HELIX ENERGY SOLUTIONS GROUP INC
Form 10-Q
July 23, 2014

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

Form 10-Q

[X] Quarterly report pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934
For the quarterly period ended June 30, 2014

or

[ ] Transition report pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934
For the transition period from__________ to__________

Commission File Number 001-32936
HELIX ENERGY SOLUTIONS GROUP, INC.
(Exact name of registrant as specified in its charter)

Minnesota (State or other jurisdiction of incorporation or organization)	95–3409686 (I.R.S. Employer Identification No.)
3505 West Sam Houston Parkway North Suite 400 Houston, Texas (Address of principal executive offices)	77043 (Zip Code)

(281) 618–0400
(Registrant's telephone number, including area code)

NOT APPLICABLE
(Former name, former address and former fiscal year, if changed since last report)

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 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 [ ] (Do not check if a smaller reporting company)	Smaller reporting company [ ]

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

As of July 18, 2014, 105,541,539 shares of common stock were outstanding.

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PART I. FINANCIAL INFORMATION

Item 1. Financial Statements

HELIX ENERGY SOLUTIONS GROUP, INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATED BALANCE SHEETS
(in thousands)

	June 30, 2014 (Unaudited)	December 31, 2013
ASSETS		
Current assets:		
Cash and cash equivalents	$ 501,457	$ 478,200
Accounts receivable:		
Trade, net of allowance for uncollectible accounts of $5,971 and $2,234, respectively	189,445	156,925
Unbilled revenue	35,797	25,732
Costs in excess of billing	1,508	1,508
Income tax receivable, net	23,771	—
Current deferred tax assets	24,370	51,573
Other current assets	41,917	29,709
Total current assets	818,265	743,647
Property and equipment	2,072,116	1,963,706
Less accumulated depreciation	(467,928)	(431,489)
Property and equipment, net	1,604,188	1,532,217
Other assets:		
Equity investments	152,877	157,919
Goodwill	63,829	63,230
Other assets, net	61,951	47,267
Total assets	$ 2,701,110	$ 2,544,280
LIABILITIES AND SHAREHOLDERS' EQUITY		
Current liabilities:		
Accounts payable	$ 157,553	$ 72,602
Accrued liabilities	79,130	96,482
Income tax payable	—	760
Current maturities of long-term debt	20,508	20,376
Total current liabilities	257,191	190,220
Long-term debt	538,254	545,776
Deferred tax liabilities	272,448	265,879
Other non-current liabilities	11,297	18,295
Total liabilities	1,079,190	1,020,170
Commitments and contingencies		
Shareholders' equity:		
Common stock, no par, 240,000 shares authorized, 105,535 and 105,640 shares issued, respectively	935,821	933,507
Retained earnings	697,733	586,232

Accumulated other comprehensive loss		(11,634)		(20,688)
Total controlling interest shareholders' equity		1,621,920		1,499,051
Noncontrolling interests		—		25,059
Total equity		1,621,920		1,524,110
Total liabilities and shareholders' equity	$	2,701,110	$	2,544,280

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

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HELIX ENERGY SOLUTIONS GROUP, INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS
(UNAUDITED)
(in thousands, except per share amounts)

	Three Months Ended June 30, 2014		Three Months Ended June 30, 2013	
	2014		2013	
Net revenues	$	305,587	$	232,178
Cost of sales		196,449		164,681
Gross profit		109,138		67,497
Loss on disposition of assets		(1,078)		(1,085)
Selling, general and administrative expenses		(29,304)		(19,215)
Income from operations		78,756		47,197
Equity in earnings (losses) of investments		(507)		683
Net interest expense		(4,517)		(11,344)
Loss on early extinguishment of long-term debt		—		(646)
Other expense, net		(17)		(566)
Other income – oil and gas		1,596		1,282
Income before income taxes		75,311		36,606
Income tax provision		17,529		8,577
Net income from continuing operations		57,782		28,029
Loss from discontinued operations, net of tax		—		(29)
Net income, including noncontrolling interests		57,782		28,000
Less net income applicable to noncontrolling interests		—		(789)
Net income applicable to Helix	$	57,782	$	27,211
Basic earnings per share of common stock:				
Continuing operations	$	0.55	$	0.26
Discontinued operations		—		—
Net income per common share	$	0.55	$	0.26
Diluted earnings per share of common stock:				
Continuing operations	$	0.55	$	0.26
Discontinued operations		—		—
Net income per common share	$	0.55	$	0.26
Weighted average common shares outstanding:				
Basic		104,992		105,046
Diluted		105,295		105,133

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

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HELIX ENERGY SOLUTIONS GROUP, INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS
(UNAUDITED)
(in thousands, except per share amounts)

	Six Months Ended June 30, 2014	Six Months Ended June 30, 2013
Net revenues	$ 559,159	$ 429,607
Cost of sales	374,175	309,543
Gross profit	184,984	120,064
Loss on commodity derivative contracts	—	(14,113)
Gain (loss) on disposition of assets, net	10,418	(1,085)
Selling, general and administrative expenses	(49,698)	(42,431)
Income from operations	145,704	62,435
Equity in earnings of investments	201	1,293
Net interest expense	(9,000)	(21,667)
Loss on early extinguishment of long-term debt	—	(3,528)
Other expense, net	(827)	(4,250)
Other income – oil and gas	13,872	4,100
Income before income taxes	149,950	38,383
Income tax provision	37,946	9,020
Net income from continuing operations	112,004	29,363
Income from discontinued operations, net of tax	—	1,029
Net income, including noncontrolling interests	112,004	30,392
Less net income applicable to noncontrolling interests	(503)	(1,566)
Net income applicable to Helix	$ 111,501	$ 28,826
Basic earnings per share of common stock:		
Continuing operations	$ 1.06	$ 0.26
Discontinued operations	—	0.01
Net income per common share	$ 1.06	$ 0.27
Diluted earnings per share of common stock:		
Continuing operations	$ 1.05	$ 0.26
Discontinued operations	—	0.01
Net income per common share	$ 1.05	$ 0.27
Weighted average common shares outstanding:		
Basic	105,059	105,039
Diluted	105,359	105,141

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

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HELIX ENERGY SOLUTIONS GROUP, INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME
(UNAUDITED)
(in thousands)

	Three Months Ended June 30, 2014	Three Months Ended June 30, 2013
Net income, including noncontrolling interests	$ 57,782	$ 28,000
Other comprehensive income (loss), net of tax:		
Unrealized loss on hedges arising during the period	(4,129)	(5,882)
Reclassification adjustments for loss included in net income	610	354
Income taxes on unrealized loss on hedges	1,232	1,935
Unrealized loss on hedges, net of tax	(2,287)	(3,593)
Foreign currency translation gain (loss)	6,931	(218)
Other comprehensive income (loss), net of tax	4,644	(3,811)
Comprehensive income	62,426	24,189
Less comprehensive income applicable to noncontrolling interests	—	(789)
Comprehensive income applicable to Helix	$ 62,426	$ 23,400

	Six Months Ended June 30, 2014	Six Months Ended June 30, 2013
Net income, including noncontrolling interests	$ 112,004	$ 30,392
Other comprehensive income (loss), net of tax:		
Unrealized loss on hedges arising during the period	(74)	(17,167)
Reclassification adjustments for loss included in net income	1,268	504
Income taxes on unrealized (gain) loss on hedges	(418)	5,832
Unrealized gain (loss) on hedges, net of tax	776	(10,831)
Foreign currency translation gain (loss)	8,278	(11,299)
Other comprehensive income (loss), net of tax	9,054	(22,130)
Comprehensive income	121,058	8,262
Less comprehensive income applicable to noncontrolling interests	(503)	(1,566)
Comprehensive income applicable to Helix	$ 120,555	$ 6,696

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

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HELIX ENERGY SOLUTIONS GROUP, INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
(UNAUDITED)
(in thousands)

	Six Months Ended June 30, 2014	Six Months Ended June 30, 2013
Cash flows from operating activities:		
Net income, including noncontrolling interests	$ 112,004	$ 30,392
Adjustments to reconcile net income, including noncontrolling interests, to net cash provided by (used in) operating activities:		
Income from discontinued operations	—	(1,029)
Depreciation and amortization	52,853	49,692
Amortization of deferred financing costs	2,435	2,824
Stock-based compensation expense	3,755	5,473
Amortization of debt discount	2,765	2,557
Deferred income taxes	27,669	16,058
Excess tax from stock-based compensation	(382)	(383)
(Gain) loss on disposition of assets, net	(10,418)	1,085
Loss on early extinguishment of debt	—	3,528
Unrealized loss and ineffectiveness on derivative contracts, net	69	638
Changes in operating assets and liabilities:		
Accounts receivable, net	(40,687)	(19,702)
Other current assets	(1,998)	15,479
Income tax payable, net of income tax receivable	(24,376)	(56,454)
Accounts payable and accrued liabilities	15,169	(35,081)
Oil and gas asset retirement costs	(857)	(5,950)
Other noncurrent, net	1,504	(7,117)
Net cash provided by operating activities	139,505	2,010
Net cash used in discontinued operations	—	(30,503)
Net cash provided by (used in) operating activities	139,505	(28,493)
Cash flows from investing activities:		
Capital expenditures	(93,001)	(102,383)
Distributions from equity investments, net	4,849	4,567
Proceeds from sale of assets	11,074	108,250
Acquisition of noncontrolling interests	(20,085)	—
Net cash provided by (used in) investing activities	(97,163)	10,434
Net cash provided by discontinued operations	—	582,965
Net cash provided by (used in) investing activities	(97,163)	593,399
Cash flows from financing activities:		
Borrowings under revolving credit facility	—	47,617
Repayment of revolving credit facility	—	(147,617)
Repurchase of Convertible Senior Notes due 2025	—	(3,487)
Repayment of term loans	(7,500)	(367,181)
Repayment of MARAD borrowings	(2,655)	(2,529)
Deferred financing costs	—	(10,932)

Distributions to noncontrolling interests	(1,018)	(2,033)
Repurchases of common stock	(6,653)	(5,562)
Excess tax from stock-based compensation	382	383
Exercise of stock options, net and other	—	(186)
Proceeds from issuance of ESPP shares	1,932	—
Net cash used in financing activities	(15,512)	(491,527)
Effect of exchange rate changes on cash and cash equivalents	(3,573)	3,048
Net increase in cash and cash equivalents	23,257	76,427
Cash and cash equivalents:		
Balance, beginning of year	478,200	437,100
Balance, end of period	$ 501,457	$ 513,527

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

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HELIX ENERGY SOLUTIONS GROUP, INC. AND SUBSIDIARIES
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

Note 1 — Basis of Presentation and Recent Accounting Standards

The accompanying condensed consolidated financial statements include the accounts of Helix Energy Solutions Group, Inc. and its wholly- and majority-owned subsidiaries (collectively, "Helix" or the "Company"). Unless the context indicates otherwise, the terms "we," "us" and "our" in this report refer collectively to Helix and its wholly- and majority-owned subsidiaries. All material intercompany accounts and transactions have been eliminated. These unaudited condensed consolidated financial statements have been prepared pursuant to instructions for the Quarterly Report on Form 10-Q required to be filed with the Securities and Exchange Commission (the "SEC"), and do not include all information and footnotes normally included in annual financial statements prepared in accordance with U.S. generally accepted accounting principles.

The accompanying condensed consolidated financial statements have been prepared in conformity with U.S. generally accepted accounting principles ("U.S. GAAP") and are consistent in all material respects with those applied in our 2013 Annual Report on Form 10-K ("2013 Form 10-K"). The preparation of these financial statements requires us to make estimates and judgments that affect the amounts reported in the financial statements and the related disclosures. Actual results may differ from our estimates. We have made all adjustments (which were normal recurring adjustments unless otherwise disclosed herein) that we believe are necessary for a fair presentation of the condensed consolidated balance sheets, statements of operations, statements of comprehensive income, and statements of cash flows, as applicable. The operating results for the three- and six-month periods ended June 30, 2014 are not necessarily indicative of the results that may be expected for the year ending December 31, 2014. Our balance sheet as of December 31, 2013 included herein has been derived from the audited balance sheet as of December 31, 2013 included in our 2013 Form 10-K. These unaudited condensed consolidated financial statements should be read in conjunction with the annual audited consolidated financial statements and notes thereto included in our 2013 Form 10-K.

Certain reclassifications were made to previously-reported amounts in the consolidated financial statements and notes thereto to make them consistent with the current presentation format.

In April 2014, the Financial Accounting Standards Board (the "FASB") issued Accounting Standards Update ("ASU") No. 2014-08, "Presentation of Financial Statements (Topic 205) and Property, Plant, and Equipment (Topic 360): Reporting Discontinued Operations and Disclosures of Disposals of Components of an Entity". This ASU changes the criteria for determining which disposals can be presented as discontinued operations and modifies related disclosure requirements. Under the new guidance, a discontinued operation is defined as a disposal of a component or group of components that is disposed of or is classified as held for sale and represents a strategic shift that has or will have a major effect on an entity's operations and financial results. The ASU applies prospectively to new disposals and new classifications of disposal groups as held for sale that occur within annual periods beginning on or after December 15, 2014, including interim periods. The adoption of this ASU is not expected to have a significant effect on our consolidated financial statements.

In May 2014, the FASB issued ASU No. 2014-09, "Revenue from Contracts with Customers (Topic 606)". This ASU provides a single five-step approach to account for revenue arising from contracts with customers. The ASU requires entities to recognize revenue in a way that depicts 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. This guidance is effective prospectively for annual reporting periods beginning after December 15, 2016, including interim periods. Early adoption is not permitted. The guidance permits companies to either apply the requirements retrospectively to all prior periods presented, or apply the requirements in the year of adoption through a cumulative adjustment. We are currently evaluating which transition approach to use and the potential impact the adoption of this new standard may have on our consolidated financial statements.

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Note 2 — Company Overview

Our Operations

We are an international offshore energy company that provides specialty services to the offshore energy industry, with a focus on well intervention and robotics operations. We seek to provide services and methodologies that we believe are critical to developing offshore reservoirs and maximizing production economics. We provide services primarily in deepwater in the Gulf of Mexico, North Sea, Asia Pacific and West Africa regions. Our "life of field" services are segregated into four business segments: Well Intervention, Robotics, Subsea Construction and Production Facilities (Note 11). Our Subsea Construction segment was significantly diminished following the sale of substantially all of our assets related to this reportable segment during 2013 and early 2014 (see Note 2 to our 2013 Form 10-K and Note 2 to our Quarterly Report on Form 10-Q for the three-month period ended March 31, 2014). Our Production Facilities segment includes the Helix Producer I ("HP I") vessel (which we now own 100% after acquiring our minority partner's noncontrolling interests in the entity that owns the vessel for $20.1 million in February 2014) as well as our equity investments in Deepwater Gateway, L.L.C. ("Deepwater Gateway") and Independence Hub, LLC ("Independence Hub") (Note 5). The Production Facilities segment also includes the Helix Fast Response System ("HFRS"), which provides certain operators access to our Q4000 and HP I vessels.

Discontinued Operations

In February 2013, we sold Energy Resource Technology GOM, Inc. ("ERT"), a former wholly-owned U.S. subsidiary that conducted our oil and gas operations in the Gulf of Mexico, for $624 million plus additional consideration in the form of overriding royalty interests in ERT's Wang well and certain exploration prospects. As a result, we have presented the historical operating results of our former Oil and Gas segment as discontinued operations in the accompanying condensed consolidated financial statements. See Note 3 to our 2013 Form 10-K for additional information regarding our discontinued operations and Note 6 regarding the use of a portion of the sale proceeds to reduce our indebtedness under our former credit agreement.

Note 3 — Details of Certain Accounts

Other current assets and other assets, net consist of the following (in thousands):

	June 30, 2014	December 31, 2013
Note receivable (1)	$ 10,000	$ —
Other receivables	1,503	785
Prepaid insurance	366	7,038
Other prepaids	16,880	12,999
Spare parts inventory	2,656	1,038
Value added tax receivable	10,318	7,589
Other	194	260
Total other current assets	$ 41,917	$ 29,709

	June 30, 2014	December 31, 2013
Note receivable (1)	$ 20,000	$ —
Deferred dry dock expenses, net	18,139	20,833

Deferred financing costs, net (Note 6)		22,055		24,297
Intangible assets with finite lives, net		654		622
Other		1,103		1,515
Total other assets, net	$	61,951	$	47,267

(1) Relates to the promissory note we received in connection with the sale of our Ingleside spoolbase in January 2014. Interest on the note is payable quarterly at a rate of 6% per annum. A $10 million principal reduction in the note's balance is required to be paid on each December 31 in 2014, 2015 and 2016.

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Accrued liabilities consist of the following (in thousands):

	June 30, 2014	December 31, 2013
Accrued payroll and related benefits	$ 41,892	$ 50,527
Current asset retirement obligations	627	2,024
Unearned revenue	15,101	19,608
Billing in excess of cost	—	1,677
Accrued interest	4,213	4,187
Derivative liability (Note 15)	3,545	2,651
Taxes payable excluding income tax payable	5,984	4,811
Pipelay assets sale deposit	—	5,000
Other	7,768	5,997
Total accrued liabilities	$ 79,130	$ 96,482

Note 4 — Statement of Cash Flow Information

We define cash and cash equivalents as cash and all highly liquid financial instruments with original maturities of three months or less. The following table provides supplemental cash flow information (in thousands):

	Six Months Ended June 30,	
	2014	2013
Interest paid, net of interest capitalized	$ 5,960	$ 20,403
Income taxes paid	$ 35,268	$ 49,981

Our non-cash investing activities include accruals for property and equipment capital expenditures. These non-cash investing accruals totaled $65.4 million for the six-month period ended June 30, 2014, which included $57.8 million related to a shipyard payment made in early July 2014, and $10.7 million for the six-month period ended June 30, 2013. Additionally, $30 million of our non-cash investing activities relates to the promissory note we received in connection with the sale of our Ingleside spoolbase in January 2014 (Note 3).

Note 5 — Equity Investments

As of June 30, 2014, we had two investments that we account for using the equity method of accounting: Deepwater Gateway and Independence Hub, both of which are included in our Production Facilities segment.

Deepwater Gateway, L.L.C. In June 2002, we, along with Enterprise Products Partners L.P. (“Enterprise”), formed Deepwater Gateway, each with a 50% interest, to design, construct, install, own and operate a tension leg platform production hub primarily for Anadarko Petroleum Corporation's Marco Polo field in the Deepwater Gulf of Mexico. Our investment in Deepwater Gateway totaled $82.3 million and $85.8 million as of June 30, 2014 and December 31, 2013, respectively (including capitalized interest of $1.3 million at June 30, 2014 and December 31, 2013).

Independence Hub, LLC. In December 2004, we acquired a 20% interest in Independence Hub, an affiliate of Enterprise. Independence Hub owns the “Independence Hub” platform located in Mississippi Canyon Block 920 in a water depth of 8,000 feet. Our investment in Independence Hub was $70.6 million and $72.1 million as of June 30, 2014 and December 31, 2013, respectively (including capitalized interest of $4.1 million and $4.3 million at June 30, 2014 and December 31, 2013, respectively).

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We received the following distributions from these equity investments (in thousands):

	Three Months Ended June 30, 2014	Three Months Ended June 30, 2013	Six Months Ended June 30, 2014	Six Months Ended June 30, 2013
Deepwater Gateway	$ 1,750	$ 2,000	$ 3,750	$ 3,500
Independence Hub	500	1,200	1,300	2,360
Total	$ 2,250	$ 3,200	$ 5,050	$ 5,860

Note 6 — Long-Term Debt

Scheduled maturities of our long-term debt outstanding as of June 30, 2014 are as follows (in thousands):

	Term Loan	MARAD Debt	2032 Notes (1)	Total
Less than one year	$ 15,000	$ 5,508	$ —	$ 20,508
One to two years	30,000	5,783	—	35,783
Two to three years	30,000	6,072	—	36,072
Three to four years	30,000	6,375	—	36,375
Four to five years	180,000	6,693	—	186,693
Over five years	—	67,082	200,000	267,082
Total debt	285,000	97,513	200,000	582,513
Current maturities	(15,000)	(5,508)	—	(20,508)
Long-term debt, less current maturities	270,000	92,005	200,000	562,005
Unamortized debt discount (2)	—	—	(23,751)	(23,751)
Long-term debt	$ 270,000	$ 92,005	$ 176,249	$ 538,254

(1) Beginning in March 2018, the holders of the Convertible Senior Notes due 2032 may require us to repurchase these notes or we may at our option elect to repurchase these notes. The notes will mature in March 2032.

(2) The Convertible Senior Notes due 2032 will increase to their principal amount through accretion of non-cash interest charges through March 2018.

Included below is a summary of certain components of our indebtedness:

Credit Agreement

In June 2013, we entered into a Credit Agreement (the “Credit Agreement”) with a group of lenders pursuant to which we borrowed $300 million under the Credit Agreement’s term loan (the “Term Loan”) component and may borrow revolving loans (the “Revolving Loans”) and/or obtain letters of credit under a revolving credit facility up to an outstanding amount of $600 million (the “Revolving Credit Facility”). Subject to customary conditions, we may request an increase of up to $200 million in aggregate commitments with respect to the Revolving Credit Facility, additional term loans or a combination thereof. The $300 million we borrowed under the Term Loan was in connection with our early redemption of the remaining $275 million Senior Unsecured Notes outstanding in July 2013 (see “Senior Unsecured Notes” below).

The Term Loan and the Revolving Loans (together, the "Loans"), at our election, will bear interest either in relation to the base rate established by Bank of America N.A. or to a LIBOR rate, provided that all Swing Line Loans (as defined in the Credit Agreement) will be base rate loans. The Term Loan currently bears interest at the one-month LIBOR rate plus 2.5%. In September 2013, we entered into various interest rate swap contracts to fix the one-month LIBOR rate on $148.1 million of the Term Loan. The fixed LIBOR rates were between 74 and 75 basis points.

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The Loans or portions thereof bearing interest at the base rate will bear interest at a per annum rate equal to the base rate plus a margin ranging from 1.00% to 2.00%. The Loans or portions thereof bearing interest at a LIBOR rate will bear interest at the LIBOR rate selected by us plus a margin ranging from 2.00% to 3.00%. A letter of credit fee is payable by us equal to our applicable margin for LIBOR rate Loans multiplied by the daily amount available to be drawn under outstanding letters of credit. Margins on the Loans will vary in relation to the consolidated coverage ratio, as provided by the Credit Agreement. We also pay a fixed commitment fee of 0.5% on the unused portion of our Revolving Credit Facility. At June 30, 2014, our availability under the Revolving Credit Facility totaled $582.5 million, net of $17.5 million of letters of credit issued.

The Term Loan is repayable in scheduled principal installments of 5% in each of the initial two loan years ($15 million per year), and 10% in each of the remaining three loan years ($30 million per year), payable quarterly, with a balloon payment of $180 million at maturity. These installment amounts are subject to adjustment for any prepayments on the Term Loan. We may elect to prepay amounts outstanding under the Term Loan without premium or penalty, but may not reborrow any amounts prepaid. We may prepay amounts outstanding under the Revolving Loans without premium or penalty, and may reborrow any amounts paid up to the amount of the Revolving Credit Facility. The Loans mature on June 19, 2018. In certain circumstances, we will be required to prepay the Loans.

The Credit Agreement and the other documents entered into in connection with the Credit Agreement (together, the "Loan Documents") include terms and conditions, including covenants, which we consider customary for this type of transaction. The covenants include restrictions on our and our subsidiaries' ability to grant liens, incur indebtedness, make investments, merge or consolidate, sell or transfer assets, pay dividends and incur capital expenditures. In addition, the Credit Agreement obligates us to meet certain financial ratios, including the Consolidated Interest Coverage Ratio and the Consolidated Leverage Ratio (as defined in the Credit Agreement). We designated one of our then existing foreign subsidiaries, and may designate any newly established foreign subsidiaries, as subsidiaries that are not generally subject to the covenants in the Credit Agreement (the "Unrestricted Subsidiaries"), provided we meet certain liquidity requirements, in which case the EBITDA of the Unrestricted Subsidiaries is not included in the calculations with respect to our financial covenants. Our obligations under the Credit Agreement are guaranteed by our domestic subsidiaries (except Cal Dive I – Title XI, Inc.) and Canyon Offshore Limited. Our obligations under the Credit Agreement, and of the guarantors under their guaranty, are secured by most of our assets and assets of the guarantors and Canyon Offshore Limited, plus pledges of up to two-thirds of the shares of certain foreign subsidiaries.

Convertible Senior Notes Due 2032

In March 2012, we completed a public offering and sale of $200.0 million in aggregate principal amount of 3.25% Convertible Senior Notes due 2032 (the "2032 Notes"). The net proceeds from the issuance of the 2032 Notes were $195.0 million after deducting the underwriter's discounts and commissions and offering expenses. We used the net proceeds to repurchase and retire $142.2 million of aggregate principal amount of our 3.25% Convertible Senior Notes due 2025 in separate, privately negotiated transactions (see Note 7 to our 2013 Form 10-K for additional information). The remaining net proceeds were used for general corporate purposes, including the repayment of other indebtedness.

The 2032 Notes bear interest at a rate of 3.25% per annum, and are payable semi-annually in arrears on March 15 and September 15 of each year, beginning on September 15, 2012. The 2032 Notes will mature on March 15, 2032, unless earlier converted, redeemed or repurchased. The 2032 Notes are convertible in certain circumstances and during certain periods at an initial conversion rate of 39.9752 shares of common stock per $1,000 principal amount (which represents an initial conversion price of approximately $25.02 per share of common stock), subject to adjustment in certain circumstances as set forth in the Indenture governing the 2032 Notes.

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Prior to March 20, 2018, the 2032 Notes are not redeemable. On or after March 20, 2018, we, at our option, may redeem some or all of the 2032 Notes in cash, at any time, upon at least 30 days' notice at a price equal to 100% of the principal amount plus accrued and unpaid interest (including contingent interest, if any) up to but excluding the redemption date. In addition, the holders of the 2032 Notes may require us to purchase in cash some or all of their 2032 Notes at a repurchase price equal to 100% of the principal amount of the 2032 Notes, plus accrued and unpaid interest (including contingent interest, if any) up to but excluding the applicable repurchase date, on March 15, 2018, March 15, 2022 and March 15, 2027, or, subject to specified exceptions, at any time prior to the 2032 Notes' maturity following a fundamental change (as defined in the Indenture governing the 2032 Notes).

In connection with the issuance of the 2032 Notes, we recorded a discount of $35.4 million as required under existing accounting rules. To arrive at this discount amount, we estimated the fair value of the liability component of the 2032 Notes as of the date of their issuance (March 12, 2012) using an income approach. To determine this estimated fair value, we used borrowing rates of similar market transactions involving comparable liabilities at the time of issuance and an expected life of 6.0 years. In selecting the expected life, we selected the earliest date upon which the holders could require us to repurchase all or a portion of the 2032 Notes (March 15, 2018). The effective interest rate for the 2032 Notes is 6.9% after considering the effect of the accretion of the related debt discount that represented the equity component of the 2032 Notes at their inception.

MARAD Debt

This U.S. government guaranteed financing (the "MARAD Debt") is pursuant to Title XI of the Merchant Marine Act of 1936 administered by the Maritime Administration, and was used to finance the construction of the Q4000. The MARAD Debt is payable in equal semi-annual installments beginning in August 2002 and matures in February 2027. The MARAD Debt is collateralized by the Q4000, is guaranteed 50% by us, and initially bore interest at a floating rate that approximated AAA Commercial Paper yields plus 20 basis points. As provided for in the MARAD Debt agreements, in September 2005, we fixed the interest rate on the debt through the issuance of a 4.93% fixed-rate note with the same maturity date.

Former Credit Facility

Similar to our current Credit Agreement, our former credit facility contained both term loan and revolving loan components. This indebtedness was scheduled to mature on July 1, 2015. In February 2013, we repaid $318.4 million of borrowings outstanding under our former credit facility with the proceeds from the sale of ERT. In connection with the repayment of this debt in February 2013, we recorded a $2.9 million charge to accelerate a pro rata portion of the deferred financing costs associated with our former term loan debt. This charge is reflected as a component of "Loss on early extinguishment of long-term debt" in the accompanying condensed consolidated statement of operations for the six-month period ended June 30, 2013. We fully repaid the remaining indebtedness outstanding under our former credit facility in June 2013.

Senior Unsecured Notes

In December 2007, we issued $550 million of 9.5% Senior Unsecured Notes due 2016 (the "Senior Unsecured Notes"). We had $275 million of the Senior Unsecured Notes outstanding at the beginning of 2013. We fully redeemed these notes in July 2013 (see Note 7 to our 2013 Form 10-K).

Other

In accordance with our Credit Agreement, the 2032 Notes and MARAD Debt agreements, we are required to comply with certain covenants, including certain financial ratios such as a consolidated interest coverage ratio and consolidated leverage ratio, as well as the maintenance of minimum net worth, working capital and debt-to-equity requirements. As of June 30, 2014, we were in compliance with these covenants.

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Unamortized deferred financing costs are included in "Other assets, net" in the accompanying condensed consolidated balance sheets and are amortized over the life of the respective debt agreements. The following table reflects the components of our deferred financing costs (in thousands):

	June 30, 2014			December 31, 2013		
	Gross Carrying Amount	Accumulated Amortization	Net	Gross Carrying Amount	Accumulated Amortization	Net
Term Loan (matures June 2018) (1)	$ 3,638	$ (728)	$ 2,910	$ 3,638	$ (364)	$ 3,274
Revolving Credit Facility (matures June 2018) (1)	13,275	(2,655)	10,620	13,275	(1,327)	11,948
2032 Notes (mature March 2032)	3,759	(1,455)	2,304	3,759	(1,148)	2,611
MARAD Debt (matures February 2027)	12,200	(5,979)	6,221	12,200	(5,736)	6,464
Total deferred financing costs	$ 32,872	$ (10,817)	$ 22,055	$ 32,872	$ (8,575)	$ 24,297

(1) Relates to amounts allocated to the existing Term Loan and Revolving Credit Facility, which became effective in June 2013.

The following table details the components of our net interest expense (in thousands):

	Three Months Ended June 30,		Six Months Ended June 30,	
	2014	2013	2014	2013 (1)
Interest expense	$ 7,160	$ 13,977	$ 15,522	$ 26,555
Interest income	(655)	(316)	(1,372)	(632)
Capitalized interest	(1,988)	(2,317)	(5,150)	(4,256)
Net interest expense	$ 4,517	$ 11,344	$ 9,000	$ 21,667

(1) Interest expense amount includes $2.8 million for the three-month period ended March 31, 2013 that was allocated to ERT and is included in discontinued operations. Following the sale of ERT in February 2013, we ceased allocating interest expense to ERT, which then constituted a discontinued operation.

Note 7 — Income Taxes

The effective tax rates for the three- and six-month periods ended June 30, 2014 were 23.3% and 25.3%, respectively. The effective tax rates for the three- and six-month periods ended June 30, 2013 were 23.4% and 23.5%, respectively. The effective tax rate for the three-month period ended June 30, 2014 was consistent with the effective tax rate for the same period in 2013. The effective tax rate for the second quarter of 2014 was adversely impacted by projected year-over-year increases in profitability in the United States offset by the recognition of previously unrecognized tax benefits. The effective tax rate for the six-month period ended June 30, 2014 was higher than the effective tax rate for the same period in 2013 as a result of projected year-over-year increases in profitability in the United States partially offset by the recognition of previously unrecognized tax benefits.

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Income taxes have been provided based on the U.S. statutory rate of 35% and at the local statutory rate for each foreign jurisdiction adjusted for items that are allowed as deductions for federal and foreign income tax reporting purposes, but not for book purposes. The primary differences between the statutory rate and our effective rate from continuing operations are as follows:

	Three Months Ended June 30, 2014	Three Months Ended June 30, 2013	Six Months Ended June 30, 2014	Six Months Ended June 30, 2013
Statutory rate	35.0 %	35.0 %	35.0 %	35.0 %
Foreign provision	(8.4)	(10.6)	(8.3)	(11.1)
Tax benefits previously unrecognized	(4.5)	—	(2.3)	—
Other	1.2	(1.0)	0.9	(0.4)
Effective rate	23.3 %	23.4 %	25.3 %	23.5 %

Note 8 — Accumulated Other Comprehensive Income (Loss) (“OCI”)

The components of Accumulated OCI are as follows (in thousands):

	June 30, 2014	December 31, 2013
Cumulative foreign currency translation adjustment	$ (2,419)	$ (10,697)
Unrealized loss on hedges, net (1)	(9,215)	(9,991)
Accumulated other comprehensive loss	$ (11,634)	$ (20,688)

(1) Amounts relate to foreign currency hedges for the Grand Canyon, the Grand Canyon II and the Grand Canyon III charters as well as interest rate swap contracts for the Term Loan, and are net of deferred income taxes totaling $5.0 million and $5.4 million as of June 30, 2014 and December 31, 2013, respectively (Note 15).

Note 9 — Earnings Per Share

We have shares of restricted stock issued and outstanding, which currently are unvested. Holders of such shares of unvested restricted stock are entitled to the same liquidation and dividend rights as the holders of our outstanding unrestricted common stock and the shares are thus considered participating securities. Under applicable accounting guidance, the undistributed earnings for each period are allocated based on the participation rights of both the common shareholders and holders of any participating securities as if earnings for the respective periods had been distributed. Because both the liquidation and dividend rights are identical, the undistributed earnings are allocated on a proportionate basis. Further, we are required to compute earnings per share (“EPS”) amounts under the two class method in periods in which we have earnings from continuing operations. For periods in which we have a net loss, we do not use the two class method as holders of our restricted shares are not contractually obligated to share in such losses.

The presentation of basic EPS amounts on the face of the accompanying condensed consolidated statements of operations is computed by dividing the net income applicable to Helix common shareholders by the weighted average shares of outstanding common stock. The calculation of diluted EPS is similar to basic EPS, except that the denominator includes dilutive common stock equivalents and the income included in the numerator excludes the effects of the impact of dilutive common stock equivalents, if any. The computations of the numerator (income) and denominator (shares) to derive the basic and diluted EPS amounts presented on the face of the accompanying condensed consolidated statements of operations are as follows (in thousands):

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	Three Months Ended June 30, 2014		Three Months Ended June 30, 2013	
	Income	Shares	Income	Shares
Basic:				
Continuing operations:				
Net income applicable to Helix	$ 57,782		$ 27,211	
Less: Loss from discontinued operations, net of tax	—		29	
Net income from continuing operations	57,782		27,240	
Less: Undistributed income allocable to participating securities – continuing operations	(300)		(203)	
Net income applicable to common shareholders – continuing operations	$ 57,482	104,992	$ 27,037	105,046
Discontinued operations:				
Loss from discontinued operations, net of tax	$—	104,992	$(29)	105,046
Diluted:				
Continuing operations:				
Net income applicable to common shareholders – continuing operations	$57,482	104,992	$27,037	105,046
Effect of dilutive securities:				
Share-based awards other than participating securities	—	303	—	87
Undistributed income reallocated to participating securities	1	—	—	—
Net income applicable to common shareholders – continuing operations	$57,483	105,295	$27,037	105,133
Discontinued operations:				
Loss from discontinued operations, net of tax	$—	105,295	$(29)	105,133

	Six Months Ended June 30, 2014		Six Months Ended June 30, 2013	
	Income	Shares	Income	Shares
Basic:				
Continuing operations:				
Net income applicable to Helix	$ 111,501		$ 28,826	
Less: Income from discontinued operations, net of tax	—		(1,029)	
Net income from continuing operations	111,501		27,797	
Less: Undistributed income allocable to participating securities – continuing operations	(586)		(201)	
Net income applicable to common shareholders – continuing operations	$ 110,915	105,059	$ 27,596	105,039
Discontinued operations:				
Income from discontinued operations, net of tax	$—		$1,029	
Less: Undistributed income allocable to participating securities – discontinued operations	—		(7)	
	$—	105,059	$1,022	105,039

Net income applicable to common shareholders –
discontinued operations

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	Six Months Ended June 30, 2014		Six Months Ended June 30, 2013	
	Income	Shares	Income	Shares
Diluted:				
Continuing operations:				
Net income applicable to common shareholders – continuing operations	$110,915	105,059	$27,596	105,039
Effect of dilutive securities:				
Share-based awards other than participating securities	—	300	—	102
Undistributed income reallocated to participating securities	2	—	1	—
Net income applicable to common shareholders – continuing operations	$110,917	105,359	$27,597	105,141
Discontinued operations:				
Income from discontinued operations, net of tax	$—	105,359	$1,029	105,141

No diluted shares were included for the 2032 Notes for the three- and six-month periods ended June 30, 2014 and 2013 as the conversion price of $25.02 and the conversion trigger of $32.53 per share were not met in either period, and because we have the right to settle any such future conversions in cash at our sole discretion (Note 6).

Note 10 — Employee Benefit Plans

Long-Term Incentive Stock-Based Plans

As of June 30, 2014, there were 6.4 million shares available for issuance under our long-term incentive stock-based plans (the "LTI Stock Plans"). During the six-month period ended June 30, 2014, the following grants of other share-based awards were made to executive officers and non-employee members of our Board of Directors under our LTI Stock Plans:

Date of Grant	Shares	Grant Date Fair Value Per Share	Vesting Period
January 2, 2014 (1)	73,609	$ 23.18	33% per year over three years
January 2, 2014 (2)	73,609	26.79	100% on January 1, 2017
January 2, 2014 (3)	2,724	23.18	100% on January 1, 2016
April 1, 2014 (3)	4,051	22.98	100% on January 1, 2016

(1) Reflects the grant of restricted shares to our executive officers.

(2) Reflects the grant of performance share units ("PSUs") to our executive officers. The estimated fair value of the PSUs on grant date was determined using a Monte Carlo simulation model. The PSUs provide for an award based on the performance of our common stock over a three-year period with the maximum award being 200% of the original awarded PSUs and the minimum amount being zero. The vested PSUs will be settled in an equivalent number of shares of our common stock unless the Compensation Committee of our Board of Directors elects to pay in cash.

(3) Reflects the grant of restricted shares to certain members of our Board of Directors who have made an election to take their quarterly fees in stock in lieu of cash.

Compensation cost is recognized over the respective vesting periods on a straight-line basis. For the three- and six-month periods ended June 30, 2014, $1.8 million and $3.5 million, respectively, were recognized as stock-based compensation expense related to share-based awards as compared with $1.9 million and $5.1 million for the three- and six-month periods ended June 30, 2013. A total of $1.3 million of the stock-based compensation expense for the six-month period ended June 30, 2013 was included within our discontinued operations.

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Long-Term Incentive Cash Plans

We have certain long-term incentive cash plans (the “LTI Cash Plans”) that provide long-term cash-based compensation to eligible employees. Cash awards historically have been both fixed sum amounts payable (for non-executive management only) as well as cash awards indexed to our common stock with the payment amount at each vesting date fluctuating based on the performance of our common stock (for both executive and non-executive management). These are measured based on the performance of our stock price over the applicable award period compared to a base price determined by the Compensation Committee of our Board of Directors at the time of the award. Cash payments under the LTI Cash Plans are made each year on the anniversary date of the award. Cash awards granted since 2012 have a vesting period of three years while those granted prior to 2012 have a vesting period of five years. The LTI Cash Plans are considered liability plans and as such are re-measured to fair value each reporting period with corresponding changes in the liability amount being reflected in our results of operations.

The cash awards granted under the LTI Cash Plans to our executive officers and selected management employees totaled $8.9 million in 2014 and $8.4 million in 2013. Total compensation expense associated with the cash awards issued pursuant to the LTI Cash Plans was $3.7 million ($1.9 million related to our executive officers) and $5.4 million ($2.8 million related to our executive officers) for the three- and six-month periods ended June 30, 2014, respectively. For the three- and six-month periods ended June 30, 2013, total compensation expense associated with the cash awards issued pursuant to the LTI Cash Plans was $1.7 million($0.8 million related to our executive officers) and $4.2 million ($2.4 million related to our executive officers), respectively. The liability balance for the cash awards issued under the LTI Cash Plans was $10.7 million at June 30, 2014 and $14.8 million at December 31, 2013, including $7.0 million at June 30, 2014 and $11.1 million at December 31, 2013 associated with the cash awards issued to our executive officers under the LTI Cash Plans.

Employee Stock Purchase Plan

We also have an employee stock purchase plan (the “ESPP”). The ESPP has 1.5 million shares authorized for issuance, of which 1.2 million shares were available for issuance as of June 30, 2014. The total value of the ESPP awards is calculated using the component approach where each award is computed as the sum of 15% of a share of non-vested stock, a call option on 85% of a share of non-vested stock, and a put option on 15% of a share of non-vested stock. Share-based compensation expense with respect to the ESPP was $0.3 million and $0.5 million for the three- and six-month periods ended June 30, 2014, respectively. For the three- and six-month periods ended June 30, 2013, share-based compensation with respect to the ESPP was $0.2 million and $0.4 million, respectively.

For more information regarding our employee benefit plans, including our stock-based compensation plans, our long-term incentive cash plans and our employee stock purchase plan, see Note 9 to our 2013 Form 10-K.

Note 11 — Business Segment Information

We have four business segments: Well Intervention, Robotics, Subsea Construction and Production Facilities. Our Well Intervention segment includes our vessels and related equipment that are used to perform well intervention services primarily in the Gulf of Mexico and North Sea regions. Our well intervention vessels include the Q4000, the Helix 534, the Seawell, the Well Enhancer and the Skandi Constructor, which is a chartered vessel. We are currently constructing two additional well intervention vessels, the Q5000 and the Q7000. We have also contracted for two newbuild chartered vessels, which are expected to be delivered in 2016 and used in connection with our contracts to provide well intervention services offshore Brazil. Our Robotics segment currently operates five chartered vessels and two spot vessels and also includes remotely operated vehicles (“ROVs”), trenchers and ROVDrills designed to complement offshore construction and well intervention services. We have sold substantially all of the assets associated with our former Subsea Construction operations, including the sale of our Ingleside spoolbase in

January 2014. The Production Facilities segment includes the HP I as well as our equity investments in Deepwater Gateway and Independence Hub that are accounted for under the equity method. All material intercompany transactions between the segments have been eliminated. In February 2013, we sold ERT and as a result, we have presented the assets and liabilities included in the sale of ERT and the historical operating results of our former Oil and Gas segment as discontinued operations in the accompanying consolidated financial statements. See Note 3 to our 2013 Form 10-K for additional information regarding our discontinued operations.

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We evaluate our performance based on operating income and income before income taxes of each segment. Segment assets are comprised of all assets attributable to each reportable segment. Corporate and other includes all assets not directly identifiable with our business segments, most notably the majority of our cash and cash equivalents. Certain financial data by reportable segment is summarized as follows (in thousands):

	Three Months Ended June 30,		Six Months Ended June 30,	
	2014	2013	2014	2013
Net revenues —				
Well Intervention	$ 181,218	$ 99,323	$ 340,918	$ 205,655
Robotics	119,704	88,374	207,594	152,570
Subsea Construction	—	37,659	358	65,185
Production Facilities	24,049	24,174	47,189	44,567
Intercompany elimination	(19,384)	(17,352)	(36,900)	(38,370)
Total	$ 305,587	$ 232,178	$ 559,159	$ 429,607
Income (loss) from operations —				
Well Intervention	$ 64,775	$ 23,912	$ 113,508	$ 60,362
Robotics	20,799	13,296	32,018	12,599
Subsea Construction (1)	145	10,392	10,830	13,943
Production Facilities	10,459	14,643	21,843	25,828
Corporate and other	(17,467)	(14,207)	(31,342)	(47,738)
Intercompany elimination	45	(839)	(1,153)	(2,559)
Total	$ 78,756	$ 47,197	$ 145,704	$ 62,435
Equity in earnings of equity investments	$ (507)	$ 683	$ 201	$ 1,293

(1) Amount in 2014 includes the $10.5 million gain on the sale in January 2014 of our Ingleside spoolbase.

Intercompany segment revenues are as follows (in thousands):

	Three Months Ended June 30,		Six Months Ended June 30,	
	2014	2013	2014	2013
Well Intervention	$ 7,956	$ 6,439	$ 13,417	$ 10,268
Robotics	11,428	10,913	23,483	23,112
Subsea Construction	—	—	—	317
Production Facilities	—	—	—	4,673
Total	$ 19,384	$ 17,352	$ 36,900	$ 38,370

Intercompany segment profits (losses), which only relate to intercompany capital projects, are as follows (in thousands):

	Three Months Ended June 30,		Six Months Ended June 30,	
	2014	2013	2014	2013
Well Intervention	$ (87)	$ (27)	$ (149)	$ (46)

Robotics	85	910	1,389	2,535
Subsea Construction	—	—	—	158
Production Facilities	(43)	(44)	(87)	(88)
Total	$ (45)	$ 839	$ 1,153	$ 2,559

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Segment assets are comprised of all assets attributable to each reportable segment. Corporate and other includes all assets not directly identifiable with our business segments, most notably the majority of our cash and cash equivalents. The following table reflects total assets by reportable segment (in thousands):

	June 30, 2014	December 31, 2013
Well Intervention	$ 1,449,790	$ 1,245,229
Robotics	324,231	282,373
Subsea Construction	33,402	38,054
Production Facilities	475,306	495,829
Corporate and other	418,381	482,795
Total	$ 2,701,110	$ 2,544,280

Note 12 — Commitments and Contingencies and Other Matters

Commitments

In March 2012, we executed a contract with a shipyard in Singapore for the construction of a newbuild semi-submersible well intervention vessel, the Q5000. This $386.5 million shipyard contract represents the majority of the expected costs associated with the construction of the Q5000. Pursuant to the terms of this contract, payments are made in a fixed percentage of the contract price, together with any variations, on contractually scheduled dates. The vessel is expected to be completed and placed in service in 2015. At June 30, 2014, our total investment in the Q5000 was $276.1 million, including $231.9 million of shipyard contract costs incurred, which included the $57.8 million milestone payment in early July 2014.

In February 2013, we contracted to charter the Grand Canyon II and Grand Canyon III for use in our robotics operations. The terms of the charters will be five years from the respective delivery dates, both of which are expected to be in 2015.

In September 2013, we executed a second contract with the same shipyard in Singapore that is currently constructing the Q5000. This contract provides for the construction of a newbuild semi-submersible well intervention vessel, the Q7000, which will be built to North Sea standards. This $346.0 million shipyard contract represents the majority of the expected costs associated with the construction of the Q7000. Pursuant to the terms of this contract, 20% of the contract price was paid upon the signing of the contract and the remaining 80% will be paid upon the delivery of the vessel, which is expected to occur in 2016. At June 30, 2014, our total investment in the Q7000 was $85.4 million, including the $69.2 million paid to the shipyard upon signing the contract.

In February 2014, we entered into agreements with Petróleo Brasileiro S.A. (“Petrobras”) to provide well intervention services offshore Brazil. The initial term of the agreements with Petrobras is for four years with options to extend. In connection with the Petrobras agreements, we entered into charter agreements with Siem Offshore AS for two newbuild monohull vessels, both of which are expected to be in service for Petrobras in 2016. At June 30, 2014, our total investment in the topside equipment for the two vessels was $3.1 million.

Contingencies and Claims

Under terms of the equity purchase agreement for the sale of ERT, we required the buyer to provide bonding in a sufficient amount as determined by the Bureau of Ocean Energy Management (the “BOEM”) to cover the decommissioning costs of ERT’s lease properties and thus to replace and allow for a full discharge of our existing guaranty to the BOEM for ERT's lease obligations. The buyer posted the bonding required by the equity purchase agreement, and a formal request to the BOEM for a release of our guaranty is pending.

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Litigation

On July 8, 2011, a shareholder derivative lawsuit styled City of Sterling Heights Police & Fire Retirement System v. Owen Kratz, et al. was filed in the United States District Court for the Southern District of Texas, Houston Division. In the suit, the plaintiff makes claims against our Board of Directors, certain of our former directors, certain of our current and former executive officers, and the independent compensation consultant to the Compensation Committee of our Board of Directors, for breaches of the fiduciary duty of loyalty, unjust enrichment and aiding and abetting the alleged breaches of fiduciary duty relating to the long-term equity awards granted in 2010 to certain of the Company's then executive officers who are defendants. The defendants filed a motion to dismiss the claim asserting that the plaintiff has not (i) pled specific facts excusing its failure to make pre-suit demand on our Board of Directors as required by Minnesota law, (ii) filed proper verification, or (iii) stated a claim. A ruling regarding the motion is pending.

On May 12, 2012, a shareholder derivative lawsuit styled Mark Lucas v. Owen Kratz, et al. was filed in the 270th Judicial District in the District Court of Harris County, Texas. In the suit, the plaintiff makes claims against our Board of Directors, certain of our former directors, certain of our current and former executive officers, and the independent compensation consultant to the Compensation Committee of our Board of Directors, for breaches of the fiduciary duties of candor, good faith and loyalty; unjust enrichment; and aiding and abetting the alleged breaches of fiduciary duty relating to the long-term equity awards granted in 2010 to certain of our executive officers. This case is essentially a "copycat" complaint asserting similar causes of action arising out of the same facts as set forth in the federal action described above. The plaintiff is generally demanding disgorgement of the excessive compensation, restraint on the disposition/exercise of the alleged improperly awarded equity, implementation of additional internal controls, and attorney's fees and costs of litigation. The defendants filed motions to stay and dismiss the proceeding, which motions were denied by the trial court judge. The defendants then filed a petition for a writ of mandamus with the state appellate court, in which they requested that court to direct the district court to grant the motion to stay or dismiss the case. The appellate court denied the request to grant mandamus with respect to this requested relief, but did grant a writ of mandamus ordering the lower court to vacate its ruling to the extent the plaintiff failed to plead with particularity that our Board of Directors wrongfully refused his demand, and that he was a shareholder of record at the relevant time. A special committee of our Board of Directors subsequently determined to reject the plaintiff's demand regarding this matter, and based on that rejection, as well as the plaintiff's pleadings, the defendants filed a motion for summary judgment in December 2013. The court granted the defendants' motion for summary judgment in March 2014, and the plaintiff appealed that ruling. Subsequently, the plaintiff filed a motion with the court to voluntarily dismiss the appeal and all claims against the defendants with prejudice, and the court issued an order dismissing the case.

We are involved in various legal proceedings, primarily involving claims for personal injury under the General Maritime Laws of the United States and the Jones Act based on alleged negligence. In addition, from time to time we incur other claims, such as contract disputes, in the normal course of business.

Note 13 — Allowance for Uncollectible Accounts

The following table sets forth the activity in our allowance for uncollectible accounts since December 31, 2013 (in thousands):

Balance at December 31, 2013	$2,234
Provision (1)	5,196
Write-offs	(1,459)
Balance at June 30, 2014	$5,971

(1) Reflects charges associated with the provision for uncertain collection of a portion of our existing trade receivables related to our Robotics segment.

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Note 14 — Fair Value Measurements

Certain of our financial assets and liabilities are measured and reported at fair value on a recurring basis as required under applicable accounting requirements. These requirements establish a hierarchy for inputs used in measuring fair value. The fair value is to be calculated based on assumptions that market participants would use in pricing assets and liabilities and not on assumptions specific to the entity. The statement requires that each asset and liability carried at fair value be classified into one of the following categories:

- Level 1. Observable inputs such as quoted prices in active markets;
- Level 2. Inputs, other than the quoted prices in active markets, that are observable either directly or indirectly; and
- Level 3. Unobservable inputs for which there is little or no market data, which require the reporting entity to develop its own assumptions.

Assets and liabilities measured at fair value are based on one or more of three valuation techniques as follows:

(a) Market Approach. Prices and other relevant information generated by market transactions involving identical or comparable assets or liabilities.
(b) Cost Approach. Amount that would be required to replace the service capacity of an asset (replacement cost).
(c) Income Approach. Techniques to convert expected future cash flows to a single present amount based on market expectations (including present value techniques, option-pricing and excess earnings models).

Our financial instruments include cash and cash equivalents, accounts receivable, accounts payable, our long-term debt and various derivative instruments. The carrying amount of cash and cash equivalents, accounts receivable and accounts payable approximates fair value due to the highly liquid nature of these instruments. The following table provides additional information related to other financial instruments measured at fair value on a recurring basis at June 30, 2014 (in thousands):

	Level 1	Level 2 (1)	Level 3	Total	Valuation Technique
Assets:					
Interest rate swaps	$ —	$ 290	$ —	$ 290	(c)
Liabilities:					
Fair value of long-term debt (2)	553,756	107,518	—	661,274	(a)
Foreign exchange contracts	—	13,701	—	13,701	(c)
Interest rate swaps	—	766	—	766	(c)
Total net liability	$ 553,756	$ 121,695	$ —	$ 675,451	

(1) Unless otherwise indicated, the fair value of our Level 2 derivative instruments reflects our best estimate and is based upon exchange or over-the-counter quotations whenever they are available. Quoted valuations may not be available due to location differences or terms that extend beyond the period for which quotations are available. Where quotes are not available, we utilize other valuation techniques or models to estimate market values. These modeling techniques require us to make estimations of future prices, price correlation and market volatility and liquidity based on market data. Our actual results may differ from our estimates, and these differences could be positive or negative. See Note 15 for further discussion on fair value of our derivative instruments.

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(2) See Note 6 for additional information regarding our long-term debt. The value of our long-term debt is as follows (in thousands):

	June 30, 2014	
	Carrying Value	Fair Value (b)
Term Loan (matures June 2018)	$ 285,000	$ 282,506
2032 Notes (mature March 2032) (a)	200,000	271,250
MARAD Debt (matures February 2027)	97,513	107,518
Total debt	$ 582,513	$ 661,274

(a) Carrying value excludes the related unamortized debt discount of $23.8 million at June 30, 2014.

(b) The estimated fair value of all debt, other than the MARAD Debt, was determined using Level 1 inputs using the market approach. The fair value of the MARAD Debt was determined using a third party evaluation of the remaining average life and outstanding principal balance of the MARAD indebtedness as compared to other governmental obligations in the marketplace with similar terms. The fair value of the MARAD Debt was estimated using Level 2 fair value inputs using the market approach.

Note 15 — Derivative Instruments and Hedging Activities

Our operations are exposed to market risk associated with interest rates and foreign currency exchange rates. Our risk management activities involve the use of derivative financial instruments to hedge the impact of market risk exposure related to variable interest rates and foreign currency exchange rates. All derivatives are reflected in the accompanying condensed consolidated balance sheets at fair value.

We engage solely in cash flow hedges. Hedges of cash flow exposure are entered into to hedge a forecasted transaction or the variability of cash flows to be received or paid related to a recognized asset or liability. Changes in the derivative fair values that are designated as cash flow hedges are deferred to the extent that the hedges are effective. These fair value changes are recorded as a component of Accumulated OCI (a component of shareholders' equity) until the hedged transactions occur and are recognized in earnings. The ineffective portion of changes in the fair value of cash flow hedges is recognized immediately in earnings. In addition, any change in the fair value of a derivative that does not qualify for hedge accounting is recorded in earnings in the period in which the change occurs.

For additional information regarding our accounting for derivatives, see Notes 2 and 16 to our 2013 Form 10-K.

Interest Rate Risk

From time to time, we enter into interest rate swaps to stabilize cash flows related to our long-term debt subject to variable interest rates. Changes in the fair value of an interest rate swap are deferred to the extent the swap is effective. These changes are recorded as a component of Accumulated OCI until the anticipated interest payments occur and are recognized in interest expense. The ineffective portion of the interest rate swap, if any, is recognized immediately in earnings within the line titled "Net interest expense." The amount of ineffectiveness associated with our interest rate swap contracts was immaterial for all periods presented. In September 2013, we entered into interest rate swap contracts to fix the interest rate on $148.1 million of our Term Loan (Note 6). These monthly contracts began in October 2013 and extend through October 2016.

Foreign Currency Exchange Rate Risk

Because we operate in various regions in the world, we conduct a portion of our business in currencies other than the U.S. dollar. We entered into various foreign currency exchange contracts to stabilize expected cash outflows relating to certain vessel charters that are denominated in British pounds and Norwegian kroner.

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In January 2013, we entered into foreign currency exchange contracts to hedge through September 2017 the foreign currency exposure associated with the Grand Canyon charter payments ($104.6 million) denominated in Norwegian kroner (NOK591.3 million). In February 2013, we entered into similar foreign currency exchange contracts to hedge our foreign currency exposure with respect to the Grand Canyon II and Grand Canyon III charter payments ($100.4 million and $98.8 million, respectively) denominated in Norwegian kroner (NOK594.7 million and NOK595.0 million, respectively), through July 2019 and February 2020, respectively. These contracts currently qualify for hedge accounting treatment. All of our remaining foreign exchange contracts that were not accounted for as hedge contracts have been settled. We had no foreign currency exchange contracts for vessel charters denominated in British pounds as of June 30, 2014.

Quantitative Disclosures Related to Derivative Instruments

As a result of the announcement in December 2012 of the sale of ERT, we de-designated all of our then remaining oil and natural gas derivative contracts as hedging instruments. In addition, under the terms of our former credit agreement (Note 6), we were required to use a portion of the proceeds from the sales of ERT, the Caesar and the Express to make payments to reduce our indebtedness. Because of the probability that the former term loan debt would be totally repaid before the expiration of our then existing interest rate swaps, we also concluded that those swaps no longer qualified as cash flow hedges. The mark-to-market adjustments related to our commodity derivative contracts and interest rate swaps are reflected in “Loss on commodity derivative contracts” and “Other expense, net,” respectively, in the accompanying condensed consolidated statements of operations.

The following table presents the fair value and balance sheet classification of our derivative instruments that were not designated as hedging instruments (in thousands):

	June 30, 2014		December 31, 2013	
	Balance Sheet Location	Fair Value	Balance Sheet Location	Fair Value
Asset Derivatives:				
Foreign exchange contracts	Other current assets	$—	Other current assets	$69
		$—		$69

The following table presents the fair value and balance sheet classification of our derivative instruments that were designated as hedging instruments (in thousands):

	June 30, 2014		December 31, 2013	
	Balance Sheet Location	Fair Value	Balance Sheet Location	Fair Value
Asset Derivatives:				
Interest rate swaps	Other assets, net	$290	Other assets, net	$446
		$290		$446
Liability Derivatives:				
Foreign exchange contracts	Accrued liabilities	$2,779	Accrued liabilities	$1,905
Interest rate swaps	Accrued liabilities	766	Accrued liabilities	746
Foreign exchange contracts	Other non-current liabilities	10,922	Other non-current liabilities	13,166
		$14,467		$15,817

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Ineffectiveness associated with our derivatives was immaterial for all periods presented. The following tables present the impact that derivative instruments designated as cash flow hedges had on our Accumulated OCI (net of tax) and our condensed consolidated statements of operations (in thousands). We estimate that as of June 30, 2014, $2.3 million of unrealized losses in Accumulated OCI associated with our derivatives is expected to be reclassified into earnings within the next 12 months.

	Gain (Loss) Recognized in OCI on Derivatives, Net of Tax (Effective Portion)			
	Three Months Ended June 30,		Six Months Ended June 30,	
	2014	2013	2014	2013
Foreign exchange contracts	$ (2,134)	$ (3,593)	$ 890	$ (10,831)
Interest rate swaps	(153)	—	(114)	—
	$ (2,287)	$ (3,593)	$ 776	$ (10,831)

	Location of Gain (Loss) Reclassified from Accumulated OCI into Earnings (Effective Portion)	Gain (Loss) Reclassified from Accumulated OCI into Earnings (Effective Portion)			
		Three Months Ended June 30,		Six Months Ended June 30,	
		2014	2013	2014	2013
Interest rate swaps	Net interest expense	$ (217)	$ —	$ (431)	$ —
Foreign exchange contracts	Cost of sales	(393)	(354)	(837)	(504)
		$ (610)	$ (354)	$ (1,268)	$ (504)

The following table presents the impact that derivative instruments not designated as hedges had on our condensed consolidated statements of operations (in thousands):

	Location of Gain (Loss) Recognized in Earnings on Derivatives	Gain (Loss) Recognized in Earnings on Derivatives			
		Three Months Ended June 30,		Six Months Ended June 30,	
		2014	2013	2014	2013
Oil and natural gas commodity contracts	Loss on commodity derivative contracts	$ —	$ —	$ —	$ (14,113)
Interest rate swaps	Other expense, net	—	—	—	(86)
Foreign exchange contracts	Other expense, net	—	53	7	(1,191)
		$ —	$ 53	$ 7	$ (15,390)

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

FORWARD-LOOKING STATEMENTS AND ASSUMPTIONS

This Quarterly Report on Form 10-Q contains various statements that contain forward-looking information regarding Helix Energy Solutions Group, Inc. and represent our expectations and beliefs concerning future events. This forward-looking information is intended to be covered by the safe harbor for “forward-looking statements” provided by the Private Securities Litigation Reform Act of 1995 as set forth in Section 27A of the Securities Act of 1933, as amended, and Section 21E of the Securities Exchange Act of 1934, as amended (the “Exchange Act”). All statements included herein or incorporated herein by reference that are predictive in nature, that depend upon or refer to future events or conditions, or that use terms and phrases such as “achieve,” “anticipate,” “believe,” “estimate,” “expect,” “forecast,” “project,” “propose,” “strategy,” “predict,” “envision,” “hope,” “intend,” “will,” “continue,” “may,” “potential,” “should,” “cou terms and phrases are forward-looking statements. Included in forward-looking statements are, among other things:

- statements regarding our business strategy or any other business plans, forecasts or objectives, any or all of which are subject to change;
- statements relating to the construction, upgrades or acquisition of vessels or equipment and any anticipated costs related thereto, including the construction of the Q5000 and the Q7000 and the construction of two chartered vessels that are expected to be delivered in 2016 and used in connection with our contracts to provide well intervention services offshore Brazil (Note 12);
- statements regarding projections of revenues, gross margin, expenses, earnings or losses, working capital or other financial items;
- statements regarding any financing transactions or arrangements, or ability to enter into such transactions;
- statements regarding anticipated legislative, governmental, regulatory, administrative or other public body actions, requirements, permits or decisions;
- statements regarding the collectability of our trade receivables;
- statements regarding anticipated developments, industry trends, performance or industry ranking;
- statements regarding general economic or political conditions, whether international, national or in the regional and local market areas in which we do business;
- statements related to our ability to retain key members of our senior management and key employees;
- statements related to the underlying assumptions related to any projection or forward-looking statement; and
- any other statements that relate to non-historical or future information.

Although we believe that the expectations reflected in these forward-looking statements are reasonable and are based on reasonable assumptions, they do involve risks, uncertainties and other factors that could cause actual results to be materially different from those in the forward-looking statements. These factors include, among other things:

- impact of domestic and global economic conditions and the future impact of such conditions on the oil and gas industry and the demand for our services;
- unexpected delays in the delivery or chartering of new vessels for our well intervention and robotics fleet, including the Q5000 (expected in 2015), the Q7000 (expected in 2016), the Grand Canyon II and the Grand Canyon III (both expected in 2015);
- unexpected delays in the delivery of the chartered vessels to be used to perform contracted well intervention work in Brazil;

- unexpected future capital expenditures (including the amount and nature thereof);
- the effectiveness and timing of completion of our vessel upgrades and major maintenance items;
- the results of our continuing efforts to control costs and improve performance;
- the success of our risk management activities;
- the effects of competition;
- the effects of indebtedness, which could adversely restrict our ability to operate, could make us vulnerable to general adverse economic and industry conditions, could place us at a competitive disadvantage compared to our competitors that have less debt and could have other adverse consequences to us;
- the impact of current and future laws and governmental regulations, including tax and accounting developments;

- the effect of adverse weather conditions and/or other risks associated with marine operations;
- the effectiveness of our current and future hedging activities;
- the long-term availability (or lack thereof) of capital (including any financing) to fund our business strategy and/or operations, and the terms of any such financing;
- the potential impact of a loss of one or more key employees; and
- the impact of general, market, industry or business conditions.

Our actual results could differ materially from those anticipated in any forward-looking statements as a result of a variety of factors, including those described in Item 1A. "Risk Factors" in our 2013 Form 10-K. All forward-looking statements attributable to us or persons acting on our behalf are expressly qualified in their entirety by these risk factors. Forward-looking statements are only as of the date they are made, and other than as required under the securities laws, we assume no obligation to update or revise these forward-looking statements or provide reasons why actual results may differ.

Executive Summary

Business Strategy

We are an international offshore energy services company that provides specialty services to the offshore energy industry, with a focus on our well intervention and robotics operations. Since 2008 we have focused on improving our balance sheet and increasing our liquidity through dispositions of non-core business assets and the related repayment of a significant portion of our indebtedness. We substantially finalized this process with the sale of ERT in February 2013, the sale of our two remaining pipelay vessels in mid-2013 and the sale of our Ingleside spoolbase in January 2014. As such, we believe that we are now positioned for growth and expansion in our well intervention and robotics operations.

Our focus is on expanding our well intervention and robotics businesses. We believe that focusing on these services will deliver higher long-term financial returns to us than the businesses and assets that we have chosen to monetize. We are making strategic investments that expand our service capabilities or add capacity to existing services in our key operating regions. Our well intervention fleet has expanded with the addition of the Helix 534, which was placed in service in February 2014. Our well intervention fleet will further expand following the completion of the two newbuild semi-submersible vessels currently under construction, the Q5000 and the Q7000, and the delivery of two newbuild chartered monohull vessels in connection with the well intervention service agreements which we entered into with Petrobras in February 2014. In addition, we are expanding our robotics operations by acquiring additional ROVs and trenchers as well as chartering two newbuild ROV support vessels, the Grand Canyon II and the Grand Canyon III, both of which are expected to be delivered in 2015.

Economic Outlook and Industry Influences

Demand for our services is primarily influenced by the condition of the oil and gas industry, and in particular, the willingness of oil and gas companies to make capital expenditures for offshore exploration, drilling and production operations. The performance of our business is also largely dependent on the prevailing market prices for oil and natural gas, which are impacted by global economic conditions, hydrocarbon production and capacity, geopolitical issues, weather, and several other factors, including but not limited to:

- worldwide economic activity, including available access to global capital and capital

	markets;								
•	demand for oil and natural gas, especially in the United States, Europe, China and India;								
•	economic and political conditions in the Middle East and other oil-producing regions;								
•	the effect of regulations on offshore Gulf of Mexico oil and gas operations;								
•	5,082	$2,918	$2,164	74.2 %	$15,596	$12,609	$2,987	23.7 %	
International	303	339	(36)	(10.6)%	1,133	1,407	(274)	(19.5)%	

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General and Administrative Expenses. The increase in general and administrative expenses for the three months ended April 30, 2018 of $8.7 million, or 24.4%, as compared to the same period last year resulted from (i) an increase in the U.S. of $5.9 million and (ii) an increase in International of $2.8 million. Excluding depreciation and amortization, the increase in the U.S. of $3.8 million resulted primarily a result of the acquisition of Cycle Express, LLC and litigation costs, and the increase in International of $2.8 million resulted primarily from growth in professional services and labor costs associated with international expansion. The increase in depreciation and amortization expenses for the three months ended April 30, 2018 as compared to the same period last year resulted primarily from amortizing intangible assets from the Cycle Express, LLC acquisition, partially offset by certain technology assets becoming fully amortized in the U.S.

The increase in general and administrative expenses for the nine months ended April 30, 2018 of $10.4 million, or 9.1%, as compared to the same period last year resulted from (i) an increase in International of $5.1 million, and (ii) an increase in the U.S. of $5.3 million. Excluding depreciation and amortization, the increase in International of $5.4 million resulted primarily from growth in professional services and labor costs associated with international expansion, and the increase in the U.S. of $2.3 million resulted primarily from increases due to the acquisition of Cycle Express, LLC, partially offset by a decrease in payroll taxes from the exercise of employee stock options. The increase in depreciation and amortization expenses for the nine months ended April 30, 2018 as compared to the same period last year resulted primarily from amortizing intangible assets from the Cycle Express, LLC acquisition, partially offset by certain technology assets becoming fully amortized in the U.S.

The following table summarizes total other expenses and income taxes for the three and nine months ended April 30, 2018 and 2017:

	Three Months Ended April 30,				Nine Months Ended April 30,			
(In thousands)	2018	2017	Change	% Change	2018	2017	Change	% Change
Total other expenses	(3,403)	(5,700)	2,297	40.3 %	(19,726)	(16,771)	(2,955)	(17.6)%
Income taxes	43,811	40,542	3,269	8.1 %	121,516	9,829	111,687	1,136.3 %

Other Expenses. The decrease in total other expenses for the three months ended April 30, 2018 of $2.3 million as compared to the same period last year was primarily due to a decrease in interest expense of $1.5 million as a result of the ongoing paydown of our Revolving Loan Facility.

The increase in total other expenses for the nine months ended April 30, 2018 of $3.0 million as compared to the same period last year was primarily due to an increase in currency losses, primarily due to the change in the British pound to U.S. dollar exchange rate, and losses on the disposal of certain non-operating assets, partially offset by a decrease in interest expense of $2.2 million as a result of the ongoing paydown of our Revolving Loan Facility.

Income Taxes. Our effective income tax rates were 25.6% and 30.9% for the three months ended April 30, 2018 and 2017, respectively, and 28.3%, and 2.9% for the nine months ended April 30, 2018 and 2017, respectively. The tax rates in the prior year were impacted primarily from the result of recognizing excess tax benefits from the exercise of employee stock options of $3.1 million and $4.0 million for the three months ended April 30, 2018 and 2017, respectively, and $9.4 million and $106.7 million for the nine months ended April 30, 2018 and 2017, respectively. The current quarter effective tax rate was computed based on the reduced blended U.S. federal corporate tax rate of 26.9% for the fiscal year ending July 31, 2018, and included the effects of the Tax Cuts and Jobs Act (“Tax Reform” or “Tax Act”). See Note 8 – Income Taxes for a detailed discussion of the Tax Act.

Liquidity and Capital Resources

The following table presents a comparison of key components of our liquidity and capital resources at April 30, 2018 and July 31, 2017 and for the nine months ended April 30, 2018 and 2017, respectively, excluding additional funds available to us through our Revolving Loan Facility:

(In thousands)	April 30, 2018	July 31, 2017	Change	% Change
Cash and cash equivalents	$204,275	$210,100	$(5,825)	(2.8)%
Working capital	360,324	285,108	75,216	26.4 %

	Nine Months Ended April 30,			
(In thousands)	2018	2017	Change	% Change
Operating cash flows	$377,197	$347,827	$29,370	8.4 %
Investing cash flows	(185,114)	(137,722)	(47,392)	(34.4)%
Financing cash flows	(204,519)	(175,559)	(28,960)	(16.5)%
Capital expenditures, including acquisitions	$(188,482)	$(134,710)	$(53,772)	(39.9)%
Net repayments on revolving loan facility	(231,000)	(73,000)	(158,000)	(216.4)%

Cash and cash equivalents decreased and working capital increased at April 30, 2018 as compared to July 31, 2017 primarily due to cash generated from operations and proceeds from the exercise of stock options, offset by capital expenditures and net repayments on our Revolving Loan Facility. Cash equivalents consisted of bank deposits, domestic certificates of deposit, and funds invested in money market accounts, which bear interest at variable rates.

Historically, we have financed our growth through cash generated from operations, public offerings of common stock, equity issued in conjunction with certain acquisitions and debt financing. Our primary source of cash generated by operations is from the collection of sellers' fees, members' fees and reimbursable advances from the proceeds of vehicle sales. Our business is seasonal as inclement weather during the winter months increases the frequency of accidents and consequently, the number of cars involved in accidents which the insurance companies salvage rather than repair. During the winter months, most of our facilities process 10% to 30% more vehicles than at other times of the year. This increased volume requires the increased use of our cash to pay out advances and handling costs of the additional business. We expect to continue to use cash flows from operations to finance our working capital needs and to develop and grow our business. In addition to our stock repurchase program, we are considering a variety of alternative potential uses for our remaining cash balances and our cash flows from operations. These alternative potential uses include additional stock repurchases, repayments of long-term debt, the payment of dividends, and acquisitions. For further detail, see Notes to Unaudited Consolidated Financial Statements, Note 2 – Long-Term Debt and Note 7 – Stock Repurchases and under the subheadings "Credit Agreement" and "Note Purchase Agreement" below.

We believe that our currently available cash and cash equivalents and cash generated from operations will be sufficient to satisfy our operating and working capital requirements for at least the next 12 months. We expect to acquire or develop additional locations and expand some of our current facilities in the foreseeable future. We may be required to raise additional cash through drawdowns on our Revolving Loan Facility or issuance of additional equity to fund this expansion. Although the timing and magnitude of growth through expansion and acquisitions are not predictable, the opening of new greenfield yards is contingent upon our ability to locate property that (i) is in an area in which we have a need for more capacity; (ii) has adequate size given the capacity needs; (iii) has the appropriate shape and topography for our operations; (iv) is reasonably close to a major road or highway; and (v) most importantly, has the appropriate zoning for our business. Costs to develop a new yard can range from $3.0 to $50.0 million, depending on size, location and developmental infrastructure requirements.

As of April 30, 2018, $108.1 million of the $204.3 million of cash and cash equivalents was held by our foreign subsidiaries. Prior to the enactment of the Tax Cuts and Jobs Act ("Tax Reform" or "Tax Act") on December 22, 2017, if these funds were needed for our operations in the U.S., we would have been required to accrue and pay U.S. taxes to repatriate these funds. However, the Tax Act imposed a one-time deemed repatriation transition tax on the undistributed and previously untaxed portion of those funds. As such, a portion of these funds are available to be repatriated into the U.S. without further accrual or payment of U.S. taxes, if these funds were needed for operations in the U.S. Our current plans do not require repatriation to fund our U.S. operations. See Notes to Unaudited Consolidated Financial Statements, Note 8 – Income Taxes for further discussion regarding U.S. tax reform and its corresponding impact on foreign cash repatriation.

Net cash provided by operating activities increased for the nine months ended April 30, 2018 as compared to the same period in 2017 due to improved cash operating results from an increase in service revenues and changes in operating assets and liabilities. The change in operating assets and liabilities was primarily the result of an increase in income taxes receivable of $28.9 million related to excess tax benefits from stock option exercises; an increase in accounts payable and accrued liabilities of $28.8 million; partially offset by a decrease in accounts receivable of $7.7 million and a decrease in inventory and vehicle pooling costs of $6.0 million.

Net cash used in investing activities increased for the nine months ended April 30, 2018 as compared to the same period in 2017 due primarily to increased capital expenditures, partially offset by an increase in proceeds from the sale of property and equipment. Our capital expenditures are primarily related to lease buyouts of certain facilities, acquiring land, opening and improving facilities, capitalized software development costs for new software for internal use and major software enhancements, and acquiring yard equipment. We continue to develop, expand and invest in new and existing facilities and standardize the appearance of existing locations.

Net cash used in financing activities increased for the nine months ended April 30, 2018 as compared to the same period in 2017 due primarily to repayments on our Revolving Loan Facility and a decrease in proceeds from the exercise of stock options, partially offset by a decrease in payments for employee stock-based tax withholdings. See Notes to Unaudited Consolidated Financial Statements, Note 2 – Long-Term Debt and Note 7 – Stock Repurchases and under the subheadings “Credit Agreement”, “Note Purchase Agreement”, and Stock Repurchases.

Credit Agreement

On December 3, 2014, we entered into a Credit Agreement (as amended from time to time, the “Credit Amendment”) with Wells Fargo Bank, National Association, as administrative agent, and Bank of America, N.A., as syndication agent. The Credit Agreement provided for (a) a secured revolving loan facility in an aggregate principal amount of up to $300.0 million (the “Revolving Loan Facility”), and (b) a secured term loan facility in an aggregate principal amount of $300.0 million (the “Term Loan”), which was fully drawn at closing. The Term Loan amortized $18.8 million per quarter.

On March 15, 2016, we entered into a First Amendment to Credit Agreement (the “Amendment to Credit Agreement”) with Wells Fargo Bank, National Association, as administrative agent and Bank of America, N.A. The Amendment to Credit Agreement amended certain terms of the Credit Agreement, dated as of December 3, 2014. The Amendment to Credit Agreement provided for (a) an increase in the secured revolving credit commitments by $50.0 million, bringing the aggregate principal amount of the revolving credit commitments under the Credit Agreement to $350.0 million, (b) a new secured term loan (the “Incremental Term Loan”) in the aggregate principal amount of $93.8 million having a maturity date of March 15, 2021, and (c) an extension of the termination date of the Revolving Loan Facility and the maturity date of the Term Loan from December 3, 2019 to March 15, 2021. The Amendment to Credit Agreement extended the amortization period for the Term Loan, and decreased the quarterly amortization payments for that loan to $7.5 million per quarter. The Amendment to Credit Agreement additionally reduced the pricing levels under the Credit Agreement to a range of 0.15% to 0.30% in the case of the commitment fee, 1.125% to 2.0% in the case of the applicable margin for LIBOR loans, and 0.125% to 1.0% in the case of the applicable margin for base rate loans, based on our consolidated total net leverage ratio during the preceding fiscal quarter. We borrowed the entire $93.8 million principal amount of the Incremental Term Loan concurrent with the closing of the Amendment to Credit Agreement.

On July 21, 2016, we entered into a Second Amendment to Credit Agreement (the “Second Amendment to Credit Agreement”) with Wells Fargo Bank, National Association, SunTrust Bank, and Bank of America, N.A., as administrative agent (as successor in interest to Wells Fargo Bank). The Second Amendment to Credit Agreement amends certain terms of the Credit Agreement, dated as of December 3, 2014 as amended by the Amendment to Credit Agreement, dated as of March 15, 2016. The Second Amendment to Credit Agreement provides for, among other things, (a) an increase in the secured revolving credit commitments by $500.0 million, bringing the aggregate principal amount of the revolving credit commitments under the Credit Agreement to $850.0 million, (b) the repayment of existing term loans outstanding under the Credit Agreement, (c) an extension of the termination date of the revolving credit facility under the Credit Agreement from March 15, 2021 to July 21, 2021, and (d) increased covenant flexibility.

Concurrent with the closing of the Second Amendment to Credit Agreement, we prepaid in full the outstanding $242.5 million principal amount of the Term Loan and Incremental Term Loan under the Credit Agreement without premium or penalty. The Second Amendment to Credit Agreement reduced the pricing levels under the Credit Agreement to a range of 0.125% to 0.20% in the case of the commitment fee, 1.00% to 1.75% in the case of the applicable margin for LIBOR loans, and 0.0% to 0.75% in the case of the applicable margin for base rate loans, in each case depending on our consolidated total net leverage ratio. The principal purposes of these financing transactions were to increase the size and availability under our Revolving Loan Facility and to provide additional long-term financing. The proceeds are being used for general corporate purposes, including working capital and capital expenditures, potential share repurchases, acquisitions, or other investments relating to our expansion strategies in domestic and international markets.

The Revolving Loan Facility under the Credit Agreement bears interest, at our election, at either (a) the Base Rate, which is defined as a fluctuating rate per annum equal to the greatest of (i) the Prime Rate in effect on such day; (ii) the Federal Funds Rate in effect on such date plus 0.50%; or (iii) an adjusted LIBOR rate determined on the basis of a one-month interest period plus 1.0%, in each case plus an applicable margin ranging from 0.0% to 0.75% based on our consolidated total net leverage ratio during the preceding fiscal quarter; or (b) an adjusted LIBOR rate plus an applicable margin ranging from 1.00% to 1.75% depending on our consolidated total net leverage ratio during the preceding fiscal quarter. Interest is due and payable quarterly, in arrears, for loans bearing interest at the Base Rate, and at the end of an interest period (or at each three month interval in the case of loans with interest periods greater than three months) in the case of loans bearing interest at the adjusted LIBOR rate. The interest rate as of April 30, 2018 on our Revolving Loan Facility was the one month LIBOR rate of 1.88% plus an applicable margin of 1.00%. The carrying amount of the Credit Agreement is comprised of borrowings under which interest accrues under a fluctuating interest rate structure. Accordingly, the carrying value approximates fair value at April 30, 2018, and was classified within Level II of the fair value hierarchy.

Amounts borrowed under the Revolving Loan Facility may be repaid and reborrowed until the maturity date of July 21, 2021. We are obligated to pay a commitment fee on the unused portion of the Revolving Loan Facility. The commitment fee rate ranges from 0.125% to 0.20%, depending on our consolidated total net leverage ratio during the preceding fiscal quarter, on the average daily unused portion of the revolving credit commitment under the Credit Agreement. We had zero and $231.0 million of outstanding borrowings under the Revolving Loan Facility as of April 30, 2018 and July 31, 2017, respectively.

Our obligations under the Credit Agreement are guaranteed by certain of our domestic subsidiaries meeting materiality thresholds set forth in the Credit Agreement. Such obligations, including the guaranties, are secured by substantially all of our assets and the assets of the subsidiary guarantors pursuant to a Security Agreement, dated December 3, 2014, among us, the subsidiary guarantors from time to time party thereto, and Wells Fargo Bank, National Association, as collateral agent.

The Credit Agreement contains customary affirmative and negative covenants, including covenants that limit or restrict us and our subsidiaries' ability to, among other things, incur indebtedness, grant liens, merge or consolidate, dispose of assets, make investments, make acquisitions, enter into transactions with affiliates, pay dividends, or make distributions on and repurchase stock, in each case subject to certain exceptions. We are also required to maintain compliance, measured at the end of each fiscal quarter, with a consolidated total net leverage ratio and a consolidated interest coverage ratio. The Credit Agreement contains no restrictions on the payment of dividends and other restricted payments, as defined, as long as (1) the consolidated total net leverage ratio, as defined, both before and after giving effect to any such dividend or restricted payment on a pro forma basis, is less than 3.25:1, in an unlimited amount, (2) if clause (1) is not available, so long as the consolidated total net leverage ratio both before and after giving effect to any such dividend on a pro forma basis is less than 3.50:1, in an aggregate amount not to exceed the available amount, as defined, and (3) if clauses (1) and (2) are not available, in an aggregate amount not to exceed $50.0 million; provided, that, minimum liquidity, as defined, shall be not less than $75.0 million both before and after giving effect to any such dividend or restricted payment. As of April 30, 2018, the consolidated total net leverage ratio was 0.33:1. Minimum liquidity as of April 30, 2018 was $1.0 billion. Accordingly, we do not believe that the provisions of the Credit Agreement represent a significant restriction to our ability to pay dividends or to the successful future operations of the business. We have not paid a cash dividend since becoming a public company in 1994. We were in compliance with all covenants related to the Credit Agreement as of April 30, 2018.

Note Purchase Agreement

On December 3, 2014, we entered into a Note Purchase Agreement and sold to certain purchasers (collectively, the "Purchasers") $400.0 million in aggregate principal amount of senior secured notes (the "Senior Notes") consisting of (i) $100.0 million aggregate principal amount of 4.07% Senior Notes, Series A, due December 3, 2024; (ii) $100.0 million aggregate principal amount of 4.19% Senior Notes, Series B, due December 3, 2026; (iii) $100.0 million aggregate principal amount of 4.25% Senior Notes, Series C, due December 3, 2027; and (iv) $100.0 million aggregate principal amount of 4.35% Senior Notes, Series D, due December 3, 2029. Interest is due and payable quarterly, in arrears, on each of the Senior Notes. Proceeds from the Note Purchase Agreement are being used for general corporate purposes.

On July 21, 2016, we entered into Amendment No. 1 to Note Purchase Agreement (the “First Amendment to Note Purchase Agreement”) which amended certain terms of the Note Purchase Agreement, including providing for increased flexibility substantially consistent with the changes included in the Second Amendment to Credit Agreement, including among other things increased covenant flexibility.

We may prepay the Senior Notes, in whole or in part, at any time, subject to certain conditions, including minimum amounts and payment of a make-whole amount equal to the discounted value of the remaining scheduled interest payments under the Senior Notes.

Our obligations under the Note Purchase Agreement are guaranteed by certain of our domestic subsidiaries meeting materiality thresholds set forth in the Note Purchase Agreement. Such obligations, including the guaranties, are secured by substantially all of our assets and the assets of the subsidiary guarantors. Our obligations and our subsidiary guarantors under the Note Purchase Agreement will be treated on a pari passu basis with the obligations of those entities under the Credit Agreement as well as any additional debt that we may obtain.

The Note Purchase Agreement contains customary affirmative and negative covenants, including covenants that limit or restrict us and our subsidiaries' ability to, among other things, incur indebtedness, grant liens, merge or consolidate, dispose of assets, make investments, make acquisitions, enter into transactions with affiliates, pay dividends, or make distributions and repurchase stock, in each case subject to certain exceptions. We are also required to maintain compliance, measured at the end of each fiscal quarter, with a consolidated total net leverage ratio and a consolidated interest coverage ratio. The Note Purchase Agreement contains no restrictions on the payment of dividends and other restricted payments, as defined, as long as (1) the consolidated total net leverage ratio, as defined, both before and after giving effect to any such dividend or restricted payment on a pro forma basis, is less than 3.25:1, in an unlimited amount, (2) if clause (1) is not available, so long as the consolidated total net leverage ratio both before and after giving effect to any such dividend on a pro forma basis is less than 3.50:1, in an aggregate amount not to exceed the available amount, as defined, and (3) if clauses (1) and (2) are not available, in an aggregate amount not to exceed $50.0 million; provided, that, minimum liquidity, as defined, shall be not less than $75.0 million both before and after giving effect to any such dividend or restricted payment. As of April 30, 2018, the consolidated total net leverage ratio was 0.33:1. Minimum liquidity as of April 30, 2018 was $1.0 billion. Accordingly, we do not believe that the provisions of the Note Purchase Agreement represent a significant restriction to our ability to pay dividends or to the successful future operations of the business. We have not paid a cash dividend since becoming a public company in 1994. We are in compliance with all covenants related to the Note Purchase Agreement as of April 30, 2018.
Related to the execution of the Credit Agreement, First Amendment to Credit Agreement, Second Amendment to Credit Agreement, and the Note Purchase Agreement, we incurred $3.4 million in costs, of which $2.0 million was capitalized as debt issuance fees and $1.4 million was recorded as a reduction of the long-term debt proceeds as a debt discount. Both the debt issuance fees and debt discount are amortized to interest expense over the term of the respective debt instruments and are classified as reductions of the outstanding liability.

Stock Repurchases

On September 22, 2011, our Board of Directors approved an 80 million share increase in the stock repurchase program, bringing the total current authorization to 196 million shares. The repurchases may be effected through solicited or unsolicited transactions in the open market or in privately negotiated transactions. No time limit has been placed on the duration of the stock repurchase program. Subject to applicable securities laws, such repurchases will be made at such times and in such amounts as we deem appropriate and may be discontinued at any time. We did not repurchase any shares of our common stock under the program during the nine months ended April 30, 2018 or 2017. As of April 30, 2018, the total number of shares repurchased under the program was 106,913,602, and 89,086,398 shares were available for repurchase under the program.
In fiscal 2017 and fiscal 2018, certain executive officers, members of the Company's Board of Directors and other employees exercised stock options through cashless exercises. A portion of the options exercised were net settled in satisfaction of the exercise price and federal and state statutory tax withholding requirements. We remitted $134.6 million for the nine months ended April 30, 2017 to the proper taxing authorities in satisfaction of the employees' statutory withholding requirements.
The exercised stock options, utilizing a cashless exercise, are summarized in the following table:

Period	Options Exercised	Weighted Average Exercise Price	Shares Net Settled for Exercise	Shares Withheld for Taxes[1]	Net Shares to Employees	Weighted Average Share Price for Withholding	Employee Stock Based Tax Withholding (in 000s)
FY 2017—Q1	18,000,000	$ 7.70	5,408,972	5,255,322	7,335,706	$ 25.62	$ 134,615
FY 2018—Q2	80,000	6.54	11,996	—	68,004	43.60	—

(1) Shares withheld for taxes are treated as a repurchase of shares for accounting purposes but do not count against our stock repurchase program.

Critical Accounting Policies and Estimates

The preparation of consolidated financial statements requires us to make estimates and judgments that affect the reported amounts of assets, liabilities, revenues and expenses, and the related disclosure of contingent assets and liabilities. On an ongoing basis, we evaluate our estimates, including costs related to vehicle pooling, self-insured

reserves, allowance for doubtful accounts, income taxes, revenue recognition, stock-based payment compensation, purchase price allocations, long-lived asset impairment calculations and contingencies. We base our estimates on historical experience and on various other assumptions that we believe are reasonable under the circumstances, the results of which form the basis for making judgments about the carrying value of assets and liabilities that are not readily apparent from other sources. Actual results may differ from these estimates under different assumptions or conditions.
Management has discussed the selection of critical accounting policies and estimates with the Audit Committee of the Board of Directors and the Audit Committee has reviewed our disclosure relating to critical accounting policies and estimates in this Quarterly Report on Form 10-Q. There have been no significant changes to the critical accounting policies and estimates from what was disclosed in our Annual Report on Form 10-K for the fiscal year ended July 31, 2017 filed with the SEC on September 27, 2017. Our significant accounting policies are described in the Notes to Unaudited Consolidated Financial Statements, Note 1 – Summary of Significant Accounting Policies in this Quarterly Report on Form 10-Q.

Recently Issued Accounting Standards

For a description of the new accounting standards that affect us, refer to the Notes to Unaudited Consolidated Financial Statements, Note 9 – Recent Accounting Pronouncements.

Contractual Obligations and Commitments

There have been no material changes during the nine months ended April 30, 2018 to our contractual obligations disclosed in our “Management’s Discussion and Analysis of Financial Condition and Results of Operations” included in our Annual Report on Form 10-K for the fiscal year ended July 31, 2017 filed with the SEC on September 27, 2017.

Off-Balance Sheet Arrangements

As of April 30, 2018, there are no off-balance sheet arrangements pursuant to Item 303(a)(4) of Regulation S-K promulgated under the Securities Exchange Act of 1934, as amended.

ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

There have been no material changes to the information required under this Item from what was disclosed in our Annual Report on Form 10-K for the fiscal year ended July 31, 2017 filed with the SEC on September 27, 2017.

ITEM 4. CONTROLS AND PROCEDURES

(a) Evaluation of Disclosure Controls and Procedures

We conducted an evaluation of the effectiveness of the design and operation of our disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e) under the Exchange Act), or Disclosure Controls, as of the end of the period covered by this Quarterly Report on Form 10-Q. This evaluation, or Controls Evaluation, was performed under the supervision and with the participation of management, including our Chief Executive Officer (CEO) and our Chief Financial Officer (CFO). Disclosure Controls are controls and procedures designed to provide reasonable assurance that information required to be disclosed in our reports filed under the Exchange Act, such as this Quarterly Report, is recorded, processed, summarized and reported within the time periods specified in the SEC’s rules and forms. Disclosure Controls include, without limitation, controls and procedures designed to provide reasonable assurance that information required to be disclosed in our reports filed under the Exchange Act is accumulated and communicated to our management, including our CEO and CFO, or persons performing similar functions, as appropriate, to allow timely decisions regarding required disclosure. Our Disclosure Controls include some, but not all, components of our internal control over financial reporting.

Based upon the Controls Evaluation, our CEO and CFO have concluded that, as of the end of the period covered by this Quarterly Report on Form 10-Q, our Disclosure Controls were effective to provide reasonable assurance that information required to be disclosed in our Exchange Act reports is accumulated and communicated to management, including the CEO and CFO, to allow timely decisions regarding required disclosure, and that such information is recorded, processed, summarized and reported within the time periods specified by the Securities and Exchange Commission.

(b) Changes in Internal Controls

There have not been any changes in our internal control over financial reporting during the most recent fiscal quarter that have materially affected or are reasonably likely to materially affect our internal control over financial reporting.

PART II — OTHER INFORMATION

ITEM 1. LEGAL PROCEEDINGS

We are subject to threats of litigation and are involved in actual litigation and damage claims arising in the ordinary course of business, such as actions related to injuries, property damage, contract disputes, and handling or disposal of vehicles. The material pending legal proceedings to which we are party, or of which our property is subject, include the following matters.

On November 1, 2013, we filed suit against Sparta Consulting, Inc. (now known as KPIT) in the 44th Judicial District Court of Dallas County, Texas, alleging fraud, fraudulent inducement, and/or promissory fraud, negligent misrepresentation, unfair business practices pursuant to California Business and Professions Code § 17200, breach of contract, declaratory judgment, and attorney's fees. We seek compensatory and exemplary damages, disgorgement of amounts paid, attorney's fees, pre- and post-judgment interest, costs of suit, and a judicial declaration of the parties' rights, duties, and obligations under the Implementation Services Agreement dated October 6, 2011. The suit arises out of our September 17, 2013 decision to terminate the Implementation Services Agreement, under which KPIT was to design, implement, and deliver a customized replacement enterprise resource planning system for us. On January 2, 2014, KPIT removed this suit to the United States District Court for the Northern District of Texas. On August 11, 2014, the Northern District of Texas transferred the suit to the United States District Court for the Eastern District of California for convenience. On January 8, 2014, KPIT filed suit against us in the United States District Court for the Eastern District of California, alleging breach of contract, promissory estoppel, breach of the implied covenant of good faith and fair dealing, account stated, quantum meruit, unjust enrichment, and declaratory relief. KPIT seeks compensatory and exemplary damages, prejudgment interest, costs of suit, and a judicial declaration of the parties' rights, duties, and obligations under the Implementation Services Agreement. On June 8, 2016, we amended our complaint to include claims that KPIT stole certain intellectual property owned by us and acted negligently in its provision of services. The case was tried in April and May 2018. On May 22, 2018, the jury returned a verdict for us on our fraud claim against KPIT for $4.7 million, and on our professional negligence claim against KPIT for $16.3 million, and the jury found for KPIT on its implied covenant counterclaim against us for $4.9 million. Post-trial proceedings are expected in this lawsuit.

We have provided for costs relating to these matters when a loss is probable and the amount can be reasonably estimated. The effect of the outcome of these matters on our future consolidated results of operations and cash flows cannot be predicted because any such effect depends on future results of operations and the amount and timing of the resolution of such matters. We believe that any ultimate liability will not have a material effect on our consolidated results of operations, financial position or cash flows. However, the amount of the liabilities associated with these claims, if any, cannot be determined with certainty. We maintain insurance which may or may not provide coverage for claims made against us. There is no assurance that there will be insurance coverage available when and if needed. Additionally, the insurance that we carry requires that we pay for costs and/or claims exposure up to the amount of the insurance deductibles negotiated when the insurance is purchased.

Governmental Proceedings

The Georgia Department of Revenue, or DOR, conducted a sales and use tax audit of our operations in Georgia for the period from January 1, 2007 through June 30, 2011. As a result of their initial audit, the DOR issued a notice of proposed assessment for uncollected sales taxes in which it asserted that we failed to collect and remit sales taxes totaling $73.8 million, including penalties and interest.

Subsequently, we engaged a Georgia law firm and outside tax advisors to review the conduct of our business operations in Georgia, the notice of proposed assessment, and the DOR's policy position. In particular, our outside legal counsel provided us with an opinion that the sales for resale to non-U.S. registered resellers should not be subject to Georgia sales and use tax. In rendering its opinion, our counsel noted that non-U.S. registered resellers are unable to comply strictly with technical requirements for a Georgia certificate of exemption but concluded that our sales for resale to non-U.S. registered resellers should not be subject to Georgia sales and use tax notwithstanding this technical inability to comply. Following our receipt of the notice of proposed assessment, we and our counsel engaged in active discussions with the DOR to resolve the matter.

On August 4, 2015, the DOR issued an official Assessment and Demand for Payment (the "Assessment") for $96.1 million for sales taxes, penalties, and interest that the DOR alleged we owe to the State of Georgia. We filed an appeal

of this Assessment from the DOR with the Georgia Tax Tribunal on September 3, 2015. On August 5, 2016, the DOR filed a response in which it denied all allegations noted in our appeal of the Assessment.
During an extended remand period, it was determined that grounds exist for a substantial reduction in the Official Assessment, on the basis that (i) the transactions and resulting tax at issue were erroneously double-counted by the DOR in the audit sales transaction work papers on which the Assessment was based; and (ii) we were ultimately able to provide documentation showing that most of the remaining transactions were sales at wholesale, therefore qualifying for the sale for resale exemption from Georgia Sales and Use Tax. After these reductions, the remaining amount of principal Georgia Sales and Use Tax still in dispute between the parties is $2.6 million, plus applicable interest. A Consent Order to this effect was entered by the Georgia Tax Tribunal on May 22, 2017. Since the date of entry of the Consent Order, we and the DOR have completed discovery, and the DOR filed a Motion for Summary Judgment related to the remaining $2.6 million in dispute. We are opposing the DOR's motion.

Based on the opinion from our outside law firm, advice from our outside tax advisors, and our best estimate of a probable outcome, we believe that we have adequately provided for the payment of any assessment in our consolidated financial statements. We believe we have strong defenses to the remaining tax liability set forth above and intend to continue to defend this matter. There can be no assurance that this matter will be resolved in our favor or that we will not ultimately be required to make a substantial payment to the DOR. We understand that litigating and defending the matter in Georgia could be expensive and time-consuming and result in substantial management distraction.

ITEM 1A. RISK FACTORS

Set forth below and elsewhere in this Quarterly Report on Form 10-Q and in other documents we file with the SEC are descriptions of the risks and uncertainties that could cause our actual results to differ materially from the results contemplated by the forward-looking statements contained in this report. The descriptions below include any material changes to and supersede the description of the risk factors affecting our business previously disclosed in “Part I, Item 1A, Risk Factors” of our Annual Report on Form 10-K for the fiscal year ended July 31, 2017.

We depend on a limited number of major vehicle sellers for a substantial portion of our revenues. The loss of one or more of these major sellers could adversely affect our consolidated results of operations and financial position, and an inability to increase our sources of vehicle supply could adversely affect our growth rates.

No single customer accounted for more than 10% of our consolidated revenue during the nine months ended April 30, 2018. Historically, a limited number of vehicle sellers have collectively accounted for a substantial portion of our revenues. Seller arrangements are either written or oral agreements typically subject to cancellation by either party upon 30 to 90 days’ notice. Vehicle sellers have terminated agreements with us in the past in particular markets, which has affected revenues in those markets. There can be no assurance that our existing agreements will not be canceled. Furthermore, there can be no assurance that we will be able to enter into future agreements with vehicle sellers or that we will be able to retain our existing supply of salvage vehicles. A reduction in vehicles from a significant vehicle seller or any material changes in the terms of an arrangement with a significant vehicle seller could have a material adverse effect on our consolidated results of operations and financial position. In addition, a failure to increase our sources of vehicle supply could adversely affect our earnings and revenue growth rates.

Our expansion into markets outside the U.S., including expansions in Europe, Brazil, and the Middle East expose us to risks arising from operating in international markets. Any failure to successfully integrate businesses acquired outside the U.S. into our operations could have an adverse effect on our consolidated results of operations, financial position or cash flows.

We first expanded our operations outside the U.S. in fiscal 2003 with an acquisition in Canada. Subsequently, in fiscal 2008 we made a significant acquisition in the U.K., followed by acquisitions in the U.A.E., Brazil, Germany, and Spain in fiscal 2013, expansions into Bahrain and Oman in fiscal 2015, expansion into the Republic of Ireland and India in fiscal 2016, and expansion into Finland in fiscal 2018. In addition, we continue to evaluate acquisitions and other opportunities outside of the U.S. Acquisitions or other strategies to expand our operations outside of the U.S. pose substantial risks and uncertainties that could have an adverse effect on our future operating results. In particular, we may not be successful in realizing anticipated synergies from these acquisitions, or we may experience unanticipated costs or expenses integrating the acquired operations into our existing business. We have and may continue to incur substantial expenses establishing new yards, operations, and shared services capabilities in international markets. Among other things, we plan to ultimately deploy our proprietary auction technologies at all of our foreign operations and we cannot predict whether this deployment will be successful or will result in increases in the revenues or operating efficiencies of any acquired companies relative to their historic operating performance. Integration of our respective operations, including information technology and financial and administrative functions, may not proceed as anticipated and could result in unanticipated costs or expenses such as capital expenditures that could have an adverse effect on our future operating results. We cannot provide any assurance that we will achieve our business and financial objectives in connection with these acquisitions or our strategic decision to expand our operations internationally. For example, we recently decided to suspend salvage operations in India until the Indian market develops in a manner better suited to our business model.

As we continue to expand our business internationally, we will need to develop policies and procedures to manage our business on a global scale. Operationally, acquired businesses typically depend on key seller relationships, and our failure to maintain those relationships would have an adverse effect on our consolidated results of operations and could have an adverse effect on our future operating results.

In addition, we anticipate our international operations will continue to subject us to a variety of risks associated with operating on an international basis, including:

- the difficulty of managing and staffing foreign offices;
- the increased travel, infrastructure and legal compliance costs associated with multiple international locations;
- the need to localize our product offerings, particularly the need to implement our online auction platform in foreign countries;

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- the need to comply with complex foreign and U.S. laws and regulations that apply to our international operations;
- tariffs and trade barriers and other regulatory or contractual limitations on our ability to operate in certain foreign markets;
- exposure to foreign currency exchange rate risk, which may have an adverse impact on our revenues and revenue growth rates;
- adapting to different business cultures and market structures, particularly where we seek to implement our auction model in markets where insurers have historically not played a substantial role in the disposition of salvage vehicles; and
- repatriation of funds currently held in foreign jurisdictions to the U.S. may result in higher effective tax rates.

As we continue to expand our business globally, our success will depend, in large part, on our ability to anticipate and effectively manage these and other risks associated with our international operations. Our failure to manage any of these risks successfully could harm our international operations and have an adverse effect on our operating results.

On June 23, 2016, the U.K. held a referendum in which voters approved an exit from the European Union, commonly referred to as “Brexit.” In February 2017, the British Parliament voted in favor of allowing the British government to begin negotiating the terms of the U.K.’s withdrawal from the European Union and discussions with the European Union began in March 2017. The ultimate effects of Brexit on us are difficult to predict, but adverse consequences concerning Brexit or the European Union could include deterioration in global economic conditions, instability in global financial markets, political uncertainty, volatility in currency exchange rates, or adverse changes in the cross-border agreements currently in place, any of which could have an adverse impact on our financial results in the future. The ultimate effects of Brexit on us will also depend on the terms of agreements, if any, that the U.K. and the European Union make to retain access to each other’s respective markets either during a transitional period or more permanently.

In addition, certain acquisitions in the U.K. may be reviewed by the Competition and Markets Authority (U.K. Regulator). If an inquiry is made by the U.K. Regulator, we may be required to demonstrate that our acquisitions will not result, or be expected to result, in a substantial lessening of competition in the U.K. market. Although we believe that there will not be a substantial lessening of competition in the U.K. market, based on our analysis of the relevant U.K. markets, there can be no assurance that the U.K. Regulator will agree with us if it decides to make an inquiry. If the U.K. Regulator determines that by our acquisitions of certain assets, there is or likely will be a substantial lessening of competition in the U.K. market, we could be required to divest some portion of our U.K. assets. In the event of a divestiture order by the U.K. Regulator, the assets disposed may be sold for substantially less than their carrying value. Accordingly, any divestiture could have a material adverse effect on our operating results in the period of the divestiture.

Our operations and acquisitions in certain foreign areas expose us to political, regulatory, economic, and reputational risks.

Although we have implemented policies, procedures and training designed to ensure compliance with anti-bribery laws, trade controls and economic sanctions, and similar regulations, our employees or agents may take actions in violation of our policies. We may incur costs or other penalties in the event that any such violations occur, which could have an adverse effect on our business and reputation.

In some cases, the enforcement practices of governmental regulators in certain foreign areas and the procedural and substantive rights and remedies available to us may vary significantly from those in the United States, which could have an adverse effect on our business.

In addition, some of our recent acquisitions have required us to integrate non-U.S. companies which had not, until our acquisition, been subject to U.S. law. In many countries outside of the United States, particularly in those with developing economies, it may be common for persons to engage in business practices prohibited by laws and regulations applicable to us, such as the U.S. Foreign Corrupt Practices Act (FCPA), U.K. Bribery Act, Brazil Clean Companies Act, India’s Prevention of Corruption Act, 1988 or similar local anti-bribery laws. These laws generally prohibit companies and their employees or agents from making improper payments for the purpose of obtaining or retaining business. Failure by us and our subsidiaries to comply with these laws could subject us to civil and criminal penalties that could have a material adverse effect on our consolidated operating results and financial position.

We face risks associated with the implementation of our salvage auction model in markets that may not operate on the same terms as the U.S. market. For example, certain markets operate on a principal rather than agent basis, which may have an adverse impact on our gross margin percentages and expose us to inventory risks that we do not experience in the U.S.

Some of our target markets outside the U.S. operate in a manner substantially different than our historic market in the U.S. For example, new markets may operate either wholly or partially on the principal model, in which the vehicle is purchased then resold for our own account, rather than the agency model employed in the U.S., in which we generally act as a sales agent for the legal owner of vehicles. Further, operating on a principal basis exposes us to inventory risks, including losses from theft, damage, and obsolescence. In addition, our business in the U.S., Canada, and the U.K. has been established and grown based largely on our ability to build relationships with insurance carriers. In other markets, insurers have traditionally been less involved in the disposition of salvage vehicles. As we expand into markets outside the U.S., Canada, and the U.K., we cannot predict whether markets will readily adapt to our strategy of online auctions of automobiles sourced principally through vehicle insurers. Any failure of new markets to adopt our business model could adversely affect our consolidated results of operations and financial position.

Acquisitions typically will increase our sales and profitability although, given the typical size of our acquisitions to date, most acquisitions will not individually have a material impact on our consolidated results of operations and financial position. We may not always be able to introduce our processes and selling platform to acquired companies due to different operating models in international jurisdictions or other facts. As a result, the associated benefits of acquisitions may be delayed for years in some international situations. During this period, the acquisitions may operate at a loss and certain acquisitions, while profitable, may operate at a margin percentage that is below our overall operating margin percentage and, accordingly, have an adverse impact on our consolidated results of operations and financial position. Hence, the conversion periods vary from weeks to years and cannot be predicted.

We have transitioned various functionality of our previously planned third-party enterprise operating system to an internally developed proprietary system, and we may experience difficulties operating our business as we work to develop and design this system.

During fiscal 2014, we terminated a contract with KPIT (formerly known as Sparta Consulting, Inc.), whereby KPIT was engaged to design and implement an SAP-based replacement for our existing business operating software that, among other things, would address our international expansion needs. Following a review of KPIT's work performed to date, and an assessment of the cost to complete, deployment risk, and other factors, we ceased development of KPIT's software and internally developed a proprietary solution in its place. The ongoing design, development, and implementation of our enterprise operating systems carry certain risks, including the risk of significant design or deployment errors causing disruptions, delays or deficiencies, which may make our website and services unavailable. This type of interruption could prevent us from processing vehicles for our sellers and may prevent us from selling vehicles through our Internet bidding platform, VB3, which would adversely affect our consolidated results of operations and financial position. In addition, the transition to our new internally developed proprietary system will require us to commit substantial financial, operational and technical resources before the volume of business increases, without assurance that the volume of business will increase. We began using our new internally developed proprietary system with our expansion into Spain in fiscal 2016 and Germany in fiscal 2017.

We may also implement additional or enhanced information systems in the future to accommodate our growth and to provide additional capabilities and functionality. The implementation of new systems and enhancements is frequently disruptive to the underlying business of an enterprise and can be time-consuming and expensive, increase management responsibilities and divert management attention. Any disruptions relating to our system enhancements or any problems with the implementation, particularly any disruptions impacting our operations or our ability to accurately report our financial performance on a timely basis during the implementation period, could materially and adversely affect our business. Even if we do not encounter these material and adverse effects, the implementation of these enhancements may be much more costly than we anticipated. If we are unable to successfully implement the information systems enhancements as planned, our financial position, results of operations and cash flows could be negatively impacted.

Our success depends on maintaining the integrity of our systems and infrastructure. As our operations continue to grow in both size and scope, domestically and internationally, we must continue to provide reliable, real-time access to our systems by our customers through improving and upgrading our systems and infrastructure for enhanced products, services, features and functionality. Any failure to maintain the integrity of our systems and infrastructure may result in loss of customers due to among other things, slow delivery times, unreliable service levels or insufficient capacity, which could have a material adverse effect on our business, consolidated financial position and results of operations.

The impairment of capitalized development costs could adversely affect our consolidated results of operations and financial condition.

We capitalize certain costs associated with the development of new software products, new software for internal use and major software enhancements to existing software. These costs are amortized over the estimated useful life of the software beginning with its introduction or roll-out. If, at any time, it is determined that capitalized software provides a reduced economic benefit, the unamortized portion of the capitalized development costs will be expensed, in part or in full, as an impairment, which may have a material impact on our consolidated results of operations and financial position. For example, during fiscal 2017, we recognized a $19.4 million charge primarily related to fully impairing costs previously capitalized in connection with the development of business operating software.

Any failure to maintain security and prevent unauthorized access to electronic and other confidential information could disrupt our business and materially and adversely affect our reputation, consolidated results of operations and financial condition.

Information security risks for online commerce companies have significantly increased in recent years because of, in addition to other factors, the proliferation of new technologies, the use of the Internet and telecommunications technologies to conduct financial transactions, and the increased sophistication and activities of organized crime, hackers, terrorists, and other external parties. These threats may derive from fraud or malice on the part of third parties or current or former employees. In addition, human error or accidental technological failure could make us vulnerable to cyber-attacks, including the introduction of malicious computer viruses or code into our system, phishing attacks, or other information technology data security incidents.

Our operations rely on the secure processing, transmission and storage of confidential, proprietary and other information in our computer systems and networks. Our customers and other parties in the payments value chain rely on our digital technologies, computer and e-mail systems, software and networks to conduct their operations. In addition, to access our products and services, our customers and cardholders increasingly use personal smartphones, tablet PCs and other mobile devices that may be beyond our control.

Cyber-attacks or other cyber security incidents could materially and adversely affect our reputation, operating results, or financial condition by, among other things, making our auction platform inoperable for a period of time, damaging our reputation with buyers, sellers, and insurance companies as a result of the unauthorized disclosure of confidential information (including account data information), or resulting in governmental investigations, litigation, liability, fines, or penalties against us. If such attacks are not detected immediately, their effect could be compounded. While we maintain insurance coverage that may, subject to policy terms and conditions, cover certain aspects of these cyber risks, our insurance coverage may be insufficient to cover all losses and would not remedy damage to our reputation.

We have in the past identified attempts by unauthorized third parties to access our systems and disrupt our online auctions. These attempts have caused minor service interruptions, which were promptly addressed and resolved, and our online service was restored to normal business. For example, in April 2015, we identified that unauthorized third parties had gained access to data provided to us by our members that is considered to be personal information in certain jurisdictions. We immediately investigated, including the engagement of an external expert security firm, and made the required notifications to members whose information may have been accessed and to regulatory agencies.

We are constantly evaluating and implementing new technologies and processes to manage risks relating to cyber-attacks and system and network disruptions, including but not limited to usage errors by our employees, power outages and catastrophic events such as fires, tornadoes, floods, hurricanes and earthquakes. We have further enhanced our security protocols based on the investigation we conducted in response to the security incident. Nevertheless, we cannot provide assurances that our efforts to address prior data security incidents and mitigate against the risk of future data security incidents or system failures will be successful. The techniques used by criminals to obtain unauthorized access to sensitive data change frequently and are often not recognized immediately. We may be unable to anticipate these techniques or implement adequate preventative measures and believe that cyber-attacks and threats against us have occurred in the past and are likely to continue in the future. If our systems are compromised again in the future, become inoperable for extended periods of time, or cease to function properly, we may have to make a significant investment to fix or replace them, and our ability to provide many of our electronic and online solutions to our customers may be impaired. In addition, as cyber-threats continue to evolve, we may be required to expend significant additional resources to continue to modify or enhance our protective measures or to investigate and remediate any information security vulnerabilities. Any of the risks described above could materially and adversely affect our consolidated financial position and results of operations.

Our business is exposed to risks associated with online commerce security and credit card fraud.

Consumer concerns over the security of transactions conducted on the Internet or the privacy of users may inhibit the growth of the Internet and online commerce. To securely transmit confidential information such as customer credit card numbers, we rely on encryption and authentication technology. Unanticipated events or developments could result in a compromise or breach of the systems we use to protect customer transaction data. Furthermore, our servers may also be vulnerable to viruses transmitted via the Internet and other points of access. While we proactively check for intrusions into our infrastructure, a new or undetected virus could cause a service disruption.

We maintain an information security program and our processing systems incorporate multiple levels of protection in order to address or otherwise mitigate these risks. Despite these mitigation efforts, there can be no assurance that we will be immune to these risks and not suffer losses in the future. Under current credit card practices, we may be held liable for fraudulent credit card transactions and other payment disputes with customers. As such, we have implemented certain anti-fraud measures, including credit card verification procedures. However, a failure to adequately prevent fraudulent credit card transactions could adversely affect our consolidated financial position and results of operations.

Our security measures may also be breached due to employee error, malfeasance, insufficiency, or defective design. Additionally, outside parties may attempt to fraudulently induce employees, users, or customers to disclose sensitive information in order to gain access to our data or our users' or customers' data. Any such breach or unauthorized access could result in significant legal and financial exposure, damage to our reputation, and a loss of confidence in the security of our products and services that could have an adverse effect on our consolidated financial position and results of operations.

Our business is subject to a variety of domestic and international laws and other obligations regarding privacy and data protection.

We are subject to federal, state and international laws, directives, and regulations relating to the collection, use, retention, disclosure, security and transfer of personal data. These laws, directives, and regulations, and their interpretation and enforcement continue to evolve and may be inconsistent from jurisdiction to jurisdiction. Recent regulatory changes in Europe have created compliance uncertainty regarding certain transfers of personal data from Europe to the United States. For example, the General Data Protection Regulation ("GDPR"), which goes into effect in the European Union ("EU") on May 25, 2018, will apply to all of our activities conducted from an establishment in the EU and may also apply to related to products and services that we offer to EU users. Complying with the GDPR and similar emerging and changing privacy and data protection requirements may cause us to incur substantial costs or require us to change our business practices. Noncompliance with our legal obligations relating to privacy and data protection could result in penalties, legal proceedings by governmental entities or others, and significant legal and financial exposure and could affect our ability to retain and attract customers. Any of the risks described above could adversely affect our consolidated financial position and results of operations.

Implementation of our online auction model in new markets may not result in the same synergies and benefits that we achieved when we implemented the model in the U.S., Canada, and the U.K.

We believe that the implementation of our proprietary auction technologies across our operations over the last decade had a favorable impact on our results of operations by increasing the size and geographic scope of our buyer base, increasing the average selling price for vehicles sold through our sales, and lowering expenses associated with vehicle sales.

We implemented our online system across all of our U.S., Canada, and U.K. salvage yards beginning in fiscal 2004 and 2008, respectively, and experienced increases in revenues and average selling prices, as well as improved operating efficiencies in those markets. In considering new markets, we consider the potential synergies from the implementation of our model based in large part on our experience in the U.S., Canada, and the U.K. However, we cannot predict whether these synergies will also be realized in new markets.

Failure to have sufficient capacity to accept additional cars at one or more of our storage facilities could adversely affect our relationships with insurance companies or other sellers of vehicles.

Capacity at our storage facilities varies from period to period and from region to region. For example, following adverse weather conditions in a particular area, our yards in that area may fill and limit our ability to accept additional salvage vehicles while we process existing inventories. For example, Hurricanes Katrina, Rita, Sandy, and Harvey had, in certain quarters, an adverse effect on our operating results, in part because of yard capacity constraints in the impacted areas of the United States. We regularly evaluate our capacity in all our markets and where appropriate, seek to increase capacity through the acquisition of additional land and yards. We may not be able to reach agreements to purchase independent storage facilities in markets where we have limited excess capacity, and zoning restrictions or difficulties obtaining use permits may limit our ability to expand our capacity through acquisitions of new land. Failure to have sufficient capacity at one or more of our yards could adversely affect our relationships with insurance companies or other sellers of vehicles, which could have an adverse effect on our consolidated results of operations and financial position.

Because the growth of our business has been due in large part to acquisitions and development of new facilities, the rate of growth of our business and revenues may decline if we are not able to successfully complete acquisitions and develop new facilities.

We seek to increase our sales and profitability through the acquisition of additional facilities and the development of new facilities. For example, in fiscal 2016, we opened new facilities in Castledermot, Republic of Ireland; Algete, Spain; and six new facilities in the U.S. In fiscal 2017, we opened a new facility in Bad Fallingbostel, Germany, a new facility in Betim, Minas Gerais, Brazil, nine new facilities in the U.S. and acquired Cycle Express, LLC, which conducts business primarily as National Powersport Auctions (NPA), a leading non-salvage auction platform for motorcycles, snowmobiles, watercraft and other powersports vehicles. NPA currently operates facilities in Atlanta, Georgia; Cincinnati, Ohio; Dallas, Texas; Philadelphia, Pennsylvania; and San Diego, California. In fiscal 2018, we opened new facilities in Andrews, Texas and Exeter, Rhode Island, a new facility in Belfast, Northern Ireland, a new facility in Nobitz, Germany, and acquired locations in the municipalities of Espoo; Pirkkala; Oulu; and Turku, Finland. Acquisitions are difficult to identify and complete for a number of reasons, including competition among prospective buyers, the availability of affordable financing in the capital markets and the need to satisfy applicable closing conditions and obtain antitrust and other regulatory approvals on acceptable terms. There can be no assurance that we will be able to:

- continue to acquire additional facilities on favorable terms;
- expand existing facilities in no-growth regulatory environments;
- increase revenues and profitability at acquired and new facilities;
- maintain the historical revenue and earnings growth rates we have been able to obtain through facility openings and strategic acquisitions;
- create new vehicle storage facilities that meet our current revenue and profitability requirements; or
- obtain necessary regulatory approvals under applicable antitrust and competition laws.

In addition, certain of the acquisition agreements by which we have acquired companies require the former owners to indemnify us against certain liabilities related to the operation of the company before we acquired it. In most of these agreements, however, the liability of the former owners is limited and certain former owners may be unable to meet their indemnification responsibilities. We cannot assure that these indemnification provisions will protect us fully or at all, and as a result we may face unexpected liabilities that adversely affect our financial statements. Any failure to continue to successfully identify and complete acquisitions and develop new facilities could have a material adverse effect on our consolidated results of operations and financial position.

As we continue to expand our operations, our failure to manage growth could harm our business and adversely affect our consolidated results of operations and financial position.

Our ability to manage growth depends not only on our ability to successfully integrate new facilities, but also on our ability to:

- hire, train and manage additional qualified personnel;
- establish new relationships or expand existing relationships with vehicle sellers;
- identify and acquire or lease suitable premises on competitive terms;
- secure adequate capital; and
- maintain the supply of vehicles from vehicle sellers.

Our inability to control or manage these growth factors effectively could have a material adverse effect on our consolidated results of operations and financial position.

Our annual and quarterly performance may fluctuate, causing the price of our stock to decline.

Our revenues and operating results have fluctuated in the past and can be expected to continue to fluctuate in the future on a quarterly and annual basis as a result of a number of factors, many of which are beyond our control. Factors that may affect our operating results include, but are not limited to, the following:

- fluctuations in the market value of salvage and used vehicles;
- fluctuations in commodity prices, particularly the per ton price of crushed car bodies;
- the impact of foreign exchange gain and loss as a result of international operations;
- our ability to successfully integrate our newly acquired operations in international markets and any additional markets we may enter;
- the availability of salvage vehicles;
- variations in vehicle accident rates;
- member participation in the Internet bidding process;
- delays or changes in state title processing;
- changes in international, state or federal laws or regulations affecting salvage vehicles;
- changes in local laws affecting who may purchase salvage vehicles;
- our ability to integrate and manage our acquisitions successfully;
- the timing and size of our new facility openings;
- the announcement of new vehicle supply agreements by us or our competitors;
- the severity of weather and seasonality of weather patterns;
- the amount and timing of operating costs and capital expenditures relating to the maintenance and expansion of our business, operations and infrastructure;
- the availability and cost of general business insurance;
- labor costs and collective bargaining;
- changes in the current levels of out of state and foreign demand for salvage vehicles;
- the introduction of a similar Internet product by a competitor; and
- the ability to obtain necessary permits to operate.

Due to the foregoing factors, our operating results in one or more future periods can be expected to fluctuate. As a result, we believe that period-to-period comparisons of our results of operations are not necessarily meaningful and should not be relied upon as any indication of future performance. In the event such fluctuations result in our financial performance being below the expectations of public market analysts and investors, the price of our common stock could decline substantially.

Our Internet-based sales model has increased the relative importance of intellectual property assets to our business, and any inability to protect those rights could have a material adverse effect on our business, financial position, or results of operations.

Our intellectual property rights include patents relating to our auction technologies, as well as trademarks, trade secrets, copyrights and other intellectual property rights. In addition, we may enter into agreements with third parties regarding the license or other use of our intellectual property. Effective intellectual property protection may not be available in every country in which our products and services are distributed, deployed, or made available. We seek to maintain certain intellectual property rights as trade secrets. The secrecy could be compromised by third parties, or intentionally or accidentally by our employees, which would cause us to lose the competitive advantage resulting from those trade secrets. Any significant impairment of our intellectual property rights, or any inability to protect our intellectual property rights, could have a material adverse effect on our consolidated results of operations and financial position.

We also may not be able to acquire or maintain appropriate domain names in all countries in which we do business. Furthermore, regulations governing domain names may not protect our trademarks and similar proprietary rights. We may be unable to prevent third parties from acquiring domain names that are similar to, infringe upon, or diminish the value of our trademarks and other proprietary rights.

We have in the past been and may in the future be subject to intellectual property rights claims, which are costly to defend, could require us to pay damages, and could limit our ability to use certain technologies in the future.

Litigation based on allegations of infringement or other violations of intellectual property rights are common among companies who rely heavily on intellectual property rights. Our reliance on intellectual property rights has increased significantly in recent years as we have implemented our auction-style sales technologies across our business and ceased conducting live auctions. Recent U.S. Supreme Court precedent potentially restricts patentability of software inventions by affirming that patent claims merely requiring application of an abstract idea on standard computers utilizing generic computer functions are patent ineligible, which may impact our ability to enforce our issued patent and obtain new patents. As we face increasing competition, the possibility of intellectual property rights claims against us increases. Litigation and any other intellectual property claims, whether with or without merit, can be time-consuming, expensive to litigate and settle, and can divert management resources and attention from our core business. An adverse determination in current or future litigation could prevent us from offering our products and services in the manner currently conducted. We may also have to pay damages or seek a license for the technology, which may not be available on reasonable terms and which may significantly increase our operating expenses, if it is available for us to license at all. We could also be required to develop alternative non-infringing technology, which could require significant effort and expense.

If we experience problems with our subhaulers and trucking fleet operations, our business could be harmed.

We rely primarily upon independent subhaulers to pick up and deliver vehicles to and from our storage facilities in the U.S., Canada, Brazil, U.A.E., Oman, Bahrain, Germany, the Republic of Ireland, Finland, and Spain. We also utilize, to a lesser extent, independent subhaulers in the U.K. Our failure to pick up and deliver vehicles in a timely and accurate manner could harm our reputation and brand, which could have a material adverse effect on our business. Further, an increase in fuel cost may lead to increased prices charged by our independent subhaulers, which may significantly increase our cost. We may not be able to pass these costs on to our sellers or buyers.

In addition to using independent subhaulers, in the U.K. we utilize a fleet of company trucks to pick up and deliver vehicles from our U.K. storage facilities. In connection therewith, we are subject to the risks associated with providing trucking services, including inclement weather, disruptions in transportation infrastructure, accidents and related injury claims, availability and price of fuel, any of which could result in an increase in our operating expenses and reduction in our net income.

We are partially self-insured for certain losses and if our estimates of the cost of future claims differ from actual trends, our results of operations could be harmed.

We are partially self-insured for certain losses related to medical insurance, general liability, workers' compensation and auto liability. Our liability represents an estimate of the ultimate cost of claims incurred as of the balance sheet date. The estimated liability is not discounted and is established based upon analysis of historical data and actuarial estimates. Further, we utilize independent actuaries to assist us in establishing the proper amount of reserves for anticipated payouts associated with these self-insured exposures. While we believe these estimates are reasonable based on the information currently available, if actual trends, including the severity of claims and medical cost inflation, differ from our estimates, our results of operations could be impacted.

Our executive officers, directors and their affiliates hold a large percentage of our stock and their interests may differ from other stockholders.

Our executive officers, directors and their affiliates beneficially own, in the aggregate, 16.0% of our common stock as of April 30, 2018. If they were to act together, these stockholders would have significant influence over most matters requiring approval by stockholders, including the election of directors, any amendments to our certificate of incorporation and certain significant corporate transactions, including potential merger or acquisition transactions. In addition, without the consent of these stockholders, we could be delayed or prevented from entering into transactions that could be beneficial to us or our other investors. These stockholders may take these actions even if they are opposed by our other investors.

We have certain provisions in our certificate of incorporation and bylaws which may have an anti-takeover effect or that may delay, defer or prevent acquisition bids for us that a stockholder might consider favorable and limit attempts by our stockholders to replace or remove our current management.

Our board of directors is authorized to create and issue from time to time, without stockholder approval, up to an aggregate of 5,000,000 shares of undesignated preferred stock, the terms of which may be established and shares of which may be issued without stockholder approval, and which may include rights superior to the rights of the holders of common stock. In addition, our bylaws establish advance notice requirements for nominations for elections to our board of directors or for proposing matters that can be acted upon by stockholders at stockholder meetings. These anti-takeover provisions and other provisions under Delaware law could discourage, delay or prevent a transaction involving a change in control of our company, even if doing so would benefit our stockholders. These provisions could also discourage proxy contests and make it more difficult for stockholders to elect directors of their choosing and cause us to take other corporate actions the stockholders desire.

If we lose key management or are unable to attract and retain the talent required for our business, we may not be able to successfully manage our business or achieve our objectives.

Our future success depends in large part upon the leadership and performance of our executive management team, all of whom are employed on an at-will basis and none of whom are subject to any agreements not to compete. If we lose the service of one or more of our executive officers or key employees, in particular Willis J. Johnson, our Chairman or A. Jayson Adair, our Chief Executive Officer, or if one or more of these executives decide to join a competitor or otherwise compete directly or indirectly with us, we may not be able to successfully manage our business or achieve our business objectives.

Cash investments are subject to risks.

We may invest our excess cash in securities or money market funds backed by securities, which may include U.S. treasuries, other federal, state and municipal debt, bonds, preferred stock, commercial paper, insurance contracts and other securities both privately and publicly traded. All securities are subject to risk, including fluctuations in interest rates, credit risk, market risk and systemic economic risk. Changes or movements in any of these risk factors may result in a loss or impairment to our invested cash and may have a material effect on our consolidated results of operations and financial position.

Rapid technological changes may render our technology obsolete or decrease the competitiveness of our services.

To remain competitive, we must continue to enhance and improve the functionality and features of our websites and software. The Internet and the online commerce industry are rapidly changing. In particular, the online commerce industry is characterized by increasingly complex systems and infrastructures. If competitors introduce new services embodying new technologies or if new industry standards and practices emerge, our existing websites and proprietary technology and systems may become obsolete. Our future success will depend on our ability to:

- enhance our existing services;
- develop and license new services and technologies that address the increasingly sophisticated and varied needs of our current and prospective customers; and
- respond to technological advances and emerging industry standards and practices in a cost-effective and timely basis.

Developing our websites and other proprietary technology entails significant technical and business risks. We may use new technologies ineffectively or we may fail to adapt our websites, transaction-processing systems and network infrastructure to customer requirements or emerging industry standards. If we face material delays in introducing new services, products and enhancements, our customers and suppliers may forego the use of our services and use those of our competitors.

New member programs could impact our operating results.
We have or will initiate programs to open our auctions to the general public. These programs include the Registered Broker program through which the public can purchase vehicles through a registered member and the Market Maker program through which registered members can open Copart storefronts with Internet kiosks enabling the general public to search our inventory and purchase vehicles. Initiating programs that allow access to our online auctions to the general public will involve material expenditures and we cannot predict what future benefit, if any, will be derived.
Factors such as mild weather conditions can have an adverse effect on our revenues and operating results, as well as our revenue and earnings growth rates, by reducing the available supply of salvage vehicles. Conversely, extreme weather conditions can result in an oversupply of salvage vehicles that requires us to incur abnormal expenses to respond to market demands.
Mild weather conditions tend to result in a decrease in the available supply of salvage vehicles because traffic accidents decrease and fewer automobiles are damaged. Accordingly, mild weather can have an adverse effect on our salvage vehicle inventories, which would be expected to have an adverse effect on our revenue and operating results and related growth rates. Conversely, our inventories will tend to increase in poor weather such as a harsh winter or as a result of adverse weather-related conditions such as flooding. During periods of mild weather conditions, our ability to increase our revenues and improve our operating results and related growth will be increasingly dependent on our ability to obtain additional vehicle sellers and to compete more effectively in the market, each of which is subject to the other risks and uncertainties described in these sections. In addition, extreme weather conditions, although they increase the available supply of salvage cars, can have an adverse effect on our operating results. For example, during fiscal 2006, fiscal 2013 and fiscal 2018, we recognized substantial additional costs associated with Hurricanes Katrina, Rita, Sandy, and Harvey. Weather events have had, in certain quarters, an adverse effect on our operating results, in part because of yard capacity constraints in the impacted areas of the U.S. These additional costs were characterized as “abnormal” under ASC 330, Inventory, and included premiums for subhaulers, payroll, equipment and facilities expenses directly related to the operating conditions created by the hurricanes. In the event that we were to again experience extremely adverse weather or other anomalous conditions that result in an abnormally high number of salvage vehicles in one or more of our markets, those conditions could have an adverse effect on our future operating results.
Macroeconomic factors such as high fuel prices, declines in commodity prices, declines in used car prices, and vehicle-related technological advances may have an adverse effect on our revenues and operating results, as well as our earnings growth rates.
Macroeconomic factors that affect oil prices and the automobile and commodity markets can have adverse effects on our revenues, revenue growth rates (if any), and operating results. Significant increases in the cost of fuel could lead to a reduction in miles driven per car and a reduction in accident rates. A material reduction in accident rates, whether due to, among other things, a reduction in miles driven per car, vehicle-related technological advances such as accident avoidance systems and, to the extent widely adopted, the advent of autonomous vehicles, could have a material impact on revenue growth. In addition, under our Percentage Incentive Program contracts, which we refer to as PIP, the cost of towing the vehicle to one of our facilities is included in the PIP fee. We may incur increased fees, which we may not be able to pass on to our vehicle sellers. A material increase in tow rates could have a material impact on our operating results. Volatility in fuel, commodity, and used car prices could have a material adverse effect on our revenues and revenue growth rates in future periods.
The salvage vehicle sales industry is highly competitive and we may not be able to compete successfully.
We face significant competition for the supply of salvage vehicles and for the buyers of those vehicles. We believe our principal competitors include other auction and vehicle remarketing service companies with whom we compete directly in obtaining vehicles from insurance companies and other sellers, and large vehicle dismantlers, who may buy salvage vehicles directly from insurance companies, bypassing the salvage sales process. Many of the insurance companies have established relationships with competitive remarketing companies and large dismantlers. Certain of our competitors may have greater financial resources than us. Due to the limited number of vehicle sellers, particularly in the U.K., the absence of long-term contractual commitments between us and our sellers and the increasingly competitive market environment, there can be no assurance that our competitors will not gain market share at our

expense.

We may also encounter significant competition for local, regional and national supply agreements with vehicle sellers. There can be no assurance that the existence of other local, regional or national contracts entered into by our competitors will not have a material adverse effect on our business or our expansion plans. Furthermore, we are likely to face competition from major competitors in the acquisition of vehicle storage facilities, which could significantly increase the cost of such acquisitions and thereby materially impede our expansion objectives or have a material adverse effect on our consolidated results of operations. These potential new competitors may include consolidators of automobile dismantling businesses, organized salvage vehicle buying groups, automobile manufacturers, automobile auctioneers and software companies. While most vehicle sellers have abandoned or reduced efforts to sell salvage vehicles directly without the use of service providers such as us, there can be no assurance that this trend will continue, which could adversely affect our market share, consolidated results of operations and financial position. Additionally, existing or new competitors may be significantly larger and have greater financial and marketing resources than us; therefore, there can be no assurance that we will be able to compete successfully in the future.

Government regulation of the salvage vehicle sales industry may impair our operations, increase our costs of doing business and create potential liability.

Participants in the salvage vehicle sales industry are subject to, and may be required to expend funds to ensure compliance with a variety of governmental, regulatory and administrative rules, regulations, land use ordinances, licensure requirements and procedures, including but not limited to those governing vehicle registration, the environment, zoning and land use. Failure to comply with present or future regulations or changes in interpretations of existing regulations may result in impairment of our operations and the imposition of penalties and other liabilities. At various times, we may be involved in disputes with local governmental officials regarding the development and/or operation of our business facilities. We believe that we are in compliance in all material respects with applicable regulatory requirements. We may be subject to similar types of regulations by federal, national, international, provincial, state and local governmental agencies in new markets. In addition, new regulatory requirements or changes in existing requirements may delay or increase the cost of opening new facilities, may limit our base of salvage vehicle buyers and may decrease demand for our vehicles.

Changes in laws or the interpretation of laws, including foreign laws and regulations, affecting the import and export of vehicles may have an adverse effect on our business and financial condition.

Our Internet-based auction-style model has allowed us to offer our products and services to international markets and has increased our international buyer base. As a result, foreign importers of vehicles now represent a significant part of our total buyer base. As a result our foreign buyers may be subject to a variety of foreign laws and regulations, including the imposition of import duties by foreign countries. Changes in laws and regulations that restrict the importation of vehicles into foreign countries may reduce the demand for vehicles and impact our ability to maintain or increase our international buyer base. In addition, we and our vehicle buyers must work with foreign customs agencies and other non-U.S. governmental officials, who are responsible for the interpretation of these laws. Any inability to obtain requisite approvals or agreements from such authorities could adversely impact the ability of our buyers to import vehicles into foreign countries. In addition, any disputes or disagreements with foreign agencies or officials over import duties or similar matters, including disagreements over the value assigned to imported vehicles, could adversely affect our costs and the ability and costs of our buyers to import vehicles into foreign countries. For example, in March 2008, a decree issued by the president of Mexico became effective that placed restrictions on the types of vehicles that can be imported into Mexico from the U.S. The adoption of similar laws or regulations in other jurisdictions that have the effect of reducing or curtailing our activities abroad, any failure to comply with non-U.S. laws or regulatory interpretations, or any legal or regulatory interpretations that significantly increase our costs or the costs of our buyers could have a material adverse effect on our consolidated results of operations and financial position by reducing the demand for our products and services and our ability to compete in non-U.S. markets.

The operation of our storage facilities poses certain environmental risks, which could adversely affect our consolidated financial position, results of operations or cash flows.

Our operations are subject to federal, state, national, provincial and local laws and regulations regarding the protection of the environment in the countries which we have storage facilities. In some cases, we may acquire land with existing environmental issues, including landfills as an example. In the salvage vehicle remarketing industry, large numbers of wrecked vehicles are stored at storage facilities and during that time, spills of fuel, motor oil and other fluids may occur, resulting in soil, surface water or groundwater contamination. In addition, certain of our facilities generate and/or store petroleum products and other hazardous materials, including waste solvents and used oil. In the U.K., we provide vehicle de-pollution and crushing services for end-of-life program vehicles. We could incur substantial expenditures for preventative, investigative or remedial action and could be exposed to liability arising from our operations, contamination by previous users of certain of our acquired facilities or facilities which we may acquire in the future, or the disposal of our waste at off-site locations. Environmental laws and regulations could become more stringent over time and there can be no assurance that we or our operations will not be subject to significant costs in the future. Although we have obtained indemnification for pre-existing environmental liabilities from many of the persons and entities from whom we have acquired facilities, there can be no assurance that such indemnifications will be adequate. Any such expenditures or liabilities could have a material adverse effect on our consolidated results of operations and financial position.

Adverse U.S. and international economic conditions may negatively affect our business, operating results, or financial condition.

The capital and credit markets have historically experienced extreme volatility and disruption, which has in the past and may in the future lead to economic downturns in the U.S. and abroad. As a result of any economic downturn, the number of miles driven may decrease, which may lead to fewer accident claims, a reduction of vehicle repairs, and fewer salvage vehicles. Increases in unemployment, as a result of any economic downturn, may lead to an increase in the number of uninsured motorists. Uninsured motorists are responsible for disposition of their vehicle if involved in an accident. Disposition generally is either the repair or disposal of the vehicle. In the situation where the owner of the wrecked vehicle, and not an insurance company, is responsible for its disposition, we believe it is more likely that vehicle will be repaired or, if disposed, disposed through channels other than us. Adverse credit markets may also affect the ability of members to secure financing to purchase salvaged vehicles which may adversely affect demand. In addition, if the banking system or the financial markets deteriorate or are volatile, our credit facility or our ability to obtain additional debt or equity financing may be affected. These adverse economic conditions and events may have a negative effect on our business, consolidated results of operations and financial position.

If we determine that our goodwill has become impaired, we could incur significant charges that would have a material adverse effect on our consolidated results of operations.

Goodwill represents the excess of cost over the fair market value of assets acquired in business combinations. As of April 30, 2018, the amount of goodwill on our consolidated balance sheet subject to future impairment testing was $342.5 million.

Pursuant to ASC 350, Intangibles—Goodwill and Other, we are required to annually test goodwill to determine if impairment has occurred, either through a quantitative or qualitative analysis. Additionally, interim reviews must be performed whenever events or changes in circumstances indicate that impairment may have occurred. If the testing performed indicates that impairment has occurred, we are required to record a non-cash impairment charge for the difference between the carrying value of the goodwill and the implied fair value of the goodwill in the period the determination is made. The annual goodwill impairment analysis, which was performed qualitatively in the fourth quarter of fiscal 2017, considered all relevant factors specific to our reporting units, including macroeconomic conditions; industry and market considerations; overall financial performance and relevant entity-specific events. Changes in these factors, or changes in actual performance, could affect the fair value of goodwill, which may result in an impairment charge. For example, deterioration in worldwide economic conditions could affect these assumptions and lead us to determine that goodwill impairment is required. We cannot accurately predict the amount or timing of any impairment of assets. We considered the above factors noting none involved significant uncertainty. In addition, the industry in which we operate improved over the observable period, and our calculated fair value exceeded carrying value for each reporting unit by a substantial amount in our prior year quantitative analysis, indicating no material risk as of April 30, 2018, with respect to potential goodwill impairments. Should the value of our goodwill become impaired, it could have a material adverse effect on our consolidated results of operations and could result in our incurring net losses in future periods.

Changes in federal, state and local, or foreign tax laws, changing interpretations of existing tax laws, or adverse determinations by tax authorities could increase our tax burden or otherwise adversely affect our financial condition or results of operations.

We are subject to taxation at the federal, state, provincial, and local levels in the United States, the United Kingdom, and various other countries and jurisdictions in which we operate, including income taxes, sales taxes, value-added (VAT) taxes, and similar taxes and assessments. The laws and regulations related to tax matters are extremely complex and subject to varying interpretations. Although we believe our tax positions are reasonable, we are subject to audit by the Internal Revenue Service in the United States, HM Revenue and Customs in the United Kingdom, state tax authorities in the states in which we operate, and other similar tax authorities in international jurisdictions. As previously disclosed, we have been subject to challenge by the Georgia Department of Revenue with respect to sales taxes and could face similar audits or challenges from applicable federal, state, or foreign tax authorities in the future. While we believe we comply with all applicable tax laws, rules, and regulations in the relevant jurisdictions, tax authorities may elect to audit us and determine that we owe additional taxes, which could result in a significant increase in our liabilities for taxes, interest, and penalties in excess of our accrued liabilities.

New tax legislative initiatives may be proposed from time to time, such as proposals for comprehensive tax reform in the United States, which may impact our effective tax rate and which could adversely affect our tax positions or tax liabilities. Our future effective tax rate could be adversely affected by, among other things, changes in the composition of earnings in jurisdictions with differing tax rates, changes in statutory rates and other legislative changes, changes in interpretations of existing tax laws, or changes in determinations regarding the jurisdictions in which we are subject to tax. From time to time, U.S. federal, state and local, and foreign governments make substantive changes to tax rules and their application, which could result in materially higher taxes than would be incurred under existing tax law and which could adversely affect our financial condition or results of operations.

The Tax Cuts and Jobs Act ("Tax Reform" or "Tax Act") was enacted on December 22, 2017. The Tax Act significantly revamped U.S. taxation of corporations, including a reduction of the federal income tax rate from 35% to 21%, a repeal of the exceptions to the $1.0 million deduction limitation for performance-based compensation to covered employees, and a new tax regime for foreign earnings. The repeal of the $1.0 million deduction limit for performance-based compensation, the new U.S. taxes on accumulated and future foreign earnings and other adverse changes resulting from the Tax Act, or a change in the mix of domestic and foreign earnings, might offset the benefit from the reduced tax rate, and our future effective tax rates and/or cash taxes may increase, even significantly, or not decrease much, compared to recent or historical trends. Many of the provisions of the Tax Act are highly complex and may be subject to further interpretive guidance from the IRS or others. Some of the provisions of the Tax Act may be changed by a future Congress or challenged by the World Trade Organization ("WTO"). Although we cannot predict the nature or outcome of such future interpretive guidance, or actions by a future Congress or WTO, they could adversely impact our consolidated results of operations and financial position. Income tax expense on accumulated foreign earnings recorded as a result of the Tax Act is a provisional amount and reflects our current best estimate, which may be adjusted over the course of the next year and could adversely affect our consolidated results of operations and financial position.

New accounting pronouncements or new interpretations of existing standards could require us to make adjustments to accounting policies that could adversely affect the consolidated financial statements.

The Financial Accounting Standards Board, the Public Company Accounting Oversight Board, and the SEC, from time to time issue new pronouncements or new interpretations of existing accounting standards that require changes to our accounting policies and procedures. To date, we do not believe any new pronouncements or interpretations have had a material adverse effect on our consolidated results of operations and financial position, but future pronouncements or interpretations could require a change or changes in our policies or procedures.

Fluctuations in foreign currency exchange rates could result in declines in our reported revenues and earnings.

Our reported revenues and earnings are subject to fluctuations in currency exchange rates. We do not engage in foreign currency hedging arrangements; consequently, foreign currency fluctuations may adversely affect our revenues and earnings. Should we choose to engage in hedging activities in the future we cannot be assured our hedges will be effective or that the costs of the hedges will exceed their benefits. Fluctuations in the rate of exchange between the U.S. dollar and foreign currencies, primarily the British pound, Canadian dollar, U.A.E. dirham, Bahraini dinar, Omani rial, Brazilian real, Indian rupee, Chinese renminbi, and European Union euro could adversely affect our consolidated results of operations and financial position.

On June 23, 2016, the U.K. held a referendum in which voters approved an exit from the European Union, commonly referred to as “Brexit.” In February 2017, the British Parliament voted in favor of allowing the British government to begin negotiating the terms of the U.K.’s withdrawal from the European Union and discussions with the European Union began in March 2017. Adverse consequences concerning Brexit or the European Union could include deterioration in global economic conditions, instability in global financial markets, political uncertainty, volatility in currency exchange rates, or adverse changes in the cross-border agreements currently in place, any of which could have an adverse impact on our financial results in the future.

ITEM 2. UNREGISTERED SALES OF EQUITY SECURITIES AND USE OF PROCEEDS

Unregistered Sales of Equity Securities

None.

Issuer Purchases of Equity Securities

None.

ITEM 6. EXHIBITS

a) Exhibits

3.1	Copart, Inc. Certificate of Incorporation
3.2	Certificate of Amendment to the Copart, Inc. Certificate of Incorporation
3.3	Bylaws of Copart, Inc.
31.1	Certification of Chief Executive Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
31.2	Certification of Chief Financial Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
32.1(1)	Certification of Chief Executive Officer pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
32.2(1)	Certification of Chief Financial Officer pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
101.INS	XBRL Instance Document
101.SCH	XBRL Taxonomy Extension Schema Document
101.CAL	XBRL Taxonomy Extension Calculation Linkbase Document
101.DEF	XBRL Taxonomy Extension Definition Linkbase Document
101.LAB	XBRL Taxonomy Extension Label Linkbase Document
101.PRE	XBRL Taxonomy Extension Presentation Linkbase Document
(1)	In accordance with Item 601(b)(32)(ii) of Regulation S-K and SEC Release No. 33-8238 and 34-47986, Final Rule: Management’s Reports on Internal Control Over Financial Reporting and Certification of Disclosure in Exchange Act Periodic Reports, the certifications furnished in Exhibits 32.1 and 32.2 hereto are deemed to accompany this Form 10-Q and will not be deemed “filed” for purposes of Section 18 of the Exchange Act. Such certifications will not be deemed to be incorporated by reference into any filings under the Securities Act or the Exchange Act, except to the extent that the registrant specifically incorporates it by reference.

SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

COPART, INC.

/s/ Jeffrey Liaw

Jeffrey Liaw, Chief Financial Officer (Principal Financial and Accounting Officer and duly Authorized Officer)

Date: May 25, 2018