

HERCULES OFFSHORE, INC.

Form 10-K/A

April 07, 2016

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UNITED STATES SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

Form 10-K/A

AMENDMENT NO. 2

ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d)  
OF THE SECURITIES EXCHANGE ACT OF 1934

For the fiscal year ended December 31, 2015

Commission file number: 001-37623

Hercules Offshore, Inc.

(Exact name of registrant as specified in its charter)

Delaware

(State or other jurisdiction of  
incorporation or organization)

56-2542838

(I.R.S. Employer  
Identification No.)

9 Greenway Plaza, Suite 2200

Houston, Texas

(Address of principal executive offices)

Registrant's telephone number, including area code:

(713) 350-5100

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

Title of Each Class

Common Stock, \$0.01 par value per share

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

Title of Class

Warrants to Purchase Common Stock

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act. Yes  No

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

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes  No

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§ 232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes  No

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K (§ 229.405 of this chapter) is not contained herein, and will not be contained, to the best of registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K.

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

Large accelerated filer  Accelerated filer  Non-accelerated filer  Smaller reporting company

(Do not check if a smaller reporting company)

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

The aggregate market value of the registrant's common stock held by non-affiliates as of June 30, 2015, based on the closing price on the NASDAQ Global Select Market on such date, was approximately \$36 million. As of such date, the registrant's directors and executive officers were considered affiliates of the registrant for this purpose.

Indicate by check mark whether the registrant has filed all documents and reports required to be filed by Section 12, 13 or 15(d) of the Securities Exchange Act of 1934 subsequent to the distribution of securities under a plan confirmed by a court.

Yes  No

As of March 24, 2016, there were 19,988,898 shares of the registrant's common stock, par value \$0.01 per share, outstanding.

DOCUMENTS INCORPORATED BY REFERENCE

None.

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EXPLANATORY NOTE

We are filing this Amendment No. 2 on Form 10-K/A (this “Amendment”) to our Annual Report on Form 10-K for the year ended December 31, 2015, which was filed with the Securities and Exchange Commission on March 30, 2016 (the “Original Filing”), as amended by Amendment No. 1 thereto filed with the Securities and Exchange Commission on April 5, 2016, in order to amend disclosure in Note 1 of Item 8 of the Original Filing and to make a conforming change to the Interactive Data Files filed as Exhibit 101 to the Original Filing.

Updated Interactive Data Files, a new consent by our Independent Registered Public Accounting Firm, and new certifications by our principal executive officer and principal financial officer are filed as exhibits to this Amendment under Item 15 of Part IV hereof. Except for the foregoing amended information, this Amendment does not alter or update any other information contained in the Original Filing, as amended. This Amendment does not reflect events that may have occurred subsequent to the Original Filing.

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PART II

Item 8. Financial Statements and Supplementary Data  
REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM  
The Board of Directors and  
Stockholders of Hercules Offshore, Inc.:

We have audited the accompanying consolidated balance sheets of Hercules Offshore, Inc. and subsidiaries as of December 31, 2015 (the "Successor Company" consolidated balance sheet) and 2014 (the "Predecessor Company" consolidated balance sheet), and the related consolidated statements of operations, equity and cash flows for the period from November 6, 2015 through December 31, 2015 (the Successor Company operations and cash flows), and for the period from January 1, 2015 through November 6, 2015, and each of the two years in the period ended December 31, 2014 (the Predecessor Company operations and cash flows). Our audits also included the financial statement schedule listed in the Index at Item 15(a). These financial statements and schedule are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements and schedule 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. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the Successor Company consolidated financial statements referred to above present fairly, in all material respects, the financial position of Hercules Offshore, Inc. and subsidiaries as of December 31, 2015, and the results of their operations and their cash flows for the period from November 6, 2015 through December 31, 2015, in conformity with U.S. generally accepted accounting principles. Further, in our opinion, the Predecessor Company consolidated financial statements referred to above present fairly, in all material respects, the financial position of the Predecessor Company as of December 31, 2014, and the results of their operations and their cash flows for the period from January 1, 2015 through November 6, 2015, and for each of the two years in the period ended December 31, 2014, in conformity with U.S. generally accepted accounting principles in the United States of America. Also, in our opinion, the related financial statement schedule, when considered in relation to the basic financial statements taken as a whole, present fairly in all material respects the information set forth therein.

As discussed in Note 4 to the consolidated financial statements, on September 24, 2015, the Bankruptcy Court entered an order confirming the plan of reorganization, which became effective on November 6, 2015. Accordingly, the accompanying consolidated financial statements and schedule have been prepared in conformity with Accounting Standards Codification 852-10, Reorganizations, for the Successor Company as a new entity with assets, liabilities and a capital structure having carrying amounts not comparable with prior periods as described in Note 1.

/s/ ERNST & YOUNG LLP

Houston, Texas

March 30, 2016, except for Note 1, as to which the date is April 7, 2016

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HERCULES OFFSHORE, INC. AND SUBSIDIARIES  
 CONSOLIDATED BALANCE SHEETS  
 (In thousands, except par value)

	Successor December 31, 2015	Predecessor December 31, 2014
<b>ASSETS</b>		
Current Assets:		
Cash and Cash Equivalents	\$ 330,780	\$ 207,937
Accounts Receivable, Net	63,668	166,359
Prepays	11,740	19,585
Current Deferred Tax Asset	—	4,461
Other	4,015	5,955
	410,203	404,297
Property and Equipment, Net	465,497	1,574,749
Restricted Cash	200,000	—
Other Assets, Net	32,440	23,361
	\$ 1,108,140	\$ 2,002,407
<b>LIABILITIES AND EQUITY</b>		
Current Liabilities:		
Accounts Payable	\$ 43,616	\$ 52,952
Accrued Liabilities	49,108	66,090
Interest Payable	—	32,008
Other Current Liabilities	6,148	13,406
	98,872	164,456
Long-term Debt	428,715	1,210,919
Deferred Income Taxes	—	4,147
Other Liabilities	16,622	7,854
Commitments and Contingencies		
Equity:		
Predecessor Common Stock, \$0.01 Par Value; 300,000 Shares Authorized, 163,540 Shares Issued and 160,818 Shares Outstanding	—	1,635
Predecessor Capital in Excess of Par Value	—	2,179,838
Predecessor Treasury Stock, at Cost, 2,722 Shares	—	(56,765 )
Successor Common Stock, \$0.01 Par Value; 139,650 Shares Authorized, 20,000 Shares Issued and 19,989 Shares Outstanding	200	—
Successor Capital in Excess of Par Value	587,725	—
Successor Treasury Stock, at Cost, 11 Shares	(325 )	—
Retained Deficit	(23,669 )	(1,509,677 )
	563,931	615,031
	\$ 1,108,140	\$ 2,002,407

The accompanying notes are an integral part of these financial statements.

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CONSOLIDATED STATEMENTS OF OPERATIONS

(In thousands, except per share data)

	Successor Period from November 6, 2015 to December 31, 2015	Predecessor Period from January 1, 2015 to November 6, 2015	Year Ended December 31,	
			2014	2013
Revenue	\$32,442	\$303,206	\$900,251	\$858,300
Costs and Expenses:				
Operating Expenses	29,675	271,988	543,236	461,332
Asset Impairment	—	—	199,508	114,168
Depreciation and Amortization	4,534	126,963	170,898	151,943
General and Administrative	7,120	79,884	75,108	79,425
	41,329	478,835	988,750	806,868
Operating Income (Loss)	(8,887 )	(175,629 )	(88,499 )	51,432 )
Other Income (Expense):				
Interest Expense	(7,939 )	(61,173 )	(99,142 )	(73,248 )
Loss on Extinguishment of Debt	—	(1,884 )	(19,925 )	(29,295 )
Gain on Equity Investment	—	—	—	14,876
Reorganization Items, Net	(1,330 )	(357,050 )	—	—
Other, Net	(4,785 )	284	(39 )	(1,518 )
Loss Before Income Taxes	(22,941 )	(595,452 )	(207,605 )	(37,753 )
Income Tax Benefit (Provision)	(728 )	(7,042 )	(8,505 )	10,944
Loss from Continuing Operations	(23,669 )	(602,494 )	(216,110 )	(26,809 )
Loss from Discontinued Operations, Net of Taxes	—	—	—	(41,308 )
Net Loss	(23,669 )	(602,494 )	(216,110 )	(68,117 )
Loss attributable to Noncontrolling Interest	—	—	—	39
Net Loss attributable to Hercules Offshore, Inc.	\$(23,669 )	\$(602,494 )	\$(216,110 )	\$(68,078 )
Net Loss attributable to Hercules Offshore, Inc. Per Share:				
Basic and Diluted:				
Loss from Continuing Operations	\$(1.18 )	\$(3.73 )	\$(1.35 )	\$(0.17 )
Loss from Discontinued Operations	—	—	—	(0.26 )
Net Loss	\$(1.18 )	\$(3.73 )	\$(1.35 )	\$(0.43 )
Basic and Diluted Weighted Average Shares Outstanding	19,989	161,430	160,598	159,501

The accompanying notes are an integral part of these financial statements.

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HERCULES OFFSHORE, INC. AND SUBSIDIARIES  
CONSOLIDATED STATEMENTS OF EQUITY  
(In thousands)

	Successor Period from November 6, 2015 to December 31, 2015		Predecessor Period from January 1, 2015 to November 6, 2015		December 31, 2014		December 31, 2013	
	Shares	Amount	Shares	Amount	Shares	Amount	Shares	Amount
<b>Common Stock:</b>								
Balance at Beginning of Period	—	\$—	163,540	\$1,635	162,144	\$1,621	160,708	\$1,607
Issuance of Successor Company Equity	20,000	200	—	—	—	—	—	—
Other	—	—	1,084	11	1,396	14	1,436	14
Cancellation of Predecessor Company Equity	—	—	(164,624)	(1,646)	—	—	—	—
Balance at End of Period	20,000	200	—	—	163,540	1,635	162,144	1,621
<b>Capital in Excess of Par Value:</b>								
Balance at Beginning of Period	—	—	—	2,179,838	—	2,170,811	—	2,159,744
Issuance of Successor Company Equity	—	587,699	—	—	—	—	—	—
Compensation Expense Recognized	—	26	—	6,922	—	8,348	—	9,960
Excess Tax Benefit From Stock-Based Arrangements, Net	—	—	—	—	—	548	—	825
Other	—	—	—	(11)	—	131	—	282
Cancellation of Predecessor Company Equity	—	—	—	(2,186,749)	—	—	—	—
Balance at End of Period	—	587,725	—	—	—	2,179,838	—	2,170,811
<b>Treasury Stock:</b>								
Balance at Beginning of Period	—	—	(2,722)	(56,765)	(2,383)	(55,165)	(2,080)	(53,100)
Repurchase of Common Stock	(11)	(325)	(261)	(178)	(339)	(1,600)	(303)	(2,065)
Cancellation of Predecessor Company Equity	—	—	2,983	56,943	—	—	—	—
Balance at End of Period	(11)	(325)	—	—	(2,722)	(56,765)	(2,383)	(55,165)



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Retained Deficit:								
Balance at Beginning of Period	—	—	—	(1,509,677)	—	(1,293,567)	—	(1,225,489)
Net Loss attributable to Hercules Offshore, Inc.	—	(23,669 )	—	(602,494 )	—	(216,110 )	—	(68,078 )
Cancellation of Predecessor Company Equity	—	—	—	2,112,171	—	—	—	—
Balance at End of Period	—	(23,669 )	—	—	—	(1,509,677)	—	(1,293,567)
Total Hercules Offshore, Inc. Stockholders' Equity	19,989	563,931	—	—	160,818	615,031	159,761	823,700
Noncontrolling Interest:								
Balance at Beginning of Period	—	—	—	—	—	—	—	—
Acquisition of Interest in Discovery	—	—	—	—	—	—	—	26,448
Acquisition of Noncontrolling Interest in Discovery	—	—	—	—	—	—	—	(26,409 )
Loss Attributable to Noncontrolling Interest	—	—	—	—	—	—	—	(39 )
Balance at End of Period	—	—	—	—	—	—	—	—
Total Equity	19,989	\$563,931	—	\$—	160,818	\$615,031	159,761	\$823,700

The accompanying notes are an integral part of these financial statements.

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CONSOLIDATED STATEMENTS OF CASH FLOWS

(In thousands)

	Successor Period from November 6, 2015 to December 31, 2015	Predecessor Period from January 1, 2015 to November 6, 2015	Year Ended December 31,	
			2014	2013
Cash Flows from Operating Activities:				
Net Loss	\$(23,669 )	\$(602,494 )	\$(216,110 )	\$(68,078 )
Adjustments to Reconcile Net Loss to Net Cash Provided by (Used in) Operating Activities:				
Depreciation and Amortization	4,534	126,963	170,898	162,841
Stock-Based Compensation Expense	26	6,922	8,348	9,960
Deferred Income Taxes	16	1,931	(7,691 )	(30,940 )
Provision for Doubtful Accounts Receivable	1,855	7,665	5,627	642
(Gain) Loss on Disposal of Assets, Net	(28 )	970	(22,598 )	7,355
Asset Impairment	—	—	199,508	158,538
Gain on Equity Investment	—	—	—	(14,876 )
Gain on Insurance Settlement	—	(1,125 )	—	(31,600 )
Non-Cash Portion of Loss on Extinguishment of Debt	—	1,818	1,900	9,012
Non-Cash Reorganization Items, Net	—	344,231	—	—
Non-Cash Loss on Derivative	4,837	—	—	—
Other	342	1,453	2,910	8,319
(Increase) Decrease in Operating Assets -				
Accounts Receivable	(1,278 )	94,449	48,153	(53,643 )
Prepaid Expenses and Other	3,875	8,860	2,323	15,214
Increase (Decrease) in Operating Liabilities -				
Accounts Payable	(5,637 )	(12,027 )	(27,066 )	20,357
Insurance Notes Payable	—	—	(9,568 )	(31,462 )
Other Current Liabilities	(11,826 )	3,146	(36,317 )	17,753
Other Liabilities	494	7,637	(5,604 )	3,078
Net Cash Provided by (Used in) Operating Activities	(26,459 )	(9,601 )	114,713	182,470
Cash Flows from Investing Activities:				
Acquisition of Assets, Net of Cash Acquired	—	—	—	(200,957 )
Capital Expenditures	(5,066 )	(78,097 )	(147,522 )	(544,987 )
(Increase) Decrease in Restricted Cash	—	(200,000 )	—	2,027
Insurance Proceeds Received	—	3,543	9,067	51,430
Proceeds from Sale of Assets, Net	78	9,697	35,135	117,350
Other	377	227	1,479	2,474
Net Cash Used in Investing Activities	(4,611 )	(264,630 )	(101,841 )	(572,663 )
Cash Flows from Financing Activities:				
Long-term Debt Borrowings	—	436,500	300,000	700,000
Redemption of 7.125% Senior Secured Notes	—	—	(300,000 )	—
Redemption of 3.375% Convertible Senior Notes	—	—	—	(61,274 )
Redemption of 10.5% Senior Notes	—	—	—	(300,000 )
Payment of Debt Issuance Costs	—	(8,356 )	(3,914 )	(10,643 )

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Other	—	—	573	1,323	
Net Cash Provided by (Used in) Financing Activities	—	428,144	(3,341	) 329,406	
Net Increase (Decrease) in Cash and Cash Equivalents	(31,070	) 153,913	9,531	(60,787	)
Cash and Cash Equivalents at Beginning of Period	361,850	207,937	198,406	259,193	
Cash and Cash Equivalents at End of Period	\$330,780	\$361,850	\$207,937	\$198,406	

The accompanying notes are an integral part of these financial statements.

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HERCULES OFFSHORE, INC. AND SUBSIDIARIES  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

1. Nature of Business

Amendment

The Company has amended the disclosures in Note 1 to clarify that the Company includes management and a majority of the Board of Directors.

Organization

Hercules Offshore, Inc., a Delaware corporation, and its majority owned subsidiaries (the "Company") provide shallow-water drilling and marine services to the oil and natural gas exploration and production industry globally through its Domestic Offshore, International Offshore and International Liftboats segments (See Note 17). At December 31, 2015, the Company operated a fleet of 27 jackup rigs (18 marketed, 9 cold stacked), including one rig under construction, and 19 liftboat vessels (18 marketed, 1 cold stacked). The Company's diverse fleet is capable of providing services such as oil and gas exploration and development drilling, well service, platform inspection, maintenance, and decommissioning operations in several key shallow-water provinces around the world.

On August 13, 2015 (the "Petition Date"), Hercules Offshore, Inc. and certain of its U.S. domestic direct and indirect subsidiaries (together with Hercules Offshore, Inc., the "Debtors") filed voluntary petitions (the "Bankruptcy Petitions") for reorganization ("Chapter 11 Cases") under Chapter 11 of the United States Bankruptcy Code (the "Bankruptcy Code") in the United States Bankruptcy Court for the District of Delaware (the "Court"). Through the Chapter 11 Cases, the Debtors implemented the Plan in accordance with the RSA that the Debtors entered into with the Steering Group Members. The Chapter 11 Cases were jointly administered under the caption In re: Hercules Offshore, Inc., et al (Case No. 15-11685). The Company's foreign subsidiaries and one U.S. domestic subsidiary ("Non-Filing Entities") were not party to the Bankruptcy filing. Since the petition date, the Debtors operated their business as "debtors-in-possession" under the jurisdiction of the Court and in accordance with applicable provisions of the Bankruptcy Code and orders of the Court until their emergence on November 6, 2015 from bankruptcy. The Non-Filing Entities continued to operate in the ordinary course of business.

Upon the Company's emergence from Chapter 11 on November 6, 2015, the Company adopted fresh-start accounting in accordance with provisions of the Financial Accounting Standards Board ("FASB") Accounting Standards Codification ("ASC") 852, "Reorganizations" ("ASC 852") which resulted in Hercules becoming a new entity for financial reporting purposes. Upon adoption of fresh-start accounting, the Company's assets and liabilities were recorded at their fair values as of the fresh-start reporting date. The fair values of the Company's assets and liabilities in conformance with ASC 805, "Business Combinations," as of that date differed materially from the recorded values of its assets and liabilities as reflected in its historical consolidated financial statements. In addition, the Company's adoption of fresh-start accounting may materially affect its results of operations following the fresh-start reporting dates, as the Company will have a new basis in its assets and liabilities. Consequently, the Company's historical financial statements may not be reliable indicators of its financial condition and results of operations for any period after it adopted fresh-start reporting. As a result of the adoption of fresh-start reporting and the effects of the implementation of the Plan, the Company's consolidated balance sheets and consolidated statements of operations subsequent to November 6, 2015 will not be comparable to its consolidated balance sheets and consolidated statements of operations prior to November 6, 2015 (See Note 5).

Subsequent to the Petition Date, expenses, realized gains and losses, and provisions for losses that can be directly associated with the reorganization of the business are reported as Reorganization Items, Net in the accompanying Consolidated Statement of Operations.

The audited consolidated financial statements included in this Annual Report on Form 10-K have been prepared assuming that the Company will continue as a going concern and contemplate the realization of assets and the satisfaction of liabilities in the ordinary course of business. During the Chapter 11 proceedings, the Company's ability to continue as a going concern, was contingent upon, among other factors, the Debtors' ability to satisfy the remaining conditions to effectiveness contemplated under the Plan and to implement such plan of reorganization, including obtaining any exit financing.

References to “Successor” or “Successor Company” relate to Hercules on and subsequent to November 6, 2015.  
References to “Predecessor” or “Predecessor Company” refer to Hercules on and prior to November 6, 2015.

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## HERCULES OFFSHORE, INC. AND SUBSIDIARIES

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

## Current Market Environment

Demand for the Company's oilfield services is driven by its exploration and production customers' capital spending, which can experience significant fluctuation depending on current commodity prices and their expectations of future price levels, among other factors. The decline in the price of crude oil that began in mid-2014 and extending into 2016 has severely impacted dayrates and demand for the Company's services. In addition to the oil price decline, the consolidation of the domestic customer base has negatively impacted demand for jackup rigs in the U.S. Gulf of Mexico. Internationally, the new capacity growth expected over the next three years could put further pressure on the operating environment for the existing jackup rig fleet. Although activity levels for liftboats are not as closely correlated to commodity prices as the Company's drilling segments, commodity prices are still a key driver of liftboat demand. Demand for liftboat services in West Africa has been weak, which the Company believes has been driven by budgetary constraints with major customers primarily in Nigeria.

The Company has taken numerous actions to mitigate the effects of the decline in activity levels, including but not limited to: (i) cold stacking nine rigs and warm stacking seven rigs since the fourth quarter of 2014 to significantly reduce operating expenses, (ii) significantly reducing its capital expenditures in 2015 and the amount planned for 2016 and (iii) significantly reducing its workforce, both onshore and offshore. The Company continues to monitor its operating environment and will respond to further activity level declines as appropriate.

Although the Company is exploring all strategic alternatives, the Company does not believe that there is substantial doubt about the Company's ability to continue as a going concern through 2016. As part of that assessment, based on facts known to the Company as of the filing of this Form 10-K, management and a majority of the members of the Company's board of directors do not believe it is more likely than not that a bankruptcy filing will occur during 2016. Further, the Company does not intend to pursue any strategic action that results in an event of default under the Credit Agreement during 2016. The Company is currently projecting, however, that they will violate the Maximum Senior Secured First Lien Leverage Ratio on March 31, 2017. If this occurs and the Company is not able to obtain a waiver from its lenders, the lenders could accelerate these debt obligations. In addition, the Company would be required to pay an additional premium of all interest that would accrue until November 6, 2018, plus a 3% premium, discounted to present value ("Applicable Premium"). Because of this Applicable Premium, it could be challenging for the Company to obtain a waiver, and further, given the current state of the drilling market, the Company does not believe refinancing would be a viable option.

Any strategic transaction we may pursue would result in potential changes to our current business strategy and future operations and prospects. If we determine to pursue an alternative strategy or engage in a strategic transaction, our future business, prospects, financial position and operating results would likely be significantly different than those in historical periods or projected by our management.

## Dayrate Reductions

On February 25, 2015, the Company received a notice from Saudi Aramco terminating for convenience its drilling contract for the Hercules 261, effective on or about March 27, 2015. The Company received subsequent notices from Saudi Aramco extending the effective date of termination to May 31, 2015. On June 1, 2015, the Company received notice from Saudi Aramco reinstating the drilling contract on the Hercules 261, in exchange for dayrate concessions on the Hercules 261, Hercules 262 and Hercules 266 from their existing contracted rates to \$67,000 per day. These reduced dayrates were effective retroactively from January 1, 2015 through December 31, 2016 for the Hercules 261 and Hercules 262, and through the remaining contract term for the Hercules 266. However, on March 9, 2016, we received a notice from Saudi Aramco further reducing the dayrates under the contracts for the Hercules 261 and Hercules 262 from \$67,000 per day to \$63,650 per day. The reduced dayrates will apply retroactively from January 1, 2016, through December 31, 2016. The dayrate for the Hercules 266 was also reduced from \$67,000 per day to \$63,650 per day effective January 1, 2016, through the remaining term of its contract, or April 7, 2016.

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HERCULES OFFSHORE, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

2. Significant Accounting Policies

Principles of Consolidation

The consolidated financial statements of the Company include the accounts of the Company and its wholly owned subsidiaries from the date a majority controlling interest was acquired (See Note 8). All intercompany account balances and transactions have been eliminated.

Use of Estimates

In preparing financial statements in conformity with accounting principles generally accepted in the United States, management makes estimates and assumptions that affect the reported amounts of assets and liabilities and disclosures of contingent assets and liabilities at the date of the financial statements, as well as the reported amounts of revenue and expenses during the reporting period. On an ongoing basis, the Company evaluates its estimates, including those related to bad debts, property and equipment, income taxes, insurance, employment benefits and contingent liabilities. The Company bases its estimates on historical experience and on various other assumptions that are believed to be reasonable under the circumstances, the results of which form the basis for making judgments about the carrying values of assets and liabilities that are not readily apparent from other sources. Actual results could differ from those estimates.

Cash and Cash Equivalents

Cash and cash equivalents include cash on hand, demand deposits with banks and investments in highly liquid investments with original maturities of three months or less.

Revenue Recognition

Revenue generated from the Company's contracts is recognized as services are performed, as long as collectability is reasonably assured. For certain contracts, the Company may receive lump-sum fees for the mobilization of equipment and personnel. Mobilization fees received and costs incurred to mobilize a rig from one location to another are recognized as services are performed over the term of the related drilling contract. For certain contracts, the Company may receive fees from its customers for capital improvements to its rigs. Such fees are deferred and recognized as services are performed over the term of the related contract. The Company capitalizes such capital improvements and depreciates them over the useful life of the asset. Certain of the Company's contracts also allow us to recover additional direct costs, such as demobilization costs, additional labor and additional catering costs and under most of our liftboat contracts, we receive a variable rate for reimbursement of costs such as catering, oil, rental equipment and other items. Revenue for the recovery or reimbursement of these costs is recognized when the costs are incurred.

Stock-Based Compensation

The Company recognizes compensation cost for all share-based payments awarded in accordance with Financial Accounting Standards Board ("FASB") Accounting Standards Codification ("ASC") 718, Compensation — Stock Compensation ("ASC 718") and in accordance with such the Company records the grant date fair value of time-based restricted stock awarded as compensation expense using a straight-line method over the requisite service period. Performance based awards were recognized using the accelerated method over the requisite service period. The fair value of the Company's awards that are share settled are based on the closing price of the Company's common stock on the date of grant. For those performance based grants that contained a market performance condition, the Monte Carlo simulation was used for valuation as of the date of grant. All of the Company's cash settled awards were recorded as a liability at fair value, which was remeasured at the end of each reporting period, over the requisite service period. The Company's cash settled liability awards that contained market performance conditions were valued using a Monte Carlo simulation. The Company also estimates future forfeitures and related tax effects. The Company's estimate of compensation expense requires a number of assumptions and changes to those assumptions could result in different valuations for individual share awards. On November 6, 2015, the date the Plan became effective pursuant to its terms and the Debtors emerged from Chapter 11, all share-based awards requiring share settlement that were granted under the Predecessor were canceled. Certain award agreements requiring cash settlement contained change of control provisions which provided for vesting (See Note 10). The Successor Company has only granted time-based restricted stock (See Note 10).

Due to the uncertainty in the level of awards to be granted in the future, the Company's estimate of future expense relating to restricted stock granted through December 31, 2015 as well as the remaining vesting period over which the associated expense is to be recognized are estimates and subject to change.



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## HERCULES OFFSHORE, INC. AND SUBSIDIARIES

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

## Accounts Receivable and Allowance for Doubtful Accounts

Accounts receivable are stated at the historical carrying amount net of write-offs and the allowance for doubtful accounts. The Company monitors the accounts receivable from its customers for any collectability issues. An allowance for doubtful accounts is established based on reviews of individual customer accounts, recent loss experience, current economic conditions, and other pertinent factors. The Company establishes an allowance for doubtful accounts based on the actual amount it believes is not collectable. During the period January 1, 2015 to November 6, 2015, the Predecessor Company's allowance for doubtful accounts increased \$7.7 million primarily due to an uncollectable receivable identified in its International Liftboats segment. In connection with the application of fresh-start accounting on November 6, 2015, the carrying value of accounts receivable was adjusted to fair value, eliminating the allowance for doubtful accounts. The Successor Company's allowance for doubtful accounts increased \$1.9 million, primarily due to a disputed receivable balance identified in its International Offshore segment. The Company had an allowance of \$1.9 million and \$5.7 million at December 31, 2015 and 2014, respectively.

## Business Combinations

The Company accounted for the 2013 acquisition of Discovery as a business combination (See Note 8).

## Property and Equipment and Impairment of Long-lived Assets

Property and equipment are recorded at cost, less accumulated depreciation. In connection with fresh-start accounting, property and equipment were adjusted to their estimated fair value and depreciable lives were revised as of November 6, 2015. Expenditures for property and equipment and items that substantially increase the useful lives of existing assets are capitalized at cost and depreciated. Routine expenditures for repairs and maintenance are expensed as incurred.

Depreciation is computed using the straight-line method, after allowing for salvage value where applicable, over the useful lives of the assets. Depreciation of leasehold improvements is computed utilizing the straight-line method over the lease term or life of the asset, whichever is shorter.

The useful lives of property and equipment for the purposes of computing depreciation are as follows:

	Years
Drilling rigs and marine equipment (salvage value of 5%) *	10–30
Drilling machinery and equipment	2–12
Other	3–20

\* Salvage value for predecessor was 10%.

The carrying value of long-lived assets, principally property and equipment, is reviewed for potential impairment when events or changes in circumstances indicate that the carrying amount of such assets may not be recoverable or when reclassifications are made between property and equipment and assets held for sale. Factors that might indicate a potential impairment may include, but are not limited to, significant decreases in the market value of the long-lived asset, a significant change in the long-lived asset's physical condition, a change in industry conditions or a substantial reduction in cash flows associated with the use of the long-lived asset. For property and equipment held for use, the determination of recoverability is made based upon the estimated undiscounted future net cash flows of the related asset or group of assets being evaluated. Actual impairment charges are recorded using an estimate of discounted future cash flows. This evaluation requires the Company to make judgments regarding long-term forecasts of future revenue and costs. In turn these forecasts are uncertain in that they require assumptions about demand for the Company's services, future market conditions and technological developments. Significant and unanticipated changes to these assumptions could require a provision for impairment in a future period. Given the nature of these evaluations and their application to specific asset groups and specific times, it is not possible to reasonably quantify the impact of changes in these assumptions.

Supply and demand are the key drivers of rig and vessel utilization and the Company's ability to contract its rigs and vessels at economical rates. During periods of an oversupply, it is not uncommon for the Company to have rigs or vessels idled for extended periods of time, which could indicate that an asset group may be impaired. The Company's rigs and vessels are mobile units, equipped to operate in geographic regions throughout the world and, consequently,

the Company may move rigs and vessels from an oversupplied region to one that is more lucrative and undersupplied when it is economical to do so. As such, the Company's rigs and vessels are considered to be interchangeable within classes or asset groups and accordingly, the Company performs its impairment evaluation by asset group.

The Company's estimates, assumptions and judgments used in the application of its property and equipment accounting policies reflect both historical experience and expectations regarding future industry conditions and operations. Using different

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## HERCULES OFFSHORE, INC. AND SUBSIDIARIES

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

estimates, assumptions and judgments, especially those involving the useful lives and salvage values of the Company's rigs and liftboats and expectations regarding future industry conditions and operations, would result in different carrying values of assets and results of operations. For example, a prolonged downturn in the drilling industry in which utilization and dayrates were significantly reduced could result in an impairment of the carrying value of the Company's assets.

Useful lives of rigs and vessels are difficult to estimate due to a variety of factors, including technological advances that impact the methods or cost of oil and gas exploration and development, changes in market or economic conditions and changes in laws or regulations affecting the drilling industry. The Company evaluates the remaining useful lives of its rigs and vessels when certain events occur that directly impact its assessment of the remaining useful lives of the rigs and vessels and include changes in operating condition, functional capability and market and economic factors. The Company also considers major capital upgrades required to perform certain contracts and the long-term impact of those upgrades on the future marketability when assessing the useful lives and salvage values of individual rigs and vessels.

When analyzing its assets for impairment, the Company separates its marketable assets, those assets that are actively marketed and can be warm stacked or cold stacked for short periods of time depending on market conditions, from its non-marketable assets, those assets that have been cold stacked for an extended period of time or those assets that the Company currently does not reasonably expect to market in the foreseeable future.

Other Intangible Assets

In connection with the application of fresh-start accounting on November 6, 2015, the Company recorded intangible assets of \$25.3 million related to the fair value of certain customer contracts and \$1.2 million related to our corporate office lease which was favorable relative to available market terms at November 6, 2015. The intangible assets related to the customer contracts are being amortized on a straight-line basis over the life of the contracts once those contracts have commenced, which in the case of one of the customer contracts commencement is not expected until mid-2016. The intangible asset related to our corporate office lease is being amortized on a straight-line basis to rental expense over the remaining lease term. Amortization expense related to intangible assets was \$0.2 million for the period November 6, 2015 to December 31, 2015. Intangible assets are included in Other Assets, Net on the Consolidated Balance Sheet at December 31, 2015.

(in thousands)	Successor December 31, 2015			Weighted-Average Amortization Period
	Gross Carrying Amount	Accumulated Amortization	Net	
Customer Contracts	\$25,300	\$117	\$25,183	4.9 years
Corporate Office Lease Intangible	1,178	91	1,087	2.2 years
Total	\$26,478	\$208	\$26,270	

Future estimated amortization expense for the carrying amount of intangible assets as of December 31, 2015 is expected to be as follows (in thousands):

2016	\$3,177
2017	5,463
2018	4,920
2019	4,920
2020	4,920
Thereafter	2,870
Total	\$26,270

Restricted Cash

Restricted cash at December 31, 2015 is \$200.0 million held in an escrow account to be used to finance the remaining installment payment on the Hercules Highlander and the expenses, costs and charges related to the construction and

purchase of the Hercules Highlander (See Note 18). The Company includes any changes in restricted cash for the purpose of financing or purchasing property and equipment to be held and used in providing services as Cash flows from investing activities.

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HERCULES OFFSHORE, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

Accrued Self-Insurance Reserves

The Company is self-insured up to certain retention limits for maritime employer's liability claims and protection and indemnity claims. The amounts in excess of the self-insured levels are fully insured, up to a limit. Self-insurance reserves are based on estimates of (i) claims reported and (ii) loss amounts incurred but not reported. Reserves for reported claims are estimated by the Company's internal risk department by evaluating the facts and circumstances of each claim and are adjusted from time to time based upon the status of each claim and the Company's historical experience with similar claims. Reserves for loss amounts incurred but not reported are estimated by the Company's third-party actuary and include provisions for expected development on claims reported due to information not yet received and expected development on claims to be reported in the future but which have occurred prior to the accounting date. As of December 31, 2015 and 2014, there was \$18.5 million and \$24.5 million in accrued self-insurance reserves, respectively, which is included in Accrued Liabilities on the Consolidated Balance Sheets. The actual outcome of any claim could differ significantly from estimated amounts.

Income Taxes

The Company uses the liability method for determining its income taxes. The Company's income tax provision is based upon the tax laws and rates in effect in the countries in which the Company's operations are conducted and income is earned. The income tax rates imposed and methods of computing taxable income in these jurisdictions vary substantially. The Company's effective tax rate is expected to fluctuate from year to year as operations are conducted in different taxing jurisdictions and the amount of pre-tax income fluctuates. Current income tax expense reflects an estimate of the Company's income tax liability for the current year, withholding taxes, changes in prior year tax estimates as returns are filed, or from tax audit adjustments, while the net deferred tax expense or benefit represents the changes in the balance of deferred tax assets and liabilities as reported on the balance sheet.

Valuation allowances are established to reduce deferred tax assets when it is more likely than not that some portion or all of the deferred tax assets will not be realized in the future.

The Company considers estimated future taxable income and ongoing prudent and feasible tax planning strategies in assessing the need for a valuation allowance. Changes in these estimates and assumptions, as well as changes in tax laws, could require the Company to adjust the valuation allowance for deferred taxes in the future. The adjustments to the valuation allowance impact the Company's income tax provision in the period in which such adjustments are identified and recorded.

Certain of the Company's international rigs and liftboats are owned or operated, directly or indirectly, by the Company's wholly owned Cayman Islands subsidiaries. U.S. Federal deferred tax liabilities are recorded for the unremitted earnings of foreign subsidiaries that are not permanently reinvested; otherwise, no U.S. Federal deferred taxes are provided on foreign subsidiaries. In certain circumstances, management expects that, due to the changing demands of the offshore drilling and liftboat markets and the ability to redeploy the Company's offshore units, certain of such units will not reside in a location long enough to give rise to future tax consequences in that location. As a result, no deferred tax asset or liability has been recognized in these circumstances. Should management's expectations change regarding the length of time an offshore drilling unit will be used in a given location, the Company would adjust deferred taxes accordingly.

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## HERCULES OFFSHORE, INC. AND SUBSIDIARIES

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

## Earnings Per Share

The reconciliation of the numerators and denominators used for the computation of basic and diluted earnings per share is as follows:

(in thousands)	Successor Period from November 6, 2015 to December 31, 2015	Predecessor Period from January 1, 2015 to November 6, 2015	Year Ended December 31, 2014	2013
Numerator:				
Loss from continuing operations	\$(23,669 )	\$(602,494 )	\$(216,110 )	\$(26,809 )
Less: Loss attributable to noncontrolling interest	—	—	—	39
Adjusted loss from continuing operations	(23,669 )	(602,494 )	(216,110 )	(26,770 )
Loss from discontinued operations, net of taxes	—	—	—	(41,308 )
Net loss attributable to Hercules Offshore, Inc.	\$(23,669 )	\$(602,494 )	\$(216,110 )	\$(68,078 )
Denominator:				
Weighted average basic and diluted shares outstanding	19,989	161,430	160,598	159,501

The Company calculates basic earnings per share by dividing both income (loss) from continuing operations and net income (loss) attributable to Hercules Offshore, Inc. by the weighted average number of shares outstanding. Diluted earnings per share is computed by dividing both income from continuing operations and net income attributable to Hercules Offshore, Inc. by the weighted average number of shares outstanding during the period as adjusted for the dilutive effect of the Company's stock equivalents, which for the Predecessor included stock option, time-based restricted stock and performance-based restricted stock awards and for the Successor included time-based restricted stock awards and warrants. The effect of stock equivalents is not included in the computation for periods in which a net loss occurs, because to do so would be anti-dilutive. The Company's diluted earnings per share calculation for the periods November 6, 2015 to December 31, 2015 and January 1, 2015 to November 6, 2015 and the years ended December 31, 2014 and 2013 excludes 5.1 million, 5.6 million, 6.4 million and 6.3 million stock equivalents, respectively, that would have potentially been included if the Company had generated income from continuing operations and net income attributable to Hercules Offshore, Inc. for the respective period, but are excluded as the Company generated a loss from continuing operations and net loss during the respective period. For the Predecessor, there were no stock equivalents to exclude from the calculation of the dilutive effect of stock equivalents for the diluted earnings per share calculations for the period January 1, 2015 to November 6, 2015 and the years ended December 31, 2014 and 2013 related to the assumed conversion of the 3.375% Convertible Senior Notes as there was no excess of conversion value in any of these periods.

### 3. Accounting Pronouncements

In April 2014, the FASB issued ASU No. 2014-08, Presentation of Financial Statements and Property, Plant, and Equipment: Reporting Discontinued Operations and Disclosures of Disposals of Components of an Entity. The amendments in this ASU require that a disposal representing a strategic shift that has (or will have) a major effect on an entity's operations and financial results should be reported as discontinued operations. The amendments also expand the disclosure requirements for discontinued operations and add new disclosures for disposals of a significant part of an organization that does not qualify as discontinued operations. The amendments in this ASU are effective prospectively for annual periods beginning on or after December 15, 2014, and interim periods within those years. The Company adopted ASU 2014-08 as of January 1, 2015 with no material impact on its consolidated financial statements.

In May 2014, the FASB issued ASU No. 2014-09, Revenue from Contracts with Customers (Topic 606), which supersedes the revenue recognition requirements in Topic 605, Revenue Recognition, and most industry-specific guidance. This ASU is based on the principle that revenue is recognized to depict the transfer of promised goods or

services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. The ASU also requires additional disclosure about the nature, amount, timing and uncertainty of revenue and cash flows arising from customer contracts. Adoption is permitted under the ASU using either a full or modified retrospective application approach. In August 2015, the FASB issued ASU No. 2015-14, Revenue from Contracts with Customers (Topic 606): Deferral of the Effective Date, which defers the effective date of ASU No. 2014-09 for all entities by one year and makes it effective for public entities to annual reporting periods beginning after December 15, 2017, including interim reporting periods within that reporting period.

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HERCULES OFFSHORE, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

Early application is permitted only as of annual reporting periods beginning after December 15, 2016, including interim reporting periods within that reporting period. The Company is in the process of evaluating the impact on its consolidated financial statements.

In August 2014, the FASB issued ASU No. 2014-15, Presentation of Financial Statements - Going Concern (Subtopic 205-40): Disclosure of Uncertainties about an Entity's Ability to Continue as a Going Concern. This ASU provides guidance on management's responsibility to evaluate whether there is substantial doubt about an entity's ability to continue as a going concern and in certain circumstances to provide related footnote disclosures. The ASU is effective for the annual period ending after December 15, 2016, and for annual and interim periods thereafter. Early adoption is permitted. The Company is in the process of evaluating the impact on its consolidated financial statements.

In April 2015, the FASB issued ASU No. 2015-03, Interest - Imputation of Interest (Subtopic 835-30): Simplifying the Presentation of Debt Issuance Costs. The amendments in this ASU require that debt issuance costs related to a recognized debt liability be presented in the balance sheet as a direct deduction from the carrying amount of that debt liability, consistent with debt discounts. The recognition and measurement guidance for debt issuance costs are not affected by the amendments in this ASU. The ASU is effective for financial statements issued for fiscal years beginning after December 15, 2015 and interim periods within those fiscal years using a retrospective approach, wherein the balance sheet of each individual period presented should be adjusted to reflect the period-specific effects of applying the new guidance. Early adoption is permitted for financial statements that have not been previously issued. As of November 6, 2015, upon the adoption of fresh-start accounting, the Successor Company adopted ASU 2015-03 as a new accounting principle. As a result, the Company has not applied ASU 2015-03 to the Predecessor Company Balance Sheets.

In November 2015, the FASB issued ASU No. 2015-17, Income Taxes (Topic 740): Balance Sheet Classification of Deferred Taxes. The amendments in this ASU require that deferred tax liabilities and assets be classified as noncurrent in a classified statement of financial position. The current requirement that deferred tax liabilities and assets of a tax-paying component of an entity be offset and presented as a single amount is not affected by the amendments in this ASU. The ASU is effective for financial statements issued for annual periods beginning after December 15, 2016, and interim periods within those annual periods. Early adoption is permitted. As of November 6, 2015, upon the adoption of fresh-start accounting, the Successor Company adopted ASU 2015-17 as a new accounting principle. As a result, the Company has not applied ASU 2015-17 to the Predecessor Company Balance Sheets.

In February 2016, the FASB issued ASU No. 2016-02, Leases (Topic 842). The FASB is issuing this Update to increase transparency and comparability among organizations by recognizing lease assets and lease liabilities on the balance sheet and disclosing key information about leasing arrangements. The core principle of Topic 842 is that a lessee should recognize in the statement of financial position a liability to make lease payments (the lease liability) and a right-of-use asset representing its right to use the underlying asset for the lease term. Under previous GAAP, lessees did not recognize lease assets and lease liabilities for those leases classified as operating leases. The ASU is effective for fiscal years beginning after December 15, 2018, including interim periods within those fiscal years. Early adoption of this amendment is permitted. The Company is in the process of evaluating the impact of this accounting standard on its consolidated financial statements.

4. Bankruptcy, Emergence from Voluntary Reorganization under Chapter 11 Proceedings and Related Events  
On June 17, 2015, Hercules Offshore, Inc. and certain of its U.S. domestic direct and indirect subsidiaries (together with Hercules Offshore, Inc., the "Debtors") entered into an agreement (the "Restructuring Support Agreement" or "RSA") with certain holders (the "Steering Group Members") collectively owning or controlling in excess of 66 2/3% of the aggregate outstanding principal amount of the Company's 10.25% senior notes due 2019, 8.75% senior notes due 2021, 7.5% senior notes due 2021 and 6.75% senior notes due 2022 (the "Outstanding Senior Notes"). The RSA set forth, subject to certain conditions, the commitment to and obligations of, on the one hand, the Debtors, and on the other hand, the Steering Group Members (and any successors or permitted assigns that become party thereto) in connection with a restructuring of the Outstanding Senior Notes, the Company's 3.375% convertible senior notes due 2038 (the "Convertible Notes"), the Company's 7.375% senior notes due 2018 (the "Legacy Notes") (collectively



all the "Outstanding Notes") and the Company's common stock, par value \$0.01 per share (the "Existing Common Stock") (the "Restructuring Transaction") pursuant to a pre-packaged or pre-negotiated plan of reorganization (the "Plan") filed under Chapter 11 ("Chapter 11") of the United States Bankruptcy Code.

Pursuant to the terms of the RSA, the Steering Group Members agreed, among other things, and subject to certain conditions: (a) not to support any restructuring, reorganization, plan or sale process that is inconsistent with the RSA, and (b) not to instruct an agent or indenture trustee for any of the Outstanding Notes to take any action that is inconsistent with the

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HERCULES OFFSHORE, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

terms and conditions of the RSA, including, without limitation, the declaration of an event of default, or acceleration of the Outstanding Notes arising from, relating to, or in connection with the execution of the RSA; and at the request of the Company, to waive or agree to forbear from exercising any right to take action in respect of any default or acceleration that may occur automatically without action of any as a result of the operation of the indentures governing the Outstanding Notes.

The Company agreed, among other things, and subject to certain conditions: (a) to take no action that was materially inconsistent with the RSA, the Term Sheet or the Plan; and (b) not to support any alternative plan or transaction other than the Plan.

The Plan contemplated that the Debtors would reorganize as a going concern and continue their day-to-day operations substantially as currently conducted. Specifically, the material terms of the Plan were expected to effect, among other things, subject to certain conditions and as more particularly set forth in the Plan, upon the effective date of the Plan, a substantial reduction in the Debtors' funded debt obligations (including \$1.2 billion of face amount of the Outstanding Notes). Certain principal terms of the Plan are outlined below.

- New capital raise of first lien debt with a maturity of 4.5 years and bearing interest at LIBOR plus 9.5% per annum (1.0% LIBOR Floor), payable in cash, issued at a price equal to 97% of the principal amount. The first lien debt will consist of \$450 million for general corporate use and to finance the remaining construction cost of the Company's newbuild rig, the Hercules Highlander, and will be guaranteed by substantially all of the Company's U.S. domestic and international subsidiaries and secured by liens on substantially all of the Company's domestic and foreign assets. The first lien debt will include financial covenants and other terms and conditions.

- Exchange of the Outstanding Notes for 96.9% of the Company's common stock issued in the reorganization ("New Common Stock").

As the Plan was consummated as contemplated, holders of the Company's Existing Common Stock would receive 3.1% of the New Common Stock and would also receive warrants to purchase New Common Stock on a pro rata basis (the "Warrants"). The Warrants are exercisable at any time until their expiration date for a per share price based upon a \$1.55 billion total enterprise value. The expiration date for the Warrants will be six years from the effective date of the reorganization, subject to the earlier expiration upon the occurrence of certain extraordinary events. If the terms for exercise of the Warrants are not met before the applicable expiration date, then holders of the Company's Existing Common Stock will receive only 3.1% of the New Common Stock and will not realize any value under the terms of the Warrants.

The entry into the RSA or the matters contemplated thereby may have been deemed to have constituted an event of default with respect to the Credit Facility and the Outstanding Notes. In connection with the RSA, the Company terminated its Credit Facility effective June 22, 2015. There were no amounts outstanding and no letters of credit issued under the Credit Facility at that time. The obligations under the Credit Facility were jointly and severally guaranteed by substantially all of the Company's domestic subsidiaries. Liens on the Company's vessels that secured the Credit Facility have been released. The Company maintained compliance with all covenants under the Credit Facility through the termination date and has paid all fees in full (See Note 13).

On August 13, 2015, the Debtors filed voluntary petitions (the "Bankruptcy Petitions") for reorganization ("Chapter 11 Cases") under Chapter 11 of the United States Bankruptcy Code (the "Bankruptcy Code") in the United States Bankruptcy Court for the District of Delaware (the "Court"). Through the Chapter 11 Cases, the Debtors implemented the Plan in accordance with the RSA that the Debtors entered into with the Steering Group Members. The Chapter 11 Cases were jointly administered under the caption In re: Hercules Offshore, Inc., et al (Case No. 15-11685). The Company's foreign subsidiaries and one U.S. domestic subsidiary ("Non-Filing Entities") were not party to the Bankruptcy filing. After the petition date, the Debtors operated their business as "debtors-in-possession" under the jurisdiction of the Court and in accordance with applicable provisions of the Bankruptcy Code and orders of the Court. Under the Chapter 11 Cases, which required Court approval, the Company's trade creditors and vendors were paid in full in the ordinary course of business, and all of the Company's contracts remained in effect in accordance with their terms preserving the rights of all parties. The Non-Filing Entities operated in the ordinary course of business.

The filing of the Chapter 11 Cases constituted an event of default with respect to the Company's Outstanding Notes. Pursuant to the Bankruptcy Code, the filing of the Bankruptcy Petitions automatically stayed most actions against the Debtors, including most actions to collect indebtedness incurred prior to the filing of the Bankruptcy Petitions or to exercise control over the Debtors' property. Accordingly, although the Bankruptcy Petitions triggered defaults under the Outstanding Notes, creditors were generally stayed from taking action as a result of these defaults.

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HERCULES OFFSHORE, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

On September 24, 2015, the Bankruptcy Court entered an order confirming the Plan (the "Confirmation Order") and such order became final on October 8, 2015. On November 6, 2015 (the "Effective Date") the Plan became effective pursuant to its terms and the Debtors emerged from Chapter 11.

On the Effective Date the following items related to the Plan occurred:

- The obligations of the Debtors with respect to the Predecessor Company Outstanding Notes were canceled.
- Herc equity interests in the Predecessor Company were canceled.
- The Successor Company issued 20.0 million shares of new common stock, par value \$0.01 per share (the "New Common Stock") of which 96.9%, or 19.4 million shares, were distributed to the holders of the Outstanding Notes of the Predecessor Company and 3.1%, or 0.6 million shares, were distributed to equity holders of the Predecessor Company.
- The Successor Company also issued 5.0 million warrants, which were distributed to equity holders of the Predecessor Company, exercisable until the Expiration Date, to purchase up to an aggregate of 5.0 million shares of New Common Stock at an initial exercise price of \$70.50 per share, subject to adjustment as provided in the Warrant Agreement. Warrants are exercisable on a cashless basis at the election of the warrant holder. All unexercised Warrants shall expire, and the rights of Initial Beneficial Holders of such Warrants to purchase New Common Stock shall terminate at the close of business on the first to occur of (i) November 8, 2021 or (ii) the date of completion of (A) any Affiliated Asset Sale or (B) a Change of Control (as defined in the warrant agreement). Warrant holders will not have any rights as stockholders until a holder of Warrants becomes a holder of record of shares of Common Stock issued upon settlement of Warrants. The number of shares of Common Stock for which a Warrant is exercisable, and the exercise price per share of such Warrant are subject to adjustment from time to time upon the occurrence of certain events, including the issuance of a dividend to all holders of Common Shares, the payment in respect to any tender offer or exchange offer by the Company for shares of Common Stock, or the occurrence of a Reorganization event defined in the Warrant Agreement as the occurrence of certain events constituting a Fundamental Equity Change (other than a Non-Affiliate Combination) or a reorganization, recapitalization, reclassification, consolidation, merger or similar event as a result of which the Common Stock would be converted into, changed into or exchanged for, stock, other securities, other property or assets (including Cash or any combination thereof), each holder of a Warrant will have the right to receive, upon exercise of a Warrant, an amount of securities, Cash or other property received in connection with such event with respect to or in exchange for the number of shares of Common Stock for which such Warrant is exercisable immediately prior to such event.
- The Successor Company entered into a Credit Agreement (See Note 13) that provides for a \$450.0 million senior secured credit facility consisting entirely of term loans. The loans were issued with 3.0% original issue discount, and \$200.0 million (the "Escrowed Amount") of the proceeds were placed into an escrow account to be used to finance the remaining installment payment on the Hercules Highlander and the expenses, costs and charges related to the construction and purchase of the Hercules Highlander. The remaining proceeds of the loans were to be used to consummate the Plan, fund fees and expenses in connection therewith, and to provide for working capital and other general corporate purposes of the Company and its subsidiaries. The Company's obligations under the Credit Agreement are guaranteed by substantially all of its domestic and foreign subsidiaries, and the obligations of the Company and the guarantors are secured by liens on substantially all of their respective assets, including their current and future vessels (including the Hercules Highlander when it is delivered), bank accounts, accounts receivable, and equity interests in subsidiaries. Loans under the Credit Agreement bear interest, at the Company's option, at either (i) the ABR (the highest of the prime rate, the federal funds rate plus 0.5%, the one-month LIBOR rate plus 1.0%, and 2.0%), plus an applicable margin of 8.50%, or (ii) the LIBOR rate plus an applicable margin of 9.50% per annum. The LIBOR rate includes a floor of 1.0%. In connection with entering into the Credit Agreement, the Company paid to the original commitment parties a put option premium equal to 2.0% of each such commitment party's commitment (one half of such fee was paid upon execution of the commitment letter, and the remaining half of such fee was paid on the Credit Agreement Closing Date), and the Company paid certain administrative and other fees to the Agent.

5. Fresh-Start Accounting

In connection with the Company's emergence from Chapter 11, the Company applied the provisions of fresh-start accounting, pursuant to Financial Accounting Standards Board ("FASB") Accounting Standards Codification ("ASC") 852, Reorganizations, ("ASC 852"), to its financial statements as (i) the holders of existing voting shares of the Predecessor Company received less than 50% of the voting shares of the emerging entity and (ii) the reorganization value of the Company's assets immediately prior to confirmation was less than the post-petition liabilities and allowed claims. The Company applied

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## HERCULES OFFSHORE, INC. AND SUBSIDIARIES

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

fresh-start accounting as of November 6, 2015. Adopting fresh-start reporting results in a new reporting entity with no beginning retained earnings or deficit. The cancellation of all existing shares outstanding on the Effective Date and issuance of new shares of the reorganized entity caused a related change of control of the Company under ASC 852. Upon the application of fresh-start accounting, the Company allocated the reorganization value to its individual assets based on their estimated fair values. Reorganization value represents the fair value of the Successor Company's assets before considering liabilities.

**Reorganization Value**

In support of the Plan, the enterprise value of the Successor Company was estimated to be in the range of \$535 million to \$725 million. The Company estimated the enterprise value of the Successor Company to be \$653.7 million .

To estimate reorganization value, the Company utilized the discounted cash flow method. The Company established an estimate of future cash flows for the period ranging from November 6, 2015 to December 31, 2022 and discounted the estimated future cash flows to present value. The expected cash flows for the period November 6, 2015 to December 31, 2022 were derived from earnings forecasts and assumptions regarding growth and margin projections, as applicable. A terminal value was included, calculated using the constant growth method, based on the cash flows of the final year of the forecast period.

The discount rate of 20.9% was estimated based on an after-tax weighted average cost of capital ("WACC") reflecting the rate of return that would be expected by a market participant. The WACC also takes into consideration a company specific risk premium reflecting the risk associated with the overall uncertainty of the financial projections used to estimate future cash flows.

The following table reconciles the enterprise value to the estimated fair value of Successor common stock as of the Effective Date:

(in thousands, except per share value)

Enterprise value	\$653,720
Plus: Cash and cash equivalents	361,850
Less: Fair value of debt	427,996
Less: Fair value of warrants	1,433
Fair value of Successor common stock	\$586,141
Shares outstanding at November 6, 2015	19,989
Per share value	\$29.32

The Company identified an embedded derivative related to a put option feature included in the Senior Secured Credit Facility, where, upon the occurrence of certain events of default and where the Company was not able to obtain a waiver from our lenders, the principal amount of the Company's debt could be accelerated and the Company would be required to pay an additional premium of all interest that would accrue until November 6, 2018, plus a 3% premium, discounted to present value. The accounting treatment of derivative financial instruments requires the Company to bifurcate and fair value the derivative as of the inception date of the Senior Secured Credit Facility and to fair value the derivative as of each subsequent reporting date.

Upon issuance of the Senior Secured Credit Facility on November 6, 2015, the Company received net proceeds of approximately \$436.5 million, incurred debt issuance costs of approximately \$11.0 million, and recognized a derivative financial instrument approximating \$8.5 million. After these adjustments, the debt approximated \$417.0 million.

In connection with fresh-start accounting, the debt was recorded at fair value of \$428.0 million which was determined using an Income Approach, specifically the risk-neutral method. The difference between the \$450.0 million face amount and the fair value recorded in fresh-start accounting is being amortized over 4.5 years, the current expected life of the debt.

The fair value of the warrants was estimated using a Black-Scholes pricing model with the following assumptions: stock price of \$10.27; strike price of \$70.50; expected volatility of 40%; expected dividend rate of 0.0%; risk free interest rate of 1.91%; expiration date of six years. The fair value of these warrants was estimated using Level 2

inputs.

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HERCULES OFFSHORE, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

The following table reconciles the enterprise value to the estimated reorganization value as of the Effective Date:  
(in thousands)

Enterprise value	\$653,720
Plus: Cash and cash equivalents	361,850
Plus: Fair value of non-debt liabilities	127,576
Reorganization value of Successor assets	\$1,143,146

The fair value of non-debt liabilities represents total liabilities of the Successor Company on the Effective Date less long-term debt.

Consolidated Balance Sheet

The adjustments set forth in the following consolidated Balance Sheet reflect the effect of the consummation of the transactions contemplated by the Plan (reflected in the column “Reorganization Adjustments”) as well as fair value adjustments as a result of the adoption of fresh-start accounting (reflected in the column “Fresh-Start Adjustments”). The explanatory notes highlight methods used to determine fair values or other amounts of the assets and liabilities as well as significant assumptions.



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## HERCULES OFFSHORE, INC. AND SUBSIDIARIES

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

(in thousands)	Predecessor Company November 6, 2015	Reorganization Adjustments	Fresh-Start Adjustments	Successor Company November 6, 2015
<b>ASSETS</b>				
Current Assets:				
Cash and Cash Equivalents	\$ 133,706	\$ 228,144	(1) \$—	\$ 361,850
Accounts Receivable, Net	64,245	—	—	64,245
Prepays	15,074	—	—	15,074
Other	4,489	—	—	4,489
	217,514	228,144	—	445,658
Property and Equipment, Net	1,514,798	—	(1,049,537 )	(12) 465,261
Restricted Cash	—	200,000	(2) —	200,000
Other Assets, Net	7,675	(147 )	(3) 24,699	(13) 32,227
	\$ 1,739,987	\$ 427,997	\$(1,024,838 )	\$ 1,143,146
<b>LIABILITIES AND EQUITY</b>				
Current Liabilities:				
Accounts Payable	\$ 49,253	\$ —	\$ —	\$ 49,253
Accrued Liabilities	55,762	2,643	(4) —	58,405
Other Current Liabilities	13,081	—	(4,454 )	(14) 8,627
	118,096	2,643	(4,454 )	116,285
Long-term Debt	—	416,998	(5) 10,998	(15) 427,996
Deferred Income Taxes	—	39,546	(6) (39,546 )	(16) —
Other Liabilities	15,062	8,503	(7) (12,274 )	(17) 11,291
Liabilities Subject to Compromise Commitments and Contingencies	1,254,845	(1,254,845 )	(8) —	—
Equity:				
Predecessor Common Stock, \$0.01 Par Value; 300,000 Shares Authorized, 164,624 Shares Issued and 161,641 Shares Outstanding	1,646	(1,646 )	(9) —	—
Predecessor Capital in Excess of Par Value	2,186,749	(2,186,749 )	(9) —	—
Predecessor Treasury Stock, at Cost, 2,983 Shares	(56,943 )	56,943	(9) —	—
Successor Common Stock, \$0.01 Par Value; 139,650 Shares Authorized, 20,000 Shares Issued and 19,989 Shares Outstanding	—	200	(10) —	200
Successor Capital in Excess of Par Value	—	587,699	(10) —	587,699
Successor Treasury Stock, at Cost, 11 Shares	—	(325 )	(10) —	(325 )
Retained Deficit	(1,779,468 )	2,759,030	(11) (979,562 )	(18) —
	351,984	1,215,152	(979,562 )	587,574
	\$ 1,739,987	\$ 427,997	\$(1,024,838 )	\$ 1,143,146

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## HERCULES OFFSHORE, INC. AND SUBSIDIARIES

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

## Reorganization Adjustments

1. Reflects the net cash payments recorded as of the Effective Date from implementation of the Plan:  
(in thousands)

## Sources:

Net proceeds from Senior Secured Credit Facility*	\$436,500
Total sources	436,500

## Uses:

Funding of escrow account	200,000
Debt issuance costs	8,356
Total uses	208,356
Net Sources	\$228,144

\*\$450 million Senior Secured Credit Facility issued at a discount of 3%

Reflects the funding of \$200 million to an escrow account to finance the remaining installment payment on the  
2. Hercules Highlander and the expenses, costs and charges related to the construction and purchase of the Hercules Highlander.

3. Reflects the reduction of tax attributes and corresponding change to the valuation allowance as a result of the Debtor's emergence from Chapter 11 bankruptcy proceedings (See Note 16).

4. Represents debt issuance costs related to the Senior Secured Credit Facility expected to be settled in cash.

Upon issuance of the Senior Secured Credit Facility, the Company received net proceeds of approximately \$436.5 million, incurred debt issuance costs of approximately \$11.0 million, and recognized a derivative financial instrument approximating \$8.5 million.

6. Reflects the reduction of tax attributes and corresponding change to the valuation allowance as a result of the Debtor's emergence from Chapter 11 bankruptcy proceedings (See Note 16).

7. Reflects the recording of the embedded put option derivative.

8. Liabilities subject to compromise were settled as follows in accordance with the Plan:

(in thousands)

8.75% Senior Notes, due July 2021	\$400,000
7.5% Senior Notes, due October 2021	300,000
6.75% Senior Notes, due April 2022	300,000
10.25% Senior Notes, due April 2019	200,000
3.375% Convertible Senior Notes, due June 2038	7,565
7.375% Senior Notes, due April 2018	3,508
Accrued Interest	43,772
Liabilities subject to compromise of the Predecessor Company (LSTC)	1,254,845
Fair value of equity issued to holders of the Senior Notes of the Predecessor	(568,286 )
Gain on settlement of liabilities subject to compromise (debt forgiveness)	\$686,559

Refer to 10. below as explanation for the determination of fair value for equity issued to holders of the Senior Notes of the Predecessor.

9. Reflects the cancellation of Predecessor Company equity to retained earnings.

Reflects the issuance of 19.4 million shares of common stock at a per share price of \$29.32 to the holders of the Senior Notes of the Predecessor and 0.6 million shares of common stock at a per share price of \$29.32 to the stockholders of the Predecessor Company as well as the repurchase of eleven thousand shares into treasury at a per share price of \$29.32. Additionally, this amount reflects the issuance of 5.0 million warrants valued at \$0.29 to the stockholders of the Predecessor Company.

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## HERCULES OFFSHORE, INC. AND SUBSIDIARIES

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

11. Reflects the cumulative impact of the reorganization adjustments discussed above:

(in thousands)

Gain on settlement of liabilities subject to compromise	\$686,559	
Net gain on reorganization adjustments	686,559	
Fair value of shares issued to stockholders	(18,180	)
Fair value of shares purchased back to treasury	325	
Fair value of warrants issued to stockholders	(1,433	)
Cancellation of Predecessor Company equity	2,131,452	
Tax impact on reorganization adjustments	(39,693	)
Net impact to retained earnings (deficit)	\$2,759,030	

The net gain on reorganization adjustments has been included in Reorganization Items, Net in the Consolidated Statement of Operations.

## Fresh-Start Adjustments

12. An adjustment of \$1.0 billion was recorded to decrease the net book value of property and equipment to estimated fair value. Fair value was determined as follows:

- We utilized the income and cost approach for drilling rigs and marine equipment. The discounted cash flow method under the Income approach estimates the future cash flow that a business or asset is expected to generate. Future cash flow is converted to a present value equivalent using an estimated discount rate such as the cost of equity or the weighted average cost of capital ("WACC" or "discount rate"), based on the type of cash flows being discounted. The Cost approach considers the amount required to construct or purchase a new asset of equal utility at current prices, with adjustments in value for physical deterioration, and functional and economic obsolescence. Physical deterioration is an adjustment made in the cost approach to reflect the real operating age of an asset with regard to wear and tear, decay and deterioration that is not prevented by maintenance. Functional obsolescence is the loss in value or usefulness of an asset caused by inefficiencies or inadequacies of the asset, as compared to a more efficient or less costly replacement asset with newer technology. Economic obsolescence is the loss in value or usefulness of an asset due to factors external to the asset, such as the economics of the industry, reduced demand, increased competition or similar factors.

- We utilized the market, sales comparison or trended cost approach for drilling machinery and equipment. This approach relies upon recent sales and offerings of similar assets to arrive at a probable selling price.

- For the land and building, included in Other below, we considered the market rents for the property and the subject property's specific characteristics as well as current market conditions and demand.

The following table summarizes the components of property and equipment, net as of November 6, 2015, and the fair value at November 6, 2015:

(in thousands)	Predecessor November 6, 2015	Successor November 6, 2015
Drilling rigs and marine equipment	\$1,485,420	\$447,571
Drilling machinery and equipment	17,365	12,609
Other	12,013	5,081
Total	\$1,514,798	\$465,261

For property and equipment owned at November 6, 2015, the depreciable lives were revised to reflect the remaining estimated useful lives (See Note 2).

The net adjustment of \$24.7 million reflects the write-off of existing deferred drydock of \$1.9 million, \$0.1 million for the recording of a valuation allowance on the federal benefit of a foreign deferred tax asset and an adjustment of \$26.5 million to record the fair value of intangibles, determined as follows:

a. Customer contract related intangibles of \$25.3 million were valued using the income approach.



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## HERCULES OFFSHORE, INC. AND SUBSIDIARIES

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

b. In addition, the Company recorded the fair value of other intangibles of \$1.2 million related to the corporate office lease which was favorable relative to available market terms.

14. Represents the revaluation of liabilities related to a previous acquisition of \$2.8 million as well as the revaluation of the current portion of deferred revenues to fair value as the Company has no related future performance obligations of \$1.4 million and the revaluation of a tenant allowance of \$0.3 million.

15. Represents the adjustment to record the Senior Secured Credit Facility at fair value.

16. Reflects the change from a deferred tax liability to a deferred tax asset associated with adjustments to fresh-start accounting and the corresponding change to the valuation allowance (See Note 16).

17. Represents the revaluation of deferred revenues to fair value as the Company has no related future performance obligations of \$12.0 million and the revaluation of the long-term portion of a tenant allowance of \$0.3 million.

18. Reflects the cumulative impact of fresh-start adjustments as discussed above.

(in thousands)

Establishment of Successor intangibles	\$26,478	
Property and equipment fair value adjustment	(1,049,537	)
Long-term debt fair value adjustment	(10,998	)
Other assets and liabilities adjustment	14,802	
Net loss on fresh-start adjustments	(1,019,255	)
Tax impact on fresh-start adjustments	39,693	
Net impact on retained earnings (deficit)	\$(979,562	)

The net loss on fresh-start adjustments has been included in Reorganization Items, Net in the Consolidated Statement of Operations.

#### 6. Reorganization Items, Net

Reorganization items represent amounts incurred subsequent to the bankruptcy filing as a direct result of the filing of the Chapter 11 Cases and are comprised of the following:

(in thousands)	Successor Period from November 6, 2015 to December 31, 2015	Predecessor Period from January 1, 2015 to November 6, 2015
Professional Fees	\$1,330	\$12,819
Net Gain on Reorganization Adjustments	—	(686,559 )
Net Loss on Fresh-Start Adjustments	—	1,019,255
Non-Cash Expense for Write-off of Debt Issuance Costs Related to Predecessor	—	11,535
Senior Notes (a)		
Reorganization Items, Net	\$1,330	\$357,050

The carrying value of debt that was subject to compromise was adjusted to include the related unamortized debt (a) issuance costs; this adjusted debt amount was compared to the probable amount of claim allowed, which resulted in a non-cash expense of \$11.5 million during the quarter ended September 30, 2015.

For the periods November 6, 2015 to December 31, 2015 and January 1, 2015 to November 6, 2015, cash payments for reorganization items totaled \$1.4 million and \$3.9 million, respectively.

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## HERCULES OFFSHORE, INC. AND SUBSIDIARIES

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

## 7. Property and Equipment, Net

The following is a summary of property and equipment, less accumulated depreciation:

(in thousands)	Successor December 31, 2015	Predecessor December 31, 2014
Drilling rigs and marine equipment	\$451,841	\$2,098,651
Drilling machinery and equipment	12,937	42,317
Other	5,081	38,195
	469,859	2,179,163
Less accumulated depreciation	(4,362 )	(604,414 )
Total property and equipment, net	\$465,497	\$1,574,749

In connection with the application of fresh-start accounting as of November 6, 2015, Hercules recorded fair value adjustments and therefore eliminated accumulated depreciation as of that date (See Note 5).

Depreciation expense was \$4.3 million, \$124.4 million, \$164.9 million and \$155.0 million for the periods November 6, 2015 to December 31, 2015 and January 1, 2015 to November 6, 2015 and the years ended December 31, 2014 and 2013, respectively, of which, \$7.1 million related to discontinued operations for the year ended December 31, 2013 is included in Loss from Discontinued Operations, Net of Taxes on the Consolidated Statement of Operations.

## 8. Business Combinations and Asset Acquisitions

## Predecessor

Prior to June 24, 2013 the Company held a 32% equity investment in Discovery, which was a development stage company whose purpose was to own new ultra high-specification jackup drilling rigs. Historically, the Company accounted for its investment in Discovery under the equity method of accounting. On June 24, 2013 ("Acquisition Date"), the Company acquired an additional 52% interest to bring the total interest held to 84%, for cash consideration, net of cash acquired of \$77.7 million ("Discovery Transaction") and began consolidating Discovery's results of operations from that date. The Discovery Transaction allowed the Company to enter into the high-specification jackup rig market, significantly expanded its service offerings and opened new international markets that had growing needs for assets of this caliber. As of December 31, 2013, the Company held a 100% interest in Discovery as a result of additional purchases of Discovery common stock shares at 15 Norwegian Kroner ("NOK") per share (USD \$26.3 million in total).

The acquisition date fair value of the Company's previously held equity interest in Discovery was \$52.0 million based on the price the Company paid for additional Discovery shares on June 24, 2013 of 15 NOK per share. The Company recognized a \$14.9 million gain, included in Gain on Equity Investment in the Consolidated Statement of Operations for the year ended December 31, 2013, as a result of remeasuring its 32% equity interest in Discovery at its fair value as of the Acquisition Date in accordance with FASB Accounting Standards Codification ("ASC") Topic 805, Business Combinations.

In connection with the Discovery Transaction, the Company settled certain pre-existing relationships including a receivable from Discovery, warrants to purchase 5 million Discovery shares (see Note 15), as well as deferred revenue in the amounts of \$14.3 million, \$3.5 million, and \$5.6 million, respectively, at the Acquisition Date.

The Company valued the noncontrolling interest at the Acquisition Date of 15 NOK per share or \$26.4 million in total.

The components of the consideration transferred on June 24, 2013 were as follows (in thousands):

Cash Paid, Net of Cash Acquired	\$77,658
Elimination of Related Party Balances	12,283
Fair Value of Discovery Equity Investment	51,959
Noncontrolling Interest	26,448
	\$168,348



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## HERCULES OFFSHORE, INC. AND SUBSIDIARIES

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

The unaudited pro forma financial information set forth below has been compiled from historical financial statements and other information, but is not necessarily indicative of the results that actually would have been achieved had the transactions occurred on the dates indicated or that may be achieved in the future:

(in millions, except per share data)	Year Ended December 31, 2013	
Revenue	\$850.2	
Loss from Continuing Operations	\$(40.4	)
Loss from Discontinued Operations, Net of Taxes	(41.3	)
Net Loss	(81.7	)
Loss attributable to Noncontrolling Interest	—	
Net Loss attributable to Hercules Offshore, Inc.	\$(81.7	)
Net Loss attributable to Hercules Offshore, Inc. Per share:		
Basic and Diluted:		
Loss from Continuing Operations	\$(0.25	)
Loss from Discontinued Operations	(0.26	)
Net Loss	\$(0.51	)

The Company incurred transaction costs in the amount of \$3.3 million for the year ended December 31, 2013 related to the Discovery Transaction which is included in General and Administrative in the Consolidated Statement of Operations.

The amount of revenue and net income of Discovery included in the Company's Consolidated Statement of Operations for the year ended December 31, 2013 is as follows:

(in millions)	Predecessor June 24, 2013 through December 31, 2013
Revenue	\$17.3
Net Income	2.5

In March 2013, the Company acquired the offshore drilling rig Hercules 267 for \$55.0 million and the liftboat Bull Ray for \$42.0 million.



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## HERCULES OFFSHORE, INC. AND SUBSIDIARIES

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

## 9. Dispositions and Discontinued Operations

From time to time the Company enters into agreements to sell assets. The following table provides information related to the sale of several of the Company's assets, excluding other miscellaneous asset sales that occur in the normal course of business, during the years ended December 31, 2015, 2014 and 2013:

Asset	Segment	Period of Sale	Predecessor Proceeds (in thousands)	Gain/(Loss)
Period from January 1, 2015 to November 6, 2015:				
Hercules 85 (a)	Domestic Offshore	May 2015	\$250	\$(2,606 )
Hercules 153 (a)	Domestic Offshore	May 2015	250	(1,039 )
Hercules 203 (a)	Domestic Offshore	May 2015	250	(1,050 )
Hercules 206 (a)	Domestic Offshore	May 2015	250	(1,039 )
Hercules 207 (a)	Domestic Offshore	June 2015	1,750	(43 )
Hercules 211 (a)	Domestic Offshore	June 2015	1,750	292
			\$4,500	\$(5,485 )
2014:				
Hercules 258 (a)	International Offshore	April 2014	\$12,000	\$10,526
Hercules 2002 (a)	Domestic Offshore	April 2014	1,750	470
Hercules 250 (a)	Domestic Offshore	June 2014	8,450	6,883
Hercules 2003 (a)	Domestic Offshore	August 2014	1,750	500
Hercules 2500 (a)	Domestic Offshore	August 2014	6,000	4,680
Hercules 156 (a)	International Offshore	September 2014	3,100	(439 )
			\$33,050	\$22,620
2013:				
Various (b) (c)	Domestic Liftboats	July 2013	\$54,447	\$—
Various (b) (d)	Inland	July 2013	44,331	—
Hercules 27 (b)	Inland	August 2013	5,149	4,834
Hercules 170 (a)	International Offshore	December 2013	8,300	(11,498 )
			\$112,227	\$(6,664 )

(a) These gains (losses) are included in Operating Expenses on the Consolidated Statements of Operations.

(b) These gains (losses) have been reflected in the Consolidated Statements of Operations as discontinued operations.

(c) The Company completed the sale of its U.S. Gulf of Mexico liftboats and related assets.

(d) The Company completed the sale of eleven inland barge rigs and related assets.

Discontinued Operations

In 2013, the Company sold its U.S. Gulf of Mexico liftboats and related assets and additionally sold twelve of its inland barge rigs and related assets, comprising the majority of the Inland segment fleet. These long-lived assets, excluding the Hercules 27, were written down to their fair value less estimated cost to sell, resulting in non-cash impairment charges (See Note 15).

Interest charges have been allocated, based on a pro rata calculation of the net assets sold as compared to the Company's consolidated net assets, to the Inland and Domestic Liftboats segments. Interest allocated to discontinued operations of the Inland and Domestic Liftboats segments was \$1.4 million and \$1.2 million for the year ended December 31, 2013, respectively.

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## HERCULES OFFSHORE, INC. AND SUBSIDIARIES

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

Operating results included in discontinued operations were as follows:

(in thousands)	Predecessor Year Ended December 31, 2013
Inland:	
Revenue	\$15,782
Loss Before Income Taxes	\$(39,585 )
Income Tax Benefit	2,587
Loss from Discontinued Operations, Net of Taxes	\$(36,998 )
Domestic Liftboats:	
Revenue	\$29,625
Loss Before Income Taxes	\$(4,310 )
Income Tax Provision	—
Loss from Discontinued Operations, Net of Taxes	\$(4,310 )
Total:	
Revenue	\$45,407
Loss Before Income Taxes	\$(43,895 )
Income Tax Benefit	2,587
Loss from Discontinued Operations, Net of Taxes	\$(41,308 )

## 10. Long-Term Incentive Awards

## Predecessor

## Stock-based Compensation

The Company's 2014 Long-Term Incentive Plan (the "2014 Plan"), provided for the granting of stock options, stock appreciation rights, restricted stock, restricted stock units, dividend equivalents, performance awards and other stock-based awards to selected employees and non-employee directors of the Company. The 2014 Plan and any shares that were available for grant or award under such were canceled on the Effective Date pursuant to the Plan. The Company's 2004 Amended and Restated Long-Term Incentive Plan (the "2004 Plan") remained in effect after the approval of the 2014 Plan only as it related to outstanding awards previously granted under such 2004 Plan, but was canceled on the Effective Date pursuant to the Plan. The Compensation Committee of the Company's Board of Directors selected participants from time to time and, subject to the terms and conditions of the 2014 Plan, determined all terms and conditions of awards. The Company issued originally issued shares upon exercise of stock options and for restricted stock grants. On the Effective Date, all share-based awards requiring share settlement that were granted under the Predecessor were canceled pursuant to the Plan. Certain award agreements requiring cash settlement contained change of control provisions which provided for vesting. The amount of liability for predecessor liability-based awards requiring cash settlement was \$4.1 million and \$2.0 million at November 6, 2015 and December 31, 2015, respectively. Cash payment related to these liability-based awards during the period November 6, 2015 to December 31, 2015 was \$2.1 million.

The Company had the following equity award grants:

**Time-based awards** The Company granted time-based restricted stock awards to its employees which vest 1/3 per year and previously to Directors which vested on the date of the Company's annual meeting of stockholders that followed the grant date. The grant-date fair value per share for these time-based restricted stock awards was equal to the closing price of the Company's stock on the grant date. Additionally, the Company previously granted stock options which vested 1/3 per year and had a maximum contractual term of 10 years.

**Objective-based awards** The Company granted compensation awards to its employees that were based on the Company's achievement of certain Company-based performance objectives as well as the Company's achievement of certain market-based objectives. The awards granted in 2015 were to cliff vest three years from the date of grant and were payable in cash, subject to vesting requirements, after the completion of all performance periods with 20% of the

award being achievable based on a one-year performance period, 30% being achievable based on a two-year performance period, and the remaining 50% being achievable based upon a three-year performance period. The CEO's

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## HERCULES OFFSHORE, INC. AND SUBSIDIARIES

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

award also contains an equity component that is earned, in addition to the cash, up to a total amount of 400,000 shares if minimum levels of performance were achieved. The awards granted in 2014 and 2013, which were to cliff vest on the third anniversary of the grant date, are payable in shares at target levels when combined and in cash for the amount above target up to maximum, as defined by the agreements. For the Chief Executive Officer ("CEO"), the portion of these awards payable in cash was based on the achievement of certain market-based and Company-based performance objectives being met at certain levels below target when combined. Additionally, for the awards granted in 2014, if either the market-based or Company-based performance objectives were met at threshold or above, but the other was not, the CEO was entitled to a cash award for that objective if it was met at target or above. For 2012, a portion of the awards were payable in shares of the Company's common stock which vest 1/3 per year. For 2012, if the highest market-based and Company-based performance objectives were met, a portion of these awards were payable in cash and cliff vested at the first anniversary of the grant date. In addition, the Company granted certain awards to its CEO in 2011 that were based upon the Company's achievement of certain market-based objectives and were paid in cash at the end of the vesting periods at March 31, 2014 and December 31, 2013 ("Performance Retention Awards"). Additionally, a retention award, granted in 2011, outside of the 2004 Plan was paid in cash at December 31, 2013, the end of a three-year vesting period.

The Company recognized a \$4.0 million expense, a \$0.4 million benefit and a \$3.4 million expense for employee compensation during the period January 1, 2015 to November 6, 2015 and the years ended December 31, 2014 and 2013, respectively, for all liability-based awards. The expense for the period January 1, 2015 to November 6, 2015 includes \$3.7 million of expense related to change of control provisions. For these awards, there was no related income tax benefit in the period January 1, 2015 to November 6, 2015 and the years ended December 31, 2014 and 2013, respectively. The Company recognized \$6.9 million, \$8.3 million and \$10.0 million in employee stock-based compensation expense for all share-settled awards during the period January 1, 2015 to November 6, 2015 and the years ended December 31, 2014 and 2013, respectively. The expense for the period January 1, 2015 to November 6, 2015 includes \$4.4 million of expense related to the cancellation of awards pursuant to the Plan, which under ASC 718 requires that any unrecognized cost on the cancellation date be recognized. For these awards, there was no related income tax benefit in the period January 1, 2015 to November 6, 2015 and the years ended December 31, 2014 and 2013, respectively. The Company classified \$0.4 million and \$1.0 million in excess tax benefits as a financing cash inflow for the years ended December 31, 2014 and 2013, respectively. There were no excess tax benefits to classify as financing cash inflow for the period January 1, 2015 to November 6, 2015.

The Company used various assumptions to estimate the fair value of its objective-based awards. The risk-free interest rate assumptions were based on observed interest rates consistent with the approximate vesting periods. For the Performance Retention Awards in 2013, the Company used the historical volatility of its common stock to estimate volatility and the dividend yield assumption was based on the historical and anticipated dividend payouts of the Company. For the 2015, 2014 and 2013 objective-based awards, the Company used the historical volatility of its common stock, as well as that of certain peer groups, as defined in the award agreements to estimate volatility and the dividend yield assumptions were based on historical and anticipated dividend payouts of the Company, as well as that of certain peer groups, as defined in the award agreements.

Objective-based Awards (cash settled)

The Company accounts for awards or the portion of the awards requiring cash settlement under stock-compensation principles of accounting as liability instruments. The fair value of all liability instruments are being remeasured based on the awards' estimated fair value at the end of each reporting period and are being recorded to expense over the vesting period. The awards that are based on the Company's achievement of market-based objectives related to its stock price performance as compared to certain peer groups, as defined in the award agreements, are valued using a Monte Carlo simulation. The following are the assumptions for the Company:

December 31,	December 31, 2013
2014	

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	Restricted Stock Market-Based	Performance Retention Awards	Restricted Stock Market-Based
Dividend yield	—	—	—
Expected price volatility	54.4	% 65.0	% 44.1
Risk-free interest rate	0.5	% 0.1	% 0.4
Stock price (a)	\$1.00	\$6.52	\$6.52
Fair value	\$0.05	\$4.19	\$6.19

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## HERCULES OFFSHORE, INC. AND SUBSIDIARIES

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

(a) The stock price represents the closing price of the Company's common stock at the valuation date.

Stock Option Awards

The following table summarizes stock option activity as of November 6, 2015 and changes during the period then ended:

Stock Options	Shares	Weighted-Average Exercise Price	Weighted-Average Remaining Contractual Term	Aggregate Intrinsic Value
				(in thousands)
Outstanding at January 1, 2015	3,005,480	\$8.91	3.87	\$—
Granted	—	—		
Exercised	—	—		
Cancelled	(1,809,358)	) 7.50		
Expired	(1,196,122)	) 11.04		
Outstanding at November 6, 2015	—	—	0.00	—
Vested or Expected to Vest at November 6, 2015	—	—	0.00	—
Exercisable at November 6, 2015	—	—	0.00	—

The intrinsic value of stock options exercised during 2014 and 2013 was \$0.2 million and \$0.4 million, respectively. Cash received from stock option exercises was \$0.1 million and \$0.3 million during the years ended December 31, 2014 and 2013, respectively. There were no stock option exercises during the period January 1, 2015 through November 6, 2015.

Objective-based Awards (share settled)

The fair value of all awards requiring share settlement were measured at the fair value on the date of grant. These awards that were based on the Company's achievement of market-based objectives related to its stock price performance as compared to certain peer groups, as defined in the award agreements, were valued at the date of grant using a Monte Carlo simulation. The following are the assumptions for the Company:

	March 2, 2015	February 19, 2014	February 28, 2013	
Dividend yield	—	—	—	
Expected price volatility	71.7	% 54.4	% 64.7	%
Risk-free interest rate	0.7	% 0.6	% 0.3	%
Stock price (a)	\$0.55	\$4.71	\$6.78	
Fair value	\$0.55	\$3.63	\$7.78	

(a) The stock price represents the closing price of the Company's common stock at March 2, 2015, February 19, 2014 and February 28, 2013, the respective grant dates.

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## HERCULES OFFSHORE, INC. AND SUBSIDIARIES

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

The following table summarizes information about objective-based restricted stock outstanding as of November 6, 2015 and changes during the period then ended:

	Objective-Based Restricted Stock	Weighted- Average Grant Date Fair Value
Non-Vested at January 1, 2015	2,125,870	\$5.36
Granted (a)	400,000	0.55
Vested	(176,211	) 5.94
Canceled	(1,718,226	) 4.22
Forfeited	(631,433	) 5.23
Non-Vested at November 6, 2015	—	—

(a) The number of objective-based restricted stock shown reflects the shares that would be granted if the maximum level of performance is achieved. The number of shares actually issued may range from zero to 400,000.

The weighted-average grant date fair value of objective-based restricted stock granted during the period January 1, 2015 to November 6, 2015 and the years ended December 31, 2014 and 2013 was \$0.55, \$4.17 and \$7.16, respectively. The total fair value of objective-based restricted stock that vested during the period January 1, 2015 to November 6, 2015 and the years ended December 31, 2014 and 2013 was \$0.1 million, \$2.0 million and \$3.1 million, respectively.

## Time-based Restricted Stock Awards

The following table summarizes information about time-based restricted stock outstanding as of November 6, 2015 and changes during the period then ended:

	Time-Based Restricted Stock	Weighted- Average Grant Date Fair Value
Non-Vested at January 1, 2015	1,849,525	\$5.08
Granted	1,600,000	0.55
Vested	(908,186	) 5.18
Canceled	(1,928,505	) 1.97
Forfeited	(612,834	) 2.90
Non-Vested at November 6, 2015	—	—

The weighted-average grant date fair value of time-based restricted stock granted during the period January 1, 2015 to November 6, 2015 and the years ended December 31, 2014 and 2013 was \$0.55, \$4.59 and \$6.86, respectively. The total fair value of time-based restricted stock that vested during the period January 1, 2015 to November 6, 2015 and the years ended December 31, 2014 and 2013 was \$0.7 million, \$4.1 million and \$6.1 million, respectively.

## Successor

On December 11, 2015, the Company's Board of Directors adopted the Hercules Offshore, Inc. 2015 Long-Term Incentive Plan (the "2015 LTIP") which subject to adjustment in accordance with the 2015 LTIP, provides that 2.0 million shares of our common stock will be available for issuance pursuant to awards under the 2015 LTIP. The 2015 LTIP provides for the granting of stock options, stock appreciation rights, restricted stock, restricted stock units, performance awards and other stock-based awards. There were 1.8 million shares available for grant at December 31, 2015. The 2015 LTIP is administered by a committee of the Company's board of directors consisting of at least two outside directors, which is referred to herein as the "committee," except in the event the Company's board of directors chooses to administer the 2015 LTIP. The committee, subject to the terms and conditions of the 2015 LTIP, determines all terms and conditions of awards, including who is eligible to receive awards.

The Company granted time-based restricted stock awards to its Directors which vest in full on the one-year anniversary of the Grant Date. Vested shares will be delivered to the Director upon a change of control of the Company or such Director's

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## HERCULES OFFSHORE, INC. AND SUBSIDIARIES

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

departure from the Board. The grant-date fair value per share for these time-based restricted stock awards is equal to the closing price of the Company's stock on the grant date.

The Company recognized twenty-six thousand dollars in stock-based compensation for the time-based restricted stock awards granted to the Company's Directors during the period of November 6, 2015 to December 31, 2015.

## Time-based Restricted Stock Awards

The following table summarizes information about time-based restricted stock outstanding as of December 31, 2015 and changes during the period November 6, 2015 to December 31, 2015:

	Time-Based Restricted Stock	Weighted- Average Grant Date Fair Value
Non-Vested at November 6, 2015	—	\$—
Granted	164,286	2.80
Vested	—	—
Forfeited	—	—
Non-Vested at December 31, 2015	164,286	2.80

The Company's estimate of future expense relating to the Successor Company's restricted stock awards granted through December 31, 2015 as well as the remaining vesting period over which the associated expense is to be recognized is \$0.4 million and 0.9 years, respectively.

## 11. Supplemental Financial Information

## Consolidated Balance Sheet Information

Accrued liabilities consisted of the following:

(in thousands)	Successor December 31, 2015	Predecessor December 31, 2014
Accrued Liabilities:		
Taxes other than Income	\$12,617	\$15,262
Accrued Payroll and Employee Benefits	17,062	25,460
Accrued Self-Insurance Reserves	18,532	24,514
Other	897	854
	\$49,108	\$66,090

Other current liabilities consisted of the following:

(in thousands)	Successor December 31, 2015	Predecessor December 31, 2014
Other Current Liabilities:		
Deferred Revenue-Current Portion	\$—	\$9,439
Other	6,148	3,967
	\$6,148	\$13,406

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## HERCULES OFFSHORE, INC. AND SUBSIDIARIES

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

## Supplemental Cash Flow Information

(in thousands)	Successor	Predecessor	Year Ended December 31,	
	Period from November 6, 2015 to December 31, 2015	Period from January 1, 2015 to November 6, 2015	2014	2013
Cash paid, net during the period for:				
Interest, net of capitalized interest	\$7,219	\$47,728	\$97,304	\$55,094
Income taxes	505	1,562	21,147	15,658

Capitalized interest was \$2.4 million, \$4.4 million and \$20.4 million for the period January 1, 2015 to November 6, 2015 and the years ended December 31, 2014 and 2013, respectively. There was no capitalized interest for the period November 6, 2015 to December 31, 2015.

## Concentration of Credit Risk

The Company maintains its cash and cash equivalents in bank deposit accounts at high credit quality financial institutions or in highly rated liquid investments with maturities of three months or less. The balances, at many times, exceed federally insured limits.

The Company provides services to a diversified group of customers in the oil and natural gas exploration and production industry. Credit is extended based on an evaluation of each customer's financial condition. The Company maintains an allowance for doubtful accounts receivable based on expected collectability and establishes a reserve when payment is unlikely to occur.

## Sales to Major Customers

The Company's customers primarily include major integrated energy companies, independent oil and natural gas operators and national oil companies. Sales to customers exceeding 10 percent or more of the Company's total revenue from continuing operations in any of the past three years are as follows:

	Successor	Predecessor	Year Ended December 31,	
	Period from November 6, 2015 to December 31, 2015	Period from January 1, 2015 to November 6, 2015	2014	2013
Saudi Aramco (a)	34 %	21 %	12 %	12 %
Chevron Corporation (b)	10	19	15	15
Arena Energy (c)	10	16	10	5
Eni (d)	15	7	—	—
Linder Oil Company (c)	12	4	—	—
Cairn Energy (a)	—	3	11	2
Energy XXI (c) (e)	8	1	14	10

(a) Revenue included in the Company's International Offshore segment.

(b) Revenue included in the Company's Domestic Offshore, International Offshore and International Liftboats segments.

(c) Revenue included in the Company's Domestic Offshore segment.

(d) Revenue included in the Company's International Offshore and Domestic Offshore segments.

(e) Includes EPL Oil and Gas since 2014 (Energy XXI acquired EPL Oil and Gas in 2014). 2013 includes only EPL Oil & Gas.

## 12. Benefit Plan

The Company currently has a 401(k) plan in which substantially all U.S. employees are eligible to participate. Effective April 1, 2013, the Company increased the Company match of participant contributions equal to 6% from 3% of a participant's eligible compensation and effective March 15, 2015 the Company eliminated the match of participant contributions. The

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## HERCULES OFFSHORE, INC. AND SUBSIDIARIES

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

Company incurred expense related to matching contributions of \$1.1 million, \$6.8 million and \$5.7 million for the period January 1, 2015 to November 6, 2015 and the years ended December 31, 2014 and 2013, respectively.

## 13. Debt

Debt is comprised of the following:

(in thousands)	Successor December 31, 2015	Predecessor December 31, 2014
Senior Secured Credit Facility, due May 2020	\$428,715	\$—
8.75% Senior Notes, due July 2021	—	400,000
7.5% Senior Notes, due October 2021	—	300,000
6.75% Senior Notes, due April 2022	—	300,000
10.25% Senior Notes, due April 2019	—	200,000
3.375% Convertible Senior Notes, due June 2038*	—	7,410
7.375% Senior Notes, due April 2018	—	3,509
Total Long-term Debt	\$428,715	\$1,210,919

\* The carrying amount of the equity component was \$30.1 million at December 31, 2014.

The following is a summary of scheduled long-term debt maturities by year (in thousands):

2016	\$—
2017	—
2018	—
2019	—
2020	428,715
Thereafter	—
	\$428,715

The Senior Secured Credit Facility accretes to the \$450.0 million aggregate principal over 4.5 years, the current expected life of the debt.

(in millions)	Successor Period from November 6, 2015 to December 31, 2015			
	Contractual Interest	Accreted Interest	Total Interest	Effective Rate
Senior Secured Credit Facility, due May 2020	\$7.2	\$0.7	\$7.9	11.6 %

The unamortized discount of the 10.5% Senior Notes was amortized to interest expense over the original expected life of the debt instrument. The unamortized discount of the 3.375% Convertible Senior Notes was amortized to interest expense over the original expected life of the debt, which was determined to be June 1, 2013, the earliest date the holders of the notes had the right to require the Company to repurchase the notes.

(in millions)	Predecessor Year Ended December 31, 2013			
	Coupon Interest	Discount Amortization	Total Interest	Effective Rate
10.5% Senior Notes, due October 2017	\$24.1	\$0.7	\$24.8	11.00 %
3.375% Convertible Senior Notes, due June 2038	1.1	1.2	2.3	7.27

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## HERCULES OFFSHORE, INC. AND SUBSIDIARIES

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

## Successor

## Senior Secured Credit Facility

On November 6, 2015 (the "Credit Agreement Closing Date"), the Company entered into a Credit Agreement (the "Credit Agreement") that provides for a \$450.0 million senior secured credit facility ("Senior Secured Credit Facility") consisting entirely of term loans. The loans were issued with 3.0% original issue discount, and \$200.0 million (the "Escrowed Amount") of the proceeds were placed into an escrow account pursuant to an Escrow Agreement and will be released pursuant to the terms of such Agreement. The Escrowed Amount is to be used to finance the remaining installment payment on the Hercules Highlander and the expenses, costs and charges related to the construction and purchase of the Hercules Highlander (See Note 18). The remaining proceeds of the loans are being used to consummate the Plan, fund fees and expenses in connection therewith, and to provide for working capital and other general corporate purposes of the Company and its subsidiaries. All loans under the Credit Agreement mature on May 6, 2020.

The Company may voluntarily prepay loans under the Credit Agreement, subject to customary notice requirements and minimum prepayment amounts, the payment of LIBOR breakage costs, if any, and (i) if such prepayment is made prior to the third anniversary of the Credit Agreement Closing Date, a prepayment premium of 3.0% of the principal amount of the loans being prepaid plus the present value of the sum of all required payments of interest on the aggregate principal amount of the loans being prepaid through the third anniversary of the Credit Agreement Closing Date, (ii) if such prepayment made after the third anniversary of the Credit Agreement Closing Date but on or prior to the fourth anniversary of the Credit Agreement Closing Date, a prepayment premium of 3.0% of the aggregate principal amount of the loans being prepaid and (iii) if such prepayment is made after the fourth anniversary of the Credit Agreement Closing Date, without premium or penalty.

The Credit Agreement requires mandatory prepayments of amounts outstanding thereunder with (i) the net proceeds of certain asset sales and casualty events, subject to certain reinvestment rights, (ii) the net proceeds of certain equity issuances, subject to certain exceptions, including with respect to equity issuances used to finance acquisitions, (iii) the net proceeds of debt issuances not permitted by the Credit Agreement, (iv) any cancellation, termination or other fee received in connection with the cancellation or termination of the construction contract or drilling contract for the Hercules Highlander, and (v) the Escrowed Amount if the Escrow Conditions are not satisfied. No prepayment premium is payable in connection with any of these mandatory prepayments, unless the mandatory prepayment is a result of the issuance of debt not permitted by the Credit Agreement. In addition, if a change of control (as defined in the Credit Agreement) occurs, each lender will have the right to require the Company to prepay its loans at 101% of the principal amount of the loans requested to be prepaid.

Loans under the Credit Agreement bear interest, at the Company's option, at either (i) the ABR (the highest of the prime rate, the federal funds rate plus 0.5%, the one-month LIBOR rate plus 1.0%, and 2.0%), plus an applicable margin of 8.50%, or (ii) the LIBOR rate plus an applicable margin of 9.50% per annum. The LIBOR rate includes a floor of 1.0%. In connection with entering into the Credit Agreement, the Company paid to the original commitment parties a put option premium equal to 2.0% of each such commitment party's commitment (one half of such fee was paid upon execution of the commitment letter, and the remaining half of such fee was paid on the Credit Agreement Closing Date) in aggregate a total of \$9.0 million, and the Company paid certain administrative and other fees to the Agent of \$1.2 million.

The Credit Agreement contains covenants that, among other things, limit the Company's ability and the ability of the Company's restricted subsidiaries to:

- incur indebtedness;
- create liens;
- enter into sale and leaseback transactions;
- pay dividends or make other distributions to equity holders;
- prepay subordinated debt or unsecured debt;
- make other restricted payments or investments (including investments in subsidiaries that are not guarantors);

- consolidate, merge or transfer all or substantially all of its assets;
- sell assets;
- engage in transactions with its affiliates;
- modify or terminate any material agreement;
- enter into agreements that restrict dividends or other transfers of assets by restricted subsidiaries; and
- engage in any new line of business.

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## HERCULES OFFSHORE, INC. AND SUBSIDIARIES

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

These covenants are subject to a number of important qualifications and limitations. In addition, the Company has to maintain compliance with (i) a maximum senior secured first lien leverage ratio (as defined in the Credit Agreement, being generally computed as the ratio of secured first lien debt to consolidated net income before interest, taxes, depreciation and amortization, which EBITDA amount will be annualized for any test period during 2017) commencing from the fiscal quarter ending March 31, 2017 and (ii) a minimum liquidity amount, consisting of unrestricted cash and cash equivalents, commencing from the Credit Agreement Closing Date. The maximum secured leverage ratio is 6.0 to 1.0 for the fiscal quarter ending March 31, 2017, 5.0 to 1.0 for the fiscal quarter ending June 30, 2017, 4.0 to 1.0 for the fiscal quarter ending September 30, 2017, and 3.5 to 1.0 for the fiscal quarter ending December 31, 2017 and thereafter. The minimum liquidity is \$100.0 million for the period beginning on the Credit Agreement Closing Date and ending on June 30, 2016, \$75.0 million for the period beginning July 1, 2016 and ending December 31, 2016, \$50.0 million for the period beginning January 1, 2017 and ending June 30, 2017, and \$25.0 million for the period beginning July 1, 2017 and thereafter. At December 31, 2015, the Company was in compliance with all covenants under our Senior Secured Credit Facility.

The Company's obligations under the Credit Agreement are guaranteed by substantially all of its domestic and foreign subsidiaries, and the obligations of the Company and the guarantors are secured by liens on substantially all of their respective assets, including their current and future vessels (including the Hercules Highlander when it is delivered), bank accounts, accounts receivable, and equity interests in subsidiaries. Upon an event of default under the Credit Agreement, the Agent may, or at the direction of lenders holding a majority of the loans under the Credit Agreement shall, declare all amounts owing under the Credit Agreement to be due and payable. In addition, upon an event of default under the Credit Agreement the Agent is empowered to exercise all rights and remedies of a secured party and foreclose upon the collateral securing the Credit Agreement, in addition to all other rights and remedies under the security documents described in the Credit Agreement. Upon any acceleration of the loans under the Credit Agreement, the prepayment premiums described above that are otherwise applicable to voluntary prepayments shall become due and payable to the lenders.

**Embedded Derivative**

The Company identified an embedded derivative related to a put option feature included in the Senior Secured Credit Facility, where, upon the occurrence of certain events of default and where the Company was not able to obtain a waiver from our lenders, the principal amount of the Company's debt could be accelerated and the Company would be required to pay an additional premium of all interest that would accrue until November 6, 2018, plus a 3% premium, discounted to present value. The accounting treatment of derivative financial instruments requires the Company to bifurcate and fair value the derivative as of the inception date of the Senior Secured Credit Facility and to fair value the derivative as of each subsequent reporting date.

Upon issuance of the Senior Secured Credit Facility on November 6, 2015, the Company received net proceeds of approximately \$436.5 million, incurred debt issuance costs of approximately \$11.0 million, and recognized a derivative financial instrument approximating \$8.5 million. After these adjustments, the debt approximated \$417.0 million.

In connection with fresh-start accounting, the debt was recorded at fair value of \$428.0 million which was determined using an Income Approach, specifically the risk-neutral method. The difference between the \$450.0 million face amount and the fair value recorded in fresh-start accounting is being amortized over 4.5 years, the current expected life of the debt.

**Predecessor****Cancellation of Indebtedness**

In accordance with the Plan, on the Effective Date all of the obligations of the Debtors with respect to the 8.75% Senior Notes, 7.5% Senior Notes, 6.75% Senior Notes, 10.25% Senior Notes, 3.375% Convertible Senior Notes and 7.375% Senior Notes were canceled (See Notes 4 and 5).

**Termination of Credit Facility**

On April 3, 2012, the Company entered into a credit agreement which as amended on July 8, 2013 (the "Predecessor Credit Agreement") governed its senior secured revolving credit facility (the "Credit Facility"). The Predecessor Credit Agreement provided for a \$150.0 million senior secured revolving credit facility.

In connection with the RSA, the Company terminated the Credit Facility effective June 22, 2015 (See Note 4). There were no amounts outstanding and no letters of credit issued under the Credit Facility at that time. Liens on the Company's vessels that secured the Credit Facility have been released. The Company maintained compliance with all covenants under the Credit Facility through the termination date and has paid all fees in full.



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HERCULES OFFSHORE, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

8.75% Senior Notes due 2021

On July 8, 2013, the Company completed the issuance and sale of \$400.0 million aggregate principal amount of senior notes at a coupon rate of 8.75% ("8.75% Senior Notes") with maturity in July 2021. These notes were sold at par and the Company received net proceeds from the offering of the notes of approximately \$393.0 million after deducting the bank fees and estimated offering expenses. The net proceeds from this offering, together with cash on hand (including the proceeds of approximately \$103.9 million the Company received from the sales of its inland barge rigs, domestic liftboats and related assets), were used to fund its acquisition of Discovery shares, the final shipyard payments totaling \$333.9 million for Hercules Triumph and Hercules Resilience, related capital expenditures, as well as general corporate purposes. In accordance with the Plan, on the Effective Date all of the obligations of the Debtors with respect to the 8.75% Senior Notes were canceled (See Notes 4 and 5).

7.5% Senior Notes due 2021

On October 1, 2013, the Company completed the issuance and sale of \$300.0 million aggregate principal amount of senior notes at a coupon rate of 7.5% ("7.5% Senior Notes") with maturity in October 2021. These notes were sold at par and the Company received net proceeds from the offering of the notes of approximately \$294.5 million after deducting the bank fees and estimated offering expenses. In accordance with the Plan, on the Effective Date all of the obligations of the Debtors with respect to the 7.5% Senior Notes were canceled (See Notes 4 and 5).

6.75% Senior Notes due 2022

On March 26, 2014, the Company completed the issuance and sale of \$300.0 million aggregate principal amount of senior notes at a coupon rate of 6.75% ("6.75% Senior Notes") with maturity in April 2022. These notes were sold at par and the Company received net proceeds from the offering of the notes of approximately \$294.8 million after deducting bank fees and estimated offering expenses. In accordance with the Plan, on the Effective Date all of the obligations of the Debtors with respect to the 6.75% Senior Notes were canceled (See Notes 4 and 5).

10.25% Senior Notes due 2019

On April 3, 2012 the Company completed the issuance and sale of \$200.0 million aggregate principal amount of senior notes at a coupon rate of 10.25% ("10.25% Senior Notes") with maturity in April 2019. These notes were sold at par and the Company received net proceeds from the offering of the notes of \$195.4 million after deducting the initial purchasers' discounts and offering expenses. In accordance with the Plan, on the Effective Date all of the obligations of the Debtors with respect to the 10.25% Senior Notes were canceled (See Notes 4 and 5).

3.375% Convertible Senior Notes due 2038

In May 2012, the Company repurchased a portion of the 3.375% Convertible Senior Notes and in accordance with ASC 470-20 Debt - Debt with Conversion and Other Options, the settlement consideration was allocated to the extinguishment of the liability component in an amount equal to the fair value of that component immediately prior to extinguishment with the difference between this allocation and the net carrying amount of the liability component and unamortized debt issuance costs recognized as a gain or loss on debt extinguishment. If there would have been any remaining settlement consideration, it would have been allocated to the reacquisition of the equity component and recognized as a reduction of equity.

On May 1, 2013, the Company made an offer to purchase all of the outstanding notes in accordance with its repurchase obligation under the indenture and on June 1, 2013 repurchased \$61.3 million aggregate principal amount of the 3.375% Convertible Senior Notes pursuant to the terms of the optional put repurchase offer. In accordance with the Plan, on the Effective Date all of the obligations of the Debtors with respect to the 3.375% Convertible Senior Notes were canceled (See Notes 4 and 5).

Retirement of 10.5% Senior Notes

In 2009, the Company issued \$300.0 million of senior notes at a coupon rate of 10.5% ("10.5% Senior Notes") with maturity in October 2017. On September 17, 2013, the Company commenced a cash tender offer (the "Tender offer") for any and all of the \$300.0 million outstanding aggregate principal amount of its 10.5% Senior Notes. Senior notes totaling approximately \$253.6 million were settled on October 1, 2013 for \$268.5 million using a portion of the proceeds from the issuance of the 7.5% Senior Notes. Additionally, on November 4, 2013 the Company redeemed all

\$46.4 million of the remaining outstanding 10.5% Senior Notes for approximately \$48.8 million using the remaining proceeds from the 7.5% Senior Notes offering, together with cash on hand.

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## HERCULES OFFSHORE, INC. AND SUBSIDIARIES

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

## Retirement of 7.125% Senior Secured Notes

In 2012, the Company issued \$300.0 million of senior secured notes at a coupon rate of 7.125% ("7.125% Senior Secured Notes") with maturity in April 2017. On March 12, 2014 the Company commenced a cash tender offer (the "Tender offer") for any and all of the \$300.0 million outstanding aggregate principal amount of its 7.125% Senior Secured Notes. Senior secured notes totaling approximately \$220.1 million were settled on March 26, 2014 for \$232.7 million using a portion of the proceeds from the issuance of the 6.75% Senior Notes. Additionally, on April 29, 2014, the Company redeemed all \$79.9 million of the remaining outstanding 7.125% Senior Secured Notes for approximately \$84.2 million using the remaining net proceeds from the 6.75% Senior Notes offering, together with cash on hand.

## Loss on Extinguishment of Debt

During the period January 1, 2015 to November 6, 2015 and the years ended December 31, 2014 and 2013, the Company incurred the following charges which are included in Loss on Extinguishment of Debt in the Consolidated Statements of Operations for their respective periods:

During the fourth quarter of 2013, the Company incurred a pretax charge of \$29.3 million, consisting of a \$17.3 million call premium, \$4.8 million unamortized debt discount costs and \$4.2 million unamortized debt issuance costs, all related to the redemption of the 10.5% Senior Notes, as well as approximately \$3.0 million of bank fees related to the issuance of the 7.5% Senior Notes;

In March 2014, the Company incurred a pretax charge of \$15.2 million, consisting of a \$12.6 million call premium and \$1.4 million of unamortized debt issuance costs related to the redemption of the 7.125% Senior Secured Notes, as well as \$1.1 million of bank fees related to the issuance of the 6.75% Senior Notes;

In April 2014, the Company incurred a pretax charge of \$4.8 million, consisting of a \$4.3 million call premium and \$0.5 million of unamortized debt issuance costs related to the redemption of the remaining 7.125% Senior Secured Notes; and

In June 2015, the Company incurred a pretax charge of \$1.9 million consisting of \$1.8 million of unamortized debt issuance costs and \$0.1 million of associated professional fees related to the termination of the Credit Facility.

## 14. Derivative Instrument

## Embedded Derivative

Bifurcated embedded derivatives are initially recorded at fair value and are then revalued at each reporting date with changes in the fair value reported as non-operating income or expense. The fair value of the embedded put option derivative was determined using the "With" and "Without" method (See Note 5 and 15).

The following table provides the fair value of the Company's derivative:

Balance Sheet Classification	Successor Fair Value December 31, 2015 (in thousands)
Derivative:	
Embedded Put Option Derivative	\$ 13,340
Other Liabilities	\$ 13,340

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## HERCULES OFFSHORE, INC. AND SUBSIDIARIES

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

The following table provides the effect of the Company's derivative on the Consolidated Statements of Operations:

(in thousands)	I.	Successor Period from November 6, 2015 to December 31, 2015
Derivative	I.	II.
Embedded Put Option Derivative	Other Income (Expense)	\$(4,837 )

I. Classification of Gain (Loss) Recognized in Income (Loss) on Derivative

II. Amount of Gain (Loss) Recognized in Income (Loss) on Derivative

15. Fair Value Measurements

Fair value measurements are generally based upon observable and unobservable inputs. Observable inputs reflect market data obtained from independent sources, while unobservable inputs reflect the Company's view of market assumptions in the absence of observable market information. The Company utilizes valuation techniques that maximize the use of observable inputs and minimize the use of unobservable inputs. The Company uses the fair value hierarchy included in FASB ASC Topic 820-10, Fair Value Measurements and Disclosure, which is intended to increase consistency and comparability in fair value measurements and related disclosures. The fair value hierarchy consists of the following three levels:

Level 1 — Inputs are quoted prices in active markets for identical assets or liabilities.

Level 2 — Inputs are quoted prices for similar assets or liabilities in an active market, quoted prices for identical or similar assets or liabilities in markets that are not active, inputs other than quoted prices that are observable and market-corroborated inputs which are derived principally from or corroborated by observable market data.

Level 3 — Inputs are derived from valuation techniques in which one or more significant inputs or value drivers are unobservable.

2013 Discovery Warrants (Predecessor)

The fair value of the settlement of the warrants issued by Discovery (See Note 8) was determined using a Monte Carlo simulation based on the following assumptions:

	Predecessor June 24, 2013	
Strike Price (NOK)	11.50	
Target Price (NOK)	23.00	
Stock Value (NOK)	15.00	
Expected Volatility (%)	40.0	%
Risk-Free Interest Rate (%)	1.42	%
Expected Life of Warrants (5 years at inception)	2.6	
Number of Warrants	5,000,000	

The Company used the historical volatility of companies similar to that of Discovery to estimate volatility. The risk-free interest rate assumption was based on observed interest rates consistent with the approximate life of the warrants. The stock price represents the closing stock price of Discovery stock at June 24, 2013. The strike price, target price, expected life and number of warrants are all contractual based on the terms of the warrant agreement. On June 24, 2013, the derivative asset was adjusted to a fair value of \$3.5 million, measured using Level 2 inputs, and was included as a purchase adjustment in connection with the purchase of a controlling interest in Discovery.

Embedded Derivative (Successor)



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## HERCULES OFFSHORE, INC. AND SUBSIDIARIES

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

The fair value of the embedded put option derivative was estimated using the “with” and “without” method. Using this methodology, the Senior Secured Credit Facility is first valued with the embedded derivative (the “with” scenario) and subsequently valued without the embedded derivative (the “without” scenario). The fair value of the embedded put option derivative is estimated as the difference between the fair value of the Senior Secured Credit Facility in the “with” and “without” scenarios. The fair value of the Senior Secured Credit Facility in the “with” and “without” scenarios was estimated using an Income Approach. Specifically, to estimate the fair value of the Senior Secured Credit Facility, the expected cash flows were modeled over the life of the debt. The significant assumptions used in the valuation of the embedded put option derivative are: the fair value of the Senior Secured Credit Facility, the expected recovery rate, the risk-neutral probability of default, and the risk-free rate (Level 3). The initial measurement of fair value for this derivative liability was at November 6, 2015, the date the Company entered into the Senior Secured Credit Facility (See Note 5 and 13).

The following table represents the Company’s derivative liability measured at fair value on a recurring basis as of December 31, 2015:

(in thousands)	Successor			
	Total Fair Value Measurement	Quoted Prices in Active Markets for Identical Asset or Liability (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Embedded Put Option Derivative	\$13,340	\$ —	\$ —	\$13,340
2014 Asset Impairments (Predecessor)				

The following table represents the Company’s assets measured at fair value on a non-recurring basis for which an impairment measurement was made during the year ended December 31, 2014:

(in thousands)	Predecessor				
	Total Fair Value Measurement	Quoted Prices in Active Markets for Identical Asset or Liability (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Total Gain (Loss)
Property and Equipment, Net (a)	\$6,000	\$ —	\$ —	\$6,000	\$(82,507)
Property and Equipment, Net (b)	7,500	—	—	7,500	(117,001)

(a) This represents a non-recurring fair value measurement made at September 30, 2014 for Hercules 202, Hercules 204, Hercules 212 and Hercules 213.

(b) This represents a non-recurring fair value measurement made at December 31, 2014 for Hercules 120, Hercules 200, Hercules 214, Hercules 251 and Hercules 253.

The Company made the decision to remove the Hercules 120, Hercules 200, Hercules 202, Hercules 204, Hercules 212, Hercules 213, Hercules 214, Hercules 251 and Hercules 253 from its marketable assets into its non-marketable assets as the Company did not reasonably expect to market these rigs in the foreseeable future. This decision resulted in a non-cash impairment charge of approximately \$199.5 million (\$199.5 million, net of tax), which is included in Asset Impairment on the Consolidated Statement of Operations for the year ended December 31, 2014, to write the rigs down to fair value based on a third-party estimate. The financial information for these rigs has been reported as part of the Domestic Offshore segment.

2013 Asset Impairments (Predecessor)

Long-lived assets held for sale at June 30, 2013 were written down to their fair value (level 2) less estimated cost to sell, resulting in non-cash impairment charges of \$40.9 million (\$40.7 million net of tax) and \$3.5 million (\$3.5 million, net of tax) for the discontinued operations of the former Inland and Domestic Liftboats segments, respectively. The impairment charges are included in Discontinued Operations on the Consolidated Statement of Operations for the year ended December 31, 2013 (See Note 9).

During December 2013, the Company made the decision to remove the Hercules 153, Hercules 203, Hercules 206 and Hercules 250 from its marketable assets into its non-marketable assets as the Company did not reasonably expect to market these rigs in the foreseeable future. This decision resulted in a non-cash impairment charge of approximately \$114.2 million

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## HERCULES OFFSHORE, INC. AND SUBSIDIARIES

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

(\$114.2 million, net of tax), which is included in Asset Impairment on the Consolidated Statement of Operations for the year ended December 31, 2013, to write the rigs down to fair value based on a third-party estimate (Level 3). The financial information for these rigs has been reported as part of the Domestic Offshore segment.

**Fair Value of Financial Instruments**

The carrying amounts of the Company's financial instruments, which include cash and cash equivalents, accounts receivable, accounts payable, accrued liabilities and other current liabilities, approximate fair values because of the short-term nature of the instruments. The fair value of the Company's cash equivalents are Level 1.

The fair value of the Successor Company's Senior Secured Credit Facility is estimated using an Income Approach, specifically the risk-neutral method. The significant assumptions used in the valuation of the Senior Secured Credit Facility are: the expected recovery rate, the risk-neutral probability of default, and the risk-free rate (Level 2). The fair value of the Predecessor Company's 8.75% Senior Notes, 7.5% Senior Notes, 6.75% Senior Notes, 10.25% Senior Notes and 3.375% Convertible Senior Notes was estimated based on quoted prices in active markets. The fair value of the Predecessor Company's 7.375% Senior Notes was estimated based on discounted cash flows using inputs from quoted prices in active markets for similar debt instruments. The inputs used to determine fair value are considered Level 2 inputs.

The following table provides the carrying value and fair value of the Company's long-term debt instruments:

(in millions)	Successor		Predecessor	
	December 31, 2015		December 31, 2014	
	Carrying Value	Fair Value	Carrying Value	Fair Value
Senior Secured Credit Facility, due May 2020	\$428.7	\$315.9	\$—	\$—
8.75% Senior Notes, due July 2021	—	—	400.0	191.0
7.5% Senior Notes, due October 2021	—	—	300.0	135.8
6.75% Senior Notes, due April 2022	—	—	300.0	132.8
10.25% Senior Notes, due April 2019	—	—	200.0	111.4
3.375% Convertible Senior Notes, due June 2038	—	—	7.4	6.5
7.375% Senior Notes, due April 2018	—	—	3.5	1.9

**Fresh-Start Accounting**

Upon the Company's emergence from Chapter 11, Hercules applied the provisions of fresh-start accounting to its financial statements, including the allocation of the reorganization value to its individual assets based on their estimated fair values (See Note 5).

**16. Income Taxes**

Income (loss) from continuing operations before income taxes consisted of the following:

(in thousands)	Successor	Predecessor	Year Ended December 31,	
	Period from November 6, 2015 to December 31, 2015	Period from January 1, 2015 to November 6, 2015	2014	2013
United States	\$(18,053 )	\$327,414	\$(211,186 )	\$(68,080 )
Foreign	(4,888 )	(922,866 )	3,581	30,327
Total	\$(22,941 )	\$(595,452 )	\$(207,605 )	\$(37,753 )



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## HERCULES OFFSHORE, INC. AND SUBSIDIARIES

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

The income tax (benefit) provision consisted of the following:

(in thousands)	Successor	Predecessor	Year Ended December 31,	
	Period from November 6, 2015 to December 31, 2015	Period from January 1, 2015 to November 6, 2015	2014	2013
Current-United States	\$—	\$161	\$642	\$2,776
Current-foreign	514	4,858	15,611	14,539
Current-state	198	92	(57	) (114
Current income tax provision	712	5,111	16,196	17,201
Deferred-United States	—	—	548	(30,124
Deferred-foreign	16	1,675	(4,407	) 1,341
Deferred-state	—	256	(3,832	) 638
Deferred income tax (benefit) provision	16	1,931	(7,691	) (28,145
Total income tax (benefit) provision	\$728	\$7,042	\$8,505	\$(10,944

A reconciliation of statutory and effective income tax rates is as shown below:

	Successor	Predecessor	Year Ended December 31,			
	Period from November 6, 2015 to December 31, 2015	Period from January 1, 2015 to November 6, 2015	2014		2013	
Statutory rate	35.0	% 35.0	% 35.0	% 35.0	% 35.0	% 35.0
Effect of:						
Taxes on foreign earnings at greater than the U.S. statutory rate	(25.4	) (48.5	) (13.3	) (23.6	)	)
Discharge of debt and other reorganization related items	—	10.8	—	—		
Officer's compensation	—	—	(0.1	) (3.3	)	)
Seahawk tax attributes	—	—	—	152.5		
Valuation allowance	(11.1	) 3.4	(30.4	) (125.9	)	)
Uncertain tax positions	—	0.1	2.4	(0.5	)	)
State income taxes	(0.8	) —	3.1	(1.5	)	)
Other	(0.9	) (2.0	) (0.8	) (3.7	)	)
Effective rate	(3.2	)% (1.2	)% (4.1	)% 29.0	%	%

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## HERCULES OFFSHORE, INC. AND SUBSIDIARIES

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

The components of and changes in the net deferred taxes were as follows:

(in thousands)	Successor December 31, 2015	Predecessor December 31, 2014
Deferred tax assets:		
Net operating loss carryforward (Federal, State & Foreign)	\$51,566	\$155,649
Fixed assets	28,940	—
Credit carryforwards	19,529	35,596
Accrued expenses	11,356	13,026
Unearned income	—	664
Intangibles	6,102	3,638
Stock-based compensation	703	5,628
Deferred expenses	4,436	5,215
Valuation allowance	(107,213)	(125,021)
Deferred tax assets	15,419	94,395
Deferred tax liabilities:		
Fixed assets	—	(89,463)
Unearned income	(6,327)	—
Convertible notes	—	(947)
Debt	(4,474)	—
Unremitted foreign earnings	(3,986)	—
Other	(228)	(1,636)
Deferred tax liabilities	(15,015)	(92,046)
Net deferred tax assets	\$404	\$2,349

Under the Plan, a substantial portion of the Company's pre-petition debt securities were extinguished. Absent an exception, a debtor recognizes cancellation of indebtedness income ("CODI") upon discharge of its outstanding indebtedness for an amount of consideration that is less than its adjusted issue price. The Internal Revenue Code of 1986, as amended ("IRC"), provides that a debtor in a bankruptcy case may exclude CODI from taxable income but must reduce certain of its tax attributes by the amount of any CODI realized as a result of the consummation of a plan of reorganization. The amount of CODI realized by a taxpayer is the adjusted issue price of any indebtedness discharged less the sum of (i) the amount of cash paid, (ii) the issue price of any new indebtedness issued and (iii) the fair market value of any other consideration, including equity, issued. As a result of the market value of equity upon emergence from Chapter 11 bankruptcy proceedings, the estimated amount of U.S. CODI is approximately \$939 million, which will reduce the value of the Company's U.S. net operating losses, alternative minimum tax credits and other assets. The actual reduction in tax attributes does not occur until the first day of the Company's tax year subsequent to the date of emergence, or January 1, 2016.

IRC Sections 382 and 383 provide an annual limitation with respect to the ability of a corporation to utilize its tax attributes, as well as certain built-in-losses, against future U.S. taxable income in the event of a change in ownership. The Debtors' emergence from Chapter 11 bankruptcy proceedings is considered a change in ownership for purposes of IRC Section 382. The limitation under the IRC is based on the value of the corporation as of the emergence date. The ownership changes and resulting annual limitation will result in the expiration of an estimated \$60 million of net operating losses generated prior to the emergence date. The expiration of these tax attributes was fully offset by a corresponding decrease in the Company's U.S. valuation allowance, which results in no net tax provision.

The amount of consolidated U.S. net operating losses ("NOLs") available as of December 31, 2015 is approximately \$146.8 million. This differs from the NOL reported in the Company's financial statements by \$4.5 million which represents the unrealized tax benefits associated with equity compensation and uncertain tax position in accordance with FASB ASC 718, Stock Compensation and FASB ASC 740, Income Taxes. These NOLs will expire in the years

2029 through 2035. The amount of foreign NOL's available as of December 31, 2015 is \$8.9 million which have an indefinite life carry-forward period. In addition, the Company has \$19.5 million of non-expiring alternative minimum tax credits.

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## HERCULES OFFSHORE, INC. AND SUBSIDIARIES

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

During 2015, the Company concluded that the undistributed earnings of its foreign subsidiaries would no longer be considered permanently reinvested. The Company recorded a deferred tax liability of \$4.0 million for the year ended December 31, 2015. This deferred tax liability was fully offset by the U.S. valuation allowance. In accordance with FASB ASC 740, the Company recognizes interest and penalties related to uncertain tax positions in income tax expense. The Company recorded interest and penalties expense (benefit) of \$(0.3) million, \$(1.8) million and \$0.2 million through the Income Tax Benefit (Provision) line of the Consolidated Statements of Operations for the period January 1, 2015 to November 6, 2015 and the years ended December 31, 2014 and 2013, respectively. There was no interest and penalties expense (benefit) for the period November 6, 2015 to December 31, 2015.

The Company, directly or through its subsidiaries, files income tax returns in the United States, and multiple state and foreign jurisdictions. The Company's tax returns for 2008 through 2014 remain open for examination by the taxing authorities in the respective jurisdictions where those returns were filed. Although the Company believes that its estimates are reasonable, the final outcome in the event that the Company is subjected to an audit could be different from that which is reflected in its historical income tax provision and accruals. Such differences could have a material effect on the Company's income tax provision and net income in the period in which such determination is made. In addition TODCO income tax obligations from periods prior to its initial public offering in 2004 are indemnified by Transocean, the former owner of TODCO, under the tax sharing agreement, except for the Trinidad and Tobago jurisdiction.

In accordance with FASB ASC 740, the Company evaluates its deferred tax assets, including net operating losses and credits, to determine if a valuation allowance should be recognized on the consideration of all available evidence using a "more likely than not" standard. Based on the analysis of all factors management concluded that due to the uncertainty regarding the future realization of the net deferred tax asset, a valuation allowance should be recorded. As of December 31, 2015 and 2014, the Company had a valuation allowance of \$107.2 million and \$125.0 million, respectively.

The following table presents the reconciliation of the total amounts of unrecognized tax benefits that, if recognized, would impact the effective income tax rate:

(in thousands)	Successor Period from November 6, 2015 to December 31, 2015	Predecessor Period from January 1, 2015 to November 6, 2015	Year Ended December 31,	
			2014	2013
Balance, beginning of period	\$3,062	\$3,605	\$5,533	\$5,533
Gross increases — tax positions in prior periods	—	—	713	—
Lapse of statute of limitation	—	(543)	(2,641)	—
Balance, end of period	\$3,062	\$3,062	\$3,605	\$5,533

The unrecognized tax benefits may change due to the settlement of audits and the expiration of statutes of limitation in the next twelve months. The Company recognized \$0.9 million of tax benefit, including accrued interest and penalties of \$0.3 million, during the year ended December 31, 2015 as a result of the tolling of statutes of limitations in foreign jurisdictions.

From time to time, the Company's tax returns are subject to review and examination by various tax authorities within the jurisdictions in which the Company operates or has operated. The Company is currently contesting tax assessments in Venezuela, and may contest future assessments where the Company believes the assessments are meritless.

In January 2014, the Federal Inland Revenue Service of Nigeria notified the Company that it will initiate an audit including calendar years 2007 through 2011, which was completed in the first quarter of 2015. In February 2015, the Federal Inland Revenue Service of Nigeria notified the Company that it will examine calendar year 2012 and 2013 corporate income tax returns. While the Company cannot predict or provide assurance regarding the outcome of these

proceedings, the Company does not expect the ultimate liability to have a material effect on its consolidated financial statements.

17. Segments

The Company currently reports its business activities in three business segments: (1) Domestic Offshore, (2) International Offshore, and (3) International Liftboats. The Company eliminates inter-segment revenue and expenses, if any.

The results of operations of the former Domestic Liftboats and Inland segments are reflected in the Consolidated Statement of Operations for the year ended December 31, 2013 as discontinued operations (See Note 9). The financial information of the Company's discontinued operations is not included in the results of operations presented for the Company's reporting segments.

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## HERCULES OFFSHORE, INC. AND SUBSIDIARIES

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

The following describes the Company's reporting segments as of December 31, 2015:

Domestic Offshore - includes 18 jackup rigs in the U.S. Gulf of Mexico that can drill in maximum water depths ranging from 120 to 350 feet. Nine of the jackup rigs are either under contract or available for contracts and nine are cold stacked.

International Offshore — includes nine jackup rigs outside of the U.S. Gulf of Mexico. The Company has three jackup rigs contracted offshore in Saudi Arabia, one jackup rig contracted offshore in Congo, one jackup rig ready stacked and one jackup rig warm stacked in Gabon, one jackup ready stacked in the Netherlands and one jackup rig warm stacked in Malaysia. Additionally, the Company has one newbuild jackup rig under construction in Singapore that is expected to be delivered in the second quarter of 2016.

International Liftboats — includes 19 liftboats. Fifteen are operating or available for contracts offshore West Africa, one is cold stacked offshore West Africa and three are operating or available for contracts in the Middle East region.

The Company's jackup rigs are used primarily for exploration and development drilling in shallow waters. The Company's liftboats are self-propelled, self-elevating vessels with a large open deck space, which provides a versatile, mobile and stable platform to support a broad range of offshore maintenance and construction services throughout the life of an oil or natural gas well.

In November 2013, the Company entered into an agreement with Perisai Drilling Sdn Bhd ("Perisai") whereby the Company agreed to market, manage and operate two Pacific Class 400 design new-build jackup drilling rigs, Perisai Pacific 101 and Perisai Pacific 102 ("Perisai Agreement"). Pursuant to the terms of the agreement, Hercules is reimbursed for all operating expenses and Perisai pays for all capital expenditures. The Company receives a daily management fee for the rig and a daily operational fee equal to 12% of the rig-based EBITDA, as defined in the Perisai Agreement. In August 2014, Perisai Pacific 101 commenced work on a three-year drilling contract in Malaysia. Perisai Pacific 102 was scheduled to be delivered by the shipyard by mid-2015, but delivery has not yet occurred. It is the Company's understanding that Perisai is in discussions with the shipyard to further delay delivery of the rig.

Specific to the Perisai Agreement, the Company recognized the following results in its International Offshore segment:

(in millions)	Successor	Predecessor	Year Ended
	Period from	Period from	
	November 6,	January 1,	December 31,
	2015 to	2015 to	2014
	December 31,	November 6,	
	2015	2015	
Revenue	\$1.3	\$12.1	\$11.1
Operating Expenses	0.8	6.3	5.6

Information regarding the Company's reportable segments is as follows:

(in thousands)	Successor			Predecessor		
	Revenue	Income (Loss) from Operations	Depreciation and Amortization	Revenue	Income (Loss) from Operations	Depreciation and Amortization
Domestic Offshore	\$9,859	\$(608)	\$1,097	\$131,308	\$(8,464)	\$39,031
International Offshore	17,321	(1,635)	1,870	113,438	(95,111)	71,033
International Liftboats	5,262	(3,245)	1,567	58,460	(13,165)	14,599
	\$32,442	\$(5,488)	\$4,534	\$303,206	\$(116,740)	\$124,663
Corporate	—	(3,399)	—	—	(58,889)	2,300

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Total Company	\$32,442	\$(8,887	) \$4,534	\$303,206	\$(175,629	) \$126,963
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## HERCULES OFFSHORE, INC. AND SUBSIDIARIES

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

(in thousands)	Predecessor Year Ended December 31, 2014			Year Ended December 31, 2013		
	Revenue	Income (Loss) from Operations	Depreciation and Amortization	Revenue	Income (Loss) from Operations	Depreciation and Amortization
Domestic Offshore	\$497,209	\$(40,588 )	\$70,576	\$522,705	\$90,202	\$78,526
International Offshore	291,486	302	75,672	190,376	(19,762 )	51,759
International Liftboats	111,556	4,434	20,763	145,219	37,575	18,627
	\$900,251	\$(35,852 )	\$167,011	\$858,300	\$108,015	\$148,912
Corporate	—	(52,647 )	3,887	—	(56,583 )	3,031
Total Company	\$900,251	\$(88,499 )	\$170,898	\$858,300	\$51,432	\$151,943
					Successor December 31, 2015	Predecessor December 31, 2014
(in thousands)						
Total Assets:						
Domestic Offshore					\$298,813	\$511,804
International Offshore					353,600	1,228,247
International Liftboats					164,814	227,776
Corporate					290,913	34,580
Total Company					\$1,108,140	\$2,002,407
			Successor Period from November 6, 2015 to December 31, 2015	Predecessor Period from January 1, 2015 to November 6, 2015	Year Ended December 31,	
(in thousands)					2014	2013
Capital Expenditures:						
Domestic Offshore			\$571	\$3,197	\$54,082	\$63,344
International Offshore (a)			3,937	67,564	83,777	459,685
Inland			—	—	—	396
Domestic Liftboats			—	—	—	5,678
International Liftboats			558	7,336	9,037	12,407
Corporate			—	—	626	3,477
Total Company			\$5,066	\$78,097	\$147,522	\$544,987

(a) 2013 includes a \$166.9 million final shipyard installment payment for each of Hercules Triumph and Hercules Resilience.



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## HERCULES OFFSHORE, INC. AND SUBSIDIARIES

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

A substantial portion of the Company's assets are mobile. Asset locations at the end of the period are not necessarily indicative of the geographic distribution of the revenue generated by such assets during the periods. The following tables present revenue and long-lived assets by country based on the location of the service provided:

(in thousands)	Successor Period from November 6, 2015 to December 31, 2015	Predecessor Period from January 1, 2015 to November 6, 2015	2014	Year Ended December 31, 2013
<b>Operating Revenue:</b>				
United States	\$10,213	\$135,063	\$503,626	\$522,705
Saudi Arabia	11,146	74,974	114,171	114,364
Nigeria	3,148	37,165	75,183	115,314
Gabon	4,897	13,158	64,537	—
India	—	9,832	96,198	17,319
Other (a)	3,038	33,014	46,536	88,598
Total Non-U.S. Countries	22,229	168,143	396,625	335,595
Total Company	\$32,442	\$303,206	\$900,251	\$858,300
			Successor December 31, 2015	Predecessor December 31, 2014
(in thousands)				
<b>Long-Lived Assets:</b>				
United States			\$38,523	\$356,656
Saudi Arabia			92,139	322,004
Nigeria			70,204	112,428
Gabon			126,151	442,192
India			—	45,296
Netherlands			68,682	272,488
Other (a)			75,968	47,046
Total Non-U.S. Countries			433,144	1,241,454
Total Company			\$471,667	\$1,598,110

(a) Other represents countries in which the Company operates that individually had operating revenue or long-lived assets representing less than 10% of total operating revenue or total long-lived assets.

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## HERCULES OFFSHORE, INC. AND SUBSIDIARIES

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

## 18. Commitments and Contingencies

## Operating Leases

The Company has non-cancellable operating lease commitments that expire at various dates through 2017. As of December 31, 2015, future minimum lease payments related to non-cancellable operating leases were as follows (in thousands):

Years Ended December 31,

2016	\$3,365
2017	2,700
2018	—
2019	—
2020	—
Thereafter	—
Total	\$6,065

Rental expense for all operating leases was \$2.5 million, \$12.1 million, \$16.9 million and \$15.1 million for the periods November 6, 2015 to December 31, 2015 and January 1, 2015 to November 6, 2015 and the years ended December 31, 2014 and 2013, respectively, of which \$0.4 million related to discontinued operations is included in Loss from Discontinued Operations, Net of Taxes on the Consolidated Statement of Operations for the year ended December 31, 2013.

## Rig Construction Contract

In May 2014, the Company signed a rig construction contract with Jurong Shipyard Pte Ltd ("JSL") in Singapore to build a High Specification, Harsh Environment rig, Hercules Highlander, which is expected to be delivered in the second quarter of 2016. The shipyard cost of the rig is estimated at approximately \$236 million. Including project management, spares, commissioning and other costs, total delivery cost is estimated at approximately \$270 million of which approximately \$211 million remains to be spent at December 31, 2015. The total delivery cost estimate excludes any customer specific outfitting that is reimbursable to the Company, costs to mobilize the rig to the first well as well as capitalized interest. The Company paid \$23.6 million, or 10% of the shipyard cost, to JSL in May 2014 and made a second 10% payment in May 2015 with the final 80% of the shipyard payment due upon delivery of the rig. \$200.0 million of the proceeds from the Senior Secured Credit Facility were placed in an escrow account and are included in Restricted Cash on the Consolidated Balance Sheet as of December 31, 2015 to be used to finance the remaining installment payment on the Hercules Highlander and the expenses, costs and charges related to the construction and purchase of the Hercules Highlander.

## Legal Proceedings

The Company is involved in various claims and lawsuits in the normal course of business. As of December 31, 2015, management did not believe any accruals were necessary in accordance with FASB ASC 450-20, Contingencies — Loss Contingencies.

## Say-on-Pay Litigation

In June 2011, two separate shareholder derivative actions were filed purportedly on the Company's behalf in response to its failure to receive a majority advisory "say-on-pay" vote in favor of the Company's 2010 executive compensation. On June 8, 2011, the first action was filed in the District Court of Harris County, Texas, and on June 23, 2011, the second action was filed in the United States Court for the District of Delaware. Subsequently, on July 21, 2011, the plaintiff in the Harris County action filed a concurrent action in the United States District Court for the Southern District of Texas. Each action named the Company as a nominal defendant and certain of its officers and directors, as well as the Company's Compensation Committee's consultant, as defendants. Plaintiffs allege that the Company's directors breached their fiduciary duty by approving excessive executive compensation for 2010, that the Compensation Committee consultant aided and abetted that breach of fiduciary duty, that the officer defendants were unjustly enriched by receiving the allegedly excessive compensation, and that the directors violated the federal securities laws by disseminating a materially false and misleading proxy. The plaintiffs seek damages in an

unspecified amount on the Company's behalf from the officer and director defendants, certain corporate governance actions, and an award of their costs and attorney's fees. The Company and the other defendants have filed motions to dismiss these cases for failure to make demand upon the Company's board and for failing to state a claim. On June 11, 2012, the plaintiff in the Harris County action voluntarily dismissed his action. On March 14, 2013, the Company's and the other defendants' motions to dismiss the Delaware federal action were granted. The motions to dismiss the Texas federal action are pending.

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HERCULES OFFSHORE, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

The Company does not expect the ultimate outcome of the shareholder derivative lawsuit to have a material adverse effect on its consolidated results of operations, financial position or cash flows.

**Hercules 265 Litigation**

In January 2015, Cameron International Corporation (“Cameron”), and Axon Pressure Products, Inc. and Axon EP, Inc. (collectively “Axon”) filed third-party complaints against the Company in a subrogation action that Walter Oil & Gas Corporation (“Walter”) and its underwriters, together with Walter’s working interest partners, Tana Exploration Company, LLC and Helis Oil & Gas Company, LLC, filed against Cameron and Axon, among others, to recover an undisclosed amount of damages relating to the well control incident at South Timbalier 220 involving the Hercules 265. In response to Cameron and Axon's third-party complaints, the Company filed counterclaims against Cameron and Axon pursuing contribution and related claims. Subsequently, Walter dismissed Cameron from the subrogation action. Separately, Cameron and Axon have filed answers and claims in a limitation of liability action that the Company filed relating to the incident. In response, the Company filed counterclaims against Axon and Cameron pursuing contribution and related claims. After Walter and the other plaintiffs in the subrogation matter dismissed Cameron, Hercules and Cameron mutually dismissed all claims against each other in both the limitation of liability and subrogation actions. The Company has tendered defense and indemnity to Walter for the remaining claims asserted by Axon and other costs and/or liabilities arising from the incident, pursuant to the terms of the drilling contract between the Company and Walter. Until such time as Walter accepts the tender, the Company will vigorously defend the claims.

**Settlement of Contractual Dispute**

In August 2015, the Company agreed to a settlement of a contractual dispute relating to the sale of certain of our assets in 2006, pursuant to which settlement the Company received a \$5.2 million payment in October 2015 and recorded a gain of the same amount, which is included in General and Administrative on the Consolidated Statement of Operations for the period January 1, 2015 to November 6, 2015.

The Company and its subsidiaries are involved in a number of other lawsuits, all of which have arisen in the ordinary course of business. The Company does not believe that the ultimate liability, if any, resulting from any such other pending litigation will have a material adverse effect on its business or consolidated financial statements.

The Company cannot predict with certainty the outcome or effect of any of the litigation matters specifically described above or of any other pending litigation. There can be no assurance that the Company’s belief or expectations as to the outcome or effect of any lawsuit or other litigation matter will prove correct, and the eventual outcome of these matters could materially differ from management’s current estimates.

**Insurance and Indemnity**

The Company maintains insurance coverage that includes coverage for physical damage, third-party liability, workers’ compensation and employer’s liability, general liability, vessel pollution and other coverages. Effective May 1, 2015, the Company completed the annual renewal of all of its key insurance policies. The Company’s insurance policies typically consist of twelve-month policy periods, and the next renewal date for its insurance program is scheduled for May 1, 2016.

The Company’s drilling contracts provide for varying levels of indemnification from its customers, including for well control and subsurface risks, and in most cases, may require the Company to indemnify its customers for certain liabilities. Under the Company’s drilling contracts, liability with respect to personnel and property is customarily assigned on a “knock-for-knock” basis, which means that the Company and its customers assume liability for their respective personnel and property, regardless of how the loss or damage to the personnel and property may be caused, and even if the Company is grossly negligent. However, some of the Company's customers have been reluctant to extend their indemnity obligations in instances where the Company is grossly negligent. The Company’s customers typically assume responsibility for and agree to indemnify the Company from any loss or liability resulting from pollution or contamination, including clean-up and removal and third-party damages arising from operations under the contract and originating below the surface of the water, including as a result of blowouts or cratering of the well (“Blowout Liability”). The customer’s assumption for Blowout Liability may, in certain circumstances, be contractually

limited or could be determined to be unenforceable in the event of the Company's gross negligence, willful misconduct or other egregious conduct. In addition, the Company may not be indemnified for statutory penalties and punitive damages relating to such pollution or contamination events. The Company generally indemnifies the customer for the consequences of spills of industrial waste or other liquids originating solely above the surface of the water and emanating from its rigs or vessels.

Control-of-well events generally include an unintended flow from the well that cannot be contained by equipment on site (e.g., a blow-out preventer), by increasing the weight of the drilling fluid, or that does not naturally close itself off through what is typically described as "bridging over". The Company carries a contractor's extra expense policy with \$50.0 million primary liability coverage for well control costs, pollution and expenses incurred to redrill wild or lost wells, with excess liability

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## HERCULES OFFSHORE, INC. AND SUBSIDIARIES

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

coverage up to \$200.0 million for pollution liability that is covered in the primary policy. Additionally, the Company carries a contractor's expense policy for the Hercules Triumph and Hercules Resilience with \$50.0 million primary liability coverage for well control costs, pollution and expenses incurred to redrill wild or lost wells, with excess coverage up to \$25.0 million for pollution liability that is covered in the primary policy. The policies are subject to exclusions, limitations, deductibles, self-insured retention and other conditions, including the requirement for Company gross negligence or willful misconduct.

Adequacy of Insurance Coverage

The Company is responsible for the deductible portion of its insurance coverage. Management believes adequate accruals have been made on known and estimated exposures up to the deductible portion of the Company's insurance coverage. Management believes that claims and liabilities in excess of the amounts accrued are adequately insured. However, the Company's insurance is subject to exclusions and limitations, and there is no assurance that such coverage will adequately protect the Company against liability from all potential consequences. In addition, there is no assurance of renewal or the ability to obtain coverage acceptable to the Company.

Hercules 265 Incident and Settlement of Property Damage Insurance Claim

In July 2013, the Company's jackup drilling rig, Hercules 265, a 250' mat-supported cantilevered unit operating in the U.S. Gulf of Mexico Outer Continental Shelf lease block South Timbalier 220, experienced a well control incident. The rig sustained substantial damage in the incident and the Company's insurance underwriters determined that the rig was a constructive total loss. The Company received gross insurance proceeds of \$50.0 million, the rig's insured value, in December 2013 from insurance underwriters and recorded a net insurance gain of \$31.6 million, which is included in Operating Expenses on the Consolidated Statement of Operations for the year ended December 31, 2013, after writing off the rig's net book value of \$18.4 million. The financial information for Hercules 265 has been reported as part of the Domestic Offshore segment. The cause of the incident is unknown. The Company has removal of wreck coverage for this incident up to a total amount of \$110.0 million. During the second quarter of 2014, the Company received gross proceeds of \$9.1 million from the insurance underwriters as reimbursement for a portion of the wreck removal and related costs incurred and used \$2.0 million to repurchase the Hercules 265 hull from the insurance underwriters, which is currently stacked in a Mississippi shipyard. During the period from January 1, 2015 to November 6, 2015, the Company received an additional \$3.5 million in gross proceeds from the insurance underwriters as reimbursement for a portion of the wreck removal and related costs incurred to date. The Company and its insurance underwriters continue to negotiate the insurance recovery amounts for costs related to the salvage of the rig and certain other insured losses.

Sales and Use Tax Audits

Certain of the Company's legal entities are under audit by various taxing authorities for several prior-year periods. These audits are ongoing and the Company is working to resolve all relevant issues. The Company has an accrual of \$10.0 million and \$6.3 million related to these sales and use tax matters, which is included in Accrued Liabilities on the Consolidated Balance Sheets as of December 31, 2015 and 2014, respectively.

19. Unaudited Interim Financial Data

Unaudited interim financial information for the years ended December 31, 2015 and 2014 is as follows:

(in thousands, except per share amounts)	Predecessor Quarter Ended		September 30 (b)	Period from October 1 to November 6 (c)	Successor Period from November 6 to December 31 (d)
	March 31	June 30 (a)			
2015					
Revenue	\$122,619	\$79,249	\$73,804	\$27,534	\$32,442
Operating Loss	(29,958)	) (60,183)	) (68,534)	) (16,954)	) (8,887)
Net Loss	(57,115)	) (88,250)	) (95,351)	) (361,778)	) (23,669)
	—	—	—	—	—

Loss attributable to Noncontrolling Interest					
Net Loss attributable to Hercules Offshore, Inc.	\$(57,115	) \$(88,250	) \$(95,351	) \$(361,778	) \$(23,669
Net Loss attributable to Hercules Offshore, Inc. Per Share:					
Basic and Diluted	\$(0.35	) \$(0.55	) \$(0.59	) \$(2.24	) \$(1.18

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## HERCULES OFFSHORE, INC. AND SUBSIDIARIES

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

(in thousands, except per share amounts)	Predecessor Quarter Ended		September 30 (g)	December 31 (h)
	March 31 (e)	June 30 (f)		
2014				
Revenue	\$256,734	\$242,963	\$221,884	\$178,670
Operating Income (Loss)	57,672	50,049	(70,898 )	(125,322 )
Net Income (Loss)	19,916	6,646	(88,553 )	(154,119 )
Loss attributable to Noncontrolling Interest	—	—	—	—
Net Income (Loss) attributable to Hercules Offshore, Inc.	\$19,916	\$6,646	\$(88,553 )	\$(154,119 )
Net Income (Loss) attributable to Hercules Offshore, Inc. Per Share:				
Basic	\$0.12	\$0.04	\$(0.55 )	\$(0.96 )
Diluted	\$0.12	\$0.04	\$(0.55 )	\$(0.96 )

(a) Includes a \$13.4 million revenue adjustment related to retroactive dayrate concessions on the Hercules 261, Hercules 262 and Hercules 266, \$10.6 million of costs related to financing and restructuring activities, a \$3.6 million net loss on the sale of assets, including six cold-stacked drilling rigs and a \$1.9 million charge related to the termination of the Predecessor Credit Facility (See Notes 1 and 13).

(b) Includes a \$7.6 million bad debt provision in our International Liftboats segment, \$8.3 million of costs related to financing and restructuring activities and a \$14.3 million charge for reorganization items (See Note 6).

(c) Includes a \$342.7 million charge for reorganization items, an \$8.1 million loss on stock-based compensation due to bankruptcy and a \$5.2 million gain on settlement of a contractual dispute (See Notes 6, 10 and 18).

(d) Includes a \$1.3 million charge for reorganization items (See Note 6).

(e) Includes a \$15.2 million charge related to the retirement of a portion of the 7.125% Senior Secured Notes and the issuance of the 6.75% Senior Notes (See Note 13).

(f) Includes a \$17.9 million gain on the sale of three cold-stacked drilling rigs and a \$4.8 million charge related to the retirement of the remaining portion of the 7.125% Senior Secured Notes (See Notes 9 and 13).

(g) Includes a \$4.7 million net gain on the sale of three cold-stacked drilling rigs and \$82.5 million in non-cash asset impairment charges (See Notes 9 and 15).

(h) Includes \$117.0 million in non-cash asset impairment charges (See Note 15).

## 20. Related Parties

The Company engages in transactions in the ordinary course of business with entities with whom certain of the Company's directors or members of management have a relationship. The Company has determined that these transactions were carried out on an arm's-length basis and are not material individually or in the aggregate. All of these transactions were approved in accordance with the Company's Policy on Covered Transactions with Related Persons. The following provides a brief description of these relationships.

The Company's former Chairman of the Board of Directors was serving as a member of the Board of Directors of Global Energy Services, which included the Southwest Oilfield Products division, an oilfield equipment manufacturing company.

A former member of the Company's Board of Directors was serving as a member of the Board of Directors of HCC Insurance Holdings, Inc., a specialty insurance group.

- A former member of the Company's Board of Directors was serving as a member of the Board of Directors of Technip, a provider of project management, engineering and construction for the energy industry.

- The Company holds a three percent ownership in each of Hall-Houston Exploration II, L.P., Hall-Houston Exploration III, L.P. and Hall-Houston Exploration IV, L.P., exploration and production funds.



As of December 31, 2012, the Company had an investment in approximately 32% of the total outstanding equity of Discovery. In 2013, through additional purchases of shares of Discovery's common stock, the Company acquired a 100% interest in Discovery (See Note 8). Two former officers of the Company served on the Board of Directors of Discovery Offshore prior to it becoming a wholly owned subsidiary.

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## PART IV

## Item 15. Exhibits, Financial Statement Schedules

(a) The following documents are included as part of this report:

- (1) Financial Statements
  - (2) Consolidated Financial Statement Schedule on page 52 of this Report.
  - (3) The Exhibits of the Company listed below in Item 15(b)
- (b) Exhibits

Exhibit Number	Description
2.1	— Asset Purchase Agreement, dated February 11, 2011, by and between Hercules Offshore, Inc., SD Drilling LLC and Seahawk Drilling, Inc., Seahawk Global Holdings LLC, Seahawk Mexico Holdings LLC, Seahawk Drilling Management LLC, Seahawk Drilling LLC, Seahawk Offshore Management LLC, Energy Supply International LLC and Seahawk Drilling USA, LLC (incorporated by reference to Exhibit 2.1 to Hercules' Current Report on Form 8-K/A dated February 15, 2011 (File No. 0-51582)).
2.2	— Plan of Conversion (incorporated by reference to Exhibit 2.1 to Hercules' Registration Statement on Form S-1 (Registration No. 333-126457), as amended (the "S-1 Registration Statement"), originally filed on July 8, 2005).
2.3	— Amended and Restated Agreement and Plan of Merger, dated effective as of March 18, 2007, by and among Hercules, THE Hercules Offshore Drilling Company LLC and TODCO (incorporated by reference to Annex A to the Joint Proxy/Statement Prospectus included in Part I of Hercules' Registration Statement on Form S-4 (Registration No. 333-142314), as amended (the "S-4 Registration Statement"), originally filed April 24, 2007).
2.4	— Confirmation Order for Joint Prepackaged Plan of Reorganization (incorporated by reference to Exhibit 2.1 to Hercules' Current Report on Form 8-K filed October 9, 2015) (File No. 0-51582).
2.5	— Solicitation and Disclosure Statement, including Joint Prepackaged Plan of Reorganization under Chapter 11 of the Bankruptcy Code (incorporated by reference to Exhibit 99.1 to Hercules' Current Report on Form 8-K filed July 14, 2015) (File No. 0-51582).
3.1	— Second Amended and Restated Certificate of Incorporation of Hercules Offshore, Inc. dated November 6, 2015 (incorporated by reference to Exhibit 3.1 to Hercules' Current Report on Form 8-A filed November 6, 2015) (File No. 1-37623).
3.2	— Second Amended and Restated By-Laws of Hercules Offshore, Inc. dated December 11, 2015 (incorporated by reference to Exhibit 3.2 to Hercules' Annual Report on Form 10-K for the year ended December 31, 2015) (File No. 1-37623).
4.1	— Form of specimen common stock certificate (incorporated by reference to Exhibit 4.1 to Hercules' Annual Report on Form 10-K for the year ended December 31, 2015) (File No. 1-37623)
4.2	— Warrant Agreement between Hercules Offshore, Inc. and American Stock Transfer & Trust Company, LLC, as Warrant Agent, dated as of November 6, 2015 (incorporated by reference to Exhibit 4.1 to Form 8-A filed November 6, 2015) (File No. 0-51582).
†10.1	— Amended and Restated Executive Employment Agreement, dated February 28, 2012, between the Company and John T. Rynd (incorporated by reference to Exhibit 10.5 to Hercules' Current Report on Form 8-K dated March 2, 2012 (the "March 2012 8-K")) (File No. 0-51582).
†10.2	— Amended and Restated Executive Employment Agreement, dated February 28, 2012, between the Company and Troy L. Carson (incorporated by reference to Exhibit 10.6 to the March 2012 8-K) (File No. 0-51582).
†10.3	— Hercules Offshore, Inc. Amended and Restated Deferred Compensation Plan (incorporated by reference to Exhibit 10.18 to Hercules' Annual Report on Form 10-K for the year ended

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December 31, 2008 (File No. 0-51582)).

- †10.4 — Special Retention Award Agreement, dated January 1, 2011, between Hercules and John T. Rynd (incorporated by reference to Exhibit 10.29 to the 2010 Form 10-K) (File No. 0-51582).
- †10.5 — Hercules Offshore, Inc. 2015 Long-Term Incentive Plan (incorporated by reference to Exhibit 10.5 to Hercules' Annual Report on Form 10-K for the year ended December 31, 2015) (File No. 1-37623).
- †10.6 — Hercules Offshore, Inc. HERO Annual Performance Bonus Plan effective January 1, 2012 (incorporated by reference to Exhibit 10.1 to Hercules' Current Report on Form 8-K dated December 15, 2011) (File No. 0-51582).

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Exhibit Number	Description
†10.7	— Form of Restricted Stock Unit Award Agreement for Directors (incorporated by reference to Exhibit 10.7 to Hercules' Annual Report on Form 10-K for the year ended December 31, 2015) (File No. 1-37623).
10.8	— Asset Purchase Agreement, dated April 3, 2006, by and between Hercules Liftboat Company, LLC and Laborde Marine Lifts, Inc. (incorporated by reference to Exhibit 10.1 to Hercules' Current Report on Form 8-K dated April 3, 2006 (File No. 0-51582)).
10.9	— Asset Purchase Agreement, dated as of August 23, 2006, by and among Hercules International Holdings, Ltd., Halliburton West Africa Ltd. and Halliburton Energy Services Nigeria Limited (incorporated by reference to Exhibit 10.1 to Hercules' Quarterly Report on Form 10-Q for the quarter ended September 30, 2006 (File No. 0-51582)).
10.10	— First Amendment to Asset Purchase Agreement, dated as of November 1, 2006, by and among Hercules International Holdings, Ltd., Hercules Oilfield Services Ltd., Halliburton West Africa Ltd. and Halliburton Energy Services Nigeria Limited (incorporated by reference to Exhibit 10.2 to Hercules' Quarterly Report on Form 10-Q for the quarter ended September 30, 2006 (File No. 0-51582)).
10.11	— Earnout Agreement, dated November 7, 2006, by and among Hercules Oilfield Services, Ltd., Halliburton West Africa Ltd. and Halliburton Energy Services Nigeria Limited (incorporated by reference to Exhibit 10.3 to Hercules' Current Report on Form 8-K dated November 7, 2006 (File No. 0-51582)).
10.12	— Credit Agreement dated as of November 6, 2015, among Hercules Offshore, Inc., the Subsidiary Guarantors, the Lenders, and Jefferies Finance LLC, as administrative agent for the Lenders and as collateral agent for the Secured Parties (incorporated by reference to Exhibit 10.1 to the Current Report on Form 8-K filed November 6, 2015) (File No. 1-37623).
21.1	— Subsidiaries of Hercules (incorporated by reference to Exhibit 21.1 to Hercules' Annual Report on Form 10-K for the year ended December 31, 2015) (File No. 1-37623).
*23.1	— Consent of Ernst & Young LLP.
*31.1	— Certification of Chief Executive Officer of Hercules pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
*31.2	— Certification of Chief Financial Officer of Hercules pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
*32.1	— Certification of the Chief Executive Officer and the Chief Financial Officer of Hercules pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
*101.INS	XBRL Instance Document
*101.SCH	XBRL Schema Document
*101.CAL	XBRL Calculation Linkbase Document
*101.DEF	XBRL Definition Linkbase Document
*101.LAB	XBRL Label Linkbase Document
*101.PRE	XBRL Presentation Linkbase Document

\* Filed herewith.

† Compensatory plan, contract or arrangement.

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## (c) Financial Statement Schedules

## (1) Valuation and Qualifying Accounts and Allowances

## SCHEDULE II

## HERCULES OFFSHORE, INC. AND SUBSIDIARIES

## VALUATION AND QUALIFYING ACCOUNTS AND ALLOWANCES

Description	Balance at Beginning of Period (in thousands)	Additions		Deductions	Balance at End of Period
		Charged to Expense, Net	Charged to Other Accounts		
Successor					
Period from November 6, 2015 to December 31, 2015					
Allowance for doubtful accounts receivable	\$—	\$1,855	\$—	\$—	\$1,855
Valuation allowance of deferred tax assets	\$104,679	\$2,534	\$—	\$—	\$107,213
Predecessor					
Period from January 1, 2015 to November 6, 2015					
Allowance for doubtful accounts receivable	\$5,677	\$7,665	\$—	\$(13,342 ) (a)	\$—
Valuation allowance of deferred tax assets	\$125,021	\$(20,342 )	\$—	\$—	\$104,679
Year Ended December 31, 2014:					
Allowance for doubtful accounts receivable	\$891	\$5,627	\$—	\$(841 )	\$5,677
Valuation allowance of deferred tax assets	61,913	62,721	387	(b) —	125,021
Year Ended December 31, 2013:					
Allowance for doubtful accounts receivable	\$788	\$642	\$—	\$(539 )	\$891
Valuation allowance of deferred tax assets	—	63,732	(1,819 ) (c)	—	61,913

(a) Includes a fresh-start accounting adjustment of \$13.2 million to adjust the carrying value of accounts receivable to fair value, eliminating the allowance for doubtful accounts (see Note 2).

(b) Adjustment to unrecognized tax benefit recorded net of valuation allowance.

(c) Adjustment to unrecognized tax balance in foreign jurisdiction to recognize impact of federal valuation allowance. All other financial statement schedules have been omitted because they are not applicable or not required, or the information required thereby is included in the consolidated financial statements or the notes thereto included in this annual report.

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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, in the City of Houston, State of Texas, on April 7, 2016.

HERCULES OFFSHORE, INC.

By: /S/ JOHN T. RYND  
John T. Rynd  
Chief Executive Officer and President

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