Atlantica Tender Drilling Ltd. & Subsidiaries

Consolidated Financial Statements

For the Quarter Ended
September 30, 2016

Atlantica Tender Drilling Ltd. & Subsidiaries

Consolidated Financial Statements

For the Quarter Ended
September 30, 2016

Atlantica Tender Drilling Ltd. & Subsidiaries

Contents

Consolidated Financial Statements

Atlantica Tender Drilling Ltd. & Subsidiaries

Consolidated Balance Sheets

	September 30, 2016	December 31, 2015 (Audited)
Assets		
Current Assets		
Cash and cash equivalents	$ 35,791,207	$ 31,552,914
Restricted cash	9,213,700	1,657,014
Accounts receivable	17,753,744	38,054,827
Accounts receivable - related parties	291,506	633,988
Note receivable - related parties	1,193,204	1,150,158
Prepaid and other current assets	3,985,946	3,879,210
Total Current Assets	68,229,307	76,928,111
Property and Equipment, Net	545,868,373	543,703,734
Equity Investment	641,018	6,069,757
Other Assets	18,820,233	18,733,627
Total Assets	$ 633,558,931	$ 645,435,229

See Notes to Consolidated Financial Statements.

Atlantica Tender Drilling Ltd. & Subsidiaries

Consolidated Balance Sheets

	September 30, 2016	December 31, 2015 (Audited)
Liabilities and Stockholders' Equity		
Current Liabilities		
Accounts payable	$ 4,048,159	$ 5,698,824
Accounts payable - related party	244,650	288,237
Accrued liabilities	8,748,509	13,570,070
Current portion of long-term debt	25,555,556	20,638,888
Deferred revenue - current	20,695,396	19,231,335
Total Current Liabilities	59,292,270	59,427,354
Long-Term Liabilities		
Deferred revenue - non-current	26,823,414	39,543,561
Long-term debt, net	324,745,674	341,520,848
Other long term liabilities	2,926,153	-
Total Long-Term Liabilities	354,495,241	381,064,409
Total Liabilities	413,787,511	440,491,763
Commitments and Contingencies (Note 9)		
Stockholders' Equity		
Common stock, $0.10 par value, 310,000,000 shares authorized at September 30, 2016 and December 31, 2015; 261,323,309 shares issued at September 30, 2016 and December 31, 2015; and 257,284,809 and 261,323,309 shares outstanding at September 30, 2016 and December 31, 2015, respectively	26,132,331	26,132,331
Additional paid-in capital	213,186,826	213,122,668
Treasury stock (4,038,500 shares at cost)	(773,620)	-
Subscription receivable	(1,500)	(1,500)
Accumulated deficit	(18,772,617)	(34,310,033)
Total Stockholders' Equity	219,771,420	204,943,466
Total Liabilities and Stockholders' Equity	$ 633,558,931	$ 645,435,229

See Notes to Consolidated Financial Statements.

Atlantica Tender Drilling Ltd. & Subsidiaries

Consolidated Statements of Income

	Three Months Ended September 30, 2016	Three Months Ended September 30, 2015	Nine Months Ended September 30, 2016	Nine Months Ended September 30, 2015
Revenues				
Contract drilling	$ 31,507,677	$ 17,232,805	$ 97,592,525	$ 48,608,746
Amortization of deferred revenue	5,183,777	3,077,349	14,523,020	9,131,699
Management fees	414,000	414,000	1,233,000	1,437,050
Total Revenues	37,105,454	20,724,154	113,348,545	59,177,495
Operating Expenses				
Operating	17,394,082	10,512,818	48,752,098	34,063,696
Depreciation and amortization	6,847,787	3,369,030	18,911,631	9,967,635
(Gain)/loss on cancellation of construction cor	(49,363)	-	174,207	-
Total Operating Expenses	24,192,506	13,881,848	67,837,936	44,031,331
Income from Operations	12,912,948	6,842,306	45,510,609	15,146,164
Other Income (Expense)				
Interest income	21,078	-	85,615	15
Interest expense	(5,036,859)	(2,826,089)	(18,687,374)	(8,810,494)
Foreign currency loss	(27,031)	(167,487)	(166,448)	(471,902)
Total Other Expense	(5,042,812)	(2,993,576)	(18,768,207)	(9,282,381)
Income Before Equity in Earnings/(Losses) of Affiliate, Loss on BDA Restructure and Foreign Income Tax Expense	7,870,136	3,848,730	26,742,402	5,863,783
Equity in Earnings/(Losses) of Affiliate	(204,452)	(1,148,088)	(2,374,115)	1,614,721
Loss on BDA Restructure	-	-	(3,054,624)	-
Foreign Income Tax Expense	(2,117,754)	(595,260)	(5,776,247)	(1,868,058)
Net Income	$ 5,547,930	$ 2,105,382	$ 15,537,416	$ 5,610,446
Net Income Per Share				
Basic and diluted	$ 0.02	$ 0.02	$ 0.06	$ 0.04
Weighted Average Shares Outstanding				
Basic and diluted	261,147,722	129,439,252	261,264,353	128,473,377

See Notes to Consolidated Financial Statements.

Atlantica Tender Drilling Ltd. & Subsidiaries

Consolidated Statements of Stockholders' Equity

	Common Stock		Additional Paid-in Capital	Treasury Stock	Subscription Receivable	Accumulated Deficit	Total Stockholders' Equity
	Shares	Amount					
Balance at January 1, 2015	127,989,977	$ 12,798,998	$ 187,109,447	$ -	$ (1,500)	$ (20,762,626)	$ 179,144,319
Common stock issued	133,333,332	13,333,333	26,666,667	-	-	-	40,000,000
Stock issuance costs	-	-	(800,089)	-	-	-	(800,089)
Stock compensation expense	-	-	146,643	-	-	-	146,643
Net loss	-	-	-	-	-	(13,547,407)	(13,547,407)
Balance at December 31, 2015	261,323,309	$ 26,132,331	$ 213,122,668	$ -	$ (1,500)	$ (34,310,033)	$ 204,943,466
Stock compensation expense	-	-	64,158		-	-	64,158
Treasury stock acquired	-	-	-	(773,620)	-	-	(773,620)
Net income	-	-	-		-	15,537,416	15,537,416
Balance at September 30, 2016	261,323,309	$ 26,132,331	$ 213,186,826	$ (773,620)	$ (1,500)	$ (18,772,617)	$ 219,771,420

See Notes to Consolidated Financial Statements.

Atlantica Tender Drilling Ltd. & Subsidiaries

Consolidated Statements of Cash Flows

	Three Months Ended September 30, 2016	Three Months Ended September 30, 2015	Nine Months Ended September 30, 2016	Nine Months Ended September 30, 2015
Cash Flows From Operating Activities				
Net income	$ 5,547,930	$ 2,105,382	$ 15,537,416	$ 5,610,446
Adjustments to reconcile net income to net cash provided by operating activities:				
Equity in (earnings)/losses of affiliate	204,452	1,148,088	2,374,115	(1,614,721)
Loss on BDA Restructure	-	-	3,054,624	-
Depreciation and amortization	6,847,787	3,369,030	18,911,631	9,967,635
(Gain)/loss on cancellation of construction contract	(49,363)	-	174,207	-
Stock compensation expense	16,626	38,046	64,158	108,597
Noncash interest (income) expense, net	(495,484)	585,274	3,461,873	1,776,874
Changes in operating assets and liabilities:				
Accounts receivable	(4,185,282)	4,059,559	(10,108,683)	126,510
Accounts and note receivable - related parties	158,719	179,367	342,482	(110,488)
Prepaid expenses and other assets	302,298	(1,207,993)	1,750,227	(382,530)
Accounts payable	(252,867)	3,628,154	(1,696,029)	(859,794)
Accounts payable - related party	(1,329)	84,855	172,439	84,855
Accrued liabilities	(283,048)	549,264	(5,037,587)	(1,429,237)
Deferred revenue	(3,947,267)	(3,077,349)	19,003,680	(9,131,699)
Net Cash Provided By Operating Activities	3,863,172	11,461,677	48,004,553	4,146,448
Cash Flows From Investing Activities				
Capital expenditures for construction in progress	-	(11,517,946)	(7,421,878)	(24,449,426)
Capital expenditures for drilling rig and equipment, furniture, office equipment and leasehold improvements	(3,319,625)	(669,596)	(13,451,218)	(2,652,302)
Net Cash Used In Investing Activities	(3,319,625)	(12,187,542)	(20,873,096)	(27,101,728)
Cash Flows from Financing Activities				
Payments on long term debt	(6,388,889)	(1,472,223)	(14,250,000)	(4,416,667)
Proceeds from common stock issuance	-	35,447,065	-	35,447,065
Change in restricted cash	834,331	92,768	(7,556,686)	(708,398)
Acquisition of treasury stock, net	(773,620)	-	(773,620)	-
Debt issuance costs	-	-	(312,858)	(305,188)
Net Cash Provided By (Used In) Financing Activities	(6,328,178)	34,067,610	(22,893,164)	30,016,812
Net Increase/(Decrease) In Cash and Cash Equivalents	(5,784,631)	33,341,745	4,238,293	7,061,532
Cash and Cash Equivalents - Beginning of Period	41,575,838	13,812,860	31,552,914	40,093,073
Cash and Cash Equivalents - End of Period	$ 35,791,207	$ 47,154,605	$ 35,791,207	$ 47,154,605
Supplemental Cash Flow Information				
Cash paid for interest	$ 6,065,020	$ 4,476,925	$ 15,386,322	$ 13,476,477
Cash paid for income taxes	2,196,103	573,176	4,719,435	1,815,815
Supplemental Non Cash Information				
Capitalization of interest to property and equipment	$ -	$ 2,733,147	$ 1,322,895	$ 7,839,656

See Notes to Consolidated Financial Statements.

1. Organization and Nature of Operations

Atlantica Tender Drilling Ltd. (“Atlantica”) was incorporated in Bermuda in September 2008 and in April 2011 became registered on the Norwegian OTC-list under the symbol “ATDL.” Atlantica is in the business of providing management and contract drilling services for oil and gas wells for the offshore tender assist market and related offshore oilfield services, for both Company-owned and affiliated vessels.

The following entities are wholly-owned subsidiaries of the Company:

- Atlantica Management (USA) Inc. (“AM”), incorporated in the state of Texas
- Atlantica International Ltd. (“AI”), a Bermuda-based entity
- Atlantica Beta Ltd. (“AB”), a Bermuda-based entity
- BassDrill Beta Ltd. (“BDB”), a Malta-based entity
- BassDrill Beta B.V. (“BDB-BV”), a Holland-based entity
- BassDrill Brasil Servicos de Petroleo Ltda. (“BBB”), a Brazil-based entity
- Atlantica International B.V. (“AI-BV”), a Holland-based entity
- Atlantica (Malta) Holding Ltd., (“AMH”), a Malta-based entity
- Atlantica Gamma Ltd. (“AG”), a Malta-based entity
- Atlantica Delta Ltd. (“AD”), a Malta-based entity

The Company’s primary assets and liabilities currently pertain to *BassDrill Beta*, owned by BDB, which the Company took delivery in November 2013 and was placed into service on a drilling contract with Petróleo Brasileiro S.A. (“Petrobras”) in March 2014; and *Atlantica Delta*, owned by AD, which the Company took delivery in December 2015 and was placed into service on a drilling contract with Total Congo E&P (“Total”) in January 2016; and AM.

As used herein, and unless otherwise required by the context, the term “Atlantica” refers to Atlantica Tender Drilling Ltd., and the terms “Company,” “we,” “our,” and words of similar import refer to Atlantica and its Subsidiaries. The use herein of such terms as “we,” “us,” “our” and “its,” or references to specific entities, is not intended to be a precise description of corporate relationships.

2. Summary of Significant Accounting Policies

The unaudited interim consolidated financial statements reflect all adjustments that are, in the opinion of management, necessary for a fair statement of the results for the interim period on a basis consistent with the annual consolidated financial statements. All such adjustments are of a normal recurring nature.

The accompanying consolidated financial statements and notes thereto should be read in conjunction with the audited consolidated financial statements and notes thereto as of December 31, 2015 and 2014.

Principles of Consolidation

The consolidated financial statements include the assets and liabilities of Atlantica and its subsidiaries. All intercompany balances and transactions have been eliminated in consolidation.

Use of Estimates

The preparation of the consolidated financial statements in conformity with accounting principles generally accepted in the United States of America ("GAAP") requires management to make estimates and assumptions that affect the reported amounts of assets, liabilities, revenues and expenses and requires management to disclose contingent assets and liabilities at the date of the financial statements. While management believes current estimates are reasonable and appropriate, actual results could differ from those estimates.

Fair Value of Financial Instruments

Financial Accounting Standards Board Accounting Standards Codification ("ASC") Topic 820, *Fair Value Measurements*, establishes a common definition for fair value to be applied to existing GAAP that require the use of fair value measurements, establishes a framework for measuring fair value and expands disclosure about such fair value measurements. GAAP defines fair value as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date and establishes a three-level valuation hierarchy for disclosure of fair value measurements. The valuation hierarchy categorizes assets and liabilities measured at fair value into one of three different levels depending on the observability of the inputs employed in the measurement. The three levels are defined as follows:

Level 1 – Observable inputs such as quoted prices in active markets at the measurement date for identical, unrestricted assets or liabilities.

Level 2 - Other inputs that are observable directly or indirectly such as quoted prices in markets that are not active, or inputs which are observable, either directly or indirectly, for substantially the full term of the asset or liability.

Level 3 – Unobservable inputs for which there is little or no market data and which the Company makes its own assumptions about how market participants would price the assets and liabilities.

The Company's fair value of financial instruments disclosure is based upon information available to management as of September 30, 2016 and December 31, 2015. Considerable judgment is necessary to interpret market data and develop estimated fair value. Accordingly, the estimates presented herein are not necessarily indicative of the amounts the Company could realize on disposition of the financial instruments. The use of different market assumptions and/or estimation methodologies may have a material effect on the estimated fair value amounts.

The Company's financial instruments consist mainly of cash and cash equivalents, restricted cash, accounts receivable, accounts payable, accrued liabilities, interest rate swaps and long-term debt. The carrying values for cash and cash equivalents, restricted cash, accounts receivable, accounts payable and accrued liabilities approximate their fair value, principally due to the short-term nature of these instruments. The carrying value of the Senior Secured Term Loan approximates fair value as the interest rate is re-determined regularly based on current interest rates. The fair value of the Senior Secured Bonds at September 30, 2016 was approximately $82.5 million based on quoted market prices, a Level 1 in the fair value hierarchy.

Revenue

Contract Drilling: Contract drilling revenue is recognized as services are performed based on contracted day-rates and the number of operating days during the period. These revenues are netted for commissions based on a percentage of the contract drilling revenue.

Amortization of deferred revenue: In connection with a customer contract, the Company may receive lump-sum fees for the mobilization of equipment and personnel. Mobilization fees and costs incurred to mobilize a rig from one geographic market to another are deferred and recognized on a straight-line basis over the initial term of such contract, excluding any option periods. Costs incurred to mobilize a rig without a contract are expensed as incurred. The costs of capital improvements are capitalized and depreciated over the useful lives of the assets.

Management Fees: AM provides management and consulting services to BassDrill Alpha Ltd. (“BDA”). Such fees are day-rate based and are recorded as revenues in the period in which they are provided to BDA.

Equity Investment

On July 20, 2016, the Company’s investment ownership in BDA was reduced from a direct interest of 25.26% to an indirect interest of 3.79% following BDA’s restructuring arrangement (see Note 5). As a result of the restructure, the Company accounts for its investment in BDA using the cost method of accounting in which the Company only recognizes dividends received from BDA as income.

Prior to July 20, 2016, the Company accounted for its investment in BDA using the equity method of accounting as the Company had the ability to exercise significant influence over, but not control of BDA’s operations and financial affairs (see Note 5). Under the equity method of accounting, the Company’s proportionate share of BDA’s income or loss was reported in the consolidated statements of income.

The Company analyzes its investment in BDA for impairment during each reporting period to evaluate whether an event or change in circumstances has occurred in that period that may have a significant, adverse effect on the fair value of its investment. The Company records an impairment charge for other-than-temporary declines in fair value when the fair value is not anticipated to recover above cost within a reasonable period after the measurement date unless there are mitigating factors that indicate impairment may not be required. If an impairment charge is recorded, subsequent recoveries in fair value are not reflected in earnings until the investee is sold. The Company recognized a $3.1 million loss in June 2016 due to the decrease in ownership associated with the BDA restructuring arrangement (see Note 5). There was no impairment for the three months ended September 30, 2016 and 2015 or the nine months ended September 30, 2015.

Cash and Cash Equivalents

The Company considers all highly liquid investments purchased with an original maturity of three months or less to be cash equivalents.

Restricted Cash

The Senior Secured Term Loan and Senior Secured Bonds (see Note 6) requires the Company to maintain a debt service account, into which one-third of the next quarterly interest and installment payment is to be paid each month.

Accounts Receivable and Allowance for Doubtful Accounts

The Company's revenue and related customer receivables are generated from services to international oil companies and government-owned or government-controlled companies. The Company does not require collateral or other security to support customer receivables.

The Company establishes an allowance for doubtful accounts on a specific identification method, considering changes in the financial position of a customer, when the Company believes the payment of a receivable is unlikely to occur. There was no allowance for doubtful accounts at September 30, 2016 and December 31, 2015.

Accounts receivable also include accrued receivables which are estimates of the Company's contract drilling revenue for the period but unbilled at period end. At September 30, 2016 and December 31, 2015, accounts receivable included $7.8 million and $1.5 million, respectively, of accrued receivables.

Concentrations of Credit Risk

The Company's customer concentration may impact its overall credit risk, either positively or negatively, in that customers may be similarly and concurrently affected by changes in economic or other conditions affecting the drilling industry. The Company's percent of revenue by major customer is as follows:

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2016	2015	2016	2015
Petrobras	61%	98%	59%	97%
Total	38%	-	40%	-

The Company is subject to concentrations of credit risk with respect to cash and cash equivalents, which the Company attempts to minimize by maintaining cash and cash equivalents with major high credit quality financial institutions. At times cash and cash equivalents balances may exceed limits federally insured by the United States Federal Deposit Insurance Corporation or other similar government institutions in other countries. Additionally, certain of the Company's cash and cash equivalents balances are maintained in foreign banks, which are not covered by deposit insurance. The Company has not experienced any losses on its cash and cash equivalents.

Foreign Exchange Transactions

The Company's functional currency is the United States (U.S.) dollar as the Company primarily contracts with contractors, finances capital, and purchases equipment and services using the U.S. dollar. Transactions that are completed in a foreign currency are translated into U.S. dollars, and any gain or loss is recorded in the consolidated statements of operations.

Property and Equipment

Property and equipment is carried at cost less accumulated depreciation and amortization. The Company capitalizes expenditures for renewals, replacements and improvements, and expenses costs of maintenance and repairs as incurred. Depreciation on property and equipment is calculated on the straight-line method over the estimated useful lives of the assets. Depreciation and amortization expense was $6.8 million and $3.4 million for the three months ended September 30, 2016 and, 2015, respectively, and $18.9 million and $10.0 million for the nine months ended September 30, 2016 and 2015, respectively. The estimated useful lives, in years, are defined below:

Drilling rigs and equipment:	
Barge and related marine equipment	30 years
Mast equipment package, spare parts and related equipment	4 - 15 years
Leasehold improvements	Remaining life of lease
Furniture and office equipment	3 - 5 years
Computer hardware and software	3 years
Vehicles	5 years

Construction in Progress and Capital Spares

The carrying value of the rigs under construction (*Atlantica Delta* at December 31, 2015) represents the accumulated costs at the balance sheet date. Cost components include payments for yard installments and variation orders, construction supervision, equipment, spare parts and capitalized interest. No charges for depreciation will be made until commissioning is completed, and the vessel is ready for its intended use.

Capital spares are not subject to depreciation until put into use on the rig.

Capitalized Interest

Interest expenses, excluding commitment fees, are capitalized during construction of the rigs based on accumulated expenditures for the applicable project at the Company's current rate of borrowing. The amount of interest expense capitalized in an accounting period is determined by applying the capitalization rate to the average amount of accumulated expenditures for the asset during the period. The capitalization rate used in an accounting period is based on the rates applicable to borrowings outstanding during the period. The Company does not capitalize amounts beyond the actual interest expense incurred in the period. As the average accumulated expenditures for *BassDrill Beta*, *Atlantica Gamma* and *Atlantica Delta* exceeded the amounts of the specific new borrowing associated with the asset, the capitalization rate applied to such expenditures was a weighted average of the rates applicable to other borrowings of the Company.

Commitment fees associated with the tranches for *Atlantica Gamma* and *Atlantica Delta* under the Senior Term Loan (discussed below in Note 6) were considered exclusively related to *Atlantica Gamma* and *Atlantica Delta* and fully capitalized to each asset. The Company capitalized commitment fees directly associated with *Atlantica Gamma* and *Atlantica Delta* of $-0- and $1.1 million for the three months ended September 30, 2016 and 2015, respectively, and $-0- and $3.1 million for the nine months ended September 30, 2016 and 2015, respectively.

Impairment of Long-lived Assets

Long-lived assets, such as property, plant, and equipment are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. If circumstances require a long-lived asset be tested for possible impairment, the Company first compares undiscounted cash flows expected to be generated by an asset to the carrying value of the asset in accordance with ASC 360, *Property, Plant and Equipment*. If the carrying value of the long-lived asset is not recoverable on an undiscounted cash flow basis, impairment is recognized to the extent that the carrying value exceeds its fair value. Fair value is determined through various valuation techniques, including undiscounted cash flow models, quoted market values and third party appraisals, as considered necessary.

Income Taxes

The Company is a Bermuda limited liability company. Bermuda does not impose corporate income taxes unless activities are carried out in Bermuda. No activities were carried out in Bermuda in the three and nine months ended September 30, 2016 and 2015. Consequently, the Company has provided income taxes based on the laws and rates in effect in the countries in which operations are conducted, or in which the Company and/or its subsidiaries are considered resident for income tax purposes. The Company and or/or its subsidiaries operates in multiple countries under different legal forms. As a result, the Company is subject to the jurisdiction of numerous domestic and foreign tax authorities, as well as to tax agreements and treaties among these governments. The Company's operations in these different jurisdictions are taxed on various bases including, actual income before taxes, deemed profits (which are generally determined by applying a tax rate to revenues rather than profits) and withholding taxes based on revenue. Determination of taxable income in any jurisdiction requires the interpretation of the related tax laws and regulations and the use of estimates and assumptions regarding significant future events, such as the amount, timing and character of deductions, permissible revenue recognition methods under the tax law and the sources and character of income and tax credits. Changes in tax laws, regulations, agreements and treaties, foreign currency exchange restrictions or the Company's level of operations or profitability in each tax jurisdiction could have an impact upon the amount of income taxes that the Company provides during any given year.

The Company follows guidance issued by the Financial Accounting Standards Board which clarifies accounting for uncertainty in income taxes by prescribing the minimum recognition threshold an income tax position is required to meet before being recognized in the financial statements and applies to all income tax positions. Each income tax position is assessed using a two-step process. A determination is first made as to whether it is more likely than not that the income tax position will be sustained, based upon technical merits, upon examination by the taxing authorities. If the income tax position is expected to meet the more likely than not criteria, the benefit recorded in the financial statements equals the largest amount that is greater than 50% likely to be realized upon its ultimate settlement.

The Company believes that it has no uncertain income tax positions and that there are no tax positions taken or expected to be taken that would significantly increase or decrease unrecognized tax benefits within the next twelve months.

In accordance with this guidance, the Company will record income tax related interest and penalties, if applicable, as a component of the provision for income tax expense. However, there were no amounts recognized for income tax related interest and penalties in the statements of income for the three and nine months ended September 30, 2016 and 2015.

Share-Based Compensation

The Company has established an employee share ownership plan under which certain of its officers and board members have been and may be allocated options to acquire shares in Atlantica Tender Drilling Ltd. The compensation cost for stock options is recognized as an expense over the service period based on the fair value of the options granted.

The fair value of the share options issued under the Company's share option plan is determined at grant date taking into account the terms and conditions upon which the options are granted, and using a valuation technique that is consistent with generally accepted valuation methodologies for pricing financial instruments, and that incorporates all factors and assumptions that knowledgeable, willing market participants would consider in determining fair value. The fair value of the share options is recognized as personnel expenses within operating expenses with a corresponding increase in stockholders' equity over the period during which the employees become vested.

Stock compensation expense is initially recognized based upon options expected to vest with appropriate adjustments to reflect actual forfeitures.

Earnings Per Share

Basic earnings per share ("EPS") is calculated based on the income (loss) for the period available to common stockholders divided by the weighted average number of shares outstanding for basic EPS for the period. Diluted EPS includes the effect of the assumed conversion of potentially dilutive instruments, which for the Company includes share options. The determination of dilutive earnings per share requires the Company to potentially make certain adjustments to the weighted average shares outstanding used to compute basic earnings per share unless anti-dilutive.

Reclassifications

Certain reclassifications have been made to prior period consolidated financial statements to conform current period presentations. These reclassifications had no effect on the Company's consolidated financial position, results of income or cash flows.

Subsequent Events

The Company evaluated all activity through December 21, 2016, the date the consolidated financial statements were available for issuance, and concluded that no subsequent events, other than those already disclosed, have occurred that would require recognition on the consolidated financial statements or disclosures in the notes to the consolidated financial statements.

3. Property and Equipment

Property and equipment consisted of the following:

	September 30, 2016	December 31, 2015
Drilling rig and equipment	$ 583,831,518	$ 299,739,754
Leasehold improvements	172,576	170,876
Furniture and office equipment	165,702	157,821
Computer hardware and software	824,398	785,897
Vehicles	181,261	181,261
	585,175,455	301,035,609
Less: accumulated depreciation	42,951,360	24,039,729
	542,224,095	276,995,880
Construction in progress	-	263,399,095
Inventory - capital spares	3,644,278	3,308,759
Property and equipment, net	$ 545,868,373	$ 543,703,734

Construction in progress – *Atlantica Delta*. At December 31, 2015, construction in progress included costs relating to *Atlantica Delta*, a semi-submersible rig, of $263.4 million. In December 2015, the Company took delivery of the rig, and the rig was deemed operational at the end of January 2016.

4. Interest Cost

The Company capitalizes interest cost as a component of construction in progress. The following is a summary of interest cost incurred:

	Three Months Ended September 30, 2016	Three Months Ended September 30, 2015	Nine Months Ended September 30, 2016	Nine Months Ended September 30, 2015
Interest cost capitalized	$ -	$ 2,733,147	$ 1,322,895	$ 7,839,656
Interest cost expensed	5,036,859	2,826,089	18,687,374	8,810,494
Total interest cost incurred	$ 5,036,859	$ 5,559,236	$ 20,010,269	$ 16,650,150

5. Equity Investment

The Company owns an investment in BDA. BDA is a Bermuda-based vessel owning company in the business of providing offshore tender assist drilling services to the offshore market. The BDA tender assist barge, *BassDrill Alpha*, was operating under a contract in West Africa. In May 2015, the contract was terminated early, and *BassDrill Alpha* is currently stacked while the Company markets the unit to other operators in West-Africa and Southeast Asia.

Prior to July 20, 2016, the Company's ownership interest in BDA was a direct interest of 25.26%. In July 2016, in order to address its liquidity needs while the *BassDrill Alpha* is stacked, the bondholders and shareholders of BDA completed a capital restructuring arrangement. The restructure resulted in the bondholders owning an indirect interest of 85% in BDA and the original

BDA shareholders owning an indirect interest of 15% in BDA. Consequently, the Company's effective ownership share in BDA was reduced to an indirect ownership of 3.79%. As result of the restructure and the corresponding reduction in ownership of BDA, the Company recorded an impairment of $3.1 million for the nine months ended September 30, 2016.

See Note 14 for an additional BDA restructuring transaction completed in November 2016.

Condensed balance sheets for BDA are as follows:

	September 30, 2016	December 31, 2015
Current assets	$ 3,503,156	$ 8,819,366
Property and equipment, net	76,777,958	80,014,927
Other assets	1,882,218	5,362,649
Total assets	$ 82,163,332	$ 94,196,942
Current liabilities	$ 501,574	$ 69,943,086
Long-term liabilities	69,419,253	-
Stockholders' equity	12,242,505	24,253,856
Total liabilities and stockholders' equity	$ 82,163,332	$ 94,196,942

Condensed statements of operations for BDA are as follows:

	Three Months Ended September 30, 2016	Three Months Ended September 30, 2015	Nine Months Ended Sepetmber 30, 2016	Nine Months Ended Sepetmber 30, 2015
Operating revenues	$ -	$ -	$ -	$ 29,153,028
Costs and expenses	(3,076,225)	(3,181,593)	(8,615,011)	(17,142,098)
Income (loss) from operations	(3,076,225)	(3,181,593)	(8,615,011)	12,010,930
Other expense, primarily interest	(342,442)	(1,413,720)	(3,396,340)	(3,035,149)
Income (loss) before income tax expense	(3,418,667)	(4,595,313)	(12,011,351)	8,975,781
Foreign income tax expense	-	(10,331)	-	(2,644,278)
Net income (loss)	$ (3,418,667)	$ (4,605,644)	$ (12,011,351)	$ 6,331,503

6. Long-Term Debt

Long-term debt consisted of the following:

	September 30, 2016	December 31, 2015
Senior Secured Term Loan	$ 209,861,111	$ 224,111,111
Senior Secured Bonds	150,000,000	150,000,000
Debt Issuance Costs	(9,559,881)	(11,951,375)
Total Long-Term Debt	$ 350,301,230	$ 362,159,736
Less Current Portion	(25,555,556)	(20,638,888)
Long-Term Debt, Net	$ 324,745,674	$ 341,520,848

Senior Secured Term Loan

In October 2014, the Company entered into a $350,000,000 Senior Secured Term Loan ("Term Loan"), maturing in October 2019, collateralized by a first lien mortgage on *BassDrill Beta* and *Atlantica Delta*; the shares of BDB, BDB-BV, BBB, AG and AD; the AM management agreements; all credit rights arising from the Company's drilling contracts; and rights in connection with the investments made with amounts deposited in the debt service reserve account. The Term Loan amount was available for drawdown independently in up to three tranches up until March 31, 2016. The initial refinancing tranche of $53.0 million (the "Beta tranche") was drawn down on October 6, 2014; the second tranche (the "Gamma tranche") of $120.0 million was void upon the cancellation of the *Atlantica Gamma* in January 2016; and the third tranche (the "Delta tranche") of $177.0 million was drawn down on December 8, 2015 with the delivery of the *Atlantica Delta*. The Term Loan tranches bear interest at 3.25% plus LIBOR, payable quarterly commencing January 2015.

In May 2016, the Term Loan agreement was amended to, among other things, reflect the cancellation of the *Atlantica Gamma,* include a mandatory prepayment up to $9.3 million upon any refund of the down payment associated with the *Atlantica Gamma*, which is under arbitration, and amend minimum liquidity and equity requirements as described below.

The Company entered into (i) a swap agreement with LIBOR fixed at 1.36% for the Beta tranche initially for $53.0 million for a period of four years that commenced November 2014, (ii) a swap agreement with LIBOR fixed at 1.31% for $130.0 million of the Delta tranche for a period of seven years that commenced February 2016 and (iii) a swap agreement with LIBOR fixed at 1.11% for $33.4 million of the Delta tranche for a period of seven years commencing July 2016. The Term Loan requires quarterly principal payments ranging from $1,472,222 to $7,638,888 that commenced February 2015, with a balloon payment of $123,194,454 at final maturity. The Term Loan further requires the Company to comply with certain financial covenants as noted below. These covenants are required to be tested and reported quarterly:

- Interest coverage ratio of not less than 2.5 : 1.0
- Debt service coverage ratio of not less than 1.1 : 1.0
- Book equity minimum of $155,000,000
- Equity ratio of minimum 0.3 : 1.0

- Liquidity, measured as freely available and unencumbered cash, the higher of $25.0 million or 6% of the outstanding interest bearing debt until the early payment of the Term Loan upon any settlement of the down payment associated with the *Atlantica Gamma*, and thereafter the higher of $20.0 million or 6% of the outstanding interest bearing debt.
- The market value of the vessels is at least 140% of the aggregated outstanding amount of the Term Loan through October 2016 and 150% of the aggregated outstanding amount of the Term Loan thereafter.

At September 30, 2016, the Company was in compliance with all financial covenants.

Senior Secured Bonds

In September 2014, the Company issued $75.0 million of Senior Secured Bonds ("Bonds") maturing in April 2018 and collateralized by *BassDrill Beta*. The Bonds bore interest at 8.5%, with semiannual interest payments that commenced October 24, 2013, with principal due at maturity.

On September 23, 2014, the Company issued an additional $75.0 million of Senior Secured Bonds ("New Bonds"), maturing in September 2019 that is collateralized by *BassDrill Beta* and *Atlantica Delta*; the shares of BDB, BDB-BV, BBB, AG and AD; the AM management agreements; all credit rights arising from the Company's drilling contracts; and rights in connection with the investments made with amounts deposited in the debt service reserve account (see Restricted Cash in Note 2). Concurrent with the issuance of these New Bonds, the holders of the Bonds agreed to amend and restate the bond agreement to be consistent with the bond agreement of the New Bonds. The New Bonds, now totaling $150.0 million, bear interest at 8.0%, with quarterly interest payments that commenced December 23, 2014, and principal due at maturity. The New Bonds are subordinated to the Term Loan. The New Bonds further require the Company to comply with certain financial covenants as noted below. These covenants are required to be tested and reported quarterly:

- Interest coverage ratio of not less than 2.5 : 1.0
- Debt service coverage ratio of not less than 1.1 : 1.0
- Book equity minimum of $155,000,000
- Equity ratio of minimum 0.3 : 1.0
- Liquidity, measured as freely available and unencumbered cash, of $20.0 million
- The market value of the vessels is at least 140% of the aggregated outstanding amount of the Term Loan through October 2016 and 150% of the aggregated outstanding amount of the Term Loan thereafter.

At September 30, 2016, the Company was in compliance with all financial covenants.

7. Stockholders' Equity

In September 2015, the Company fully subscribed an equity raise through a private placement of 133,333,332 shares of common stock with proceeds of $39.2 million, net of issuance costs, for the purpose of partially financing the take-out of *Atlantica Delta* from the shipyard, strengthening the Company's working capital and for general corporate purposes.

8. Income Per Share

The components of the numerator and denominator for the calculation of basic and diluted income per share resulting from continuing operations are as follows:

	Three Months Ended September 30, 2016	2015	Nine Months Ended September 30, 2016	2015
Numerator for income per share				
Net income	$ 5,547,930	$ 2,105,382	$ 15,537,416	$ 5,610,446
Denominator for income per share				
Weighted-average shares outstanding	261,147,722	129,439,252	261,264,353	128,478,377
Effect of stock options *	-	-	-	-
Weighted-average shares for per share calculation	261,147,722	129,439,252	261,264,353	128,478,377
Per share income - basic and diluted	$ 0.02	$ 0.02	$ 0.06	$ 0.04

* For the three and nine months ended September 30, 2016 and 2015, all share based awards (see Note 10) were excluded from the calculation since the effect would have been anti-dilutive.

9. Commitments and Contingencies

Construction Obligations

In October 2012, AG entered into a turn-key contract with DSIC to design, engineer and construct a tender support barge (*Atlantica Gamma*) for a contract price of $124.0 million subject to adjustment in accordance with certain provisions. AG made a refundable 15% installment payment of $18.6 million in October 2012 with the final installment payment of $105.4 million, plus any adjustments, due upon delivery. The *Atlantica Gamma* was to be delivered on or before July 15, 2015 (the “Delivery Date”), and if the delivery was delayed beyond 180 days from the Delivery Date, absent any permissible delays as defined in the construction contract, AG was inter alia entitled to terminate the contract.

In January 2016, AG cancelled the contract and submitted a claim for the refund of the $18.6 million down payment made to the shipyard in 2012. DSIC refuted AG’s cancellation of the contract and in March 2016 cancelled the construction contract citing breach of contract by the Company. The dispute is in arbitration as required by the construction contract terms.

The Company believes AG had the right to cancel the construction contract and is entitled to the refund of $18.6 million for the down payment. However, there is the possibility that arbitration proceedings could favor the position of DSIC and that AG could lose a portion or all of its claim to the $18.6 million down payment and incur claims for damages representing the further loss alleged to have been suffered by DSIC on account of the cancellation of the construction contract.

As a result of the cancellation, in December 2015 the Company wrote-off construction in progress of $22.3 million and reclassified the 15% installment payment of $18.6 million from construction in progress to other assets on the consolidated balance sheet.

Other Commitments and Contingencies

The Company may in the future be party to various legal proceedings that are incidental to the ordinary course of business. The Company regularly analyzes current information and, as necessary, provides accruals for probable liabilities on the eventual disposition of these matters. As of September 30, 2016, there were no threatened or pending legal matters that would have a material impact on the Company's consolidated financial statements.

10. Share Option Plan

The Atlantica Share Option Plan (the "Plan") permits the Board of Directors, at its discretion, to grant options to acquire shares in the Company to employees of the Company or its subsidiaries. The options granted are not transferable, and the subscription price is set at $1.706 per share adjusted upwards by 12% per annum from the date of grant until the date the option is exercised. Options granted under the plan will vest three years after the date of the grant and may be exercised up to five years after the grant date. The maximum number of shares authorized for awards of equity share options was amended in 2015 to 6,484,000. The Company, at its discretion, may buy shares on the open market or use treasury shares to satisfy such exercised options, or it may settle the exercised options in a cash settlement.

The fair value of share options granted is recognized as operating expenses over the vesting period. During the three months ended September 30, 2016 and 2015, $17,000 and $38,000 respectively, was expensed in the consolidated statements of operations. During the nine months ended September 30, 2016 and 2015, $64,000 and $109,000 respectively, was expensed in the consolidated statements of operations. There was no effect on income taxes in the consolidated financial statements related to the options. However, if the options are exercised, a tax benefit will be recorded if the gain is recorded as deductible in any jurisdiction for tax purposes. If the Company has to expense social security taxes related to the benefit of options exercised, such expenses will be recorded at the exercise date.

During the nine months ended September 30, 2016 3,313,800 options expired. At September 30, 2016, 2,763,334 options were outstanding.

11. Defined Contribution Retirement Plan

In August 2011, the Company introduced a defined contribution plan for all employees based in the United States. Under the plan, the Company contributes to the employee's retirement plan amounts ranging from one to four percent of the employee's annual salary. Such contributions for the three months ended September 30, 2016 and 2015 were $31,000 and $36,000, respectively, and $115,000 and $123,000 for the nine months ended September 30, 2016 and 2015, respectively.

12. Related Party Transactions

The Company transacts business with the following related parties:

- BassInvest AS
- BDA
- AXON Energy Products, AXON Drilling Products, AXON Pressure Products ("AXON")
- HitecVision Advisory AS ("HitecVision")

- Bassoe Offshore AS (“BassOff AS”)
- Bassoe Offshore USA (“BassOff USA”)

Management Fees. AM has a management services agreement with BDA to provide management services for the operation of *BassDrill Alpha* based on a daily rate. Additionally, AM is eligible for a performance bonus based upon BDA’s earnings. Fees for such services were $0.4 million for the each of the three months ended September 30, 2016 and 2015, and $1.2 million and $1.4 million for the nine months ended September 30, 2016 and 2015, respectively. See Note 14 for discussion of temporary reduction of management fees in connection with the restructuring of BDA completed in November 2016.

Congo Shared Services. AD has a shared services agreement with BDA in regards to certain shore-based costs in the Congo. Fees for shared, shore-based costs billed between BDA and AD were $84,000 and $0.3 million for the three months ended September 30, 2016 and 2015, respectively, and $0.5 million and $0.3 million for the nine months ended September 30, 2016 and 2015, respectively.

Commission Fees. The Company pays a commission of 1.25% of the revenue received from Petrobras to Bassoe entities. Fees and reimbursements for such services were approximately $0.3 million for each of the three months ended September 30, 2016 and 2015, and $0.8 million and $0.7 million for the nine months ended September 30, 2016 and 2015, respectively.

Rig Services and Products. The Company received consulting services for the *Atlantica Delta* from HitecVision of $-0- and $3,000 for the three months ended September 30, 2016 and 2015, respectively, and $6,000 and $24,000 for the nine months ended September 30, 2016 and 2015, respectively. The Company received products and services from AXON for the *BassDrill Beta* of $-0- and $55,000 for the three months ended September 30, 2016 and 2015, respectively, and $51,000 and $582,000 for the nine months ended September 30, 2016 and 2015, respectively.

AXON Note Receivable. In October 2013, the Company loaned AXON, a company with common ownership, $1.4 million to assist AXON with completion of the mast equipment package (MEP) needed for construction of *BassDrill Beta*. This loan earned interest at 0.5% and was to mature three days after AXON received payment in full from Dalian Shipbuilding Industry Corporation for the guideline winch skid AXON constructed for *BassDrill Beta*. In November 2014, the Company and AXON agreed to terminate this loan and replace it with a non-interest bearing loan for $2.2 million due December 31, 2015. In December 2015, AXON repaid approximately $1.0 million of the loan. Subsequent to this payment, the note was amended to bear interest of 5.0% per annum and extend the final payment of $1.2 million to no later than December 30, 2016.

For the three and nine months ended September 30, 2016, the Company recorded $14,000 and $43,000, respectively, of interest income associated with the AXON note.

Accounts Receivable and Accounts Payable. The Company had the following receivable and payable balances with related parties:

		September 30, 2016		December 31, 2015
BDA	$	207,568	$	506,479
Employees receivables		83,938		127,509
Accounts receivable - related parties	$	291,506	$	633,988

		September 30, 2016		December 31, 2015
AXON	$	68,344	$	68,344
Bassoe		170,089		216,026
Other		6,217		3,867
Accounts payable - related parties	$	244,650	$	288,237

13. Risk Management and Financial Instruments

All of the Company's gross earnings from management and consulting fees are receivable in U.S. dollars, and the majority of its other transactions, assets and liabilities are denominated in U.S. dollars, the functional currency of the Company. However, the Company has operations and assets in a number of countries worldwide and incurs expenditures in other currencies, causing its results from operations to be affected by fluctuations in currency exchange rates, primarily relative to the U.S. dollar. The Company is also exposed to changes in interest rates on floating interest rate debt. There is, thus, a risk that currency and interest rate fluctuations will have a negative effect on the value of the Company's cash flows.

Interest Rate Risk Management

The Company's exposure to interest rate risk relates mainly to its floating interest rate debt and balances of surplus funds placed with financial institutions. The Company's intention is to obtain the most favorable interest rate borrowings available without increasing its foreign currency exposure. Surplus funds are generally placed in deposits in banks. Such deposits are available daily in order to provide the Company with flexibility to meet all requirements for working capital and capital investments. The extent to which the Company plans to utilize interest rate swaps and other derivatives to manage its interest rate risk will be determined by the net debt exposure and its views on future interest rates.

The objective of the interest rate swaps is to manage interest rate risk exposure on variable interest rate debt arrangements such as the Term Loan debt arrangement (see Note 6). The interest rate swap agreements effectively modify the Company's exposure to interest rate risk by converting a portion of the variable-rate debt to a fixed rate, thus reducing the impact of the interest rate changes on future interest expense. The Company has not designated these interest rate swaps as hedges and does not apply hedge accounting to its interest rate derivative instruments. At September 30, 2016, the Company had interest rate swaps associated with the Term Loan with a notional amount of $209.9 million that effectively fixed the variable rate on the Term Loan between 1.11% and 1.36%. At December 31, 2015, the Company had an interest rate swap with a notional amount of $47.1 million for the Beta tranche that effectively fixed the variable rate on the Term Loan to approximately 1.36%. At September 30, 2016 and December 31, 2015, the Company valued the interest rate swaps as a liability of approximately $1.0 million and $132,000, respectively. The Company determined the fair value of the interest rate swaps based on indirect market prices, and accordingly classified such fair value measurement as Level 2.

14. Subsequent Events

In October 2016, the Company bought $7.5 million of its Senior Secured Bonds for approximately $4.7 million.

In October 2016, the Company reacquired 5,085,645 shares of its own stock for approximately $1.5 million.

In November 2016, the bondholders and shareholders of BDA completed an additional capital restructuring arrangement in which the Company acquired an additional indirect ownership interest in BDA of 49.9% in exchange for approximately $8 in cash and a temporary reduction in the management fee commencing September 1, 2016 and ending the earlier of (i) September 1, 2018 (2 years) or (ii) the date on which the *BassDrill Alpha* is subject to a binding charter contract (see Note 12 for discussion of the management fee between the Company and BDA). As a result of this transaction, the Company now effectively owns 51.80% of BDA.