum will be present if a majority of the shares entitled to vote are represented in person or by proxy at the meeting. Shares represented by a proxy with instructions to withhold authority to vote or to abstain from voting on any matter will be considered present for purposes of determining the existence of a quorum. Shares represented by a proxy as to which a broker, bank, custodian, or other nominee has indicated that it does not have discretionary authority to vote on any matter (sometimes referred to as a “broker non-vote”) will also be considered present for purposes of determining the existence of a quorum.

Vote Required

Directors will be elected by a plurality of the votes cast. Thus the five nominees who receive the most votes will be elected to fill the available positions. Stockholders do not have the right to vote cumulatively in electing directors. Withholding authority in your proxy to vote for a nominee will result in the nominee receiving fewer votes. Abstentions and broker non-votes will not be counted for purposes of determining the number of votes cast.

PROPOSAL — ELECTION OF DIRECTORS

Nominees for Election as Directors

All five of the persons nominated for election to the Board of Directors at the annual meeting are currently serving as directors of the Company. The Company is not aware of any nominee who will be unable or will decline to serve as a director. If a nominee becomes unable or declines to serve, the accompanying proxy may be voted for a substitute nominee, if any, designated by the Board of Directors. The term of office of each person elected as a director will continue until the later of the next annual meeting of stockholders or until such time as his or her successor has been duly elected and qualified.

The following table lists the nominees for election and information about each.

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Name	Age	Principal Occupation and Background
Doron Roethler	52	Chairman of the Board and Interim President and Chief Executive Officer. Mr. Roethler was appointed as Chairman of the Company's Board of Directors on November 27, 2007 and as its Interim President and Chief Executive Officer on December 9, 2008. He has been the managing director and indirect majority owner of TMF Airmarine BV, an independent aviation spare parts company, since 1988. He is also the indirect owner of Smart IL, Ltd., a software development company that had been a development partner and customer of the Company. He received a B.A. in behavioral science from Ben Gurion University, Beer Sheva, Israel.
Shlomo Elia	66	Director. Mr. Elia has served on the Company's Board of Directors since November 2006 and was originally recommended for appointment to the Board by Atlas Capital SA ("Atlas"), one of the Company's stockholders. Mr. Elia is a Director of 3Pen Ltd. ("3Pen"), a private holding company focusing on business opportunities in Internet infrastructure and telecommunications. Prior to founding 3Pen in 1999, Mr. Elia held several senior positions in the Israeli Defense Forces ("I.D.F."), including the post of the Military Governor of the West-Bank (1982-1984) and Commander of the Liaison Unit for South Lebanon (1984-1985). During his service, among other activities, General Elia was engaged for a year as a Research Fellow in the Institute of International Strategic Affairs at U.C.L.A. Since his retirement from the I.D.F., he has been involved in communication projects in Nigeria and West Africa and construction projects in Romania. Among his civilian activities, Mr. Elia was Chairman of the National Tourist Board and currently is Chairman of 3Pen Technologies Ltd. and co-chairman of the Israeli Soldiers Welfare Association. Mr. Elia holds a B.A. degree in Modern History of the Middle-East from Tel Aviv University.
Roberta B. Hardy	61	Director. Ms. Hardy has served on the Company's Board of Directors since March 17, 2009. She is the founder and managing partner of Silk Road Partners, LLC, a "Mentor Capital" firm providing guidance to early stage companies and exit strategies for later stage companies since its formation in 2005. She is also the Chairman and founder of A Million Dreams Across America, a non-profit organization founded in 2008 that provides intensive training for entrepreneurs, and the founding Chairman of the Atlantis Group, LLC, an angel investment group started in 2000 designed to capitalize on the growth in the entrepreneurial activity and venture financing primarily in North Carolina. Prior to 2000, Ms. Hardy founded and was CEO of CI Technologies Inc., served as Vice President with American Management Systems, Inc., and was the MIS Director for the Commonwealth of Massachusetts.
C. James Meese, Jr.	67	Director. Mr. Meese has served on the Company's Board of Directors since November 2006. Mr. Meese is President and founder of Business Development Associates, Inc. ("BDA"), a strategic advisory firm. Since 1989, BDA has provided advice and assistance to both middle market and emerging companies on issues of company valuations, acquisitions and divestitures, market development, corporate governance, capital acquisition, strategic planning, exit strategies, and organizational structuring. Prior to 1989, Mr. Meese spent approximately 20 years in various senior corporate marketing, business development, and finance

		positions. Sixteen of those years were spent with West Pharmaceutical Services, Inc. (“West”). He was a member of the company’s Top Management Committee during his last four years with West. Mr. Meese is also a director of DRI Corporation (NASDAQ:TBUS) (“DRI”), The Altoona Railroaders Memorial Museum, and The Raleigh Rescue Mission and its Foundation. He is a former Chair and current member of the DRI Audit Committee, President of the Raleigh Rescue Mission Board, and serves on a variety of committees in his directorships. He is a member of the National Association of Corporate Directors (“NACD”) and is designated as the Company’s audit committee financial expert. Mr. Meese received a B.A. degree in Economics from the University of Pennsylvania and an M.B.A. from Temple University.
Dror Zoreff	63	Director. Mr. Zoreff has served on the Company’s Board of Directors since April 1, 2008. Since 2008, he has served as the President and CEO of Donor Management Services, Inc., a New York-based company that provides major donors, corporations, and foundations a unique set of tools and services to ensure their charitable gifts are properly used and achieve the desired impact. From 1999 to 2008, Mr. Zoreff served as Consultant to the President and CEO of United Retail Group Inc., a specialty retailer of large size women’s fashions. From 1997 to 1999, he was Vice President of International Operations at Russ Berrie, Inc., a designer, importer, marketer, and distributor of gift and infant and juvenile consumer products. Prior to 1997, Mr. Zoreff held positions with The College of Judea & Samaria, Glenoit Industries Ltd, and the Jewish Agency for Israel. Mr. Zoreff holds a B.A. degree in Business Administration from Manchester University and an M.A. degree in Business Administration from Tel Aviv University.

The Board of Directors recommends stockholders
vote FOR election of the nominees named above.

Executive Officers

The names of the Company's current executive officers are listed below. The Company's executive officers are appointed by its Board of Directors to hold office until their successors are appointed.

Name	Age	Position
Doron Roethler	52	Chairman of the Board, Interim President and Chief Executive Officer
Timothy L. Krist	41	Chief Financial Officer, Secretary
Neile King	38	Chief Operating Officer, Vice President, Sales and Marketing

Timothy L. Krist, Chief Financial Officer, Secretary. Mr. Krist was appointed as the Company's Chief Financial Officer on July 15, 2008. He was employed with KB Home, a homebuilder, as Director of Finance from 2005 to 2008 and as Finance Manager from 2004 to 2005. Prior to joining KB Home, Mr. Krist served as Director of Finance of Blackboard, Inc., an e-education software and hardware manufacturing company, from 2001 to 2003; as Director of Corporate Integration of International Fibercom, Inc., a telecommunications infrastructure company, from 2000 to 2001; and as Director of Financial Analysis of Main Street and Main Incorporated, a multi-concept restaurant company, from 1997 to 2000. Mr. Krist has also worked with the public accounting firm of Deloitte & Touche, LLP. He holds a B.S. degree in Accountancy from Miami University and an M.B.A. from Arizona State University.

Neile King, Chief Operating Officer, Vice President, Sales and Marketing. Mr. King was appointed as the Company's Chief Operating Officer on March 25, 2009 in addition to his position as Vice President, Sales and Marketing. He was appointed Vice President, Sales and Marketing on November 10, 2008 after serving as the Company's Chief Operating Officer between February 2008 and his appointment as Vice President, Sales and Marketing. Mr. King served as the Company's Director of Operations and Vice President of Business Services from September 2007 to February 2008. Prior to joining the Company, from March 2006 to September 2007, Mr. King was the Director of Operations at DataFlux Corporation, a SAS company and data quality vendor. From April 1999 to July 2005, Mr. King held several management positions within the IT Solutions group in the Operations, Marketing, Contracts Management, and Sales Operations organizations with Hill-Rom Company, Inc., a healthcare information technology services provider.

Code of Ethics

The Company has adopted a Code of Ethics applicable to its executives, including the principal executive officer, principal financial officer, and principal accounting officer, as defined by applicable rules of the Securities and Exchange Commission (“SEC”). It is publicly available on the Company’s website at www.smartonline.com. If the Company makes any amendments to the Code of Ethics other than technical, administrative, or other non-substantive amendments, or grants any waivers, including implicit waivers, from a provision of the Code of Ethics to the Company’s Chief Executive Officer, Chief Financial Officer, or certain other finance executives, the Company will disclose the nature of the amendment or waiver, its effective date, and to whom it applies on the Company’s website at www.smartonline.com or in a report on Form 8-K filed with the SEC.

Board Composition and Independence of Directors

The size of the Board of Directors is currently fixed at six members. Five persons have been nominated for election at the annual meeting. The Board of Directors believes that the current number of directors is appropriate at this time. Under the rules of the SEC, the accompanying proxy cannot be voted for more than five nominees.

The Company is not required to comply with the listing requirements of The Nasdaq Stock Market (“Nasdaq”) since its securities are not listed on Nasdaq. Nasdaq listing requirements mandate that a majority of the members of a listed company’s board of directors be “independent directors” as defined under Nasdaq Marketplace Rules. Although not currently required, the Board has determined that four of the present directors — Messrs. Elia, Meese, and Zoreff and Ms. Hardy — are each an “independent director” within the meaning of Nasdaq Marketplace Rules. All are standing for re-election. Therefore, assuming all five nominees are elected at the annual meeting, the Board will have a majority of “independent directors” after the annual meeting.

Philippe Pouponnot, a former director who completed his term of service on the Board of Directors on June 19, 2008 and did not stand for re-election, was also determined by the Board of Directors to be an “independent director” within the meaning of the Nasdaq Marketplace Rules. Two other directors also resigned from the Company’s Board of Directors in 2008. Effective October 15, 2008, Thomas P. Furr resigned, and effective December 10, 2008, David E. Colburn resigned. The Board of Directors had determined that Mr. Furr and Mr. Colburn were not considered “independent directors” as they also served as executive officers of the Company.

Attendance at Meetings

The Board of Directors held four meetings during the fiscal year ended December 31, 2008. Each incumbent director attended or participated in at least 75% of the aggregate of (1) the number of meetings of the Board of Directors held in fiscal 2008 during the period he served as a director and (2) the number of meetings of committees on which he served that were held during the period of his service.

The Company expects all directors to attend each annual meeting of stockholders, absent good reason. Six directors attended the annual meeting of stockholders in 2008.

Standing Committees

The Company’s Board of Directors has three standing committees: the Audit Committee, the Compensation Committee, and the Corporate Governance and Nominating Committee. Copies of the charters of these committees, as they may be amended from time to time, are available on the Company’s website at www.smartonline.com.

Audit Committee. The Audit Committee is composed of Mr. Meese and Mr. Elia. Mr. Meese serves as Chairman of the Audit Committee. The Company’s Board of Directors has determined that Mr. Meese and Mr. Elia meet the

definition of "independent director," as that term is defined by Nasdaq Marketplace Rules and SEC rules, and they each meet the special independence requirements applicable to audit committee members. Both members have past financial experience resulting in their financial sophistication as would be required by Nasdaq Marketplace Rules. The Board of Directors has determined that Mr. Meese meets the definition of "audit committee financial expert" as that term is defined in Regulation S-K. The Company's securities are quoted on the OTC Bulletin Board and are not listed on a national securities exchange. Therefore, neither the SEC rules nor the Nasdaq Marketplace Rules regarding audit committees are applicable to the Company's Board of Directors.

The Audit Committee was established by the Board of Directors for the purpose of assisting it in fulfilling its responsibilities with respect to its oversight of (1) the quality and integrity of the Company's financial statements, (2) compliance with legal and regulatory requirements, (3) the independent auditor's qualifications and independence, and (4) the performance of the Company's internal audit function and independent auditors. The Audit Committee is also responsible for the preparation of reports required to be included in the Company's annual proxy statement or other documents from time to time required with respect to the Audit Committee's functions. The Audit Committee met seven times during 2008.

Compensation Committee. The Compensation Committee is composed of Mr. Elia and Mr. Meese. Mr. Elia serves as Chairman of the Compensation Committee. The Company's Board of Directors has determined that Mr. Elia and Mr. Meese are "independent directors" within the meaning of the Nasdaq Marketplace Rules.

The Compensation Committee was established by the Company's Board of Directors for the purpose of assisting it in discharging its duties with respect to (1) the formulation, implementation, review, and modification of the compensation of the Company's officers and directors and (2) the preparation of the annual report on executive compensation for inclusion in the Company's annual proxy statement, if required. The Compensation Committee's duties include, among other things, setting the compensation for officers and directors, making recommendations to the Board of Directors with respect to incentive compensation plans and equity-based compensation plans, approving grants of stock options and other awards under the Company's 2004 Equity Compensation Plan, and administering the Company's defined benefit and defined contribution plans, if any.

In fulfilling its responsibilities, the Compensation Committee is entitled to delegate any or all of its responsibilities to a subcommittee of the Compensation Committee, to the extent consistent with applicable law, the Company's certificate of incorporation, bylaws, corporate governance guidelines, and rules of any exchange or market on which the securities of the Company are then traded if compliance with such rules are required to begin or continue trading.

As part of its review and establishment of the performance criteria and compensation of officers and directors of the Company, the Compensation Committee must separately meet at least annually with the Company's Chief Executive Officer, the principal human resources executive and compliance officer, and with any other corporate officers as the Compensation Committee deems appropriate. However, the Compensation Committee must also meet regularly without such officers present, and in all cases such officers must not be present at the meetings at which their performance and compensation is being discussed and determined. The Compensation Committee must consult with the Chief Executive Officer regarding compensation of the other officers of the Company. The Compensation Committee has not engaged any compensation consultant to determine or recommend the amount or form of executive and director compensation. The Compensation Committee met four times during 2008.

Corporate Governance and Nominating Committee. The Corporate Governance and Nominating Committee is composed of Mr. Meese and Mr. Zoreff. Mr. Zoreff serves as Chairman of the Corporate Governance and Nominating Committee. The Company's Board of Directors has determined that Mr. Meese and Mr. Zoreff are "independent directors" within the meaning of the Nasdaq Marketplace Rules.

The Corporate Governance and Nominating Committee was established by the Board of Directors for the purpose of assisting it in discharging its duties with respect to (1) the identification of individuals qualified to become directors and the selection or recommendation of candidates for directorships to be filled by the Board of Directors or the stockholders, and (2) the development, maintenance, and recommendation of a set of corporate governance principles applicable to the Company, and the periodic review of such principles. The Corporate Governance and Nominating Committee met four times during 2008.

Section 16(a) Beneficial Ownership Reporting Compliance

The members of the Company's Board of Directors, its executive officers, and persons who hold more than 10% of its outstanding common stock are subject to the reporting requirements of Section 16(a) of the Securities Exchange Act of 1934, as amended (the "Exchange Act"), which requires them to file reports with respect to their ownership of the Company's common stock and their transactions in such common stock. Based upon the Company's review of the Section 16(a) reports in its records for fiscal 2008 transactions in the Company's common stock, the Company believes that, except as noted below, all reporting requirements under Section 16(a) for fiscal 2008 were met in a timely manner by its directors, executive officers, and greater than 10% beneficial owners.

The following reports were filed late on behalf of Atlas:

- A Form 4 filed on March 25, 2008 reporting a purchase of the Company's common stock on March 20, 2008 and a purchase of the Company's common stock on March 24, 2008.
- A Form 4 filed on July 11, 2008 reporting a purchase of the Company's common stock on July 7, 2008, a purchase of the Company's common stock on July 9, 2008, and a purchase of the Company's common stock on July 10, 2008.
- A Form 4 filed on September 11, 2008 reporting a purchase of the Company's convertible secured subordinated notes due November 14, 2010 on November 14, 2007 and a purchase of the Company's convertible secured subordinated notes due November 14, 2010 on August 12, 2008.
- A Form 4 filed on December 9, 2008 reporting a purchase of the Company's common stock on December 3, 2008 and a purchase of the Company's common stock on December 8, 2008.

The following report was filed late on behalf of Doron Roethler:

- A Form 4 filed on September 12, 2008 reporting a purchase of the Company's convertible secured subordinated notes due November 14, 2010 on November 14, 2007 and a purchase of the Company's convertible secured subordinated notes due November 14, 2010 on August 12, 2008.

The following report was filed late on behalf of Neile King:

- A Form 4 filed on November 13, 2008 reporting a payment of taxes on the lapsing of restrictions on restricted stock with shares of the Company's common stock on September 5, 2008.

Certain Relationships and Related Transactions

Non-Compete Payments Made to Former Chief Operating Officer of Smart Commerce. In October 2005, the Company purchased all of the stock of iMart Incorporated ("iMart"). One of the Company's former executive officers, Gary Mahieu, was a founder and shareholder of iMart, and was its principal executive officer. Following the purchase of iMart's stock, Mr. Mahieu entered into an employment agreement with Smart Commerce, Inc., the Company's former wholly-owned subsidiary that was subsequently merged into the Company. Under the terms of that agreement, the Company agreed to make non-competition payments to Mr. Mahieu in an aggregate amount of $510,000 to be made in eight equal quarterly installments of $63,750 through October 1, 2007. In connection with obtaining a loan from Fifth Third Bank, the payment schedule was modified to require all outstanding non-compete payments to be made by February 2007. This amount was paid in full on February 7, 2007, and no additional non-compete payments are owed to Mr. Mahieu.

Loans Made by Certain Parties to the Former Chief Executive Officer. During 2005, the following loans were made by certain investors, consultants, and/or stockholders to Michael Nouri, the Company's then serving Chief Executive Officer: (i) $809,736.49 was borrowed from Leon Sokolic, one of the Company's stockholders, (ii) $77,971.20 was borrowed from Atlas, one of the Company's stockholders, (iii) $80,000 was borrowed from Pete Coker, a principal of

Tryon Capital, which provided financial consulting services to the Company and received a warrant and cash fees, and (iv) $296,589 was borrowed from Berkley Financial Services, Ltd. ("Berkley"), which received compensation for services rendered to the Company for investment banking and investor relations services, including during the period in which Berkley was making loans to Mr. Nouri (collectively, the "Lenders"). Under Section 402 of the Sarbanes-Oxley Act of 2002, the Company is prohibited from making personal loans to its directors and executive officers, directly and indirectly. The Company believes that the loans to Mr. Nouri described above are not personal loans made directly or indirectly by it to the Chief Executive Officer.

On January 19, 2007, Mr. Nouri entered into note cancellation agreements with each of the Lenders. Under the terms of these note cancellation agreements, Mr. Nouri transferred his personally held shares of the Company's common stock to the Lenders as consideration for the cancellation of promissory notes held by the Lenders. Under these agreements, Mr. Nouri transferred a total of 521,699 shares of common stock for the cancellation of principal and interest totaling $1,306,178.66 as of December 31, 2006. The agreed-upon per share value ranged from $1.50 to $4.22 per share.

In connection with the note cancellation agreements, the Company entered into registration rights agreements with each of the Lenders described in the preceding paragraphs. Under the terms of these registration rights agreements, each Lender was required to be given notice when the Company filed a registration statement under the Securities Act of 1933, as amended (the "Securities Act"). Each Lender was then permitted to include its shares received in such registration statement. Under the registration rights agreements, parties electing to include such shares in the registration were to bear their proportionate share of the registration expenses. The Company has satisfied its obligations under these registration rights agreements.

Private Placement of Common Stock to a Certain Director. In a transaction that closed on August 21, 2006, Philippe Pouponnot, a former member of the Company's Board of Directors, purchased 50,000 shares of the Company's common stock in a private placement transaction. The private placement shares were sold at $2.50 per share pursuant to subscription agreements between Mr. Pouponnot and the Company. The Company entered into a subscriber rights agreement with Mr. Pouponnot whereby it was obligated to register these shares for resale by the purchaser by filing a registration statement on or before September 30, 2006. If a registration statement was not filed by that date, the Company was obligated to pay a penalty obtained by multiplying the total purchase price for the shares by 0.5% by the number of prorated 30-day periods after the target registration date. At the Company's sole discretion, this penalty could be paid in the number of shares obtained by dividing the total penalty amount by the per share purchase price. The Company filed a registration statement for these shares on April 3, 2007. In January 2007, the Company entered into an amendment to the registration rights agreement with Mr. Pouponnot. Under this amendment, the penalty for late registration was set at a fixed amount. The Company subsequently issued Mr. Pouponnot 750 shares of its common stock as payment for this late registration penalty with an aggregate value of $2,100 based upon a closing price per share of $2.80 on the OTC Bulletin Board on the date of issuance. The Company has satisfied its obligations under the subscriber rights agreement.

Mr. Pouponnot also entered into a dribble out agreement with the Company pursuant to which he was permitted to sell up to 25% of these shares during any rolling 30-day period following the effective date of the registration statement. This agreement has expired. At the time of the sale to Mr. Pouponnot, he had not been appointed a member of the Company's Board of Directors.

Private Placement of Common Stock to a Certain Affiliate by Former Chief Executive Officer. On October 10, 2006, Michael Nouri, the Company's then serving Chief Executive Officer, entered into a stock purchase agreement with Doron Roethler, a stockholder who subsequently became the Company's Chairman of the Board in November 2007 and Interim President and Chief Executive Officer in December 2008. Pursuant to this agreement, Mr. Nouri sold 247,043 shares of the Company's common stock from his personal holdings at a price of $1.5176 per share. The Company entered into a registration rights agreement with Mr. Roethler in connection with this transaction under which it had an obligation to register the shares sold by Mr. Nouri to Mr. Roethler on the first registration statement filed by the Company following the sale, with Mr. Roethler bearing his proportionate share of the registration expenses. Under the terms of this agreement, the shares were delivered following the Company's execution of such registration rights agreement, which occurred on January 19, 2007. The Company has satisfied its obligations under the registration rights agreement.

Issuance of Warrant and Letter of Credit Arrangements with a Certain Affiliate. On November 14, 2006, the Company entered into a revolving credit arrangement with Wachovia Bank, NA ("Wachovia") for $1.3 million to be used for

general working capital. The line of credit was secured by the Company’s deposit account at Wachovia and an irrevocable standby letter of credit in the amount of $1.3 million issued by HSBC Private Bank (Suisse) SA with Atlas, a current stockholder, as account party. In connection with the establishment of the line of credit, Atlas and the Company entered into a Reimbursement Agreement on November 10, 2006 providing that in the event of a default by the Company in the repayment of the line of credit that results in the letter of credit being drawn, it shall reimburse Atlas any sums that Atlas is required to pay under the letter of credit. At the sole discretion of the Company, these payments to Atlas could be made in cash or by issuing shares of the Company’s common stock at a set price of $2.50 per share.

On January 24, 2007, the Company entered into an amendment to its line of credit with Wachovia to increase the available principal from $1.3 million to $2.5 million and to extend the maturity date from August 1, 2007 to August 1, 2008. The amended line of credit was secured by the Company's deposit account at Wachovia and a modified irrevocable standby letter of credit in the amount of $2.5 million issued by HSBC Private Bank (Suisse) SA with Atlas as account party. As incentive to modify the letter of credit relating to the Wachovia line of credit, the Company entered into a Stock Purchase Warrant and Agreement (the "Warrant Agreement") with Atlas on January 15, 2007. Under the terms of the Warrant Agreement, Atlas received a warrant containing a provision for cashless exercise to purchase up to 444,444 shares of the Company's common stock at $2.70 per share at the termination of the line of credit or if the Company is in default under the terms of the line of credit with Wachovia. If the warrant is exercised in full, it will result in gross proceeds to the Company of approximately $1.2 million.

On February 15, 2008, the Company paid off the Wachovia line of credit, and on February 20, 2008, the Company entered into a new revolving credit arrangement with Paragon Commercial Bank ("Paragon") that is renewable on an annual basis subject to mutual approval. The line of credit advanced by Paragon is $2.47 million and can be used for general working capital. The line of credit is secured by an irrevocable standby letter of credit in the amount of $2.5 million issued by HSBC Private Bank (Suisse) SA with Atlas as account party that expires on February 18, 2010. In connection with establishing the Paragon line of credit, Atlas and the Company amended the Reimbursement Agreement to provide that in the event of a default by the Company in the repayment of the Paragon line of credit that results in the letter of credit being drawn, the Company shall reimburse Atlas any sums that Atlas is required to pay under the letter of credit. At the sole discretion of the Company, these payments may be made in cash or by issuing shares of the Company's common stock at a set price of $2.50 per share. Also in consideration for Atlas providing the Paragon line of credit, the Company agreed to amend the Warrant Agreement to provide that the warrant is exercisable within 30 business days of the termination of the Paragon line of credit or if the Company is in default under the terms of the line of credit.

Sale of Convertible Notes to Certain Affiliates. On November 14, 2007, in an initial closing, the Company sold $3.3 million aggregate principal amount of convertible secured subordinated notes due November 14, 2010 (the "notes") to certain existing stockholders. These stockholders (referred to in this discussion as the "noteholders") and the amount of notes they purchased in the initial closing are as follows: (i) The Blueline Fund, which originally recommended Philippe Pouponnot, one of the Company's former directors, for appointment to the Company's Board of Directors - $500,000; (ii) Atlas, an affiliate of the Company that originally recommended Shlomo Elia, one of the Company's directors, for appointment to the Board of Directors - $2,050,000; (iii) Crystal Management Ltd., which is owned by Doron Roethler, a stockholder who subsequently became Chairman of the Company's Board of Directors and Interim President and Chief Executive Officer - $500,000; and (iv) William Furr, who is the father of Thomas Furr, one of the Company's former directors and executive officers - $250,000. The noteholders also committed to purchase on a pro rata basis up to $5.2 million aggregate principal of additional convertible secured subordinated notes in future closings upon approval and call by the Company's Board of Directors.

On August 12, 2008, the Company exercised its option to sell $1.5 million aggregate principal amount of additional notes with substantially the same terms and conditions as the notes sold on November 14, 2007. Atlas purchased $1,250,000 aggregate principal amount of these notes and Crystal Management Ltd. purchased $250,000 aggregate principal amount of these notes. In connection with the sale of the additional notes, the noteholders holding a majority of the aggregate principal amount of the notes outstanding agreed to increase the aggregate principal amount of notes that they are committed to purchase from $8.5 million to $15.3 million.

On November 21, 2008, the Company sold $500,000 aggregate principal amount of notes to two new investors, and on January 6, 2009, the Company sold $500,000 aggregate principal amount of notes to Atlas, all on substantially the same terms and conditions as the previously issued notes.

On February 24, 2009, the Company sold $500,000 aggregate principal amount of notes to Atlas on substantially the same terms and conditions as the previously issued notes. On the same date, the noteholders holding a majority of the aggregate principal amount of the notes outstanding agreed that the Company may sell up to $6 million aggregate principal amount of additional notes to new investors or existing noteholders at any time on or before December 31, 2009 with a maturity date of November 14, 2010 or later. In addition, the maturity date definition for each of the notes was changed from November 14, 2010 to the date upon which the note is due and payable, which is the earlier of (1) November 14, 2010, (2) a change of control, or (3) if an event of default occurs, the date upon which noteholders accelerate the indebtedness evidenced by the notes. The formula for calculating the conversion price of the notes was also amended such that the conversion price of each outstanding note and any additional note sold in the future would be the same and set at the lowest applicable conversion price, as described below.

On April 3, 2009, the Company sold $500,000 aggregate principal amount of notes to Atlas on substantially the same terms and conditions as the previously issued notes.

The Company is obligated to pay interest on the notes at an annualized rate of 8% payable in quarterly installments commencing three months after the purchase date of the notes. As of April 20, 2009, $6.8 million aggregate principal amount of notes are outstanding and the Company has paid $410,955 in interest on the notes. The Company does not have the ability to prepay the notes without approval of at least a majority of the principal amount of the notes then outstanding.

On the earlier of November 14, 2010, or a merger or acquisition or other transaction pursuant to which the Company's existing stockholders hold less than 50% of the surviving entity, or the sale of all or substantially all of the Company's assets, or similar transaction, or event of default, each noteholder in its sole discretion shall have the option to (i) convert the principal then outstanding on its notes into shares of the Company's common stock, or (ii) receive immediate repayment in cash of the notes, including any accrued and unpaid interest. If a noteholder elects to convert its notes under these circumstances, the conversion price will be the lowest "applicable conversion price" determined for each note. The "applicable conversion price" for each note shall be calculated by multiplying 120% by the lowest of (i) the average of the high and low prices of the Company's common stock on the OTC Bulletin Board averaged over the five trading days prior to the closing date of the issuance of such note, (ii) if the Company's common stock is not traded on the Over-The-Counter market, the closing price of the common stock reported on the Nasdaq National Market or the principal exchange on which the common stock is listed, averaged over the five trading days prior to the closing date of the issuance of such note, or (iii) the closing price of the Company's common stock on the OTC Bulletin Board, the Nasdaq National Market, or the principal exchange on which the common stock is listed, as applicable, on the trading day immediately preceding the date such note is converted, in each case as adjusted for stock splits, dividends or combinations, recapitalizations, or similar events.

Payment of the notes will be automatically accelerated if the Company enters voluntary or involuntary bankruptcy or insolvency proceedings.

If the Company proposes to file a registration statement to register any of its common stock under the Securities Act in connection with the public offering of such securities solely for cash, subject to certain limitations, the Company shall give each noteholder who has converted its notes into common stock the opportunity to include such shares of converted common stock in the registration. The Company has agreed to bear the expenses for any of these registrations, exclusive of any stock transfer taxes, underwriting discounts, and commissions.

We sell a significant portion of styrene to international customers. Reliance on overseas markets subjects us to significant risks inherent in operating internationally.

Our international operations are subject to a number of risks inherent to any business operating in foreign countries. As we continue to sell our products to such countries, our operations will encounter the following risks, among others:

- political and economic instability and disruptions;
- the inability to collect amounts owed;
- the inability to secure adequate shipping space for our products at acceptable prices, which could adversely affect our competitiveness relative to producers located in close proximity to our foreign customers;
- terrorism, civil uprisings, riots and war, which can make it unsafe to continue operations;
- the imposition of duties and tariffs, import and export controls;

decrees, laws, regulations, interpretations and court decisions under legal systems, such as in the Peoples Republic of China, which are not always fully developed and which may be retroactively applied and cause us to incur unanticipated or unrecoverable costs, as well as delays which may result in real or opportunity costs; and

transportation delays and interruptions.

We cannot predict the nature or the likelihood of any of these events. However, the occurrence of any one or more of these events could have an adverse effect on our international sales by reducing the demand for our products, decreasing the prices at which we can sell our products or otherwise having an adverse effect on our business, financial condition, results of operations or cash flows.

The markets for our products, and the prices we receive for our products, are based on international supply and demand. In recent years, demand in Asia, particularly China, and capacity expansions in Asia and the Middle East, have driven product price trends. China has pursued an aggressive economic expansion in recent years. If this expansion ceased, or significantly slowed, the markets for our products could be materially adversely affected. Countries in Asia and in the Middle East have also completed or announced significant capacity increases for most of the products we produce, and may expand production even further in the future. These developments could have a significant negative impact on our ability to maintain existing market share, sell products in the foreign or domestic markets or may adversely impact our profit margins.

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We depend upon the continued operation of a single site for all of our production.

All of our products are produced at our Texas City site. Significant unscheduled downtime at our Texas City site could have a material adverse effect on our business, financial condition, results of operations or cash flows. Unanticipated downtime can occur for a variety of reasons, including equipment breakdowns, interruptions in the supply of raw materials, power failures, sabotage, natural forces or other hazards associated with the production of petrochemicals. Although we maintain business interruption insurance, this insurance does not provide coverage for business interruptions of less than 45 days and is limited in its overall coverage.

Our operations involve risks that may increase our operating costs, which could reduce our profitability.

Although we take precautions to enhance the safety of our operations and minimize the risk of disruptions, our operations are subject to hazards inherent in the manufacturing and marketing of chemical products. These hazards include:

- pipeline or storage tank leaks and ruptures, explosions and fires;
- severe weather and natural disasters;
- mechanical failures, unscheduled downtimes, labor difficulties and transportation interruptions;
- environmental remediation complications and
- chemical spills and discharges or releases of toxic or hazardous substances or gases.

Many of these hazards can cause bodily injury or loss of life, severe damage to or destruction of property or equipment or environmental damage, and may result in suspension of operations or the imposition of civil or criminal penalties and liabilities. Furthermore, we are subject to present and future claims with respect to workplace exposure of our employees or contractors on our premises or other persons located nearby, workers compensation and other matters.

Our operations are subject to operating hazards and unforeseen interruptions for which we may not be adequately insured.

We maintain insurance coverage at levels that we believe are reasonable and typical for our industry, portions of which are provided by a captive insurance company maintained by us and a few other chemical companies. However, we are not fully insured against all potential hazards incident to our business. Accordingly, our insurance coverage may be inadequate for any given risk or liability, such as property damage suffered in hurricanes or from terrorist acts or business interruption incurred from a loss of our supply of electricity or carbon monoxide. In addition, our insurance companies may be incapable of honoring their commitments if an unusually high number of claims are concurrently made against their policies. As a result of market conditions, premiums and deductibles for certain insurance policies can increase substantially and, in some instances, certain insurance may become unavailable or available only for reduced amounts of coverage. If we were to incur a significant liability for which we were not fully insured, it could have a material adverse effect on our business, financial condition, results of operations or cash flows. We can make no assurances that we can renew our existing insurance coverages at commercially reasonable rates or that such coverage will be adequate to cover future claims that may arise.

In addition, concerns about terrorist attacks, as well as other factors, have caused significant increases in the cost of our insurance coverage. We have determined that it is not economically prudent to obtain terrorism insurance and we do not carry terrorism insurance on our property at this time. In the event of a terrorist attack impacting one or more of our production units, we could lose the production and sales from one or more of these facilities, and the facilities themselves, and could become liable for contamination or personal or property damage from exposure to hazardous materials caused by a terrorist attack. Such loss of production, sales, facilities or incurrence of liabilities could materially adversely affect our business, financial condition, results of operations or cash flows.

Terrorist attacks, the current military action in Iraq, general instability in various OPEC member nations and other attacks or acts of war in the United States and abroad may adversely affect the markets in which we operate.

The attacks of September 11, 2001 and subsequent events, including the current military action in Iraq, have caused instability in the United States and other financial markets and have led, and may continue to lead, to further armed hostilities, prolonged military action in Iraq or further acts of terrorism in the United States or abroad, which could

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cause further instability in the financial markets and in the markets for our products. Current regional tensions and conflicts in various OPEC member nations, including the current military action in Iraq, have caused, and may continue to cause, increased raw materials costs, specifically raising the prices of oil and gas, which are used in our operations or affect the prices of our raw materials. Furthermore, the terrorist attacks, subsequent events or future developments in any of these areas may result in reduced demand from our customers for our products. These developments could subject our operations to increased risks and, depending on their magnitude, could have a material adverse effect on our business, financial condition, results of operations or cash flows.

New regulations concerning the transportation of hazardous chemicals and the security of chemical manufacturing facilities could result in higher operating costs.

Chemical manufacturing facilities may be at greater risk of future terrorist attacks than other potential targets in the United States. As a result, the chemical industry has responded to the issues surrounding the terrorist attacks of September 11, 2001 by starting new initiatives relating to the security of chemicals industry facilities and the transportation of hazardous chemicals in the United States. Simultaneously, local, state and federal governments have begun a regulatory process that could lead to new regulations impacting the security of chemical plant locations and the transportation of hazardous chemicals. Our business or our customers businesses could be adversely affected because of the cost of complying with new security regulations.

We are subject to many environmental and safety regulations that may result in significant unanticipated costs or liabilities or cause interruptions in our operations.

Our operations involve the handling, production, transportation, treatment and disposal of materials that are classified as hazardous or toxic and that are extensively regulated by environmental and health and safety laws, regulations and permit requirements. We may incur substantial costs, including fines, damages and criminal or civil sanctions, or experience interruptions in our operations for actual or alleged violations or compliance requirements arising under environmental laws, any of which could have a material adverse effect on our business, financial condition, results of operations or cash flows. Our operations could result in violations of environmental laws, including spills or other releases of hazardous substances to the environment. In the event of a catastrophic incident, we could incur material costs. Furthermore, we may be liable for the costs of investigating and cleaning up environmental contamination on or from our properties or at off-site locations where we disposed of or arranged for the disposal or treatment of hazardous materials. Based on available information, we believe that the costs to investigate and remediate known contamination will not have a material adverse effect on our business, financial condition, results of operations or cash flows. However, if significant previously unknown contamination is discovered, or if existing laws or their enforcement change, then the resulting expenditures could have a material adverse effect on our business, financial condition, results of operations or cash flows.

Environmental, health and safety laws, regulations and permit requirements, and the potential for further expanded laws, regulations and permit requirements may increase our costs or reduce demand for our products and thereby negatively affect our business. Environmental permits required for our operations are subject to periodic renewal and may be revoked or modified for cause or when new or revised environmental requirements are implemented. Changing and increasingly strict environmental requirements and the potential for further expanded regulation may increase our costs and can affect the manufacturing, handling, processing, distribution and use of our products. If so affected, our business and operations may be materially and adversely affected. In addition, changes in these requirements may cause us to incur substantial costs in upgrading or redesigning our facilities and processes, including our waste treatment, storage, disposal and other waste handling practices and equipment. For these reasons, we may need to make capital expenditures beyond those currently anticipated to comply with existing or future environmental or safety laws.

Approximately 37% of our employees are covered by a collective bargaining agreement that expires on May 1, 2007. Disputes with the union representing these employees or our inability to conclude a favorable renewal of the collective bargaining agreement may negatively affect our business.

As of December 31, 2006, we had 274 employees, of whom approximately 37% (all of our hourly employees at our Texas City site) are covered by a collective bargaining agreement which expires on May 1, 2007, and we expect to engage in negotiations for a new collective bargaining agreement in April 2007. In connection with two previous

renegotiations of this collective bargaining agreement, we locked out our employees for 16 weeks and our hourly employees engaged in a one-week strike. Any further labor disturbances could have a material adverse effect on our business, financial condition, results of operations or cash flows. During the lockout and the strike, our Texas City site was operated by our salaried workers and contract workers at comparable cost without interruption, loss of production or environmental incident. Neither the lockout nor the strike had a material adverse effect on our business, financial

condition, results of operations or cash flows, although we can give no assurances that future similar occurrences will not have such an impact.

A failure to retain our key employees could adversely affect our business.

We are dependent on the services of the members of our senior management team to remain competitive in our industry. There is a risk that we will not be able to retain or replace these key employees. Our current key employees are subject to employment conditions or arrangements that permit the employees to terminate their employment without notice. The loss of any member of our senior management team could materially adversely affect our business, financial condition, results of operations or cash flows.

Transactions consummated pursuant to our plan of reorganization could result in the imposition of material tax liabilities.

Prior to our emergence from bankruptcy, we eliminated our holding company structure by merging Sterling Chemicals Holdings, Inc. with and into us. We believe that this merger qualifies as a tax-free reorganization pursuant to Section 368(a)(1)(G) of the Internal Revenue Code (commonly referred to as a G Reorganization) for United States federal income tax purposes. However, a judicial determination that this merger did not qualify as a G Reorganization would result in additional federal income tax liability which could materially adversely affect our business, financial condition, results of operations and cash flows.

We may not successfully implement our acquisition strategy, and acquisitions that we pursue may present unforeseen integration obstacles or costs, increase our leverage or negatively impact our performance.

We may not be able to identify suitable acquisition candidates, and the expense incurred in consummating acquisitions of related businesses, or our failure to integrate such businesses successfully into our existing businesses, could affect our growth or result in our incurring unanticipated expenses and losses. Furthermore, we may not be able to realize any anticipated benefits from acquisitions. From time to time we evaluate potential acquisitions and may complete one or more significant acquisitions in the future. To finance an acquisition we may need to incur debt or issue equity. However, we may not be able to obtain favorable debt or equity financing to complete an acquisition, or at all. In particular, the lack of an active trading market in our common stock, as well as the dilutive terms of our outstanding Series A convertible preferred stock, may make our common stock unattractive as consideration for an acquisition. The process of integrating acquired operations into our existing operations may result in unforeseen operating difficulties and may require significant financial resources that would otherwise be available for the ongoing development or expansion of existing operations. Some of the risks associated with our acquisition strategy, which could materially adversely affect our business, financial condition, results of operations or cash flows, include:

- potential disruption of our ongoing business and distraction of management;
- unexpected loss of key employees or customers of an acquired business;
- conforming an acquired business standards, processes, procedures or controls with our operations;
- coordinating new product and process development;
- hiring additional management or other critical personnel;
- encountering unknown contingent liabilities which could be material; and
- increasing the scope, geographic diversity and complexity of our operations.

Our acquisition strategy may not be favorably received by customers, and we may not realize any anticipated benefits from acquisitions.

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Risks Relating to the Ownership of our Common Stock

Our common stock is thinly traded. There is no active trading market for our common stock and an active trading market may not develop.

Our common stock is not listed on any national or regional securities exchange. Quotations for shares of our common stock are listed by certain members of the National Association of Securities Dealers, Inc. on the OTC Electronic Bulletin Board. In recent years, the trading volume of our common stock has been very low and the transactions that have occurred were typically effected in transactions for which reliable market quotations have not been available. An active trading market may not develop or, if developed, may not continue for our equity securities, and a holder of any of these securities may find it difficult to dispose of, or to obtain accurate quotations as to the market value of such securities.

We have a significant stockholder which has the ability to control our actions.

Resurgence Asset Management, L.L.C. and its and its affiliates managed funds and accounts (collectively, Resurgence) own in excess of 98% of our preferred stock and over 60% of our common stock, representing ownership of over 82% of the total voting power of our equity. The interests of Resurgence may differ from our other stockholders and Resurgence may vote their interests in a manner that may adversely affect our other stockholders. Through their direct and indirect interests in us, Resurgence is in a position to influence the outcome of most matters requiring a stockholder vote. This concentrated ownership makes it less likely that any other holder or group of holders of common stock would be able to influence the way we are managed or the direction of our business. These factors also may delay or prevent a change in our management or voting control.

Our preferred stock pays a quarterly stock dividend that is dilutive to the holders of our common stock.

Our shares of preferred stock carry a cumulative dividend rate of 4% per quarter, payable in additional shares of preferred stock. Our shares of preferred stock are convertible at the option of the holder into shares of our common stock and vote as if so converted on all matters presented to the holders of our common stock for a vote. Consequently, each dividend paid in additional shares of our preferred stock has a dilutive effect on our shares of common stock and increases the percentage of the total voting power of equity owned by Resurgence. In 2006, we issued an additional 594.832 shares of our preferred stock (which is convertible into 594,832 shares of our common stock) in dividends, which represents 8.6% of the current total voting power of our equity securities.

The existence of our preferred stock and limited liquidity of our common stock may limit our ability to utilize our equity to pursue strategic initiatives that may otherwise exist.

The existence of our preferred stock and the limited trading market of our common stock (as discussed above) could make it more difficult to use these instruments as part of implementing our strategy to grow the business.

Item 2. ***Properties***

Our petrochemicals site is located in Texas City, Texas, approximately 45 miles south of Houston, on a 290-acre site on Galveston Bay near many other chemical manufacturing complexes and refineries. We own all of the real property which comprises our Texas City site and we own the acetic acid, styrene and plasticizers manufacturing facilities located at the site. We also lease a portion of our Texas City site to Praxair, who constructed a partial oxidation unit on that land, and lease a portion of our Texas City site to S&L Cogeneration Company, a 50/50 joint venture between us and Praxair Energy Resources, Inc., who constructed a cogeneration facility on that land. Our Texas City site offers approximately 135 acres for future expansion by us or by other companies who could benefit from our existing infrastructure and facilities, and includes a greenbelt around the northern edge of the plant site. We own 126 railcars and, at our Texas City site, we have facilities to load and unload our products and raw materials in ocean-going vessels, barges, trucks and railcars.

Substantially all of our Texas City, Texas site, and the tangible properties located thereon, are subject to a lien securing our obligations under our Secured Notes.

We lease the space for our principal executive offices, located at 333 Clay Street, Suite 3600 in Houston, Texas.

We believe our properties and equipment are sufficient to conduct our business.

Item 3. ***Legal Proceedings***

On July 5, 2005, Patrick B. McCarthy, an employee of Kinder-Morgan, was seriously injured at Kinder-Morgan, Inc. s facilities near Cincinnati, Ohio while attempting to offload a railcar containing one of our plasticizers products. On October 28, 2005, Mr. McCarthy and his family filed a suit in the Court of Common Pleas, Hamilton County, Ohio (Case No. A0509144) against us, BASF and five other defendants. The plaintiffs are seeking a minimum amount of $150,000 in damages related to medical expenses and loss of earnings and earnings capacity, among other things, and punitive damages. Discovery is ongoing in this case as to the underlying cause of the accident and the parties respective liability, if any. At this time, it is impossible to determine what, if any, liability we will have for this incident and we will vigorously defend the suit. We believe that all, or substantially all, of any liability imposed upon us as a result of this suit and our related out-of-pocket costs and expenses will be covered by our insurance policies, subject to a $1 million deductible. We do not believe that this incident will have a material adverse affect on our business, financial position, results of operations or cash flows, although we cannot guarantee that a material adverse effect will not occur.

On August 17, 2006, we initiated an arbitration proceeding against BP Chemicals to resolve a dispute involving the interpretation of provisions of our acetic acid production agreement with BP Chemicals. Under the production agreement, BP Chemicals reimburses our manufacturing expenses and pays us a percentage of the profits derived from the sales of the acetic acid we produce. Historically, the costs of manufacturing charged to our acetic acid business, and reimbursed by BP Chemicals, included the amounts we paid Praxair for carbon monoxide, hydrogen and a blend of carbon monoxide and hydrogen commonly referred to as blend gas . Our acetic acid business has always used all of the carbon monoxide produced by Praxair, other than the small amount of carbon monoxide included in the blend gas. Until recently, all of the blend gas produced by Praxair was used by the oxo-alcohols plant included in our plasticizers business. During the period when the oxo-alcohols plant was operating, BP Chemicals was compensated for the use of this blend gas by our oxo-alcohols plant through a credit to the amount of our manufacturing expenses reimbursed by BP Chemicals. Effective July 1, 2006, we permanently closed our oxo-alcohols plant. BP Chemicals has taken the position that it is entitled to continue to deduct a portion of the blend gas credit from the reimbursement of our manufacturing expenses, even though our oxo-alcohols plant has been closed and is no longer taking any blend gas and the Praxair facilities have been modified so that the carbon monoxide previously used in blend gas is now being delivered to our acetic acid operations. Effective August 1, 2006, BP Chemicals began short paying our invoices for manufacturing expenses by the portion of the credit that BP Chemicals claims should continue through July 31, 2016. The disputed portion of the credit averaged approximately $0.3 million per month during 2006. We are also seeking additional damages from BP Chemicals in the arbitration based on what we believe are breaches of duty by BP Chemicals. The arbitration hearing was scheduled for August 6, 2007. However, pursuant to an agreement reached in principle on January 31, 2007, the parties will abate the arbitration proceeding for a period of at least six months while they attempt to reach a negotiated settlement. As part of the agreement, BP Chemicals reimbursed us $0.8 million on February 5, 2007, which was 50% of the accrued disputed credit, and will continue to pay 50% of the disputed amount each month during the period of negotiation. The parties have stipulated that the payments are made without prejudice, in that BP Chemicals is not admitting liability and continues to insist that we remain liable for the disputed portion of the blend gas credit. According to the agreement, if a settlement is not reached within six months, either party may reinstate the arbitration process, and seek a hearing date consistent with the current schedule, or approximately seven months thereafter. Under the January 31, 2007 agreement, if the arbitration proceeds to an award, the amounts paid by BP Chemicals will be credited against any sums awarded to us or refunded by us to BP Chemicals, depending on the ruling of the arbitration panel. We believe that our acetic acid production agreement does not contemplate the continuation of any portion of the blend gas credit under these circumstances and will vigorously pursue our position.

Although we are in a dispute with BP Chemicals over the interpretation of this contractual provision, we believe that we continue to have a constructive working relationship with BP Chemicals, as has been the case since 1986. As part of the settlement negotiations over the blend gas calculation, we may discuss an extension of the term of the acetic acid production agreement.

On February 21, 2007, we received a summons naming us as a defendant in a class action suit, Case No. H-07-0625 filed in the United States District Court, Southern District of Texas, Houston Division. The plaintiffs comprising the

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proposed class are employees and retired employees of Sterling Fibers, Inc., one of our former subsidiaries that was sold in connection with our Plan of Reorganization in 2002. The plaintiffs are alleging that we were not permitted to increase their premiums for retiree medical insurance based on a provision contained in the asset purchase agreement between us and Cytec Industries Inc. governing our purchase of our former acrylic fibers business in 1997. During our bankruptcy, we specifically rejected this asset purchase agreement. The plaintiffs are making claims for breach of contract and claims under the Employee Retirement Income Security Act and seek damages, declaratory relief, punitive damages and attorneys fees. At this time, we have not determined what, if any, liability we may have in this matter and intend to vigorously defend this action. We do not believe a loss related to this matter is probable, therefore no liability associated with this matter has been accrued. Currently, we are unable to determine the possible range of loss related to this matter, if any.

We are subject to various other claims and legal actions that arise in the ordinary course of our business. We do not believe that any of these claims and actions, separately or in the aggregate, will have a material adverse effect on our business, financial position, results of operation or cash flows, although we cannot guarantee that a material adverse effect will not occur.

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

No matters were submitted to a vote of security holders during the fourth quarter of 2006.

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PART II

Item 5. ***Market for Registrant s Common Equity and Related Stockholder Matters***

Our common stock, par value $0.01 per share, is currently quoted on the Over-the-Counter (OTC) Electronic Bulletin Board maintained by the National Association of Securities Dealers, Inc. under the symbol SCHI. The following table contains information about the high and low sales prices per share of our common stock for the last two years. Information about OTC Electronic Bulletin Board bid quotations represents prices between dealers, does not include retail mark-ups, mark-downs or commissions, and may not necessarily represent actual transactions. Quotations on the OTC Electronic Bulletin Board are sporadic, and currently there is no established public trading market for our common stock.

	First Quarter	Second Quarter	Third Quarter	Fourth Quarter
2006 High	$11.50	$15.00	$14.90	$15.00
Low	$10.00	$10.25	$13.10	$12.48
2005 High	$46.50	$41.00	$37.00	$25.50
Low	$35.05	$26.00	$22.00	$11.77

The last reported sale price per share of our common stock as reported on the OTC Electronic Bulletin Board on March 9, 2007 was $11.00. As of March 9, 2007, there were 328 holders of record of our common stock. This number does not include stockholders for whom shares are held in a nominee or street name.

Dividend Policy

We have not declared or paid any cash dividends with respect to our common stock since we emerged from bankruptcy in December 2002. We do not presently intend to pay cash dividends with respect to our common stock for the foreseeable future. In addition, we cannot pay dividends on our shares of common stock under the indenture for our Secured Notes or under our revolving credit facility. The payment of cash dividends, if any, will be made only from assets legally available for that purpose, and will depend on our financial condition, results of operations, current and anticipated capital requirements, general business conditions, restrictions under our existing debt instruments and other factors deemed relevant by our Board of Directors.

Equity Compensation Plan

Under our 2002 Stock Plan, officers, key employees and consultants, as designated by our Board of Directors or Compensation Committee, may be issued stock options, stock awards, stock appreciation rights or stock units. Our 2002 Stock Plan is administered by our Board of Directors, in consultation with our Compensation Committee, and may be amended or modified from time to time by our Board of Directors in accordance with its terms. Our Board of Directors or Compensation Committee determines the exercise price of stock options, any applicable vesting provisions and other terms and provisions of each grant in accordance with our 2002 Stock Plan. Options granted under our 2002 Stock Plan become fully exercisable in the event of the optionee s termination of employment by reason of death, disability or retirement, and may become fully exercisable in the event of a change of control. No option may be exercised after the tenth anniversary of the date of grant or the earlier termination of the option. We have reserved 363,914 shares of our common stock for issuance under the 2002 Stock Plan (subject to adjustment). On February 11, 2003, we granted certain of our officers and key employees, options to purchase 326,000 shares of our common stock under our 2002 Stock Plan at an exercise price of $31.60 per share, 15,833 of which have been exercised and 59,167 of which have lapsed or expired without being exercised. On November 5, 2004, we granted one of our officers options to purchase 27,500 shares of our common stock under our 2002 Stock Plan at an exercise price of $31.60 per share. We have not made any other awards under our 2002 Stock Plan.

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The following table provides information regarding securities authorized for issuance under our 2002 Stock Plan as of December 31, 2006:

Plan Category	Number of securities to be issued upon exercise of outstanding options, warrants and rights	Weighted-average exercise price of outstanding options, warrants and rights	Number of securities remaining available for future issuance under equity compensation plans (excluding securities reflected in first column
Equity compensation plans approved by security holders[1]	278,500	$ 31.60	85,414
Equity compensation plans not approved by security holders			
Total	278,500	$ 31.60	85,414

(1) Our 2002 Stock Plan was authorized and established under our Plan of Reorganization, which became effective on December 19, 2002. Our Plan of Reorganization provided that, without any further act or authorization, confirmation of our Plan of Reorganization and entry of the confirmation order was deemed to satisfy all applicable

federal and state law requirements and all listing standards of any securities exchange for approval by the board of directors or the stockholders of our 2002 Stock Plan. No additional stockholder approval of our 2002 Stock Plan has been obtained.

Performance Graph

The following performance graph compares our cumulative total stockholder return on shares of our common stock for a four-year period with the cumulative total return of the Standard & Poor s 500 Stock Index (the S & P 500 Index) and the Standard & Poor s Diversified Chemicals Index (the S & P Chemicals Index). The graph assumes the investment of $100 on December 31, 2002 in shares of our common stock, the S & P 500 Index and the S & P Chemicals Index and the reinvestment of dividends.

COMPARISON OF 4 YEAR CUMULATIVE TOTAL RETURN*

Among Sterling Chemicals Inc., The S & P 500 Index
And The S & P Diversified Chemicals Index

* $100 invested on 1/3/03 in stock or on 12/31/02 in index-including reinvestment of dividends. Fiscal year ending December 31.

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Item 6. ***Selected Financial Data***

The following table sets forth selected financial data with respect to our consolidated financial condition and consolidated results of operations and should be read in conjunction with our historical consolidated financial statements and related notes, Item 7. Management s Discussion and Analysis of Financial Condition and Results of Operations and our Financial Statements and Supplementary Data included in Item 8 of this Form 10-K.

On July 16, 2001, Sterling Chemicals Holdings, Inc. and its subsidiaries, including us, filed voluntary petitions for reorganization under Chapter 11 of the United States Bankruptcy Code. Our Plan of Reorganization was confirmed on November 20, 2002 and, on December 19, 2002, we emerged from bankruptcy. Due to the implementation of fresh-start accounting upon our emergence from bankruptcy, we refer to ourselves as Predecessor Sterling for periods on or before December 19, 2002 and Reorganized Sterling for periods after December 19, 2002. Prior to December 6, 2002, all issued and outstanding shares of Predecessor Sterling s capital stock were held by Sterling Chemicals Holdings, Inc. and, accordingly, per share data prior to December 19, 2002 is not presented.

The consolidated statements of operations information for the years ended December 31, 2006, 2005, 2004 and 2003 and the transition period from December 20, 2002 to December 31, 2002, and the consolidated balance sheet information as of December 31, 2006, 2005, 2004, 2003 and 2002, reflect the financial position and operating results after giving effect to our plan of reorganization and the application of the principles of fresh-start accounting in accordance with the provisions of Statement of Position 90-7, Financial Reporting by Entities in Reorganization under the Bankruptcy Code . Accordingly, such financial information is not comparable to the historical financial information before December 20, 2002. During 2002, we changed our fiscal year end from September 30 to December 31.

	Reorganized Sterling					Predecessor Sterling	
	Year ended December 31, 2006	Year ended December 31, 2005	Year ended December 31, 2004	Year ended December 31, 2003	December 20 to December 31, 2002	October 1 to December 19, 2002	Fiscal Year Ended September 30, 2002
	(In Thousands, Except Per Share Data)						
Operating Data:							
Revenues	$ 667,544	$ 641,886	$ 655,353	$ 518,772	$ 12,211	$ 98,575	$ 375,095
Gross profit (loss)	12,826	(11,248)	22,344	23,790	1,494	6,471	47,530
Income (loss) from continuing operations[(1)]	(104,622)	(18,508)	(39,881)	1,270	(553)	230,145	(32,685)
Income (loss) from discontinued operations[(2)]	(997)	(11,060)	(22,763)	(15,469)	(991)	188,466	(3,301)
Per Share Data:							
Net loss attributable to common stockholders	$ (40.26)	$ (12.94)	$ (24.30)	$ (6.84)	$ (0.61)	$	$
	(39.91)	(9.03)	(16.24)	(1.36)	(0.26)		

Net loss from
continuing operations
attributable to
common stockholders

Cash dividends

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	Reorganized Sterling					Predecessor Sterling	
	Year ended December 31, 2006	Year ended December 31, 2005	Year ended December 31, 2004	Year ended December 31, 2003	December 20 to December 31, 2002	October 1 to December 19, 2002	Fiscal Year Ended September 30, 2002
	(Dollars in Thousands)						
Balance Sheet Data:							
Working capital[3][6]	$ 90,124	$ 76,605	$106,767	$ 137,412	$ 149,518	$163,638	$ 154,988
Total assets	245,823	386,594	473,553	550,503	547,170	546,014	489,648
Long-term debt (excluding current portion of long-term debt)[4][6]	100,579	100,579	100,579	100,579	94,275	94,275	
Stockholders equity (deficiency in assets)[5]	(22,766)	80,285	120,083	189,436	209,011	210,725	(611,477)

(1) During 2006, we recorded a $127.7 million impairment charge to our styrene assets. There was a deferred tax benefit of $45 million in connection with this impairment, which was offset by deferred tax expense of $28 million in connection with the recording of a valuation allowance against our deferred tax assets. During 2004, we recorded a

$48.5 million goodwill impairment charge. Also during 2004, we recorded a pension curtailment gain of $13 million. The period from October 1, 2002 through December 19, 2002 includes a net loss on fresh-start adjustments of $203 million, along with a net gain on debt restructuring of $458 million. During fiscal year ended September 30, 2002, we recorded $56.8 million of deferred tax expense to reflect a full valuation allowance on our U.S. deferred tax assets.

(2) During 2005, we announced that we were exiting the acrylonitrile business and related derivatives operations. During 2004, we recorded a $22 million pre-tax impairment

charge related to our acrylonitrile long-lived assets. On December 19, 2002, pursuant to our plan of reorganization, we sold our pulp chemicals business to Superior Propane, Inc. for approximately $373 million and our acrylic fibers business to local management of that business for nominal consideration. The operating results of these businesses have been reported as discontinued operations in the consolidated statement of operations and cash flows, and the assets and liabilities of these businesses have been presented separately as assets and liabilities related to discontinued operations in our consolidated balance sheet.

(3) Working capital as of December 31, 2006, 2005, 2004, 2003,

2002 and September 30, 2002 includes net assets (liabilities) of discontinued operations of $(0.2) million, $(2) million, $55 million, $57 million, $27 million and $164 million, respectively. Working capital as of September 30, 2002 excludes pre-petition liabilities.

(4) The balance as of September 30, 2002 excludes long-term debt of $418.4 million and $295.0 million, classified as pre-petition liabilities subject to compromise and pre-petition liabilities not subject to compromise, respectively.

(5) The balance as of December 31, 2006 includes an increase in Stockholders equity of $6.7 million (net of tax) due to the adoption of Statement of

Financial Accounting Standards No. 158, Employers Accounting for Defined Benefit Pension and Other Postretirement Plans (SFAS No. 158).

(6) As of December 31, 2006, we reclassified $101 million of debt due in December 2007 to long-term based on our ability and intent to refinance the debt on a long-term basis.

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Item 7. ***Management s Discussion and Analysis of Financial Condition and Results of Operations***

Overview

Business

We are a leading North American producer of selected petrochemicals used to manufacture a wide array of consumer goods and industrial products throughout the world. Our primary products are acetic acid, styrene and plasticizers.

Our acetic acid is used primarily to manufacture vinyl acetate monomer, which is used in a variety of products, including adhesives and surface coatings. All of our acetic acid production is sold to BP Amoco Chemical Company (BP Chemicals), and we are BP Chemicals sole source of acetic acid production in the Americas. We sell our acetic acid to BP Chemicals pursuant to the Production Agreement that extends until 2016. The Production Agreement provides us with a portion of the profits derived from BP Chemicals sales of the acetic acid we produce and reimbursement of 100% of our fixed and variable costs of production. This Production Agreement has provided us with a steadily increasing source of income since the inception of this relationship in 1986 and, over the last three years, we have operated at over 100% of capacity and at utilization rates greater than the industry average. We believe we have one of the lowest cost acetic acid facilities in the world. Our acetic acid facility utilizes BP Chemicals proprietary carbonylation technology, or Cativa Technology, which we believe offers several advantages over competing production methods, including lower energy requirements and lower fixed and variable costs. We also jointly invest with BP Chemicals in capital expenditures related to our acetic acid facility. Acetic acid production has two major raw materials requirements methanol and carbon monoxide. BP Chemicals, a producer of methanol, supplies 100% of our methanol requirements related to our production of acetic acid. All of the carbon monoxide we use in the production of acetic acid is supplied by Praxair Hydrogen Supply, Inc. (Praxair) from a partial oxidation unit constructed by Praxair on land leased from us at our Texas City site.

Styrene is a commodity chemical used to produce intermediate products such as polystyrene, expandable polystyrene resins and ABS plastics, which are used in a wide variety of products such as household goods, foam cups and containers, disposable food service items, toys, packaging and other consumer and industrial products. Approximately 30% to 40% of our styrene capacity is currently committed for sales in North America under long-standing customer relationships. In addition, approximately 30% to 40% of our styrene capacity is sold on the spot market, with the balance of our capacity available to produce styrene for sales throughout the world when market conditions warrant. We had one customer contract, which represented a significant portion of our 2006 North American committed sales volumes, expire at the end of 2006 and that contract was not renewed. We are currently pursuing renewal of another contract that expires in 2007, as well as additional contract volumes with new customers. We may not be successful in renewing these expiring contracts or obtaining new contract customers. If we are unsuccessful, we may lower our styrene production levels or sell more of our styrene production in the spot markets, both domestic and export, which could materially adversely affect our business, financial condition, results of operations or cash flows.

All of our plasticizers, which are used to make flexible plastics, such as shower curtains, floor coverings, automotive parts and construction materials, are produced exclusively for BASF Corporation (BASF) pursuant to a long-term production agreement that extends until 2013, subject to some limited early termination rights held by BASF beginning in 2010. Under our agreement with BASF, BASF provides us with most of the required raw materials, markets the plasticizers we produce, and is obligated to make certain fixed quarterly payments to us and to reimburse us monthly for our actual production costs and capital expenditures relating to our plasticizers facility.

We manufacture all of our petrochemicals products at our site in Texas City, Texas. In terms of production capacity, our Texas City site has the sixth largest acetic acid facility in the world and the 3rd largest styrene facility in North America. Our Texas City site, which covers an area of 290 acres, is strategically located on Galveston Bay and benefits from a deep-water dock capable of handling ships with up to a 40-foot draft, as well as four barge docks, direct access to Union Pacific and Burlington Northern railways with in-motion rail scales on site, truck loading racks and weigh scales, stainless and mild steel storage tanks, three waste deepwells, 135 acres of available land zoned for heavy industrial use, additional land zoned for light industrial use and a supportive political environment for growth. In addition, we are in the heart of one of the largest petrochemical complexes on the Gulf Coast and as a result have

on-site access to a number of key raw material pipelines as well as close proximity to a number of the larger refinery complexes that provide some of our principal raw materials.

As shown below, our rated annual production capacity as of December 31, 2006 is among the highest in North America for styrene and acetic acid.

Product	**Rated Annual Production Capacity**	**Percent of Total North American Capacity**	**North American Market Position**	**Global Production Capacity**
Acetic Acid	1.1 billion pounds	17%	3	24 billion pounds
Styrene	1.7 billion pounds	11%	4	63 billion pounds

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We generally sell our petrochemicals products to customers for use in the manufacture of other chemicals and products, which in turn are used in the production of a wide array of consumer goods and industrial products throughout the world. The North American acetic acid industry tends to sell most of its products through long-term sales agreements having cost plus pricing mechanisms, eliminating much of the volatility seen in other petrochemicals products and resulting in more stable and predictable earnings and profit margins. Styrene is a commodity and exhibits wide swings in prices and profit margins based upon current and anticipated levels of supply and demand. Although exceptions occasionally occur, as a general rule, if styrene profit margins are favorable, our overall financial performance is good, but our overall financial performance suffers when styrene margins are unfavorable. The market for styrene roughly follows repetitive cycles, and general trends in the supply and demand balance may be observed over time. However, it is difficult, if not impossible, to definitively predict when market conditions will be favorable or unfavorable.

Acetic Acid. The North American acetic acid industry is enjoying a period of sustained domestic demand growth. as well as substantial export demand. This has led to current North American industry utilization rates of 86% and Tecnon OrbiChem projects utilization rates to increase to over 98% by 2013. The North American acetic acid industry is inherently less cyclical than many other petrochemical products due to a number of important features.

There are only four large producers of acetic acid in North America and historically these producers have made capacity additions in a disciplined and incremental manner, primarily using small expansion projects or exploiting debottlenecking opportunities. In addition, the leading technology required to manufacture acetic acid is controlled by two global companies, which permits these companies to control the pace of new capacity additions through the licensing or development of such additional capacity. The limited availability of this technology also creates a significant barrier to entry into our industry by potential competitors. Additionally, currently there is no planned development of new acetic acid capacity contemplated in the Middle East, primarily due to the higher costs of feedstocks in that region.

Global production capacity of acetic acid as of December 31, 2006 was approximately 24 billion pounds per year, with current North American production capacity at approximately 7 billion pounds per year. The North American acetic acid market is mature and well developed and is dominated by four major producers that account for over 94% of the production capacity of acetic acid in North America. Demand for acetic acid is linked to the demand for vinyl acetate monomer, a key intermediate in the production of a wide array of polymers. Vinyl acetate monomer is the largest derivative of acetic acid, representing over 40% of total demand. Annual global production of vinyl acetate monomer is expected to increase from 10.4 billion pounds in 2005 to 12.2 billion pounds in 2010.

The North American acetic acid industry tends to sell most of its products through long-term sales agreements having cost plus pricing mechanisms, eliminating much of the volatility seen in other petrochemicals products and resulting in more stable and predictable earnings and profit margins.

Several acetic acid capacity additions have occurred since 1998, including an expansion of our acetic acid unit from 800 million pounds of rated annual production capacity to 1.1 billion pounds during 2005. These capacity additions were somewhat offset by reductions of approximately 1.6 billion pounds in annual global capacity from the shutdown of various outdated acetic acid plants from 1999 through 2001. In 2006, BP Chemicals closed two of its outdated acetic acid production units in Hull, England that had a combined annual capacity of approximately 500 million pounds (which had been sold primarily in Europe and South America). We and BP Chemicals are reviewing further expansion of our acetic acid plant in 2008 or 2009.

Styrene. The North American styrene industry is currently in a protracted down cycle, primarily as a result of over-supply. This shift is the result of two major developments. Export demand has historically represented over 20% of North American production capacity. Regional cost pressures in addition to new production capacity being added in Asia and the Middle East, have made it difficult for North American producers to compete in these export markets on a continuous basis. In addition, a significant amount of styrene capacity has been added globally over the past five to ten years by producers of propylene oxide using so-called PO-SM technology, which produces styrene as a co-product. Propylene oxide is a key intermediate in the production of polyurethane, and polyurethane demand growth has been significantly greater than demand growth for styrene, exacerbating the over-supply of styrene. During periods of over-supply, production rates for styrene producers decrease significantly. Production rates in North

America are currently estimated by Chemical Market Associates, Inc. (CMAI) to be 75% of capacity. When production rates are low, unit production costs increase due to the allocation of fixed costs over a lower production volume and a reduction in the efficiency of the manufacturing unit, both in energy usage and in the conversion rates for raw materials. Compounding these cost impacts, prices for the principal styrene raw materials, benzene and ethylene, are currently near historical highs, putting pressure on margins on styrene sales even though styrene contract prices are at near historic highs.

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According to CMAI, benzene and ethylene prices are expected to decline by approximately 8% and 7%, respectively, on average over each of the next five years.

The financial performance of styrene is primarily a function of sales prices, the costs of raw materials and energy and sales volumes. In contrast, under the Production Agreement with BP Chemicals and our agreement with BASF, BP Chemicals is required to provide the methanol to produce acetic acid and BASF is required to provide us with most of the major raw materials necessary to plasticizers. These sources of raw materials tend to mitigate certain risks typically associated with fluctuating raw materials costs, as well as decrease our working capital requirements. While changes in the prices for styrene may be tracked through a variety of sources, a change in price does not necessarily result in a corresponding change in our financial performance. When the price of styrene increases or decreases, our overall financial performance may improve, decline or stay roughly the same depending upon the extent and direction of changes in our costs for raw materials and energy and our production rates. The aggregate cost of raw materials and energy resources is far greater than all other costs of producing styrene combined. We use significant amounts of natural gas as fuel in the production of styrene, and the producers of most of our raw materials use significant amounts of natural gas in their production. As a result, our production and raw materials costs increase or decrease based upon changes in the price for natural gas. Natural gas and most of our raw materials are commodities and, consequently, are subject to wide fluctuations in prices, which can, and often do, move independently of changes in the prices for our products. Prices for, and the availability of, natural gas and many of our raw materials are largely based on regional factors, which can result in wide disparities in prices in different parts of the world or shortages or unavailability in some regions at the same time when these raw materials are plentiful in other parts of the world. Prices for styrene, on the other hand, tend to be more consistent throughout the world, after taking into account transportation costs. Consequently, changes in prices for natural gas and raw materials tend to impact the margin on our styrene sales rather than the price of styrene, with margins increasing when natural gas and raw materials costs decline and *vice versa.* In addition, many producers in other parts of the world use oil-based processes rather than natural gas-based processes. Subsequently, the relationship between the price of crude oil and the price of natural gas can either increase or decrease our competitiveness depending on their relative values at any particular point in time. Sales volumes influence our overall financial performance in a variety of ways. As a general rule, increases in sales volumes will result in an increase in overall revenues and *vice versa,* although this is not necessarily the case since the price for styrene can change dramatically from month-to-month. More importantly, changes in production rates impact the average cost per pound of styrene produced. If more pounds are produced, our fixed costs are spread over a greater number of pounds resulting in a lower average cost to produce each pound. In addition, our styrene production rates influence the overall efficiency of our styrene manufacturing unit and the yields we receive from our raw materials.

Over the last five years, China has been the driver for growth in styrene demand, representing approximately 75% of the world s styrene demand growth in that period. Historically, we have positioned ourselves to take advantage of peaks in the Asian styrene markets, with a large portion of our styrene capacity not being committed under long-term arrangements. However, over the last two years, relatively high benzene and domestic natural gas prices have significantly limited our ability to sell styrene into the Asian markets, and high styrene prices have reduced styrene global demand growth rates. In addition, several of our competitors have announced their intention to build new styrene production units outside the United States, further complicating our ability to sell styrene into the Asian markets. In 2006, our competitors added 2.6 billion pounds of new styrene capacity in Asia. The majority of the remaining announced construction projects are scheduled to start up between 2007 and 2009, although it is not uncommon for announced construction to be delayed. For example, Shell Oil Company and Saudi Basic Industries Corporation recently announced their decision to suspend the development of a 600,000 metric ton per year styrene project in Al Jubail, Saudi Arabia, which was scheduled to come on-stream in 2007, due to rising construction expenses and the high cost of benzene feedstock. In addition, much of this new capacity is being constructed in politically unstable regions of the world, such as the Middle East, which may impact the timing of the start-up of this new capacity. If and when these new units are completed, we would anticipate more difficult market conditions, especially in the export markets, until the additional supply is absorbed by growth in styrene demand or significant capacity rationalization occurs.

Given the market conditions in Asia and the high domestic raw materials and energy costs we have been experiencing, most of our styrene sales over the last two years have been to customers in the United States, Mexico, Canada and South America. We expect most of our styrene sales over the next three to five years to also be in these geographic regions. Consequently, we are focusing our efforts on increasing market share in these areas, while continuing to make occasional styrene sales in Asia on an opportunistic basis. We may not, however, be successful in increasing our market share in these geographic regions during this period and we cannot guarantee when, or if, export market conditions to Asia will improve for North American styrene producers. We may also explore mergers, acquisitions, and joint ventures with other North American styrene producers that could improve the domestic balance of supply and demand for styrene and provide us with improved cash flows.

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CMAI currently is not projecting any additional capacity increases in North America through 2010, with projected operating rates reaching a trough of 75% in 2007, and less than 80% operating rates through 2010, without any major industry restructuring. Although we believe an improved North American industry outlook is possible, this largely depends on a significant industry restructuring. Styrene and polystyrene industry participants, including The DOW Chemical Company and NOVA Chemicals Corporation have recently announced a desire to seek transactions which would restructure the North American styrene and polystyrene industries, thereby improving the balance of supply and demand in North America. Separately, new technology for the manufacture of propylene oxide has been developed that should result in lower manufacturing costs for propylene oxide and which does not produce styrene as a co-product, which could significantly reduce the future growth of plants utilizing PO-SM technology.

Our styrene facilities consist of two reaction trains, a north train and a south train. On September 22, 2005, during a shut down of our plant in anticipation of Hurricane Rita, the superheater in the south train of our styrene facility was significantly damaged by a fire, forcing a closure of the south train until repairs could be completed. In addition, the north train reactor of our styrene facility sustained internal damage as a result of this incident and, although still capable of producing product, the reactor damage caused significant raw material yield and energy inefficiencies. On January 12, 2006, we shut down the north train of our styrene facilities to make repairs to the reactor and replace the existing catalyst. In February 2006, both the north and south trains were re-started. During these shutdowns, we fully met our supply obligations to our contract styrene customers through the operation of the north train of our styrene facilities, supplemented by open market purchases of styrene. The total cost for these repairs was approximately $11 million. We also filed a claim for approximately $12 million under our business interruption insurance policies. During the second quarter of 2006, we received an advance payment from our insurance companies of $3 million. In August 2006, we settled the claim with our insurance carriers for a total of $15 million, including the $3 million advance payment.

During the fourth quarter of 2006, we performed an asset impairment analysis on our styrene production unit. This analysis was performed due to recent industry forecasts, forecasted negative cash flow generated by our styrene business over the next few years and the uncertainty surrounding the ability of the North American styrene industry to successfully restructure. Our management determined that a triggering event, as defined in Statement of Financial Accounting Standards No. 144, Accounting for the Impairment or Disposal of Long Lived Assets (SFAS No. 144), had occurred and an asset impairment analysis was performed. We analyzed the undiscounted cash flow stream from our styrene business over the next seven years, which represents the remaining book life of our styrene assets, and compared it to the $128 million net book carrying value of our styrene unit and related assets. This analysis showed that the undiscounted projected cash flow stream from our styrene business was less than the net book carrying value of our styrene unit and related assets. As a result, we performed a discounted cash flow analysis and subsequently concluded that our styrene unit and related assets were impaired. While we are still operating our styrene unit, our analysis led us to conclude that our styrene assets should be written down to zero. This write-down caused us to record a $128 million impairment in December 2006.

Plasticizers. Historically, we have produced ethylene-based linear plasticizers, which typically receive a premium over competing branched propylene-based products for customers that require enhanced performance properties. However, the markets for competing plasticizers can be affected by the cost of the underlying raw materials, especially when the cost of one olefin rises faster than the other, or by the introduction of new products. One of the raw materials for linear plasticizers is a product known as linear alpha-olefins. Over the last few years, the price of linear alpha-olefins has increased sharply as supply has declined, which has caused many consumers to switch to lower cost branched propylene-based products and C4-based products, despite the loss of some performance properties. Ultimately, we expect branched plasticizers to replace linear plasticizers for most applications over the long-term. As a result, we modified our plasticizers facilities during the third quarter of 2006 to produce lower cost branched plasticizers products.

In 2005, BP Chemicals announced the permanent closure of its linear alpha-olefins production facility in Pasadena, Texas, the primary source of supply of this feedstock to the oxo-alcohols production unit at our plasticizers facility. After pursuing various alternative uses for our oxo-alcohols unit, we were unable to secure an alternative use for this facility. As a result, we permanently shut down our oxo-alcohols production unit on July 31, 2006. Due to the closure

of our oxo-alcohols unit and our conversion to the production of branched plasticizers, the phthalate esters production unit at our plasticizers facility now uses oxo-alcohols supplied by BASF that have a different chemical composition.

Discontinued Operations

On September 16, 2005, we announced that we were exiting the acrylonitrile business and related derivative operations. Our decision was based on a history of operating losses incurred by our acrylonitrile and derivatives

businesses, and was made after a full review and analysis of our strategic alternatives. Our acrylonitrile and derivatives businesses had sustained losses in recent years and had been shut down since February of 2005.

In accordance with SFAS No. 144, we have reported the operating results of these businesses as discontinued operations in our consolidated statement of operations and cash flows, and we have presented the assets and liabilities of these businesses separately in our consolidated balance sheet.

Results of Operations

The following table sets forth revenues, gross profit (loss) and net loss from continuing operations for 2006, 2005 and 2004:

	Year ended December 31,		
	2006	2005	2004
	(Dollars in Thousands)		
Revenues	$ 667,544	$641,886	$655,353
Gross profit (loss)	12,826	(11,248)	22,344
Loss from continuing operations	(104,662)	(18,508)	(39,881)

Comparison of 2006 to 2005

Revenues and Loss from continuing operations

Our revenues were $668 million in 2006, an increase of 4% over the $642 million in revenues we recorded in 2005. This increase in revenues resulted primarily from an increase in acetic acid and styrene sales prices. We recorded a net loss from continuing operations of $105 million in 2006, compared to the net loss of $19 million we recorded in 2005. This increase in net loss was primarily due to the $128 million impairment charge to our styrene assets that we recorded in 2006.

Revenues from acetic acid and plasticizers were $143 million in 2006, a 12% increase over the $128 million in revenues we recorded in 2005. This increase in revenues was due to a 14% increase in acetic acid revenues and a 6% increase in plasticizers revenues, primarily due to increases in sales prices. We achieved both monthly and annual production records in our acetic acid business during 2006.

Revenues from our styrene operations were $525 million in 2006, an increase of 2% over the $514 million in revenues we recorded in 2005. Direct sales prices for styrene increased 10% from those realized during 2005. Spot prices for styrene, a component of our direct sales prices, ranged from $0.45 to $0.60 per pound during 2006, compared to $0.44 to $0.62 per pound during 2005. Our total sales volumes for styrene in 2006 were 7% lower than in 2005. During 2006, prices for benzene, one of the primary raw materials required for styrene production, increased 10% over the prices we paid for benzene in 2005, and prices for ethylene, the other primary raw material required for styrene production, increased 2% over the prices we paid for ethylene in 2005. Average costs for natural gas, another major component in the cost of manufacturing styrene, decreased 13% during 2006 compared to average natural gas costs during 2005. Margins on our styrene sales in 2006 increased from those realized in 2005, primarily due to slightly improved market conditions. As noted previously, we recorded an impairment of $128 million in 2006 related to our styrene production unit.

Selling, general & administrative expenses

Our selling, general and administrative expenses were $10 million in 2006 compared to $8 million in 2005. This increase in 2006 was primarily due to the approximately $1 million in expenditures we incurred in professional fees to explore potential new business opportunities, and the $1 million we expensed for bad debts in 2006 compared to the $2 million credit for bad debts we recorded in 2005. This increase in the allowance for doubtful accounts balance as of December 31, 2006 resulted primarily from the cumulative sum of disputed invoices related to our disagreement with BP Chemicals described in Item 3, Part I of this Form 10-K.

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Other expense (income)

We recorded other income of $16 million in 2006, which primarily consisted of the recognition of final settlement of our claims under our property damage and business interruption insurance policies related to the September 2005 fire that occurred in our styrene unit.

Provision (benefit) for income taxes

During 2006, our effective tax rate was 12% compared to 37% in 2005. This change in the effective rate was the result of a $28 million increase in the valuation allowance related to certain deferred tax assets during 2006. The styrene impairment discussed above resulted in the reversal of $45 million in deferred tax liabilities. As of December 31, 2006, we had an available U.S. federal income tax net operating loss carryforward (NOL) of approximately $85 million (representing a deferred tax asset of $30 million), which expires during the years 2023 through 2026. Deferred tax assets are regularly assessed for recoverability based on both historical and anticipated earnings levels, and a valuation allowance is recorded when it is more likely than not that these amounts will not be recovered. As a result of our analysis, we have concluded that an additional valuation allowance is needed against our deferred tax assets in the amount of $28 million, which brings our total valuation allowance to $30 million and results in an overall net deferred tax asset balance of $4 million. We have also recorded a $4 million liability relating to certain tax contingencies that we have identified.

Loss from discontinued operations, net of tax

We recorded a net loss from discontinued operations of $1 million in 2006 compared to a loss of $11 million in 2005. The $1 million loss in 2006 represents closure costs related to our acrylonitrile business, partially offset by asset sales related to that business. We expect to incur approximately $1 million of costs during the first half of 2007 to complete the dismantling of this facility. The loss of $11 million in 2005 included costs of $9 million related to our exit from the acrylonitrile and related derivatives businesses.

Comparison of 2005 to 2004

Revenues and Loss from continuing operations

Our revenues were $642 million in 2005, a decrease of 2% from the $655 million in revenues we recorded in 2004. This decrease in revenues resulted primarily from a reduction in styrene revenues due to a change in customer mix and lost volumes of styrene following the fire that occurred in our styrene unit in September 2005. As a result of this curtailed ability to produce styrene, we sold a larger percentage of our overall styrene sales under conversion arrangements during 2005. We recorded a net loss from continuing operations of $19 million for 2005, compared to a net loss of $40 million recorded in 2004. This difference between these two years was significantly influenced by the $48 million impairment to goodwill we recorded in 2004 and a reduction in gross profit in 2005 due to the impact of Hurricane Rita and the fire in our styrene unit.

Revenues from acetic acid and plasticizers were $128 million in 2005, a slight increase from the $126 million in revenues we recorded in 2004. This slight increase in revenues resulted from a 7% increase in acetic acid revenues offset by a 6% decrease in plasticizers revenues. We achieved record monthly production rates in our acetic acid business during 2005.

Revenues from our styrene operations were $514 million in 2005, a decrease of 3% from the $530 million in revenues we recorded in 2004. Direct sales prices for styrene increased 6% from those realized during 2004. Spot prices for styrene, a component of our direct sales prices, ranged from $0.44 to $0.62 per pound during 2005, compared to $0.37 to $0.63 per pound during 2004. Our total sales volumes for styrene in 2005 were 1% lower than in 2004. During 2005, prices for benzene, one of the primary raw materials required for styrene production, increased 2% over the prices we paid for benzene in 2004, and prices for ethylene, the other primary raw material required for styrene production, were 35% higher than the prices we paid for ethylene in 2004. Average costs for natural gas, another major component in the cost of manufacturing styrene, increased 23% during 2005 compared to average natural gas costs during 2004. Margins on our styrene sales in 2005 decreased from those realized in 2004, primarily as a result of higher raw materials costs and the impact of Hurricane Rita and the fire in our styrene unit.

Selling, general & administrative expenses

Our selling, general and administrative expenses were $8 million in 2005 compared to $11 million in 2004. This reduction was primarily due to a $2 million reduction in our allowance for doubtful accounts resulting from a decrease in total accounts receivable, as well as a decrease in balances with customers having greater credit risk.

Organizational efficiency project

During the last half of 2004, we developed an organizational efficiency project involving the design, development and implementation of uniform and standardized systems, processes and policies to improve our production, maintenance and process efficiencies, and our logistics materials management and procurement functions. During 2005, we reduced our fixed costs by more than $20 million per year, representing a 15% reduction in our annual fixed costs. Approximately 10% to 15% of these cost savings accrue to the benefit of some of our customers under the cost reimbursement provisions of our production agreements.

Provision (benefit) for income taxes

During 2005, our effective tax rate was 37% compared to 16% in 2004. This difference in the effective rate was a result of the $48.5 million impairment of goodwill recorded during 2004, which was a non-tax deductible charge.

Loss from discontinued operations, net of tax

We recorded a net loss from discontinued operations of $11 million in 2005 compared to a loss of $23 million in 2004. The loss of $11 million in 2005 included costs of $9 million related to our exit from the acrylonitrile and related derivatives businesses. These costs included accruals for contractual obligations due in 2006 and asset impairments. The loss of $23 million in 2004 included a pre-tax impairment charge of our long-lived acrylonitrile assets of $22 million.

Liquidity and Capital Resources

On December 19, 2002, we issued $94.3 million in original principal amount of our Secured Notes. Our Secured Notes are senior secured obligations and rank equally in right of payment with all of our other existing and future senior indebtedness, and senior in right of payment to all of our existing and future subordinated indebtedness. Our Secured Notes are guaranteed by Sterling Chemicals Energy, Inc. (Sterling Energy), our only wholly owned subsidiary. Sterling Energy s guaranty ranks equally in right of payment with all of its existing and future senior indebtedness, and senior in right of payment to all of its existing and future subordinated indebtedness. Our Secured Notes and Sterling Energy s guaranty are secured by a first priority lien on all of our production facilities and related assets.

Our Secured Notes bear interest at an annual rate of 10%, payable semi-annually on June 15 and December 15 of each year. Until December 19, 2004, we were permitted under certain circumstances to pay interest on our Secured Notes through the issuance of additional Secured Notes rather than the payment of cash at an interest rate of 13 3/8% per annum. In December 2003, we made an interest payment on our Secured Notes at the higher rate through the issuance of $6.3 million in original principal amount of additional Secured Notes, increasing the aggregate principal amount of outstanding Secured Notes to $100.6 million. We have made all other interest payments on our Secured Notes in cash. We may redeem our Secured Notes at any time at a redemption price of 100% of the outstanding principal amount thereof plus accrued and unpaid interest, subject to compliance with the terms of our revolving credit facility. In addition, in the event of a specified change of control or the sale of our facility in Texas City, Texas, we are required to offer to repurchase our Secured Notes at 101% of the outstanding principal amount thereof plus accrued and unpaid interest. Under certain circumstances, we are also required to use the proceeds of other asset sales to repurchase those Secured Notes tendered by the holders at a price equal to 100% of the outstanding principal amount thereof plus accrued and unpaid interest.

The indenture governing our Secured Notes contains numerous covenants and conditions, including, but not limited to, restrictions on our ability to incur indebtedness, create liens, sell assets, make investments, make capital expenditures, engage in mergers and acquisitions and pay dividends. The indenture also includes various circumstances and conditions that would, upon their occurrence and subject in certain cases to notice and grace periods, create an event of default thereunder. However, the indenture does not require us to satisfy any financial ratios or maintenance tests.

On March 1, 2007, we commenced an offer to repurchase all of our outstanding Secured Notes (our tender offer).

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Concurrently with our tender offer, we solicited consents from the holders of our Secured Notes to, among other things, eliminate certain covenants contained in the indenture governing our Secured Notes. The consent solicitation expired at 5:00 p.m., New York Time, on March 14, 2007, at which time we received consents from the requisite principal amount of Secured Notes to amend our indenture. The supplemental indenture we entered into to effect these amendments will only be effective if and when we consummate our tender offer for the Secured Notes.

Our tender offer is scheduled to expire at 12:00 midnight, New York City time, on March 28, 2007, unless extended or earlier terminated. The total consideration payable in connection with our tender offer and the consent solicitation for each $1,000 principal amount of our existing notes will be $1,002.50, plus accrued and unpaid interest to, but not including, the date of payment.

We expect to refinance our Secured Notes with an offering of up to $125 million of new senior secured notes (New Notes). In connection with our proposed offering of New Notes, we have also received a firm commitment letter from a national investment banking firm with respect to an alternate long-term debt financing. In the event our offering of the New Notes is not consummated, we intend to issue $111 million in debt financing pursuant to this commitment letter in order to refinance our Secured Notes.

We will use the net proceeds of the New Notes (or the debt financing effected pursuant to the commitment referenced above) to fund amounts payable in connection with the tender offer, the consent solicitation and to redeem any remaining Secured Notes not repurchased pursuant thereto.

On December 19, 2002, we also established our revolving credit facility, which provides up to $100 million in revolving credit loans, subject to borrowing base limitations. Our revolving credit facility has an initial term ending on September 19, 2007. Under our revolving credit facility, we and Sterling Energy are co-borrowers and are jointly and severally liable for any indebtedness thereunder. Our revolving credit facility is secured by first priority liens on all of our accounts receivable, inventory and other specified assets, as well as all of the issued and outstanding capital stock of Sterling Energy.

Borrowings under our revolving credit facility bear interest, at our option, at an annual rate of either the Alternate Base Rate plus 0.75% or the LIBO Rate (as defined in our revolving credit facility) plus 2.75%. The Alternate Base Rate is equal to the greater of the Base Rate as announced from time to time by JPMorgan Chase Bank in New York, New York, or 0.50% per annum above the latest Federal Funds Rate (as defined in our revolving credit facility). The average interest rate for borrowings under our revolving credit facility for the year ended December 31, 2006 was 8.94%. Under our revolving credit facility, we are also required to pay an aggregate commitment fee of 0.50% per year (payable monthly) on any unused portion. Available credit is subject to a monthly borrowing base of 85% of eligible accounts receivable plus the lesser of $50 million and 65% of eligible inventory. In addition, the borrowing base for our revolving credit facility must exceed outstanding borrowings thereunder by $8 million at all times. As of December 31, 2006, total credit available under our revolving credit facility was limited to $72 million due to these borrowing base limitations. As of December 31, 2006, there were no loans outstanding under our revolving credit facility, and we had $3 million in letters of credit outstanding.

Our revolving credit facility contains numerous covenants and conditions, including, but not limited to, restrictions on our ability to incur indebtedness, create liens, sell assets, make investments, make capital expenditures, engage in mergers and acquisitions and pay dividends. Our revolving credit facility also contains a covenant that requires us to earn a specified amount of earnings before interest, income taxes, depreciation and amortization (as defined in our revolving credit facility) on a monthly basis if, for 15 consecutive days, unused availability under our revolving credit facility plus cash on hand is less than $20 million. Our revolving credit facility includes various circumstances and conditions that would, upon their occurrence and subject in certain cases to notice and grace periods, create an event of default thereunder. In addition, our revolving credit facility includes both a subjective acceleration clause and a lock-box arrangement. Based on this, any balances outstanding under our revolving credit facility are classified as a current portion of long-term debt. We are currently negotiating to amend our revolving credit facility to extend the term for five years and to make certain other changes to the borrowing base calculation and interest rates. We expect this amendment to be effective by March 31, 2007.

Our liquidity (i.e., cash and cash equivalents plus total credit available under our revolving credit facility) was $90 million as of December 31, 2006, an increase of $4 million compared to our liquidity as of December 31, 2005.

The stated term of our revolving credit facility ends on September 19, 2007 and our Secured Notes become due on December 19, 2007. As mentioned above, we have started the process of refinancing the indebtedness under our Secured Notes and amending our revolving credit facility prior to their stated maturities. Subject to the successful refinancing of our Secured Notes and amendment of our revolving credit facility, we believe that our cash on hand,

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together with the credit available under our amended revolving credit facility, is sufficient to meet our short-term and long-term liquidity needs, although our liquidity may not be adequate during any particular period.

Working Capital

Our working capital, excluding assets and liabilities from discontinued operations, was $90 million as of December 31, 2006, an increase of $12 million from December 31, 2005. This increase in working capital resulted primarily from an increase in accounts receivable and inventories.

Cash Flow

Net cash used in our operations was $14 million in 2006, compared to net cash provided by our operations of $68 million in 2005. This reduction in net cash flow in 2006 was primarily driven by an increase in accounts receivable and inventories.

Net cash flow used in our investing activities was $7 million in 2006 and $10 million in 2005. Cash flows from investing activities in 2006 included insurance proceeds of $2 million and proceeds from the sale of fixed assets of $3 million.

There were no net repayments under our revolving credit facility during 2006 compared to $18 million of net repayments in 2005.

Capital Expenditures

Our capital expenditures were $12 million in 2006, $9 million in 2005 and $15 million in 2004. Capital expenditures are expected to be approximately $15 million in 2007. These capital expenditures will primarily be for routine safety, environmental and replacement capital.

Our capital expenditures for environmentally related prevention, containment and process improvements were $2 million in both 2006 and 2005 and we anticipate spending approximately $2 million on these types of expenditures during 2007.

Contractual Cash Obligations

The following table summarizes our significant contractual obligations at December 31, 2006, and the effect such obligations are expected to have on our liquidity and cash flows in future periods:

	Less than 1 year[(1)]	1-3 years	4-5 years	More than 5 years	Total
	(Dollars in Thousands)				
Secured Notes	$100,579	$	$	$	$100,579
Interest payments on debt	10,170				10,170
Operating leases	293	879	586	220	1,978
Purchase obligations [(2)]	72,000	117,000	65,000	120,000	374,000
Pension and other postretirement benefits	9,675	16,717	7,230	31,113	64,735
Contractual obligations of discontinued operations	217				217
Total	$192,934	$134,596	$72,816	$151,333	$551,679

(1) Payment obligations under our revolving credit facility are not presented because there were no

outstanding borrowings as of December 31, 2006, and interest payments fluctuate depending on the interest rate and outstanding balance under our revolving credit facility at any point in time. As discussed above, we have started the process of refinancing the indebtedness under our Secured Notes and our revolving credit facility prior to their stated maturities.

(2) For the purposes of this table, we have considered contractual obligations for the purchase of goods or services as agreements involving more than $1 million that are enforceable and legally binding and that specify all significant terms, including: fixed or minimum quantities to be purchased, fixed, minimum

or variable price
provisions and
the

approximate timing of the transaction. Most of the purchase obligations identified include variable pricing provisions. We have estimated the future prices of these items, utilizing forward curves where available. The pricing estimated for use in this table is subject to market risk.

Critical Accounting Policies, Use of Estimates and Assumptions

A summary of our significant accounting policies is included in Note 1 of the Notes to Consolidated Financial Statements included in Item 8, Part II of this Form 10-K. We believe that the consistent application of these policies enables us to provide readers of our financial statements with useful and reliable information about our operating results and financial condition. The following accounting policies are the ones we believe are the most important to the portrayal of our financial condition and results and require our most difficult, subjective or complex judgments.

Revenue Recognition

We generally recognize revenue from sales in the open market, raw materials conversion agreements and long-term supply contracts at the time the products are shipped and title passes. One of our contractual arrangements includes a profit sharing component, and we estimate and accrue our expected revenues from this profit sharing arrangement on a monthly basis. Shipping and handling costs associated with the delivery of our products to customers are included in cost of goods sold.

Inventories

Inventories are carried at the lower-of-cost-or-market value. Cost is primarily determined on a first-in, first-out basis, except for stores and supplies, which are valued at average cost. The comparison of cost to market value involves estimation of the market value of our products. For the years ended December 31, 2006, 2005 and 2004, this comparison led to a lower-of-cost-or-market adjustment of zero, $3 million and $16 million, respectively. We enter into agreements with other companies to exchange chemical inventories in order to minimize working capital requirements and to facilitate distribution logistics. Balances related to quantities due to or payable by us in connection with these exchange agreements are included in inventory.

Long-Lived Assets

We assess our long-lived assets for impairment whenever facts and circumstances indicate that the carrying amount may not be fully recoverable. To analyze recoverability, we project undiscounted net future cash flows over the remaining book life of these assets. If these projected cash flows from these assets are less than the carrying amount of these assets, an impairment would be recognized. Any impairment loss would be measured based upon the difference between the carrying amount and the fair value of the relevant assets. For these impairment analyses, recoverability is determined by comparing the estimated fair value of these assets, utilizing the present value of expected net cash flows, to the carrying value of these assets. In determining the present value of expected net cash flows, we estimate

future net cash flows from these assets and the timing of those cash flows and then apply a discount rate to reflect the time value of money and the inherent uncertainty of those future cash flows. The discount rate we use is based on our estimated cost of capital. The assumptions we use in estimating future cash flows are consistent with our internal planning. As mentioned above, during 2006, we recorded an impairment charge of $128 million related to our long-lived styrene assets.

Income Taxes

Deferred income taxes are provided for revenue and expenses which are recognized in different periods for income tax and financial statement purposes. Deferred tax assets are regularly assessed for recoverability based on both historical and anticipated earnings levels, and a valuation allowance is recorded when it is more likely than not that these amounts will not be recovered. As of December 31, 2006, we had an available U.S. federal income tax net NOL of approximately $85 million (representing a deferred tax asset of $30 million), which expires during the years 2023 through 2026. As a result of our analysis, we have concluded that an additional valuation allowance is needed against our deferred tax assets in the amount of $28 million, which brings our total valuation allowance to $30 million and results in an overall net deferred tax asset balance of $4 million. We have also recorded a $4 million liability relating to certain tax contingencies that we have identified.

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Employee Benefit Plans

We sponsor domestic defined benefit pension and other postretirement plans. Major assumptions used in the accounting for these employee benefit plans include the discount rate, expected return on plan assets and health care cost increase projections. Assumptions are determined based on our historical data and appropriate market indicators, and are evaluated each year as of the plans measurement dates. A change in any of these assumptions would have an effect on net periodic pension and postretirement benefit costs reported in our financial statements. As mentioned below, in accordance with SFAS No. 158, Employers Accounting for Defined Benefit Pension and Other Postretirement Plans (SFAS No. 158), we have recognized the funded status of our defined benefit postretirement plans on our balance sheet and have provided the required disclosures as of our fiscal year-ended December 31, 2006. We have also measured the assets and benefit obligations of our defined benefit postretirement plans as of the date of our fiscal year-end statement of financial position. The effect of the adoption of SFAS 158 was a reduction in our liabilities of $10 million and an increase in stockholders equity, net of tax, of $7 million.

Plant Turnaround Costs

As a part of normal recurring operations, each of our manufacturing units is completely shut down from time to time, for a period typically lasting two to four weeks, to replace catalysts and perform major maintenance work required to sustain long-term production. These periods are commonly referred to as turnarounds or shutdowns. While actual timing is subject to a number of variables, turnarounds of our styrene unit typically occur every two to three years. We currently expense the costs of turnarounds as the associated expenses are incurred. Prior to our adoption of fresh-start accounting, we had accrued these costs over the expected period between turnarounds. As expenses for turnarounds can be significant, the impact of expensing turnaround costs as they are incurred can be material for financial reporting periods during which the turnarounds actually occur. Turnaround costs expensed during 2006, 2005 and 2004 were $10 million, $4 million and $12 million, respectively.

New Accounting Standards

In July 2006, the FASB issued FASB Interpretation No. 48, Accounting for Uncertainty in Income Taxes an interpretation of FASB Statement No. 109, (FIN 48) to clarify the accounting for uncertain tax positions accounted for in accordance with FASB Statement No. 109, Accounting for Income Taxes. This interpretation prescribes a two-step approach for recognizing and measuring tax benefits and requires explicit disclosure of any uncertain tax position. FIN 48 is effective for us on January 1, 2007. We do not expect the adoption of FIN 48 to have a material impact on our consolidated financial statements.

Item 7A. *Quantitative and Qualitative Disclosures about Market Risk*

The table below provides information about our market sensitive financial instruments and constitutes a forward-looking statement.

Expected Maturity Dates	**2007**	**2008**	**2009**	**2010**	**2011**	**Thereafter**	**Total**	**Fair Value December 31, 2006**
				(Dollars in Thousands)				
Secured Notes	$100,579						$100,579	$96,125

Our Secured Notes bear interest at an annual rate of 10%, payable semi-annually on June 15 and December 15 of each year. The fair value of our Secured Notes is based on their quoted price.

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Item 8. ***Financial Statements and Supplementary Data***

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Sterling Chemicals, Inc.

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STERLING CHEMICALS, INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF OPERATIONS

	Year ended December 31,		
	2006	**2005**	**2004**
	(Dollars in Thousands, Except Share Data)		
Revenues	$ 667,544	$ 641,886	$ 655,353
Cost of goods sold	654,718	653,134	633,009
Gross profit (loss)	12,826	(11,248)	22,344
Selling, general and administrative expenses	9,968	7,811	11,413
Impairment of long-lived assets	127,653		48,463
Gain on pension curtailment			(12,944)
Gain on sale of methanol plant			(2,396)
Other expense (income)	(15,724)		
Interest and debt related expenses, net of interest income	10,079	10,090	10,427
Loss from continuing operations before income tax	(119,150)	(29,149)	(32,619)
Provision (benefit) for income taxes	(14,488)	(10,641)	7,262
Loss from continuing operations	(104,662)	(18,508)	(39,881)
Loss from discontinued operations, net of tax	(997)	(11,060)	(22,763)
Net loss	(105,659)	(29,568)	(62,644)
Preferred stock dividends	8,205	7,014	5,994
Net loss attributable to common stockholders	$ (113,864)	$ (36,582)	$ (68,638)
Loss per share of common stock, basic and diluted:			
Loss from continuing operations	$ (39.91)	$ (9.03)	$ (16.24)
Loss from discontinued operations	(0.35)	(3.91)	(8.06)
Net loss per share, basic and diluted	$ (40.26)	$ (12.94)	$ (24.30)
Weighted average shares outstanding:			
Basic and diluted	2,828,460	2,827,795	2,825,000

The accompanying notes are an integral part of the consolidated financial statements.

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STERLING CHEMICALS, INC. AND SUBSIDIARIES
CONSOLIDATED BALANCE SHEETS

	December 31, 2006	December 31, 2005
	(Dollars in Thousands)	
ASSETS		
Current assets:		
Cash and cash equivalents	$ 20,690	$ 42,197
Accounts receivable, net of allowance of $1,987 and $953, respectively	63,289	57,261
Inventories, net	62,078	39,094
Prepaid expenses and other current assets	3,215	4,888
Deferred tax asset	3,044	2,802
Assets of discontinued operations	20	1,791
Total current assets	152,336	148,033
Property, plant and equipment, net	83,833	230,018
Other assets, net	9,654	8,543
Total assets	$ 245,823	$ 386,594
LIABILITIES AND STOCKHOLDERS EQUITY (DEFICIENCY IN ASSETS)		
Current liabilities:		
Accounts payable	$ 39,123	$ 43,912
Accrued liabilities	22,872	23,690
Current portion of long-term debt		
Liabilities of discontinued operations	217	3,826
Total current liabilities	62,212	71,428
Long-term debt	100,579	100,579
Deferred income tax liability		8,196
Deferred credits and other liabilities	49,291	77,804
Redeemable preferred stock	56,507	48,302
Commitments and contingencies (Note 9)		
Stockholders equity:		
Common stock, $.01 par value	28	28
Additional paid-in capital	184,500	192,551
Accumulated deficit	(213,614)	(107,955)
Accumulated other comprehensive income (loss)	6,320	(4,339)
Total stockholders equity (deficiency in assets)	(22,766)	80,285
Total liabilities and stockholders equity (deficiency in assets)	$ 245,823	$ 386,594

The accompanying notes are an integral part of the consolidated financial statements.

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STERLING CHEMICALS, INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF
CHANGES IN STOCKHOLDERS EQUITY (DEFICIENCY IN ASSETS)

	Common Stock		Additional Paid-In	Accumulated	Accumulated Other Comprehensive Income	
	Shares	Amount	Capital	Deficit	(Loss)	Total
			(Amounts in Thousands)			
Balance, December 31, 2003	2,825	$ 28	$ 205,402	$ (15,743)	$ (251)	$ 189,436
Comprehensive loss:						
Net loss				(62,644)		
Other comprehensive loss:						
Pension adjustment					(715)	
Comprehensive loss						(63,359)
Preferred stock dividends			(5,994)			(5,994)
Balance, December 31, 2004	2,825	$ 28	$ 199,408	$ (78,387)	$ (966)	$ 120,083
Comprehensive loss:						
Net loss				(29,568)		
Other comprehensive loss:						
Pension adjustment					(3,373)	
Comprehensive loss						(32,941)
Preferred stock dividends			(7,014)			(7,014)
Exercised stock options	3		157			157
Balance, December 31, 2005	2,828	$ 28	$ 192,551	$ (107,955)	$ (4,339)	$ 80,285
Comprehensive loss:						
Net loss				(105,659)		
Other comprehensive loss:						
Pension adjustment					3,903	
Comprehensive loss						(101,756)
SFAS 158 adoption					6,756	6,756
Preferred stock dividends			(8,205)			(8,205)
Stock-based compensation			154			154
Balance, December 31, 2006	2,828	$ 28	$ 184,500	$ (213,614)	$ 6,320	$ (22,766)

The accompanying notes are an integral part of the consolidated financial statements.

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STERLING CHEMICALS, INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF CASH FLOWS

	Year ended December 31,		
	2006	**2005**	**2004**
	(Dollars in Thousands)		
Cash flows from operating activities:			
Net loss	$(105,659)	$(29,568)	$(62,644)
Adjustments to reconcile net loss to net cash provided by (used in) operating activities:			
Depreciation and amortization	30,476	33,342	28,693
Interest amortization	400	400	398
Impairment of long-lived assets	127,653		70,498
Gain on pension curtailment			(12,944)
Lower-of-cost-or-market adjustment		2,738	16,407
Deferred tax benefit	(8,438)	(18,905)	(16,529)
Gain on disposal of property, plant and equipment	(4,917)		(2,396)
Other	154	156	1
Change in assets/liabilities:			
Accounts receivable	(5,085)	54,850	(25,509)
Inventories	(22,608)	45,772	(42,804)
Prepaid expenses	1,673	(690)	2,232
Other assets	(2,105)	(1,003)	(3,650)
Accounts payable	(4,140)	(23,348)	2,427
Accrued liabilities	(3,758)	4,396	(1,879)
Other liabilities	(17,854)	(33)	286
Net cash provided by (used in) operating activities	(14,208)	68,107	(47,413)
Cash flows from investing activities:			
Capital expenditures	(11,547)	(9,460)	(14,771)
Insurance proceeds relating to property, plant and equipment	1,960		
Cash used for dismantling	(669)	(667)	
Net proceeds from the sale of fixed assets assets	2,957		4,017
Net cash used in investing activities	(7,299)	(10,127)	(10,754)
Net cash provided by (used in) financing activities net borrowings (repayments) under the revolving credit facility		(17,684)	17,684
Net increase (decrease) in cash	(21,507)	40,296	(40,483)
Cash and cash equivalents beginning of period	42,197	1,901	42,384
Cash and cash equivalents end of year	$ 20,690	$ 42,197	$ 1,901
Supplement disclosures of cash flow information:			
Interest paid, net of interest income received	$ 10,508	$ 10,726	$ 10,957
Cash paid for income taxes	60	59	50

The accompanying notes are an integral part of the consolidated financial statements.

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STERLING CHEMICALS, INC. AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

1. BASIS OF PRESENTATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Unless otherwise indicated, references to we, us, our and ours refer collectively to Sterling Chemicals, Inc. and i wholly-owned subsidiaries. We own or operate facilities at our petrochemicals complex located in Texas City, Texas, approximately 45 miles south of Houston, on a 290-acre site on Galveston Bay near many other chemical manufacturing complexes and refineries. Currently, we produce acetic acid, styrene and plasticizers. We own all of the real property which comprises our Texas City facility and we own the acetic acid, styrene and plasticizers manufacturing units located at the site. Our Texas City site offers approximately 135 acres for future expansion by us or by other companies that could benefit from our existing infrastructure and facilities, and includes a greenbelt around the northern edge of the plant site. We also lease a portion of our Texas City site to Praxair Hydrogen Supply, Inc. (Praxair), who constructed a partial oxidation unit on that land, and lease a portion of our Texas City site to S&L Cogeneration Company, a 50/50 joint venture between us and Praxair Energy Resources, Inc., who constructed a cogeneration facility on that land. We generally sell our petrochemicals products to customers for use in the manufacture of other chemicals and products, which in turn are used in the production of a wide array of consumer goods and industrial products. We operate in one segment, petrochemicals.

Principles of Consolidation

The consolidated financial statements include the accounts of our wholly-owned subsidiary, with all significant intercompany accounts and transactions having been eliminated. Our 50% equity investment in a cogeneration joint venture is not material to our financial position or results of operations.

Cash and Cash Equivalents

We consider all investments having an initial maturity of three months or less to be cash equivalents.

Allowance for Doubtful Accounts

Accounts receivable is presented net of allowance for doubtful accounts. We regularly review our accounts receivable balances and, based on estimated collectibility, adjust the allowance account accordingly. As of December 31, 2006 and 2005, the allowance for doubtful accounts was $2 million and $1 million, respectively. Bad debt expense (benefit) for 2006, 2005 and 2004, was $1 million, ($2 million) and $0.4 million, respectively.

Inventories

Inventories are stated at the lower-of-cost-or-market. For the years ended December 31, 2006, 2005 and 2004, a lower-of-cost-or-market adjustment was recorded of zero, $3 million and $16 million, respectively. Cost is primarily determined on a first-in, first-out basis, except for stores and supplies, which are valued at average cost. We enter into agreements with other companies to exchange chemical inventories in order to minimize working capital requirements and to facilitate distribution logistics. Balances related to quantities due to or payable by us are included in inventory.

Property, Plant and Equipment

Property, plant and equipment are recorded at cost. Major renewals and improvements, which extend the useful lives of equipment, are capitalized. Disposals are removed at carrying cost less accumulated depreciation with any resulting gain or loss reflected in operations. Depreciation is provided using the straight-line method over estimated useful lives ranging from five to 25 years, with the predominant life of plant and equipment being 15 years. We capitalize interest costs, which are incurred as part of the cost of constructing major facilities and equipment. The amount of interest capitalized for 2006, 2005 and 2004 was $0.8 million, $1.0 million and $0.9 million, respectively.

Plant Turnaround Costs

As a part of normal recurring operations, each of our manufacturing units is completely shut down from time to time, for a period typically lasting two to four weeks, to replace catalysts and perform major maintenance work required to sustain long-term production. These periods are commonly referred to as turnarounds or shutdowns. While

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STERLING CHEMICALS, INC. AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

actual timing is subject to a number of variables, turnarounds of our styrene unit typically occur every two to three years. Costs of turnarounds are expensed as incurred. As expenses for turnarounds can be significant, the impact of expensing the costs of turnarounds can be material for financial reporting periods during which the turnarounds actually occur. Turnaround costs expensed during 2006, 2005 and 2004 were $10 million, $4 million and $12 million, respectively.

Long-Lived Assets

We assess our long-lived assets for impairment whenever facts and circumstances indicate that the carrying amount may not be fully recoverable. To analyze recoverability, we project undiscounted net future cash flows over the remaining book life of these assets. If these projected cash flows from these assets are less than the carrying amount of these assets, an impairment would be recognized. Any impairment loss would be measured based upon the difference between the carrying amount and the fair value of the relevant assets. For these impairment analyses, recoverability is determined by comparing the estimated fair value of these assets, utilizing the present value of expected net cash flows, to the carrying value of these assets. In determining the present value of expected net cash flows, we estimate future net cash flows from these assets and the timing of those cash flows and then apply a discount rate to reflect the time value of money and the inherent uncertainty of those future cash flows. The discount rate we use is based on our estimated cost of capital. The assumptions we use in estimating future cash flows are consistent with our internal planning. During 2006, we recorded a pre-tax impairment charge of approximately $128 million relating to our long-lived styrene assets.

Debt Issue Costs

Debt issue costs relating to long-term debt are amortized over the term of the related debt instrument using the straight-line method, which is materially consistent with the effective interest method, and are included in other assets. Debt issue cost amortization, which is included in interest and debt-related expenses, was $0.4 million for each of the years ended December 31, 2006, 2005 and 2004.

Income Taxes

Deferred income taxes are provided for revenues and expenses which are recognized in different periods for income tax and financial statement purposes. Deferred tax assets are regularly assessed for recoverability based on both historical and anticipated earnings levels, and a valuation allowance is recorded when it is more likely than not that these amounts will not be recovered.

Environmental Costs

Environmental costs are expensed as incurred, unless the expenditures extend the economic useful life of the related assets. Costs that extend the economic life of assets are capitalized and depreciated over the remaining book life of those assets. Liabilities are recorded when environmental assessments or remedial efforts are probable and the cost can be reasonably estimated.

Revenue Recognition

We generate revenues through sales in the open market, raw materials conversion agreements and long-term supply contracts. In addition, we have entered into profit sharing arrangements with respect to some of our petrochemicals products. We recognize revenue from sales in the open market, raw materials conversion agreements and long-term supply contracts when the products are shipped and title passes. Revenues from profit sharing arrangements are estimated and accrued monthly. Deferred credits are amortized over the life of the contracts which gave rise to them.

Earnings (Loss) Per Share

Basic earnings per share (EPS) is computed using the weighted-average number of shares outstanding during the year. Diluted EPS includes common stock equivalents, which are dilutive to earnings per share. For the years ending December 31, 2006, 2005 and 2004, we had no dilutive securities outstanding due to all common stock equivalents having an anti-dilutive effect during these periods.

STERLING CHEMICALS, INC. AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

Disclosures about Fair Value of Financial Instruments

In preparing disclosures about the fair value of financial instruments, we have assumed that the carrying amount approximates fair value for cash and cash equivalents, accounts receivable, accounts payable and certain accrued liabilities due to the short maturities of these instruments. The fair values of long-term debt instruments are estimated based upon quoted market values (if applicable) or on the current interest rates available to us for debt with similar terms and remaining maturities.

Accounting Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reported periods. Significant estimates include impairment considerations, allowance for doubtful accounts, inventory valuation, revenue recognition related to profit sharing accruals, environmental and litigation reserves and provision for income taxes.

2. STOCK-BASED COMPENSATION PLAN

On December 19, 2002, we adopted our 2002 Stock Plan and reserved 379,747 shares of our common stock for issuance under the plan (subject to adjustment). Under our 2002 Stock Plan, officers and key employees, as designated by our Board of Directors, may be issued stock options, stock awards, stock appreciation rights or stock units. There are currently options to purchase a total of 278,500 shares of our common stock outstanding under our 2002 Stock Plan, all at an exercise price of $31.60, and an additional 85,414 shares of common stock available for issuance under our 2002 Stock Plan.

On January 1, 2006, we adopted Statement of Financial Accounting Standards (SFAS) No. 123-Revised 2004, Share-Based Payments (SFAS No. 123(R)), using the modified prospective method. SFAS No. 123(R) is a revision of SFAS No. 123, Accounting for Stock-Based Compensation (SFAS No. 123), and superseded Accounting Principals Board No. 25, Accounting for Stock Issued to Employees (APB No. 25). Under SFAS No. 123(R), the cost of employee services received in exchange for a stock-based award is determined based on the grant-date fair value (with limited exceptions). That cost is then recognized over the period during which the employee is required to provide services in exchange for the award (usually the vesting period).

On January 1, 2006, using the modified prospective method under SFAS No. 123(R), we began recognizing expense on any unvested awards under our 2002 Stock Plan that were granted prior to that time. Any awards granted under our 2002 Stock Plan after December 31, 2005 will be expensed over the vesting period of the award. Stock based compensation expense was $153,809 for the year ended December 31, 2006.

Prior to January 1, 2006, we had adopted the disclosure-only provisions of SFAS No. 123 and accounted for substantially all of our stock-based compensation using the intrinsic value method prescribed in APB No. 25. Under APB No. 25, no compensation expense was recognized for any of our stock option grants because all of the stock options issued under our 2002 Stock Plan were granted with exercise prices at estimated fair value at the time of grant.

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STERLING CHEMICALS, INC. AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

A summary of our stock option activity for the years ended December 31, 2006, 2005 and 2004 is presented below:

	December 31, 2006		December 31, 2005		December 31, 2004	
	Shares	Weighted-average exercise price	Shares	Weighted-average exercise price	Shares	Weighted-average exercise price
Outstanding at beginning of year	278,500	$ 31.60	294,334	$ 31.60	326,000	$ 31.60
Granted					27,500	31.60
Exercised			(15,834)	31.60	(59,166)	31.60
Outstanding at end of year	278,500	$ 31.60	278,500	$ 31.60	294,334	$ 31.60
Options exercisable at end of year	269,333		176,500		99,500	

As noted above, no options were granted in 2006 or 2005. The fair value of the grants in 2004 was estimated on the date of grant using the Black-Scholes option pricing model with the following weighted-average assumptions:

	2004
Expected life (years)	10.0
Expected volatility	42.0%
Expected dividend yield	
Risk-free interest rate	3.85%
Weighted-average fair value of options granted during the year	$12.95

The following table illustrates the effect on our net loss and loss per share attributable to common stockholders if compensation costs for stock options had been recorded pursuant to SFAS No. 123(R), for the years prior to adoption.

	For the Year Ended December 31, 2005	For the Year Ended December 31, 2004
	(Dollars in Thousands, Except Share Data)	
Net loss attributable to common stockholders, as reported	$ (36,582)	$ (68,638)
Add: Stock-based employee compensation expense included in reported net loss, net of related tax effects	157	
Deduct: Total stock-based employee compensation expense determined under fair value based method for all awards, net of related tax effects	(606)	(1,147)
Pro forma net loss	$ (37,031)	$ (69,785)
Loss per share attributable to common stockholders:		
As reported	$ (12.94)	$ (24.30)

Pro forma	(13.10)	(24.70)

3. DISCONTINUED OPERATIONS

On September 16, 2005, we announced that we were exiting the acrylonitrile business and related derivative operations, which included sodium cyanide and disodium iminodiacetic acid (DSIDA) production, and had been shut down since February 2005. As a result of the exit from these businesses, we shut down the production facilities and are currently in the process of dismantling these facilities. Our decision was based on a history of operating losses incurred

STERLING CHEMICALS, INC. AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

by our acrylonitrile and derivatives businesses, and was made after a full review and analysis of our strategic alternatives.

In accordance with SFAS No. 144, Accounting for the Impairment and Disposal of Long Lived Assets, we have reported the operating results of these businesses as discontinued operations in our consolidated financial statements.

The carrying amounts of the major classes of assets and liabilities related to discontinued operations as of December 31, 2006 and 2005 were as follows:

	Year ended December 31,	
	2006	**2005**
	(Dollars in Thousands)	
Assets of discontinued operations:		
Accounts receivable, net	$ 20	$ 963
Inventories		376
Other assets		452
Total	$ 20	$ 1,791
Liabilities of discontinued operations:		
Accrued liabilities	$ 217	$ 3,826

Revenues and pre-tax losses from discontinued operations for the years ended December 31, 2006, 2005 and 2004 are presented below:

		Year ended December 31,	
	2006	**2005**	**2004**
		(Dollars in Thousands)	
Revenues	$ 258	$43,374	$196,309
Loss before income taxes	1,135	17,420	42,025

Current severance and contractual obligations are detailed below:

	Accrued in 2005	**Cash Payments**	**Accrued as of December 31, 2005**	**Accrued in 2006**	**Cash payments**	**Accrued as of December 31, 2006**
Severance accrual	$ 568	$ (91)	$ 477	$ 386	$ (646)	$ 217
DSIDA contractual obligation	2,853		2,853	147	(3,000)	
DSIDA dismantling costs	496		496	62	(558)	
Totals	$3,917	$ (91)	$ 3,826	$ 595	$(4,204)	$ 217

Prior to our decision to exit the acrylonitrile and derivative businesses, on May 31, 2005, we entered into a Separation Agreement with O&D USA LLC (d/b/a Innovene Chemicals), ANEXCO, LLC and BP Amoco Chemical Company (BP Chemicals). Under the Separation Agreement:

- a prior force majeure dispute among the parties was settled;
- most of the acrylonitrile-related agreements between the parties were terminated as of May 31, 2005, including the Amended and Restated Production Agreement dated March 31, 1998, the Joint Venture Agreement dated March 31, 1998, the Acrylonitrile Expanded Relationship and Master Modification Agreement dated June 19, 2003 and the European Distribution Agreement dated March 31, 1998;
- we assigned our interest in ANEXCO, LLC to Innovene Chemicals; and
- we and Innovene Chemicals entered into amended and restated versions of our acrylonitrile License Agreement and Catalyst Sales Contract.

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STERLING CHEMICALS, INC. AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

In addition, on May 31, 2005, Innovene Chemicals made a one-time payment to us of $0.7 million; ANEXCO, LLC made an initial distribution to us of $4.8 million and we made a few small payments to Innovene Chemicals and ANEXCO, LLC for services performed prior to the termination of the agreements. ANEXCO, LLC made a subsequent distribution to us of $1.5 million on July 15, 2005, and we received a final distribution of $1.2 million on November 30, 2005. No other payments were or are required in connection with the settlement of the force majeure dispute or the termination of the acrylonitrile-related agreements.

4. DETAIL OF CERTAIN BALANCE SHEET ACCOUNTS

	December 31,	
	2006	2005
	(Dollars in Thousands)	
Inventories:		
Finished products	$ 38,485	$ 30,162
Raw materials	17,841	7,974
Inventories at lower-of-cost-or-market	56,326	38,136
Inventories under exchange agreements	1,818	(2,807)
Stores and supplies (net of obsolescence reserve of $2,149 and $2,573, respectively)	3,934	3,765
	$ 62,078	$ 39,094
Property, plant and equipment, net:		
Land	$ 7,149	$ 7,149
Buildings	4,506	4,497
Plant and equipment	306,352	286,049
Construction in progress	1,761	12,993
Less: accumulated depreciation	(235,935)	(80,670)
	$ 83,833	$ 230,018
Other assets, net:		
S&L Cogen joint venture	$ 4,733	$ 3,567
Deferred catalyst	1,959	2,156
Long-term deferred tax asset	641	
Other	2,321	2,820
	$ 9,654	$ 8,543
Accrued liabilities:		
Employee compensation and benefits	$ 13,434	$ 12,164
Property taxes	4,301	5,236
Other	5,137	6,290
	$ 22,872	$ 23,690

Deferred credits and other liabilities:		
Accrued postretirement, pension and post employment benefits	$ 35,596	$ 62,885
Deferred revenue	8,000	9,000
Other	5,695	5,919
	$ 49,291	$ 77,804

5. VALUATION AND QUALIFYING ACCOUNTS

Below is a summary of valuation and qualifying accounts related to continuing operations for the years ended December 31, 2006, 2005 and 2004:

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STERLING CHEMICALS, INC. AND SUBSIDIARIES
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	December 31,		
	2006	2005	2004
Allowance for doubtful accounts:			
Balance at beginning of year	$ 953	$ 3,092	$ 2,592
Add: bad debt expense/(credit)	1,049	(2,133)	500
Deduct: written-off accounts	(15)	(6)	
Balance at end of year	$ 1,987	$ 953	$ 3,092
Reserve for inventory obsolescence:			
Balance at beginning of year	$ 2,573	$ 1,938	$ 1,370
Add: obsolescence accrual	81	1,492	969
Deduct: disposal of inventory	(505)	(857)	(401)
Balance at end of year	$ 2,149	$ 2,573	$ 1,938

6. DEBT

On December 19, 2002, we issued $94.3 million in original principal amount of our 10% Senior Secured Notes due 2007 (our Secured Notes). Our Secured Notes are senior secured obligations and rank equally in right of payment with all of our other existing and future senior indebtedness, and senior in right of payment to all of our existing and future subordinated indebtedness. Our Secured Notes are guaranteed by Sterling Energy, Inc. (Sterling Energy), our only wholly owned subsidiary. Sterling Energy s guaranty ranks equally in right of payment with all of its existing and future senior indebtedness, and senior in right of payment to all of its existing and future subordinated indebtedness. Separate financial information is not presented for Sterling Energy as it is not material. Our Secured Notes and Sterling Energy s guaranty are secured by a first priority lien on all of our production facilities and related assets.

Our Secured Notes bear interest at an annual rate of 10%, payable semi-annually on June 15 and December 15 of each year. Until December 19, 2004, we were permitted under certain circumstances to pay interest on our Secured Notes through the issuance of additional Secured Notes rather than the payment of cash at an interest rate of 13 3 / 8 % per annum. In December 2003, we made an interest payment on our Secured Notes at the higher rate through the issuance of $6.3 million in original principal amount of additional Secured Notes, increasing the aggregate principal amount of outstanding Secured Notes to $100.6 million. We have made all other interest payments on our Secured Notes in cash. We may redeem our Secured Notes at any time at a redemption price of 100% of the outstanding principal amount thereof plus accrued and unpaid interest, subject to compliance with the terms of our revolving credit facility. In addition, in the event of a specified change of control or the sale of our facility in Texas City, Texas, we are required to offer to repurchase our Secured Notes at 101% of the outstanding principal amount thereof plus accrued and unpaid interest. Under certain circumstances, we are also required to use the proceeds of other asset sales to repurchase those Secured Notes tendered by the holders at a price equal to 100% of the outstanding principal amount thereof plus accrued and unpaid interest.

The indenture governing our Secured Notes contains numerous covenants and conditions, including, but not limited to, restrictions on our ability to incur indebtedness, create liens, sell assets, make investments, make capital expenditures, engage in mergers and acquisitions and pay dividends. The indenture also includes various circumstances and conditions that would, upon their occurrence and subject in certain cases to notice and grace periods, create an event of default thereunder. However, the indenture does not require us to satisfy any financial ratios or maintenance tests.

On March 1, 2007, we commenced an offer to repurchase all of our outstanding Secured Notes (our tender offer). Concurrently with our tender offer, we solicited consents from the holders of our Secured Notes to, among other things, eliminate certain covenants contained in the indenture governing our Secured Notes. The consent solicitation expired at 5:00 p.m., New York Time, on March 14, 2007, at which time we received consents from the requisite principal amount of Secured Notes to amend our indenture. The supplemental indenture we entered into to effect these amendments will only be effective if and when we consummate our tender offer for the Secured Notes.

Our tender offer is scheduled to expire at 12:00 midnight, New York City time, on March 28, 2007, unless extended or earlier terminated. The total consideration payable in connection with our tender offer and the consent solicitation for each $1,000 principal amount of our existing notes will be $1,002.50, plus accrued and unpaid interest to, but not including, the date of payment.

STERLING CHEMICALS, INC. AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

We expect to refinance our Secured Notes with an offering of up to $125 million of new senior secured notes (New Notes). In connection with our proposed offering of New Notes, we have also received a firm commitment letter from a national investment banking firm with respect to an alternate long-term debt financing. In the event our offering of the New Notes is not consummated, we intend to issue $111 million in debt financing pursuant to this commitment letter in order to refinance our Secured Notes.

We will use the net proceeds of the New Notes (or the debt financing effected pursuant to the commitment referenced above) to fund amounts payable in connection with the tender offer, the consent solicitation and to redeem any remaining Secured Notes not repurchased pursuant thereto.

On December 19, 2002, we also established our Revolving Credit Agreement with The CIT Group/Business Credit, Inc., as administrative agent and a lender, and certain other lenders (our revolving credit facility), which provides up to $100 million in revolving credit loans, subject to borrowing base limitations. Our revolving credit facility has an initial term ending on September 19, 2007. Under our revolving credit facility, we and Sterling Energy are co-borrowers and are jointly and severally liable for any indebtedness thereunder. Our revolving credit facility is secured by first priority liens on all of our accounts receivable, inventory and other specified assets, as well as all of the issued and outstanding capital stock of Sterling Energy.

Borrowings under our revolving credit facility bear interest, at our option, at an annual rate of either the Alternate Base Rate plus 0.75% or the LIBO Rate (as defined in our revolving credit facility) plus 2.75%. The Alternate Base Rate is equal to the greater of the Base Rate as announced from time to time by JPMorgan Chase Bank in New York, New York, or 0.50% per annum above the latest Federal Funds Rate (as defined in our revolving credit facility). The average interest rate for borrowings under our revolving credit facility for the year ended December 31, 2006 was 8.94%. Under our revolving credit facility, we are also required to pay an aggregate commitment fee of 0.50% per year (payable monthly) on any unused portion. Available credit is subject to a monthly borrowing base of 85% of eligible accounts receivable plus the lesser of $50 million and 65% of eligible inventory. In addition, the borrowing base for our revolving credit facility must exceed outstanding borrowings thereunder by $8 million at all times. As of December 31, 2006, total credit available under our revolving credit facility was limited to $72 million due to these borrowing base limitations. As of December 31, 2006, there were no loans outstanding under our revolving credit facility, and we had $3 million in letters of credit outstanding. Pursuant to Emerging Issues Task Force Issue No. 95-22, Balance Sheet Classification of Borrowings under Revolving Credit Agreements That Include both a Subjective Acceleration Clause and a Lock-Box Arrangement, any balances outstanding under our revolving credit facility are classified as a current portion of long-term debt. We are currently negotiating to amend our revolving credit facility to extend the term for five years and to make certain other changes to the borrowing base calculation and interest rates. We expect this amendment to be effective by March 31, 2007.

The stated term of our revolving credit facility ends on September 19, 2007 and our Secured Notes become due on December 19, 2007. As mentioned above, we have started the process of refinancing the indebtedness under our Secured Notes and amending our revolving credit facility prior to their stated maturities. Subject to the successful refinancing of our Secured Notes and amendment of our revolving credit facility, we believe that our cash on hand, together with the credit available under our amended revolving credit facility, is sufficient to meet our short-term and long-term liquidity needs, although our liquidity may not be adequate during any particular period.

Debt Maturities

The Secured Notes, which had an aggregate principal balance of $100.6 million outstanding as of December 31, 2006, are due on December 19, 2007. As a result of the financing arrangement entered into during March 2007, as discussed above, we have reclassified the debt from current to long-term as we have the ability and intent to refinance the Secured Notes on a long-term basis.

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STERLING CHEMICALS, INC. AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

7. INCOME TAXES

A reconciliation of federal statutory income taxes to our effective tax benefit is as follows:

	Year Ended December 31,		
	2006	2005	2004
	(Dollars in Thousands)		
Benefit for income taxes at statutory rates	$ (42,100)	$ (16,299)	$ (26,125)
Non-deductible expenses	19	19	26
Non-deductible goodwill impairment			16,962
State income taxes	(1,262)	(956)	(1,933)
Change in valuation allowance	27,621		
Other	1,096	235	(930)
Effective tax benefit	$ (14,626)	$ (17,001)	$ (12,000)

The benefit for income taxes is comprised of a tax benefit for continuing operations and a tax benefit for discontinued operations as shown below:

	Year Ended December 31,		
	2006	2005	2004
	(Dollars in Thousands)		
Tax expense continuing operations	$ (14,488)	$ (10,641)	$ 7,262
Tax expense discontinued operations	(138)	(6,360)	(19,262)
Total tax benefit	$ (14,626)	$ (17,001)	$ (12,000)

The benefit for income taxes is composed of the following:

	Year Ended December 31,		
	2006	2005	2004
	(Dollars in Thousands)		
Current federal	$ 299	$	$
Deferred federal	(13,685)	(16,066)	(10,105)
State income taxes	(1,240)	(935)	(1,895)
Total tax benefit	$ (14,626)	$ (17,001)	$ (12,000)

The components of our deferred income tax assets and liabilities are summarized below:

	December 31,	
	2006	2005
	(Dollars in Thousands)	
Deferred tax assets:		
Accrued liabilities	$ 1,292	$ 787
Accrued postretirement cost	7,518	12,552
Accrued pension cost	4,537	10,770
Tax loss and credit carry forwards	32,506	46,734

State deferred taxes	77	
Other	3,797	2,385
Total deferred tax assets	$ 49,727	$ 73,228
Deferred tax liabilities:		
Property, plant and equipment	$ (16,458)	$ (66,571)
State deferred taxes		(3,219)
Subtotal	(16,458)	(69,790)
Less: valuation allowance	(29,584)	(8,832)
Total deferred tax liabilities	(46,042)	(78,622)
Net deferred tax assets (liabilities)	$ 3,685	$ (5,394)

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STERLING CHEMICALS, INC. AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

As of December 31, 2006, we had an available U.S. federal income tax net operating loss carryforward (NOL) of approximately $85 million, which expires during the years 2023 through 2026. Deferred tax assets are regularly assessed for recoverability based on both historical and anticipated earnings levels, and a valuation allowance is recorded when it is more likely than not that these amounts will not be recovered. As a result of our analysis, we have concluded that a valuation allowance should be established in the amount of $28 million relating to our federal deferred tax assets as of December 31, 2006. At December 31, 2005, we had deferred tax assets relating to state NOLs of $12 million, which had a related valuation allowance of $9 million. Under the provisions of the new Texas Margin Tax that was enacted in 2006, these NOLs were converted into state tax credits of $3 million, $2 million of which relate to pre-bankruptcy items that we do not believe will be utilized. As such, the valuation allowance relating to these state deferred tax assets was reduced to $2 million at December 31, 2006. Future recognition of these items would be recorded as an increase in our paid-in capital under purchase accounting rules rather than as a reduction in our provision for income taxes. We have also recorded a $4 million liability relating to certain tax contingencies that we have identified, which has been included in accrued liabilities.

8. EMPLOYEE BENEFITS

We have established the following benefit plans:

Retirement Benefit Plans

We have non-contributory pension plans which cover all salaried and hourly wage employees. Under our hourly plan, the benefits are based primarily on years of service and employees pay near retirement. Under our salaried plan, the benefits are based primarily on years of service and an employee s pay as of the earlier of the employee s retirement or January 1, 2005. Our funding policy is consistent with the funding requirements of federal law and regulations.

Pension plan assets are invested in a balanced portfolio managed by an outside investment manager. Our investment policy is to generate a total return that, over the long term, provides sufficient assets to fund its liabilities, reduces risk through diversification of investments within asset classes and complies with the Employee Retirement Income Security Act of 1974 (ERISA) by investing in a manner consistent with ERISA s fiduciary standards. Within this balanced fund, assets are invested as follows:

	As of December 31,	
	2006	**2005**
Equities	64%	57%
Bonds	23%	38%
Other	13%	5%
Total	100%	100%

Information concerning the pension obligation, plan assets, amounts recognized in our financial statements and underlying actuarial assumptions is stated below:

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STERLING CHEMICALS, INC. AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

	December 31, 2006	December 31, 2005
	(Dollars in Thousands)	
Change in projected benefit obligation:		
Benefit obligation at beginning of year	$ 125,694	$ 119,682
Service cost	593	622
Interest cost	7,610	6,993
Actuarial loss	820	6,259
Benefits paid	(8,582)	(7,862)
Benefit obligation at end of year	$ 126,135	$ 125,694

	December 31, 2006	December 31, 2005
	(Dollars in Thousands)	
Change in plan assets:		
Fair value at beginning of year	$ 95,690	$ 89,250
Actual return on plan assets	14,684	7,643
Employer contributions	7,862	6,659
Benefits paid	(8,582)	(7,862)
Fair value at end of year	$ 109,654	$ 95,690
Reconciliation of amounts recognized:		
Funded status	$ (16,481)	$ (30,004)
Unrecognized actuarial loss		6,874
Net amount recognized	$ (16,481)	$ (23,130)

	December 31, 2006	December 31, 2005
Amounts recognized in the balance sheet consist of:		
Current liabilities	$ (8,270)	$ (7,602)
Non-current liabilities	(8,211)	(22,357)
Accumulated other comprehensive income		6,829
Net amount recognized in financial position	$ (16,481)	$ (23,130)

	December 31, 2006
Amount recognized in accumulated other comprehensive loss consists of (pre-tax):	

Net loss	$	(764)
Prior service costs		
Net amount recognized in accumulated other comprehensive loss	$	(764)

All plans have projected benefit obligations and accumulated benefit obligation in excess of plan assets as of December 31, 2006. The total accumulated benefit obligation was $126 million as of December 31, 2006 and 2005, respectively. Estimated contributions for 2007 are expected to be approximately $8.5 million, a portion of which are above the minimum funding requirements. The expected amortization of the actuarial loss for 2007 is $11,000.

Effective as of January 1, 2005, we froze all accruals under our defined benefit pension plan for our salaried employees, which resulted in a plan curtailment under SFAS No. 88 Employers Accounting for Settlement and Curtailments of Defined Benefit Pension Plans and for Termination Benefits. As a result, we recorded a pretax curtailment gain of $13 million in the fourth quarter of 2004. At the time we froze accruals under our defined benefit pension plan, we also increased the company match for employee contributions under our 401(k) plan.

STERLING CHEMICALS, INC. AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

Net periodic pension costs consist of the following components:

	Year ended December 31,		
	2006	2005	2004
	(Dollars In Thousands)		
Components of net pension costs:			
Service cost-benefits earned during the year	$ 593	$ 622	$ 3,466
Interest on prior year s projected benefit obligation	7,610	6,993	7,561
Expected return on plan assets	(7,767)	(6,641)	(5,934)
Net amortization of actuarial loss (gain)	13	8	
Settlement/curtailment			(12,944)
Net pension costs	$ 449	$ 982	$ (7,851)
Weighted-average assumptions:			
Discount Rate	5.75%	5.75%	6.25%
Rates of increase in salary compensation level	3.50%	5.00%	5.00%
Expected long-term rate of return on plan assets	7.50%	7.50%	7.50%

Postretirement Benefits Other than Pensions

We provide certain health care benefits and life insurance benefits for retired employees. Substantially all of our employees become eligible for these benefits at early retirement age. We accrue the cost of these benefits during the period in which the employee renders the necessary service.

Health care benefits are currently provided to employees hired prior to June 7, 2004, who retire from us with ten or more years of credited service. Some of our employees are eligible for postretirement life insurance, depending on their hire date. Postretirement health care benefits plans are contributory. Benefit provisions for most hourly employees are subject to collective bargaining. In general, retiree health care benefits are paid as covered expenses are incurred.

In September 2005, we recorded a curtailment gain totaling $1.2 million due to workforce reductions related to our exit from the acrylonitrile and related derivatives businesses. We also recorded a curtailment gain of $0.5 million attributable to a reduction in our workforce that occurred in late 2004.

In June 2004, we had a reduction in force at our Texas City plant. This reduction in force led to a curtailment of our postretirement benefit plan resulting in a $1.4 million curtailment gain, with $1.3 million of the gain reflected in cost of goods sold and $0.1 million reflected in selling, general and administrative expenses. In addition, our plan was amended as of June 1, 2004 as follows: employees hired after this date are not eligible for retiree medical benefits, our contribution rates for retiree medical coverage are frozen at the 2004 level and prescription drug co-pays were increased. This amendment reduced the accumulated postretirement benefit obligation by $9.2 million, which is being amortized over the average remaining service period to full eligibility of the active plan participants (which is 8.5 years).

On December 8, 2003, the Medicare Prescription Drug Improvement and Modernization Act of 2003 (the Act) was passed. The Act introduces a prescription drug benefit under Medicare (Medicare Part D), as well as a federal subsidy to sponsors of retiree health care benefit plans that provide a benefit that is at least actuarially equivalent to Medicare Part D. We measured the effects of the Act on our accumulated postretirement benefit obligation and determined that, based on the regulatory guidance currently available, benefits provided by our postretirement plan are at least actuarially equivalent to Medicare Part D, and accordingly, we expect to be entitled to the federal subsidy through 2009. In 2006, we received a subsidy of $0.2 million under the Act.

Information concerning the plan obligation, the funded status, amounts recognized in our financial statements and underlying actuarial assumptions are stated below:

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STERLING CHEMICALS, INC. AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

	December 31, 2006	December 31, 2005
	(Dollars in Thousands)	
Change in projected benefit obligation:		
Benefit obligation at beginning of year	$ 27,834	$ 27,745
Service cost	174	208
Interest cost	1,463	1,558
Plan amendments		46
Actuarial loss (gain)	(1,728)	1,392
Benefits paid	(1,801)	(3,115)
Benefit obligation at end of year	$ 25,942	$ 27,834
Funded plan assets	$	$
Funded status at end of year	$ (25,942)	$ (27,834)
Unrecognized cost:		
Actuarial loss		6,048
Plan amendment/prior service cost		(15,691)
Accrued benefit cost	$ (25,942)	$ (37,477)

	December 31, 2006
Amounts recognized in accumulated other comprehensive income (loss) consist of (pre-tax):	
Net loss	$ (3,695)
Plan amendment/prior service costs	14,257
Net amount recognized in accumulated other comprehensive income (loss)	$ (10,562)

Net periodic plan costs consist of the following components:

	Year ended December 31, 2006	2005	2004
	(Dollars in Thousands)		
Components of net plan costs:			
Service cost	$ 174	$ 208	$ 310
Interest cost	1,463	1,558	1,864
Net amortization:			
Actuarial loss	99	333	21
Plan amendment/prior service costs	(1,434)	(1,485)	(1,223)
Curtailment and special termination benefits		(1,727)	(1,418)

Net plan costs (benefit)	$ 302	$(1,113)	$ (446)
Weighted-average assumptions:			
Discount rate	5.75%	5.75%	5.75%

The weighted-average annual assumed health care trend rate is assumed to be 9% for 2007. The rate is assumed to decrease gradually to 4.5% by 2014 and remain level thereafter. Estimated contributions for 2007 are expected to be approximately $1.4 million. The expected amortization of the plan amendment prior service costs for 2007 is $1.4 million. Based on plan changes enacted, assumed health care cost trend rates no longer have a significant effect on the amounts reported for the health care plans. A one percentage point change in assumed health care trend rates would have the following effects:

STERLING CHEMICALS, INC. AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

	1% Increase	1% Decrease
	(Dollars in Thousands)	
Effect on total of service and interest cost components	$ 34	$ (30)
Effect on post-retirement benefit obligation	619	(547)

In September 2006, the Financial Accounting Standards Board (the FASB) issued SFAS No. 158, Employers Accounting for Defined Benefit Pension and Other Postretirement Plans (SFAS No. 158). SFAS No. 158 requires the recognition of the funded status of pension and other postretirement benefit plans on the balance sheet. The overfunded or underfunded status are recognized as an asset or liability on the balance sheet with changes occurring during the current year reflected through the comprehensive income portion of equity. SFAS No. 158 also requires the measurement date of the funded status of our defined benefit postretirement plans match the date of our fiscal year-end financial statements, eliminating the use of earlier measurement dates that were previously permissible. We have recognized the funded status of our defined benefit postretirement plans on our balance sheet and have provided the required disclosures as of our fiscal year-ended December 31, 2006. We have also measured the assets and benefit obligations of our defined benefit postretirement plans as of the date of our fiscal year-end statement of financial position. The incremental effect of applying SFAS No. 158 to our employee benefit plans as of December 31, 2006 is summarized below (in thousands):

	Pension plan	Other postretirement benefits plan
Increase (decrease) in liabilities	$ 87	$ (10,562)
Increase (decrease) in accumulated other comprehensive income	(56)	6,812
Increase (decrease) in deferred income tax liabilities	(31)	3,750

Estimated Future Benefits Payable

We estimate that the future benefits payable under our pension and other post-retirement benefits as of December 31, 2007 are as follows (in thousands):

	Pensions-hourly	Pensions-salaried	Other postretirement benefits	Total
2007	$ 3,414	$ 4,299	$ 1,275	$ 8,988
2008	3,270	4,327	1,214	8,811
2009	3,158	4,449	1,178	8,785
2010	2,952	4,570	2,225	9,647
2011	2,941	4,755	2,179	9,875
2012-2016	16,361	26,204	10,567	53,132
Total	$32,096	$48,604	$ 18,638	$99,238

Savings and Investment Plan

Our Seventh Amended and Restated Savings and Investment Plan covers substantially all employees, including executive officers. This Plan is qualified under Section 401(k) of the Internal Revenue Code. Each participant has the option to defer taxation of a portion of his or her earnings by directing us to contribute a percentage of such earnings

to the Plan. A participant may direct up to a maximum of 20% of eligible earnings to this Plan, subject to certain limitations set forth in the Internal Revenue Code. A participant s contributions become distributable upon the termination of his or her employment. Beginning January 1, 2005, we began matching 100% of salaried employees contributions, to the extent such contributions do not exceed 6% of such participant s base compensation (excluding bonuses, profit sharing and similar types of compensation). Our expense under this plan was $1 million in 2006, $1.1 million in 2005 and $0.8 million in 2004.

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STERLING CHEMICALS, INC. AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

Bonus Plan and Gain Sharing Plan

In February 2002, our Board of Directors, upon recommendation of its Compensation Committee, approved the establishment of a Bonus Plan and a Gain Sharing Plan. The Bonus Plan is designed to benefit all qualified salaried employees, while the Gain Sharing Plan is designed to benefit all qualified hourly employees. Both plans provide our qualified employees the opportunity to earn bonuses depending on, among other things, our annual financial performance. In January 2006, our Compensation Committee amended our Bonus Plan in a manner that allows each of our salaried employees the ability to earn a bonus each year based on their individual performance, irrespective of our overall financial performance. However, if a bonus is paid for any year based upon our financial performance, no additional bonus is paid under the new individual performance provision of the Plan. Our Chief Executive Officer and each of our four Senior Vice Presidents are excluded from this portion of our Bonus Plan. Whether a bonus will be paid to our Chief Executive Officer or any of our Senior Vice Presidents in any year when a bonus is not paid based on our financial performance, and if so, the amount to be paid, will be determined at that time by our Compensation Committee.

In 2006, after authorization from our Compensation Committee, we accrued $1.4 million pursuant to this Plan to be paid out no later than March 1, 2007. Although we did not meet the minimum financial threshold of these plans for 2005, in February 2006, our Compensation Committee authorized the payment of $725,000 in bonuses based upon our achieving our target goal of $20 million in fixed cost savings during 2005, and we accrued that amount in 2005. In addition, although we did not meet the minimum financial threshold of these plans for 2004, on February 11, 2005, our Board authorized the payment of $0.9 million in bonuses related to our performance in 2004, and we accrued that amount in 2004.

Key Employee Protection Plan

On January 26, 2000, we instituted our Key Employee Protection Plan, which has subsequently been amended several times. We established this Plan to help us retain certain of our employees and motivate them to continue to exert their best efforts on our behalf during periods when we may be susceptible to a change of control, and to assure their continued dedication and objectivity during those periods. Our Compensation Committee has designated a select group of management or highly compensated employees as participants under our Key Employee Protection Plan, and has established their respective applicable multipliers and other variables for determining benefits. Our Compensation Committee is also authorized to designate additional management or highly compensated employees as participants under our Key Employee Protection Plan and set their applicable multipliers. Our Compensation Committee may also terminate any participant s participation under this Plan with 60 days prior notice if it determines that the participant is no longer one of our key employees.

Under our Key Employee Protection Plan, any participant under the Plan that terminates his or her employment for Good Reason or is terminated by us for any reason other than Misconduct or Disability within his or her Protection Period is entitled to benefits under the Plan. A participant s Protection Period commences 180 days prior to the date on which a specified change of control occurs and ends either two years or 18 months after the date of that change of control, depending on the size of the participant s applicable multiplier. A participant may also be entitled to receive payments under this Plan in the absence of a change of control if he or she terminates his or her employment for Good Reason or is terminated by us for any reason other than Misconduct or Disability, but in these circumstances his or her applicable multiplier is reduced by 50%. If a participant becomes entitled to benefits under our Key Employee Protection Plan, we are required to provide the participant with a lump sum cash payment that is determined by multiplying the participant s applicable multiplier by the sum of the participant s highest annual base compensation during the last three years plus the participant s targeted bonus for the year of termination, and then deducting the sum of any other separation, severance or termination payments made by us to the participant under any other plan or agreement or pursuant to law.

In addition to the lump sum payment, the participant is entitled to receive any accrued but unpaid compensation, compensation for unused vacation time and any unpaid vested benefits earned or accrued under any of our benefit plans (other than qualified plans). Also, for a period of 24 months (including 18 months of COBRA coverage), the

participant will continue to be covered by all of our life, health care, medical and dental insurance plans and programs (other than disability), as long as the participant makes a timely COBRA election and pays the regular employee premiums required under our plans and programs and by COBRA. In addition, our obligation to continue to provide coverage under our

STERLING CHEMICALS, INC. AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

plans and programs to any participant ends if and when the participant becomes employed on a full-time basis by a third party which provides the participant with substantially similar benefits.

If any payment or distribution under our Key Employee Protection Plan to any participant is subject to excise tax pursuant to Section 4999 of the Internal Revenue Code, the participant is entitled to receive a gross-up payment from us in an amount such that, after payment by the participant of all taxes on the gross-up payment, the amount of the gross-up payment remaining is equal to the excise tax imposed under Section 4999 of the Internal Revenue Code. However, the maximum amount of any gross-up payment is 25% of the sum of the participant s highest annual base compensation during the last three years plus the participant s targeted bonus for the year of payment.

We may terminate our Key Employee Protection Plan at any time and for any reason but any termination does not become effective as to any participant until 90 days after we give the participant notice of the termination of the Plan. In addition, we may amend our Key Employee Protection Plan at any time and for any reason, but any amendment that reduces, alters, suspends, impairs or prejudices the rights or benefits of any participant in any material respect does not become effective as to that participant until 90 days after we give him or her notice of the amendment of the Plan. No termination of our Key Employee Protection Plan, or any of these types of amendments to the Plan, can be effective with respect to any participant if the termination or amendment is related to, in anticipation of or during the pendency of a change of control, is for the purpose of encouraging or facilitating a change of control or is made within 180 days prior to any change of control. Finally, no termination or amendment of our Key Employee Protection Plan can affect the rights or benefits of any participant that are accrued under the Plan at the time of termination or amendment or that accrue thereafter on account of a change of control that occurred prior to the termination or amendment or within 180 days after such termination or amendment. We expensed zero, $0.4 million and $0.3 million in 2006, 2005 and 2004, respectively, pursuant to this Plan.

Severance Pay Plan

On March 8, 2001, our Board of Directors approved our Severance Pay Plan, which has subsequently been amended. This Plan covers all of our non-unionized employees and was established to help us retain these employees by assuring them that they will receive some compensation in the event that their employment is adversely affected in specified ways. Under our Severance Pay Plan, any participant that terminates his or her employment for Good Reason or is terminated by us for any reason other than Misconduct or Disability is entitled to benefits under our Severance Pay Plan. If a participant becomes entitled to benefits under our Severance Pay Plan, we are required to provide the participant with a lump sum cash payment in an amount equivalent to two weeks of such participant s base salary for each credited year of service, with a maximum payment of one year s base salary. The amount of this lump sum payment is reduced, however, by the amount of any other separation, severance or termination payments made by us to the participant under any other plan or agreement, including our Key Employee Protection Plan, or pursuant to law.

In addition to the lump sum payment, for a period of six months after the participant s termination date, the COBRA premium required to be paid by such participant for coverage under our medical and dental plans may not be increased beyond that required to be paid by active employees for similar coverage under those plans, as long as the participant makes a timely COBRA election and pays the regular employee premiums required under those plans and otherwise continues to be eligible for coverage under those plans.

We may terminate or amend our Severance Pay Plan at any time and for any reason but no termination or amendment of our Severance Pay Plan can affect the rights or benefits of any participant that are accrued under the plan at the time of termination or amendment. We had zero expense and less than $0.1 million under this Plan in 2006 and 2005, respectively, for continued operations. In 2004, we expensed $2.4 million under this Plan, with approximately $2 million paid out in 2005 with the remaining balance yet to be paid.

Due to the exit from our acrylonitrile and derivatives businesses and subsequent workforce reduction, we expensed $0.4 million in 2006 and $0.5 million in 2005 pursuant to this Plan, of which $0.7 million has been paid to date, with the balance to be paid in 2007. These amounts are included in the results from discontinued operations.

STERLING CHEMICALS, INC. AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

9. COMMITMENTS AND CONTINGENCIES

Product Contracts

We have certain long-term agreements, which provide for the dedication of 100% of our production of acetic acid and plasticizers, each to one customer. We also have various sales and conversion agreements, which dedicate significant portions of our production of styrene to various customers. Some of these agreements generally provide for cost recovery plus an agreed margin or element of profit based upon market price.

Lease Commitments

We have entered into various non-cancelable long-term operating leases. Future minimum lease commitments at December 31, 2006, are as follows: 2007 $0.3 million; 2008 $0.3 million; 2009 $0.3 million; 2010 $0.3 million; 2011 $0.3 million and thereafter $0.5 million.

Environmental, Health and Safety

Our operations involve the handling, production, transportation, treatment and disposal of materials that are classified as hazardous or toxic and that are extensively regulated by environmental and health and safety laws, regulations and permit requirements. Environmental permits required for our operations are subject to periodic renewal and may be revoked or modified for cause or when new or revised environmental requirements are implemented. Changing and increasingly strict environmental requirements can affect the manufacturing, handling, processing, distribution and use of our chemical products and, if so affected, our business and operations may be materially and adversely affected. In addition, changes in environmental requirements may cause us to incur substantial costs in upgrading or redesigning our facilities and processes, including our waste treatment, storage, disposal and other waste handling practices and equipment.

Our operating expenditures for environmental matters, mostly waste management and compliance, were $20 million in both 2006 and 2005. We also spent $2 million for environmentally-related capital projects in both 2006 and 2005.

Air emissions from our Texas City facility are subject to certain permit requirements and self-implementing emission limitations and standards under state and federal laws. Our Texas City facility is located in an area that the Environmental Protection Agency (EPA) has classified as not having attained the ambient air quality standards for ozone, which is controlled by direct regulation of volatile organic compounds and nitrogen oxide (NOx) emissions. Our Texas City facility is also subject to the federal government s June 1997 National Ambient Air Quality Standards, which lower the ozone and particulate matter concentration thresholds for attainment. The Texas Commission for Environmental Quality (TCEQ) has imposed strict requirements on regulated facilities, including our Texas City facility, to ensure that the air quality control region will achieve the ambient air quality standards for ozone. Local authorities also may impose new ozone and particulate matter standards. Compliance with these stricter standards may substantially increase our future NOx, volatile organic compounds and particulate matter emissions control costs, the amount and full impact of which cannot be determined at this time.

On December 13, 2002, the TCEQ adopted a revised State Implementation Plan (SIP) to achieve compliance with the 1-hour ozone standard of the Clean Air Act. The EPA approved this 1-hour SIP, which calls for reduction of emissions of NOx at our Texas City facility by approximately 80% by the end of 2007. The current 1-hour SIP also requires monitoring of emissions of highly reactive volatile organic carbons (HRVOCs), such as ethylene. The cost of compliance with the 1-hour SIP at our Texas City facility is estimated to be between $12 million and $14 million. This estimate includes our share of capital expenditures needed to be made by S&L Cogeneration Company. To date we have spent $10 million in capital on NOx reductions and HRVOC monitoring, with $1 million of that amount spent in 2006. In April 2004, the Houston-Galveston region was designated a moderate non-attainment area with respect to the 8-hour ozone standard of the Clean Air Act, and compliance with this standard is required no later than June 15, 2010. In December 2006, the TCEQ formally proposed revisions to the SIP in order to achieve compliance with the 8-hour ozone standard. This 8-hour SIP will undergo review and revisions before final adoption by the TCEQ, which is expected in May 2007, and will then be submitted to the EPA for approval one month after adoption. The current proposed 8-hour SIP calls for relatively modest additional controls which we believe

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STERLING CHEMICALS, INC. AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

would require very little expense on our part. However, the proposed package may not receive EPA approval in its current form, in which case additional controls or monitoring could be added before the rule becomes finalized. Based on these developments, it is difficult to predict our final cost of compliance under the 8-hour SIP, but we estimate that the additional cost of compliance will range from zero to $16 million in capital expenditures and the purchase of allowances, depending on the terms of the final 8-hour SIP.

To reduce the risk of offsite consequences from unanticipated events, we acquired a greenbelt buffer zone adjacent to our Texas City facility in 1991. We also participate in a regional air monitoring network to monitor ambient air quality in the Texas City community.

Legal Proceedings

On July 5, 2005, Patrick B. McCarthy, an employee of Kinder-Morgan, was seriously injured at Kinder-Morgan, Inc. s facilities near Cincinnati, Ohio while attempting to offload a railcar containing one of our plasticizers products. On October 28, 2005, Mr. McCarthy and his family filed a suit in the Court of Common Pleas, Hamilton County, Ohio (Case No. A0509144) against us, BASF Corporation and five other defendants. The plaintiffs are seeking a minimum amount of $150,000 in damages related to medical expenses and loss of earnings and earnings capacity, among other things, and punitive damages. Discovery is ongoing in this case as to the underlying cause of the accident and the parties respective liabilities, if any. At this time, it is impossible to determine what, if any, liability we will have for this incident and we will vigorously defend the suit. We believe that all, or substantially all, of any liability imposed upon us as a result of this suit and our related out-of-pocket costs and expenses will be covered by our insurance policies, subject to a $1 million deductible. We do not believe that this incident will have a material adverse affect on our business, financial position, results of operations or cash flows, although we cannot guarantee that a material adverse effect will not occur.

On August 17, 2006, we initiated an arbitration proceeding against BP Chemicals to resolve a dispute involving the interpretation of provisions of our acetic acid production agreement with BP Chemicals. Under the production agreement, BP Chemicals reimburses our manufacturing expenses and pays us a percentage of the profits derived from the sales of the acetic acid we produce. Historically, the costs of manufacturing charged to our acetic acid business, and reimbursed by BP Chemicals, included the amounts we paid Praxair for carbon monoxide, hydrogen and a blend of carbon monoxide and hydrogen commonly referred to as blend gas . Our acetic acid business has always used all of the carbon monoxide produced by Praxair, other than the small amount of carbon monoxide included in the blend gas. Until recently, all of the blend gas produced by Praxair was used by the oxo-alcohols plant included in our plasticizers business. During the period when the oxo-alcohols plant was operating, BP Chemicals was compensated for the use of this blend gas by our oxo-alcohols plant through a credit to the amount of our manufacturing expenses reimbursed by BP Chemicals. Effective July 1, 2006, we permanently closed our oxo-alcohols plant. BP Chemicals has now taken the position that it is entitled to continue to deduct a portion of the blend gas credit from the reimbursement of our manufacturing expenses, even though our oxo-alcohols plant has been closed and is no longer taking any blend gas and the Praxair facilities have been modified so that the carbon monoxide previously used in blend gas is now being delivered to our acetic acid operations. Effective August 1, 2006, BP Chemicals began short paying our invoices for manufacturing expenses by the portion of the credit that BP Chemicals claims should continue through July 31, 2016. The disputed portion of the credit averaged approximately $0.3 million per month during 2006. We are also seeking additional damages from BP Chemicals in the arbitration based on what we believe are breaches of duty by BP Chemicals. The arbitration hearing was scheduled for August 6, 2007. However, pursuant to an agreement reached in principle on January 31, 2007, the parties will abate the arbitration proceeding for a period of at least six months while they attempt to reach a negotiated settlement. As part of the agreement, BP Chemicals reimbursed us $0.8 million on February 5, 2007 which was 50% of the accrued disputed credit, and will continue to pay 50% of the disputed amount each month during the period of negotiation. The parties have stipulated that the payments are made without prejudice, in that BP Chemicals is not admitting liability and continues to insist that we remain liable for the disputed portion of the blend gas credit. According to the agreement, if a settlement is not reached within six months, either party may reinstate the arbitration process, and seek a hearing date consistent with

the current schedule, or approximately seven months thereafter. Under the January 31, 2007 agreement, if the arbitration proceeds to an award, the amounts paid by BP Chemicals will be credited against any sums awarded to us or refunded by us to BP Chemicals, depending on the ruling of the arbitration panel. We believe that our acetic acid production agreement does not contemplate the continuation of any portion of the blend gas credit under these circumstances and will vigorously pursue our position. Although we are in a dispute with BP Chemicals over the interpretation of this contractual provision, we believe that we

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STERLING CHEMICALS, INC. AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

continue to have a constructive working relationship with BP Chemicals, as has been the case since 1986. As part of the settlement negotiations over the blend gas calculation, we may discuss an extension of the term of the acetic acid production agreement.

On February 21, 2007, we received a summons naming us as a defendant in a class action suit, Case No. H-07-0625 filed in the United States District Court, Southern District of Texas, Houston Division. The plaintiffs comprising the proposed class are employees and retired employees of Sterling Fibers, Inc., one of our former subsidiaries that was sold in connection with our Plan of Reorganization. The plaintiffs are alleging that we were not permitted to increase their premiums for retiree medical insurance based on a provision contained in the asset purchase agreement between us and Cytec Industries Inc. governing our purchase of our former acrylic fibers business in 1997. During our bankruptcy, we specifically rejected this asset purchased agreement. The plaintiffs are making claims for breach of contract and claims under the Employee Retirement Income Security Act and seek damages, declaratory relief, punitive damages and attorneys fees. At this time, we have not determined what, if any, liability we may have in this matter and intend to vigorously defend this action. We do not believe a loss related to this matter is probable, therefore no liability associated with this matter has been accrued. Currently, we are unable to determine the possible range of loss related to this matter, if any.

We are subject to various other claims and legal actions that arise in the ordinary course of our business. We do not believe that any of these claims and actions, separately or in the aggregate, will have a material adverse effect on our business, financial position, results of operation or cash flows, although we cannot guarantee that a material adverse effect will not occur.

10. SALES INFORMATION

Sales by product, sales to major customers constituting 10% or more of total revenues and export sales from continuing operations were as follows:

	Year ended December 31,		
	2006	2005	2004
	(Dollars in Thousands)		
Sales by product:			
Acetic acid	$ 98,344	$ 86,125	$ 81,069
Styrene	524,665	513,788	529,729
Plasticizers	44,535	41,973	44,555
Major customers:			
BP Chemicals	$ 98,344	$ 86,125	$ 81,069
Customer A	111,075	93,752	127,956
Customer B	144,278	124,149	116,912
Customer C	67,802	77,570	*
Export sales:			
Export revenues	$ 69,926	$143,448	$152,211
Percentage of total revenues	10%	22%	23%

* Does not comprise more than 10% of total revenue for the periods indicated,

therefore not
presented.

11. FINANCIAL INSTRUMENTS

Concentrations of Risk

We sell our products primarily to companies involved in the petrochemicals industry. We perform ongoing credit evaluations of our customers and generally do not require collateral for accounts receivable. However, letters of credit are required by us on many of our export sales. Historically, our credit losses have been minimal.

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We maintain cash deposits with major banks, which from time to time may exceed federally insured limits. We periodically assess the financial condition of these institutions and believe that the likelihood of any possible loss is minimal.

Fair Value of Financial Instruments

The carrying amounts reflected in the consolidated balance sheets for cash and cash equivalents, accounts receivable, accounts payable and certain accrued liabilities approximate fair value due to the short maturities of these instruments. As of December 31, 2006, the fair value of our Secured Notes was $96 million based on its quoted price.

12. CAPITAL STOCK

Under our Certificate of Incorporation, we are authorized to issue 20,125,000 shares of capital stock, consisting of 20,000,000 shares of common stock, par value $0.01 per share, and 125,000 shares of preferred stock, par value $0.01 per share. In connection with our Plan of Reorganization and the merger of Sterling Chemicals Holdings, Inc. into us, we issued a total of 2,825,000 shares of common stock. Subject to applicable law and the provisions of our Certificate of Incorporation, the indenture governing our Secured Notes and the revolving credit facility, dividends may be declared on our shares of capital stock at the discretion of our Board of Directors and may be paid in cash, in property or in shares of our capital stock.

Upon the effective date of our Plan of Reorganization, we authorized 25,000 shares and issued 2,175 shares of our Series A Convertible Preferred Stock (Series A Preferred Stock). Each share of Series A Preferred Stock is convertible at the option of the holder thereof at any time into 1,000 shares of our common stock, subject to adjustments. The Series A Preferred Stock has a cumulative dividend rate of 4% per quarter, payable in additional shares of Series A Preferred Stock in arrears on the first business day of each calendar quarter. As our shares of Series A Preferred Stock are convertible into shares of our common stock (currently on a one to 1,000 share basis), each dividend paid in additional shares of our Series A Preferred Stock has a dilutive effect on our shares of common stock. Since the initial issuance of Series A Preferred Stock, we have issued an additional 1,921.760 shares of our Series A Preferred Stock (convertible into 1,921,760 shares of our common stock) in dividends.

Our Series A Preferred Stock carries a liquidation preference of $13,793.11 per share, subject to adjustments. We may redeem all or any number of our shares of Series A Preferred Stock at any time after December 19, 2005, at a redemption price determined in accordance with Certificate of Designations, Preferences, Rights and Limitations of our Series A Preferred Stock, provided that the current equity value of our capital stock issued on the effective date of our Plan of Reorganization exceeds specified levels. The holders of our Series A Preferred Stock may elect to have us redeem all or any of their shares of Series A Preferred Stock following a specified change of control at a redemption price equal to the greater of:

- the liquidation preference for such shares (plus accrued and unpaid dividends);
- in the event of a merger or consolidation, the fair market value of the consideration that would have been received in such merger or consolidation in respect of the shares of our common stock into which such shares of Series A Preferred Stock were convertible immediately prior to such merger or consolidation had such shares of Series A Preferred Stock been converted prior thereto; or
- in the event of some other specified change of control, the current market value of the shares of our common stock into which such shares of Series A Preferred Stock were convertible immediately prior to such change of control had such shares of Series A Preferred Stock been converted prior thereto (plus accrued and unpaid dividends).

Upon the effective date of our Plan of Reorganization, we also issued warrants (the Warrants) to purchase, in the aggregate, 949,367 shares of common stock. Each Warrant represents the right, at any time on or before December 19, 2008, to purchase one share of our common stock at an exercise price of $52 per share (subject to adjustments).

STERLING CHEMICALS, INC. AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

13. RELATED PARTY TRANSACTIONS

Resurgence Asset Management, L.L.C. (Resurgence) has beneficial ownership of a substantial majority of the voting power of our equity securities due to its investment and disposition authority over securities owned by its and its affiliates managed funds and accounts. Currently, Resurgence has beneficial ownership of over 98% of our Series A Preferred Stock and over 60% of our common stock, representing ownership of over 82% of the total voting power of our equity. Each share of our Series A Preferred Stock is convertible at the option of the holder thereof at any time into 1,000 shares of our common stock, subject to adjustments. The holders of our Series A Preferred Stock are entitled to designate a number of our directors roughly proportionate to their overall equity ownership, but in any event not less than a majority of our directors as long as they hold in the aggregate at least 35% of the total voting power of our equity. As a result, these holders have the ability to control our management, policies and financing decisions, elect a majority of our Board and control the vote on most matters presented to a vote of our stockholders. In addition, our shares of Series A Preferred Stock, almost all of which are beneficially owned by Resurgence, carry a cumulative dividend rate of 4% per quarter, payable in additional shares of Series A Preferred Stock. Each dividend paid in additional shares of our Series A Preferred Stock has a dilutive effect on our shares of common stock and increases the percentage of the total voting power of our equity beneficially owned by Resurgence. Series A Preferred Stock dividends were 594.832 shares, 508.465 shares and 434.638 shares during 2006, 2005 and 2004, respectively. Four of our directors, Messrs. Steve Gidumal, Byron Haney, Karl Schwarzfeld and Philip Sivin, are currently employed by Resurgence. Pursuant to established policies of Resurgence, all director compensation earned by employees of Resurgence is paid directly to Resurgence. During 2006, 2005 and 2004, we paid Resurgence an aggregate amount equal to $115,000, $177,500 and $190,750, respectively, related to director compensation for Messrs. Gidumal, Haney, Schwarzfeld and Sivin, along with reimbursement of an immaterial amount of direct, out-of-pocket expenses incurred in connection with services as directors. Mr. Gidumal became a director in November 2006.

14. NEW ACCOUNTING STANDARDS

In July 2006, the FASB issued FASB Interpretation No. 48, Accounting for Uncertainty in Income Taxes an interpretation of FASB Statement No. 109, (FIN 48) to clarify the accounting for uncertain tax positions accounted for in accordance with FASB Statement No. 109, Accounting for Income Taxes. This interpretation prescribes a two-step approach for recognizing and measuring tax benefits and requires explicit disclosure of any uncertain tax position. FIN 48 is effective for us on January 1, 2007. We do not expect the adoption of FIN 48 to have a material impact on our consolidated financial statements.

REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

To the Board of Directors and Stockholders of Sterling Chemicals, Inc.:

We have audited the accompanying consolidated balance sheets of Sterling Chemicals, Inc. and its subsidiary (the Company) as of December 31, 2006 and 2005, and the related consolidated statements of operations, changes in stockholders equity (deficiency in assets), and cash flows for each of the three years in the period ended December 31, 2006. These financial statements are the responsibility of the Company s management. Our responsibility is to express an opinion on the financial statements based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. The Company is not required to have, nor were we engaged to perform, an audit of its internal control over financial reporting. Our audits included consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Company s internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, such consolidated financial statements present fairly, in all material respects, the financial position of the Company as of December 31, 2006 and 2005, and the results of its operations and its cash flows for each of the three years in the period ended December 31, 2006, in conformity with accounting principles generally accepted in the United States of America.

As discussed in Note 8 to the Consolidated Financial Statements, the Company changed its method of accounting for defined benefit pension and other postretirement plans as of December 31, 2006.

DELOITTE & TOUCHE LLP

Houston, Texas
March 15, 2007

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STERLING CHEMICALS, INC.

SUPPLEMENTAL FINANCIAL INFORMATION
QUARTERLY FINANCIAL DATA (unaudited)

	Year	First Quarter	Second Quarter	Third Quarter	Fourth Quarter
		(Dollars in Thousands, Except Per Share Data)			
Revenues	2006	$136,670	$150,385	$189,916	$ 190,573
	2005	180,207	163,515	148,733	149,431
Gross profit (loss)	2006	(11,853)	5,482	13,334	5,863
	2005	14,370	(17,124)	4,854	(13,348)
Income (loss) from continuing operations [1]	2006	(9,135)	2,137	9,949	(107,613)
	2005	5,645	(12,965)	115	(11,303)
Income (loss) from discontinued operations, net of tax	2006	(1,254)	(496)	625	128
	2005	(3,839)	(885)	(9,164)	2,828
Net income (loss) attributable to common stockholders	2006	(12,321)	(368)	8,484	(109,659)
	2005	154	(15,569)	(10,835)	(10,332)
Net income (loss) per share of common stock:					
Basic	2006	(4.36)	(0.13)	3.00	(38.77)
	2005	0.05	(5.50)	(3.83)	(3.66)
Diluted	2006	(4.36)	(0.13)	1.60	(38.77)
	2005	0.05	(5.50)	(3.83)	(3.66)

(1) In the fourth quarter of 2006, we recorded a $128 million impairment charge to our styrene assets.

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

None.

Item 9A. ***Controls and Procedures***

We maintain disclosure controls and procedures that are designed to ensure that information required to be disclosed in our Exchange Act reports is recorded, processed, summarized and reported within the time periods specified in the rules and forms of the Securities and Exchange Commission, and that such information is accumulated and communicated to our management, including our Chief Executive Officer and Chief Financial Officer, as

appropriate, to allow timely decisions regarding required disclosure. Management necessarily applied its judgment in assessing the costs and benefits of such controls and procedures which, by their nature, can provide only reasonable assurance regarding management s control objectives.

We carried out an evaluation, under the supervision and with the participation of our management, including our Chief Executive Officer and Chief Financial Officer, of the effectiveness of the design and operation of our disclosure controls and procedures pursuant to Exchange Act Rule 13a-15, as of the end of the fiscal period covered by this Form 10-K. Based upon that evaluation, each of our Chief Executive Officer and our Chief Financial Officer concluded that our disclosure controls and procedures are effective in timely alerting them to material information relating to us (including our consolidated subsidiaries) required to be disclosed in our Exchange Act reports. In connection with our evaluation, no change was identified in our internal controls over financial reporting that occurred during the fourth

quarter of 2006 that has materially affected, or is reasonably likely to materially affect, our internal controls over financial reporting.

Beginning with our annual report on Form 10-K for 2007, we will be subject to the provisions of Section 404 of the Sarbanes-Oxley Act that require an annual management assessment of our internal controls over financial reporting.

Item 9B. ***Other Information***

In connection with our expected offering of New Notes described in Management s Discussion and Analysis of Financial Condition and Results of Operations above, we received on March 14, 2007 a firm commitment letter from Jefferies & Company, Inc. with respect to an alternate long-term debt financing. In the event our offering of New Notes is not consummated, we intend to issue $111 million in debt financing pursuant to this commitment letter in order to refinance our existing Secured Notes.

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PART III

Item 10. ***Directors, Executive Officers and Corporate Governance***

Reference is made to the information responsive to Item 10 of this Part III contained in our definitive proxy statement for our 2007 Annual Meeting of Stockholders which is hereby incorporated herein by reference in response to this item.

Item 11. ***Executive Compensation***

Reference is made to the information responsive to Item 11 of this Part III contained in our definitive proxy statement for our 2007 Annual Meeting of Stockholders which is hereby incorporated herein by reference in response to this item.

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

Reference is made to the information responsive to Item 12 of this Part III contained in our definitive proxy statement for our 2007 Annual Meeting of Stockholders which is hereby incorporated herein by reference in response to this item.

Item 13. ***Certain Relationships and Related Transactions***

Reference is made to the information responsive to Item 13 of this Part III contained in our definitive proxy statement for our 2007 Annual Meeting of Stockholders which is hereby incorporated herein by reference in response to this item.

Item 14. ***Principal Accountant Fees and Services***

Reference is made to the information responsive to Item 14 of this Part III contained in our definitive proxy statement for our 2007 Annual Meeting of Stockholders which is hereby incorporated herein by reference in response to this item.

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PART IV

Item 15. ***Exhibits and Consolidated Financial Statement Schedules***

(a) Financial Statements, Financial Statement Schedules and Exhibits.

1. Consolidated Financial Statements. See Item 8. Financial Statements and Supplementary Data Index to Financial Statements.

2. Consolidated Financial Statement Schedules. All schedules for which provision is made in Regulation S-X either are not required under the related instruction or are inapplicable and, therefore, have been omitted.

3. Exhibits. See the Exhibit Index for a list of those exhibits filed herewith, which index also includes and identifies management contracts or compensatory plans or arrangements required to be filed as exhibits to this Form 10-K by Item 601(b)(10)(iii) of Regulation S-K.

(b) Exhibit index.

Exhibit Number	Description of Exhibit
2.1	Certificate of Ownership and Merger merging Sterling Chemicals Holdings, Inc. into Sterling Chemicals, Inc. (incorporated herein by reference from Exhibit 2.1 to our Annual Report on Form 10-K for the fiscal year ended September 30, 2002).
2.2	Joint Plan of Reorganization of Sterling Chemicals Holdings, Inc., *et. al.*, Debtors, dated October 14, 2002 (incorporated herein by reference from Exhibit 2.1 to our Form 8-K filed on November 26, 2002).
2.3	First Modification to Joint Plan of Reorganization of Sterling Chemicals Holdings, Inc., *et. al.*, Debtors, dated November 18, 2002 (incorporated herein by reference from Exhibit 2.2 to our Form 8-K filed on November 26, 2002).
3.1	Amended and Restated Certificate of Incorporation of Sterling Chemicals, Inc. (conformed copy) (incorporated herein by reference from Exhibit 3.1 to our Quarterly Report on Form 10-Q for the quarterly period ended March 31, 2005).
3.2	Restated Certificate of Designations, Preferences, Rights and Limitations of Series A Convertible Preferred Stock of Sterling Chemicals, Inc. (incorporated herein by reference from Exhibit 3.2 to our Annual Report on Form 10-K for the fiscal year ended December 31, 2003).
3.3	Restated Bylaws of Sterling Chemicals, Inc. (conformed copy) (incorporated herein by reference from Exhibit 3.3 to our Quarterly Report on Form 10-Q for the quarterly period ended June 30, 2003).
4.1	Warrant Agreement dated as of December 19, 2002 by and between Sterling Chemicals, Inc., and Wells Fargo Bank Minnesota, N.A., as warrant agent (incorporated herein by reference from Exhibit 5 to our Form 8-A filed on December 19, 2002).
4.2	Registration Rights Agreement dated as of December 19, 2002 by and between Sterling Chemicals, Inc. and Resurgence Asset Management, L.L.C. (incorporated herein by reference from Exhibit 7 to our Form 8-A filed on December 19, 2002).

4.3	Tag Along Agreement dated as of December 19, 2002 by and among Sterling Chemicals, Inc., Resurgence Asset Management, L.L.C. and the Official Committee of the Unsecured Creditors (incorporated herein by reference from Exhibit 8 to our Form 8-A filed on December 19, 2002).
4.4	Indenture dated December 19, 2002 by and among Sterling Chemicals, Inc., as Issuer, Sterling Chemicals Energy, Inc., as Guarantor, and National City Bank, as Trustee, governing the 10% Senior Secured Notes due 2007 of Sterling Chemicals, Inc. (incorporated herein by reference from Exhibit T3-C to Amendment No. 3 to our Form T-3 filed on December 19, 2002).

Exhibit Number	Description of Exhibit
4.5	Deed of Trust, Assignment of Leases and Rents, Security Agreement and Fixture Filing dated December 19, 2002 made by Sterling Chemicals, Inc., as Trustor, to Thomas S. Henderson, as Individual Trustee for the benefit of National City Bank, in its capacity as described therein, as Beneficiary (incorporated herein by reference from Exhibit 4.2 to our Transition Report on Form 10-Q for the transition period ended December 31, 2002).
4.6	Security Agreement dated as of December 19, 2002 by and among Sterling Chemicals, Inc. and Sterling Chemicals Energy, Inc., as Assignors, National City Bank, as Collateral Agent, and National City Bank, as Indenture Trustee for the benefit of the holders the 10% Senior Secured Notes due 2007 of Sterling Chemicals, Inc. (incorporated herein by reference from Exhibit 4.3 to our Transition Report on Form 10-Q for the transition period ended December 31, 2002).
10.1	Revolving Credit Agreement dated as of December 19, 2002 by and among Sterling Chemicals, Inc. and Sterling Chemicals Energy, Inc., as Borrowers, the various financial institutions as are or may become parties thereto from time to time, as the Lenders, and The CIT Group/Business Credit, Inc., as the Administrative Agent for the Lenders (incorporated herein by reference from Exhibit 4.4 to our Transition Report on Form 10-Q for the transition period ended December 31, 2002).
10.1(a)	First Amendment to Revolving Credit Agreement dated as of February 12, 2003 by and among Sterling Chemicals, Inc. and Sterling Chemicals Energy, Inc., as Borrowers, the various financial institutions party thereto, as the Lenders, and The CIT Group/Business Credit, Inc., as the Administrative Agent for the Lenders (incorporated herein by reference from Exhibit 4.8 to our Transition Report on Form 10-Q for the transition period ended December 31, 2002).
10.2	Security Agreement dated as of December 19, 2002 made by Sterling Chemicals, Inc. and Sterling Chemicals Energy, Inc., as Grantors, in favor of The CIT Group/Business Credit, Inc., as Administrative Agent for the Secured Parties (incorporated herein by reference from Exhibit 4.5 to our Transition Report on Form 10-Q for the transition period ended December 31, 2002).
10.3	Pledge Agreement dated as of December 19, 2002 made by Sterling Chemicals, Inc. and Sterling Chemicals Energy, Inc., as Pledgors, in favor of The CIT Group/Business Credit, Inc., as Administrative Agent for the Secured Parties (incorporated herein by reference from Exhibit 4.6 to our Transition Report on Form 10-Q for the transition period ended December 31, 2002).
10.4*	Sterling Chemicals, Inc. Amended and Restated 2002 Stock Plan (incorporated herein by reference to Exhibit 10.1 to our Quarterly Report on Form 10-Q for the quarterly period ended September 30, 2006).
10.5*	Fifth Amended and Restated Key Employee Protection Plan (incorporated herein by reference from Exhibit 10.2 to our Quarterly Report on Form 10-Q for the quarterly period ended September 30, 2006).

10.6*	Third Amended and Restated Severance Pay Plan (incorporated herein by reference from Exhibit 10.7 to our Annual Report on Form 10-K for the fiscal year ended December 31, 2003).
10.7*	Sterling Chemicals, Inc. Amended and Restated Salaried Employees Pension Plan (incorporated herein by reference from Exhibit 10.3 to our Quarterly Report on Form 10-Q for the quarterly period ended September 30, 2006).
**10.7(a)*	First Amendment to the Sterling Chemicals, Inc. Amended and Restated Salaried Employees Pension Plan.
10.8*	Sterling Chemicals, Inc. Pension Benefit Equalization Plan (incorporated herein by reference from Exhibit 10.10 to our Registration Statement on Form S-1 (Registration No. 33-24020)).
10.8(a)*	First Amendment to Sterling Chemicals, Inc. Pension Benefit Equalization Plan (incorporated herein by reference from Exhibit 10.9(a) to our Annual Report on Form 10-K for the fiscal year ended December 31, 2004).
10.9*	Sterling Chemicals, Inc. Amended and Restated Supplemental Employee Retirement Plan (incorporated herein by reference from Exhibit 10.34 to our Annual Report on Form 10-K for the fiscal year ended September 30, 1989 (SEC File Number 1-10059)).
10.9(a)*	First Amendment to Sterling Chemicals, Inc. Amended and Restated Supplemental Employee Retirement Plan (incorporated herein by reference from Exhibit 10.10(a) to our Annual Report on Form 10-K for the fiscal year ended December 31, 2004).

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Exhibit Number	Description of Exhibit
10.10	Sterling Chemicals, Inc. Amended and Restated Hourly Paid Employees Pension Plan (Effective as of May 1, 1996) (incorporated herein by reference from Exhibit 10.3(c) to our Annual Report on Form 10-K for the fiscal year ended September 30, 1996 (SEC File Number 333-04343-01)).
10.10(a)	First Amendment to the Sterling Chemicals, Inc. Amended and Restated Hourly Paid Employees Pension Plan (Effective as of December 31, 1998) (incorporated herein by reference from Exhibit 10.7(a) to our Annual Report on Form 10-K for the fiscal year ended September 30, 2000).
10.10(b)	Second Amendment to the Sterling Chemicals, Inc. Amended and Restated Hourly Paid Employees Pension Plan (Effective as of December 17, 1998) (incorporated herein by reference from Exhibit 10.7(b) to our Annual Report on Form 10-K for the fiscal year ended September 30, 2000).
10.10(c)	Third Amendment to the Sterling Chemicals, Inc. Amended and Restated Hourly Paid Employees Pension Plan (Effective as of September 20, 1999) (incorporated herein by reference from Exhibit 10.7(c) to our Annual Report on Form 10-K for the fiscal year ended September 30, 2000).
10.10(d)	Fourth Amendment to the Sterling Chemicals, Inc. Amended and Restated Hourly Paid Employees Pension Plan (incorporated herein by reference from Exhibit 10.4 to our Transition Report on Form 10-Q for the transition period ended December 31, 2002).
10.10(e)	Fifth Amendment to the Sterling Chemicals, Inc. Amended and Restated Hourly Paid Employees Pension Plan (incorporated herein by reference from Exhibit 10.5 to our Transition Report on Form 10-Q for the transition period ended December 31, 2002).
10.10(f)	Sixth Amendment to the Sterling Chemicals, Inc. Hourly Paid Employees Pension Plan (incorporated herein by reference from Exhibit 10.3 to our Quarterly Report on Form 10-Q for the quarterly period ended June 30, 2003).
10.10(g)	Seventh Amendment to the Sterling Chemicals, Inc. Hourly Paid Employees Pension Plan (incorporated herein by reference from Exhibit 10.11(g) to our Annual Report on Form 10-K for the fiscal year ended December 31, 2003).
10.10(h)	Eighth Amendment to the Sterling Chemicals, Inc. Hourly Paid Employees Pension Plan (incorporated herein by reference from Exhibit 10.3 to our Quarterly Report on Form 10-Q for the quarterly period ended June 30, 2004).
10.10(i)	Ninth Amendment to the Sterling Chemicals, Inc. Hourly Paid Employees Pension Plan (incorporated herein by reference from Exhibit 10.3 to our Quarterly Report on Form 10-Q for the quarterly period ended June 30, 2005).
10.11*	

	Sterling Chemicals, Inc. Seventh Amended and Restated Savings and Investment Plan (incorporated herein by reference from Exhibit 10.3 to our Quarterly Report on Form 10-Q for the quarterly period ended June 30, 2006).
**10.11(a)*	First Amendment to the Seventh Amended and Restated Savings and Investment Plan.
10.12	Bonus Plan (incorporated herein by reference from Exhibit 10.12 to our Annual Report on Form 10-K for the fiscal year ended December 31, 2005).
10.13	Articles of Agreement between Sterling Chemicals, Inc., its successors and assigns, and Texas City, Texas Metal Trades Council, AFL-CIO Texas City, Texas, May 27, 2004 to May 1, 2007. (incorporated herein by reference from Exhibit 10.5 to our Quarterly Report on Form 10-Q for the quarterly period ended June 30, 2004).
10.14*	Form of Indemnity Agreement with each of its officers and directors (incorporated herein by reference from Exhibit 10.17 to our Annual Report on Form 10-K for the fiscal year ended September 30, 1996 (SEC File Number 333-04343-01)).
10.15	Separation Agreement effective as of May 31, 2005 by and among Sterling Chemicals, Inc., O&D USA LLC (d/b/a Innovene Chemicals), ANEXCO, LLC and BP Amoco Chemical Company (incorporated by reference from Exhibit 10.1 to our Form 8-K filed on May 31, 2005).
+10.16	Second Amended and Restated Production Agreement dated effective as of August 1, 1996 between BP Chemicals Inc. (predecessor in interest to BP Amoco Chemical Company) and Sterling Chemicals, Inc. (incorporated herein by reference from Exhibit 10.3 to our Quarterly Report on Form 10-Q for the quarterly period ended March 31, 1998 (SEC File Number 333-04343-01)).

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Exhibit Number	Description of Exhibit
+10.16(a)	Amendment to Second Amended and Restated Production Agreement dated as of March 1, 2001 between BP Chemicals Inc. (predecessor in interest to BP Amoco Chemical Company) and Sterling Chemicals, Inc. (incorporated herein by reference from Exhibit 10.1 to our Quarterly Report on Form 10-Q for the quarterly period ended March 31, 2001).
++10.16(b)	Amendment to Second Amended and Restated Production Agreement dated effective as of April 1, 2005 between BP Amoco Chemical Company and Sterling Chemicals, Inc.
+10.17	Second Amended and Restated Plasticizers Production Agreement dated effective as of January 1, 2006 between BASF Corporation and Sterling Chemicals, Inc. (incorporated herein by reference from Exhibit 10.19 to our Annual Report on Form 10-K for the fiscal year ended December 31, 2005).
10.18	License Agreement dated August 1, 1986 between Monsanto Company and Sterling Chemicals, Inc. (incorporated herein by reference from Exhibit 10.25 to our Registration Statement on Form S-1 (Registration No. 33-24020)).
14.1	Sterling Chemicals, Inc. Code of Ethics for the Chief Executive Officer and Senior Financial Officers (incorporated herein by reference from Exhibit 14.1 to our Quarterly Report on Form 10-Q for the quarterly period ended June 30, 2003).
**21.1	Subsidiaries of Sterling Chemicals, Inc.
**23.1	Consent of Deloitte & Touche LLP.
**31.1	Rule 13a-14(a) Certification of the Chief Executive Officer
**31.2	Rule 13a-14(a) Certification of the Chief Financial Officer
**32.1	Section 1350 Certification of the Chief Executive Officer
**32.2	Section 1350 Certification of the Chief Financial Officer
99.1	Amended and Restated Audit Committee Charter of Sterling Chemicals, Inc. (incorporated herein by reference from Exhibit 99.1 to our Annual Report on Form 10-K for the fiscal year ended December 31, 2005).
99.2	Amended and Restated Corporate Governance Committee Charter of Sterling Chemicals, Inc. (incorporated herein by reference from Exhibit 99.1 to our Quarterly Report on Form 10-Q for the quarterly period ended September 30, 2005).
99.3	Compensation Committee Charter of Sterling Chemicals, Inc. (incorporated herein by reference from Exhibit 99.1 to our Quarterly Report on Form 10-Q for the quarterly period ended September 30, 2006).

* Management contracts or compensatory plans or arrangements.

** Filed or furnished herewith.

\+ Portions of the exhibit have been omitted and filed separately with the Securities and Exchange Commission pursuant to a request for confidential treatment.

++ Filed herewith. Portions of the exhibit have been omitted and filed separately with the Securities and Exchange Commission pursuant to a request for confidential treatment.

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SIGNATURES

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

STERLING CHEMICALS, INC.
(Registrant)

By: /s/ RICHARD K. CRUMP
Richard K. Crump
President, Chief Executive Officer and Director

By: /s/ PAUL G. VANDERHOVEN
Paul G. Vanderhoven
Senior Vice President-Finance and Chief Financial Officer

Date: March 15, 2007

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

Signature	Title	Date
Principal Executive Officer:		
/s/ RICHARD K. CRUMP Richard K. Crump	President, Chief Executive Officer and Director	March 15, 2007
Principal Financial Officer:		
/s/ PAUL G. VANDERHOVEN Paul G. Vanderhoven	Senior Vice President-Finance and Chief Financial Officer	March 15, 2007
Principal Accounting Officer:		
/s/ JOHN R. BEAVER John R. Beaver	Vice President, Corporate Controller	March 15, 2007
/s/ STEVEN L. GIDUMAL Steve L. Gidumal	Director	March 15, 2007
/s/ JOHN W. GILDEA John W. Gildea	Director	March 15, 2007

/s/ BYRON J. HANEY Byron J. Haney	Director	March 15, 2007
/s/ KARL W. SCHWARZFELD Karl W. Schwarzfeld	Director	March 15, 2007
/s/ PHILIP M. SIVIN Philip M. Sivin	Director	March 15, 2007
/s/ DR. PETER TING KAI WU Dr. Peter Ting Kai Wu	Director	March 15, 2007

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EXHIBIT INDEX

Exhibit Number	Description of Exhibit
2.1	Certificate of Ownership and Merger merging Sterling Chemicals Holdings, Inc. into Sterling Chemicals, Inc. (incorporated herein by reference from Exhibit 2.1 to our Annual Report on Form 10-K for the fiscal year ended September 30, 2002).
2.2	Joint Plan of Reorganization of Sterling Chemicals Holdings, Inc., *et. al.*, Debtors, dated October 14, 2002 (incorporated herein by reference from Exhibit 2.1 to our Form 8-K filed on November 26, 2002).
2.3	First Modification to Joint Plan of Reorganization of Sterling Chemicals Holdings, Inc., *et. al.*, Debtors, dated November 18, 2002 (incorporated herein by reference from Exhibit 2.2 to our Form 8-K filed on November 26, 2002).
3.1	Amended and Restated Certificate of Incorporation of Sterling Chemicals, Inc. (conformed copy) (incorporated herein by reference from Exhibit 3.1 to our Quarterly Report on Form 10-Q for the quarterly period ended March 31, 2005).
3.2	Restated Certificate of Designations, Preferences, Rights and Limitations of Series A Convertible Preferred Stock of Sterling Chemicals, Inc. (incorporated herein by reference from Exhibit 3.2 to our Annual Report on Form 10-K for the fiscal year ended December 31, 2003).
3.3	Restated Bylaws of Sterling Chemicals, Inc. (conformed copy) (incorporated herein by reference from Exhibit 3.3 to our Quarterly Report on Form 10-Q for the quarterly period ended June 30, 2003).
4.1	Warrant Agreement dated as of December 19, 2002 by and between Sterling Chemicals, Inc., and Wells Fargo Bank Minnesota, N.A., as warrant agent (incorporated herein by reference from Exhibit 5 to our Form 8-A filed on December 19, 2002).
4.2	Registration Rights Agreement dated as of December 19, 2002 by and between Sterling Chemicals, Inc. and Resurgence Asset Management, L.L.C. (incorporated herein by reference from Exhibit 7 to our Form 8-A filed on December 19, 2002).
4.3	Tag Along Agreement dated as of December 19, 2002 by and among Sterling Chemicals, Inc., Resurgence Asset Management, L.L.C. and the Official Committee of the Unsecured Creditors (incorporated herein by reference from Exhibit 8 to our Form 8-A filed on December 19, 2002).
4.4	Indenture dated December 19, 2002 by and among Sterling Chemicals, Inc., as Issuer, Sterling Chemicals Energy, Inc., as Guarantor, and National City Bank, as Trustee, governing the 10% Senior Secured Notes due 2007 of Sterling Chemicals, Inc. (incorporated herein by reference from Exhibit T3-C to Amendment No. 3 to our Form T-3 filed on December 19, 2002).
4.5	Deed of Trust, Assignment of Leases and Rents, Security Agreement and Fixture Filing dated December 19, 2002 made by Sterling Chemicals, Inc., as Trustor, to Thomas S. Henderson, as Individual Trustee for the benefit of National City Bank, in its capacity as described therein, as Beneficiary (incorporated herein by reference from Exhibit 4.2 to our Transition Report on

	Form 10-Q for the transition period ended December 31, 2002).
4.6	Security Agreement dated as of December 19, 2002 by and among Sterling Chemicals, Inc. and Sterling Chemicals Energy, Inc., as Assignors, National City Bank, as Collateral Agent, and National City Bank, as Indenture Trustee for the benefit of the holders the 10% Senior Secured Notes due 2007 of Sterling Chemicals, Inc. (incorporated herein by reference from Exhibit 4.3 to our Transition Report on Form 10-Q for the transition period ended December 31, 2002).
10.1	Revolving Credit Agreement dated as of December 19, 2002 by and among Sterling Chemicals, Inc. and Sterling Chemicals Energy, Inc., as Borrowers, the various financial institutions as are or may become parties thereto from time to time, as the Lenders, and The CIT Group/Business Credit, Inc., as the Administrative Agent for the Lenders (incorporated herein by reference from Exhibit 4.4 to our Transition Report on Form 10-Q for the transition period ended December 31, 2002).

Exhibit Number	Description of Exhibit
10.1(a)	First Amendment to Revolving Credit Agreement dated as of February 12, 2003 by and among Sterling Chemicals, Inc. and Sterling Chemicals Energy, Inc., as Borrowers, the various financial institutions party thereto, as the Lenders, and The CIT Group/Business Credit, Inc., as the Administrative Agent for the Lenders (incorporated herein by reference from Exhibit 4.8 to our Transition Report on Form 10-Q for the transition period ended December 31, 2002).
10.2	Security Agreement dated as of December 19, 2002 made by Sterling Chemicals, Inc. and Sterling Chemicals Energy, Inc., as Grantors, in favor of The CIT Group/Business Credit, Inc., as Administrative Agent for the Secured Parties (incorporated herein by reference from Exhibit 4.5 to our Transition Report on Form 10-Q for the transition period ended December 31, 2002).
10.3	Pledge Agreement dated as of December 19, 2002 made by Sterling Chemicals, Inc. and Sterling Chemicals Energy, Inc., as Pledgors, in favor of The CIT Group/Business Credit, Inc., as Administrative Agent for the Secured Parties (incorporated herein by reference from Exhibit 4.6 to our Transition Report on Form 10-Q for the transition period ended December 31, 2002).
10.4*	Sterling Chemicals, Inc. Amended and Restated 2002 Stock Plan (incorporated herein by reference to Exhibit 10.1 to our Quarterly Report on Form 10-Q for the quarterly period ended September 30, 2006).
10.5*	Fifth Amended and Restated Key Employee Protection Plan (incorporated herein by reference from Exhibit 10.2 to our Quarterly Report on Form 10-Q for the quarterly period ended September 30, 2006).
10.6*	Third Amended and Restated Severance Pay Plan (incorporated herein by reference from Exhibit 10.7 to our Annual Report on Form 10-K for the fiscal year ended December 31, 2003).
10.7*	Sterling Chemicals, Inc. Amended and Restated Salaried Employees Pension Plan (incorporated herein by reference from Exhibit 10.3 to our Quarterly Report on Form 10-Q for the quarterly period ended September 30, 2006).
**10.7(a)*	First Amendment to the Sterling Chemicals, Inc. Amended and Restated Salaried Employees Pension Plan.
10.8*	Sterling Chemicals, Inc. Pension Benefit Equalization Plan (incorporated herein by reference from Exhibit 10.10 to our Registration Statement on Form S-1 (Registration No. 33-24020)).
10.8(a)*	First Amendment to Sterling Chemicals, Inc. Pension Benefit Equalization Plan (incorporated herein by reference from Exhibit 10.9(a) to our Annual Report on Form 10-K for the fiscal year ended December 31, 2004).
10.9*	Sterling Chemicals, Inc. Amended and Restated Supplemental Employee Retirement Plan (incorporated herein by reference from Exhibit 10.34 to our Annual Report on Form 10-K for

	the fiscal year ended September 30, 1989 (SEC File Number 1-10059)).
10.9(a)*	First Amendment to Sterling Chemicals, Inc. Amended and Restated Supplemental Employee Retirement Plan (incorporated herein by reference from Exhibit 10.10(a) to our Annual Report on Form 10-K for the fiscal year ended December 31, 2004).
10.10	Sterling Chemicals, Inc. Amended and Restated Hourly Paid Employees Pension Plan (Effective as of May 1, 1996) (incorporated herein by reference from Exhibit 10.3(c) to our Annual Report on Form 10-K for the fiscal year ended September 30, 1996 (SEC File Number 333-04343-01)).
10.10(a)	First Amendment to the Sterling Chemicals, Inc. Amended and Restated Hourly Paid Employees Pension Plan (Effective as of December 31, 1998) (incorporated herein by reference from Exhibit 10.7(a) to our Annual Report on Form 10-K for the fiscal year ended September 30, 2000).
10.10(b)	Second Amendment to the Sterling Chemicals, Inc. Amended and Restated Hourly Paid Employees Pension Plan (Effective as of December 17, 1998) (incorporated herein by reference from Exhibit 10.7(b) to our Annual Report on Form 10-K for the fiscal year ended September 30, 2000).
10.10(c)	Third Amendment to the Sterling Chemicals, Inc. Amended and Restated Hourly Paid Employees Pension Plan (Effective as of September 20, 1999) (incorporated herein by reference from Exhibit 10.7(c) to our Annual Report on Form 10-K for the fiscal year ended September 30, 2000).

Exhibit Number	Description of Exhibit
10.10(d)	Fourth Amendment to the Sterling Chemicals, Inc. Amended and Restated Hourly Paid Employees Pension Plan (incorporated herein by reference from Exhibit 10.4 to our Transition Report on Form 10-Q for the transition period ended December 31, 2002).
10.10(e)	Fifth Amendment to the Sterling Chemicals, Inc. Amended and Restated Hourly Paid Employees Pension Plan (incorporated herein by reference from Exhibit 10.5 to our Transition Report on Form 10-Q for the transition period ended December 31, 2002).
10.10(f)	Sixth Amendment to the Sterling Chemicals, Inc. Hourly Paid Employees Pension Plan (incorporated herein by reference from Exhibit 10.3 to our Quarterly Report on Form 10-Q for the quarterly period ended June 30, 2003).
10.10(g)	Seventh Amendment to the Sterling Chemicals, Inc. Hourly Paid Employees Pension Plan (incorporated herein by reference from Exhibit 10.11(g) to our Annual Report on Form 10-K for the fiscal year ended December 31, 2003).
10.10(h)	Eighth Amendment to the Sterling Chemicals, Inc. Hourly Paid Employees Pension Plan (incorporated herein by reference from Exhibit 10.3 to our Quarterly Report on Form 10-Q for the quarterly period ended June 30, 2004).
10.10(i)	Ninth Amendment to the Sterling Chemicals, Inc. Hourly Paid Employees Pension Plan (incorporated herein by reference from Exhibit 10.3 to our Quarterly Report on Form 10-Q for the quarterly period ended June 30, 2005).
10.11*	Sterling Chemicals, Inc. Seventh Amended and Restated Savings and Investment Plan (incorporated herein by reference from Exhibit 10.3 to our Quarterly Report on Form 10-Q for the quarterly period ended June 30, 2006).
**10.11(a)*	First Amendment to the Seventh Amended and Restated Savings and Investment Plan.
10.12	Bonus Plan (incorporated herein by reference from Exhibit 10.12 to our Annual Report on Form 10-K for the fiscal year ended December 31, 2005).
10.13	Articles of Agreement between Sterling Chemicals, Inc., its successors and assigns, and Texas City, Texas Metal Trades Council, AFL-CIO Texas City, Texas, May 27, 2004 to May 1, 2007. (incorporated herein by reference from Exhibit 10.5 to our Quarterly Report on Form 10-Q for the quarterly period ended June 30, 2004).
10.14*	Form of Indemnity Agreement with each of its officers and directors (incorporated herein by reference from Exhibit 10.17 to our Annual Report on Form 10-K for the fiscal year ended September 30, 1996 (SEC File Number 333-04343-01)).
10.15	Separation Agreement effective as of May 31, 2005 by and among Sterling Chemicals, Inc., O&D USA LLC (d/b/a Innovene Chemicals), ANEXCO, LLC and BP Amoco Chemical Company (incorporated by reference from Exhibit 10.1 to our Form 8-K filed on May 31, 2005).
+10.16	Second Amended and Restated Production Agreement dated effective as of August 1, 1996 between BP Chemicals Inc. (predecessor in interest to BP Amoco Chemical Company) and

	Sterling Chemicals, Inc. (incorporated herein by reference from Exhibit 10.3 to our Quarterly Report on Form 10-Q for the quarterly period ended March 31, 1998 (SEC File Number 333-04343-01)).
+10.16(a)	Amendment to Second Amended and Restated Production Agreement dated as of March 1, 2001 between BP Chemicals Inc. (predecessor in interest to BP Amoco Chemical Company) and Sterling Chemicals, Inc. (incorporated herein by reference from Exhibit 10.1 to our Quarterly Report on Form 10-Q for the quarterly period ended March 31, 2001).
++10.16(b)	Amendment to Second Amended and Restated Production Agreement dated effective as of April 1, 2005 between BP Amoco Chemical Company and Sterling Chemicals, Inc.
+10.17	Second Amended and Restated Plasticizers Production Agreement dated effective as of January 1, 2006 between BASF Corporation and Sterling Chemicals, Inc. (incorporated herein by reference from Exhibit 10.19 to our Annual Report on Form 10-K for the fiscal year ended December 31, 2005).
10.18	License Agreement dated August 1, 1986 between Monsanto Company and Sterling Chemicals, Inc. (incorporated herein by reference from Exhibit 10.25 to our Registration Statement on Form S-1 (Registration No. 33-24020)).

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Exhibit Number	Description of Exhibit
14.1	Sterling Chemicals, Inc. Code of Ethics for the Chief Executive Officer and Senior Financial Officers (incorporated herein by reference from Exhibit 14.1 to our Quarterly Report on Form 10-Q for the quarterly period ended June 30, 2003).
**21.1	Subsidiaries of Sterling Chemicals, Inc.
**23.1	Consent of Deloitte & Touche LLP.
**31.1	Rule 13a-14(a) Certification of the Chief Executive Officer
**31.2	Rule 13a-14(a) Certification of the Chief Financial Officer
**32.1	Section 1350 Certification of the Chief Executive Officer
**32.2	Section 1350 Certification of the Chief Financial Officer
99.1	Amended and Restated Audit Committee Charter of Sterling Chemicals, Inc. (incorporated herein by reference from Exhibit 99.1 to our Annual Report on Form 10-K for the fiscal year ended December 31, 2005).
99.2	Amended and Restated Corporate Governance Committee Charter of Sterling Chemicals, Inc. (incorporated herein by reference from Exhibit 99.1 to our Quarterly Report on Form 10-Q for the quarterly period ended September 30, 2005).
99.3	Compensation Committee Charter of Sterling Chemicals, Inc. (incorporated herein by reference from Exhibit 99.1 to our Quarterly Report on Form 10-Q for the quarterly period ended September 30, 2006).

* Management contracts or compensatory plans or arrangements.

** Filed or furnished herewith.

\+ Portions of the exhibit have been omitted and filed separately with the Securities and Exchange

Commission pursuant to a request for confidential treatment.

++ Filed herewith. Portions of the exhibit have been omitted and filed separately with the Securities and Exchange Commission pursuant to a request for confidential treatment.